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CAYMAN ISLANDS
INSURANCE COMPANIES

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Insurance Companies

FOREWORD

This memorandum has been prepared to assist those who are interested in forming an insurance company in the Cayman Islands. This memorandum is general in scope and is not intended to be comprehensive. It is not a substitute for legal advice. We recommend that our clients and prospective clients seek legal, tax and regulatory advice in all relevant jurisdictions on their specific questions.

The law and practice discussed in this memorandum is as of the date referred to below.

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Grand Cayman, Cayman Islands
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INTRODUCTION

The Cayman Islands recently updated its existing legislative regime with respect to insurers and reinsurers. The Insurance Law, 2010, which came into effect in November 2012, and its accompanying regulations (hereinafter collectively referred to as the "**Insurance Law**") establishes a more flexible and modern regime for the insurance industry while at the same time ensuring compliance with international regulatory standards.

The Insurance Law is the result of significant input from the public and private sectors. The goals of the legislation are to strengthen the regulatory powers of the Cayman Islands Monetary Authority ("**CIMA**"), enhance protection for policyholders in Cayman's domestic insurance market and facilitate the further development of Cayman's insurance linked securities ("**ILS**") and commercial reinsurance industries.

Insurance Licensing and Regulation

Under the Insurance Law, a person shall not carry on: (a) insurance business; (b) reinsurance business; or (c) business as an insurance agent, insurance broker, or insurance manager in or from within the Cayman Islands unless that person holds a valid licence issued for that purpose under the Insurance Law.

The Insurance Law defines long term insurance business, general insurance business and reinsurance business as follows:

1. Long term insurance business consists of the business of accepting life, annuity, accident and disability risks by effecting or carrying out insurance contracts, whether directly or indirectly, and certain other types of contracts expressed to be in effect for a period of not less than five years or without limit of time.

2. General insurance business is described as any business which is not long term business and also refers to the business of accepting risks by effecting or carrying out contracts of insurance, whether directly or indirectly, and includes running-off business including the settlement of claims.

3. Reinsurance business means the business of accepting risks by effecting or carrying out one or more contracts of reinsurance, whether directly or indirectly.

CIMA is responsible for the licensing, supervision, regulation and inspection of Cayman's (re)insurers, insurance agents, brokers and managers. Regulation of licensees under the Insurance Law consists of a combination of statutory filings, self-regulation and the potential review and investigation by CIMA in certain circumstances.

CIMA has wide powers under the Insurance Law to amongst other things, revoke licences and examine the affairs or business of a (re)insurer including, without limitation, obtaining access to the books, records and other documents of such companies, as well as the ability to request any information or thing from any person carrying on insurance or reinsurance business.

Categories of Licence

Under the previous legislation, insurers were categorized as either Class A insurers (those insurers incorporated either locally or overseas carrying on domestic insurance business in the Cayman Islands) or Class B insurers (typically insurers carrying on captive insurance business on a restricted or unrestricted licensed basis).

Under the newly enacted Insurance Law, Class A insurers continue to be those companies that are incorporated locally or overseas and are licensed to carry on domestic insurance business in the Cayman Islands.

The Class B licence intended for captives is no longer issued on a restricted or unrestricted basis - it is now divided into 4 proposed sub-categories depending on the percentage of net premiums written that originates from the captive insurance company's related business. "Related business" is defined as business originating from the insurer's members or the members of any group with which the insurer is related through common ownership or a common risk management plan, or as CIMA may determine. The Class B(i) licence is for those insurers carrying on non-domestic insurance business in respect of which 95% or more of the net premiums written will originate from the insurer's related business. The threshold is over 50% for the Class B(ii) insurer licence. Pursuant to a recently enacted but not yet fully in force amendment to the Insurance Law: (a) an insurer will now fall within Class B(iii) if 50% or less of its net written premiums originate from the insurer's related business and annual net earned premiums are *less* than US$20 million; and (b) an insurer will fall within Class B(iv) if 50% or less of its net written premiums originate from the insurer's related business and annual net earned premiums are *equal to or greater* than US$20 million.

