

EUROPE: BERMUDA AND ITS SOLVENCY II EQUIVALENCE MEET THE HIGHEST STANDARDS

by Gavin Woods

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Bermuda has been granted equivalent status under the Solvency II directive, besides being approved as a qualified jurisdiction by the US National Association of Insurance commissioners. In the current socio-economic climate, one could be forgiven for thinking that international businesses use offshore jurisdictions to conduct their activities under a veil of secrecy, taking advantage of passive legislation and benevolent regulators.

However, Bermuda has taken significant steps to place itself as the benchmark for regulation and innovation. On 24 March, the European Commission awarded the British Overseas Territory with equivalent status under the Solvency II Directive.

This award came hard on the heels of another important accolade, as Bermuda was approved as a qualified jurisdiction by the US National Association of Insurance Commissioners. In addition, Bermuda was an early adopter of the Organisation for Economic Co-operation and Development's common reporting standards and recently signed up to country-by-country reporting.

The result is that Bermuda's insurance and reinsurance industry operates in a legal and regulatory environment that is on par with Europe and the US and, when measured against other offshore jurisdictions, stands in a peer group of one.

Solvency II finds its origin in the financial crisis of 2007-2008. Following calls for preventing excessive risks within the financial system, the European Union identified shortcomings in national supervisory models. The Solvency II directive sets up a risk-based prudential regime that regulates capital, governance and supervision, and disclosure and transparency requirements for the insurance and reinsurance industry.

THE EFFECTS OF EQUIVALENCY UNDER SOLVENCY II

Solvency II applies to insurance and reinsurance activity within the EU and so the advent of the regulation heralded significant hurdles for insurers based outside the EU, which will now be expected to satisfy additional collateral requirements for business ceded by EU companies.

Many insurers in non-EU jurisdictions pushed back against these requirements, either because they were not prepared to comply with the strict requirements of Solvency II or because the level of their EU-related business did not justify enacting measures to replicate Solvency II in their jurisdiction.

However, Bermuda's insurance industry operates on a global scale, with Bermuda-based insurers and reinsurers active in all major insurance hubs.

Bermuda's equivalency with Solvency II has many benefits, for example:

- contracts between EU insurers and Bermuda reinsurers are treated in the same manner as reinsurance contracts entered into between EU entities;
- EU insurers with a Bermuda subsidiary can use Bermuda's solvency rules to calculate group solvency and capital requirements; and
- the Bermuda regulator may be regarded as the group supervisor for Bermuda-based insurance groups operating in the EU.

In addition, Bermuda is home to a significant captive industry, as well as being the jurisdiction of choice for a majority of the world's insurance-linked securities. However, Bermuda was able to bifurcate its regulatory regime so that the requirements of Solvency II did not extend to limited-purpose insurers. As a result, Bermuda is in the unique position of being able to maintain a regulatory regime that is appropriate for both commercial insurers and reinsurers and limited-purpose insurers.

HEAD OFFICE REQUIREMENTS

One requirement resulting from equivalence under Solvency II was the need to maintain a 'head office' in Bermuda.

At first, there was some consternation among insurers, which queried whether this meant moving their offices and personnel to Bermuda. However, they need only demonstrate that they have a sufficient nexus with Bermuda.

The following factors can be used in assessing the nexus with Bermuda:

- where the underwriting, risk management and operational decision-making occur;
- whether senior executives, officers, insurance managers or employees are located in Bermuda;
- where board meetings occur; and
- the nature, scale and complexity of the insurer's business.

BERMUDA AS AN NAIC-APPROVED JURISDICTION

Bermuda was the first offshore jurisdiction to be granted 'qualified jurisdiction' status by the NAIC. As a result, its reinsurers are eligible for reduced collateral requirements in US jurisdictions that have adopted the revised Credit for Reinsurance Model Law and Regulations.

A non-US reinsurer will only be certified if it is licensed and domiciled in a qualified jurisdiction. Therefore, Bermuda's designation represents a significant benefit to Bermuda insurers or reinsurers in the US insurance market, resulting in less costs and greater efficiencies in conducting business across the insurance markets.

COUNTRY-BY-COUNTRY REPORTING

In April 2016, Bermuda adopted the OECD's country-by-country reporting regime. As a result, multinational enterprises headquartered in Bermuda will be required to file reportable information with the Bermuda Minister of Finance, starting 31 December 2017.

This start date is in line with a number of other countries (including France and the UK) and is an extension of Bermuda's move to become an early adopter of the OECD's other automatic exchange of tax information regime, the common reporting standards.

In conclusion, the use of offshore jurisdictions by international businesses has been much maligned in the current political climate. This is due, in part, to the perception that offshore jurisdictions allow business to be conducted in secrecy, hidden from the laws, regulations and oversight of onshore governments. It is inevitable, therefore, that offshore jurisdictions will be expected to increase their levels of regulatory scrutiny and oversight.

Through the recognition granted by the EU and the US, as well as the developments introduced through the common reporting standards and country-by-country reporting, Bermuda's legal and regulatory regime has proven that it meets the highest standards set by the international community.

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