Most single parent captives would fall within Class B(i). The capital requirements for each category will vary depending on the types of business being written (e.g., the more related business that is being written, the less minimum capital will be required under the Insurance Law).

While existing captives will have 18 months from November 1, 2012 to apply to be re-licensed in one of the Class B licence sub-categories, the practical impact of the Insurance Law on the captive insurance industry is not expected to be significant because many of the new provisions in the Insurance Law simply introduce into law CIMA's existing practices which were not enshrined in legislation (e.g., a licensee cannot change its name or establish a subsidiary, branch, agency or representative office outside Cayman without CIMA's approval). Nevertheless, if an existing licensee fails to file its re-licensing application by April 30, 2014, its old licence will expire, it will cease to be licensed and it will no longer be able to conduct insurance business.

The Insurance Law further defines the classes of insurer licences. The Cayman Islands is one of the leading jurisdictions for ILS, particularly catastrophe bonds. Under the old law, special purpose insurers ("**SPIs**") applied for a Class B licence which although generally designed for captives was sufficiently flexible to permit CIMA to licence and regulate SPIs as Class B insurers.

There are now two new categories of licence: the Class C licence and the Class D licence. The Class C licence is directed at those SPIs carrying on insurance business through the provision of reinsurance arrangements financed through the issuance of catastrophe bonds or similar instruments. Whereas, the Class D licence is intended to create a regulatory framework for those insurers carrying on commercial reinsurance business and "such other business as may be approved in respect of any individual licence" by CIMA. This class of insurer's licence designed primarily for commercial reinsurers provides CIMA with the flexibility to licence a range of business that may or may not fall within traditional insurance or reinsurance structures.

Licensing Procedure

A person desiring to carry on: (a) insurance business; (b) reinsurance business; or (c) business as an insurance agent, insurance broker or insurance manager in or from within the Cayman

Islands must submit an application in writing to CIMA in the prescribed form. All applications must be accompanied by a business plan containing the details outlined in the Insurance Law (which are discussed in further detail below); and the prescribed application fee which will be refunded if the licence application is not successful. Applicants must also include details of the proposed authorised capital and the method of capitalisation of the company and provide confirmation and details of the source of funds for the company's initial statutory capital.

CIMA has full discretion to approve or reject an application for licensing. Once approval has been granted, the company can be incorporated normally in accordance with the Companies Law (Revised). After incorporation, evidence of both the company's incorporation and the requisite capital funding as required under the Insurance Law is forwarded to CIMA pursuant to which it will issue the relevant licence. Upon receiving such licence, the company can commence operations.

Business Plan

Business plan requirements under the Insurance Law differ depending on which class of licence the applicant is seeking. However, most insurers submitting a licensing application must include a three year business plan including the following information:

(a) classes of insurance to be written;
(b) volume of premium to be written for each class;
(c) proportion of business to be reinsured and nature of reinsurance program;
(d) reserving philosophy with evidence of loss history where available;
(e) financial projections covering at least three years by class of business, identifying assumptions;
(f) underwriting procedures, guidelines and authorities (including pricing philosophies);
(g) claims management policy;
(h) investment policy;
(i) dividend policy; and
(j) corporate governance policies and internal controls.

Personnel

Licensees are required to employ fit and proper persons. In determining whether a person is "fit and proper", CIMA will consider all circumstances, including a person's (a) honesty, integrity and reputation, (b) competence and capability, and (c) financial soundness. CIMA is also bound by the Insurance Law to have regard to whether the applicant will be able to comply with the requirements of the Insurance Law and with the Cayman Islands' anti-money laundering legislation and whether the applicant has appropriate facilities, books and records and personnel with the necessary skills, knowledge and experience.

For each and every director, officer and if relevant manager, applicants for insurer licences must include with their respective licensing application:

(a) a personal questionnaire;
(b) three references acceptable to CIMA, comprising two character references and one reference verifying the person's good financial standing;
(c) police or other certificate satisfactory to CIMA confirming that the person in question has not been convicted of a serious crime or any offence involving dishonesty;
(d) curriculum vitae; and
(e) photo identification (passport or driver's licence) and proof of home address.

Capital Requirements

Minimal Capital and Prescribed Capital Requirements

A Class A insurer shall maintain adequate financial resources to meet its insurance business commitments and adequately manage its risks as required by the Insurance Law. The minimum capital requirement in respect of a Class A insurer that is an external insurer shall be the greater of US$1,000,000 or policy liabilities. The "available capital" (defined as total assets located in the Cayman Islands less total liabilities and any other deductions applicable relating to the company's Cayman risks) of a Class A insurer that is an external insurer shall at all times exceed the minimum capital requirement. The prescribed capital requirement for a Class A external insurer is 150% of the minimum capital requirement.

For a Class A insurer that is a local insurer, the minimum capital requirement is the greater of US$300,000 or the square root of the sum of the square of: (i) capital required for assets; (ii) margin for policy liabilities; (iii) capital for subsidiaries; (iv) margin for catastrophes; and (v) margin for foreign exchange risk as determined in accordance with the Insurance Law. The "available capital" (defined in the case of a local insurer as capital and surplus made up of issued share capital; additional paid in capital, including share premiums; retained earnings; investment reserves; currency translation reserves; and other equity reserves, less any applicable deductions or accumulated deficits) of a Class A insurer that is a local insurer shall at all times exceed the minimum capital requirement. The prescribed capital requirement for a Class A local insurer is 125% of the minimum capital requirement.

"Minimum capital requirements" for a Class B, C and D insurer means the minimum capital that such an insurer must maintain in order to operate in accordance with the Insurance Law. The minimum capital requirements are as follows:

Class	General	Long-term	Composite
B(i)	US$100,000	US$200,000	US$300,000
B(ii)	US$150,000	US$300,000	US$450,000
B(iii)	US$200,000	US$400,000	US$600,000
C	US$500	US$500	US$500
D	US$50,000,000	US$50,000,000	US$50,000,000

As of the date of this publication the minimum capital and prescribed capital requirements for Class B(iv) insurers had not yet been published.

In order to ensure that Class B, C or D insurers are operating safely, the Insurance Law also sets forth prescribed capital requirements. For Class B(i) and Class C insurers, the prescribed capital requirements are equal to the minimum capital requirements. In respect of Class B(ii), B(iii) and D insurers, the prescribed capital requirements are a formula based on premiums and reserves. Harneys would be pleased to provide specific advice, guidelines and calculations relating to prescribed capital requirements for these insurers upon request.

Enhanced Capital Requirements

Notwithstanding the capital requirements prescribed under the Insurance Law, CIMA may require any insurer to maintain a higher level of capital based on risk factors specific to that insurer and CIMA may exclude from the calculations any assets that it deems inappropriate.

Margins of Solvency

Unless otherwise approved by CIMA, a Class B, C or D insurer shall maintain minimum margin of solvency equal to or in excess of the total prescribed capital requirement.

Reporting Requirements

At the end of each quarter each Class A insurer shall calculate, using net written premium for the twelve months ending in that quarter, and record the minimum capital requirement and prescribed capital requirement and if required the enhanced prescribed capital requirement in accordance with the Insurance Law. A Class A insurer shall notify CIMA within thirty business days of the end of each quarter where it fails to meet the minimum capital requirement, prescribed capital requirement or enhanced prescribed capital requirement (if any).

As of each annual filing date, a Class B, C or D insurer shall calculate and record its respective minimum capital requirement and prescribed capital requirement, and if required, the enhanced capital requirement. A Class B, C or D insurer shall, on or before its requisite annual filing date, also furnish CIMA with the insurer's capital and solvency return.

Where the capital of an insurer falls below the prescribed capital requirement but is greater than the minimum capital requirement, the licensee shall meet with CIMA and present a remedial action plan. If the capital of a licensee falls below its minimum capital requirement, CIMA may consider regulatory action.

All insurers shall, except as otherwise approved by CIMA in writing, submit to CIMA by way of annual return, within six months of the end of its financial year, the information prescribed by the Insurance Law, including, without limitation, written confirmation that the information set out in the application for the licence, as modified by any subsequent changes approved by CIMA, remains correct. Every Class B insurer that writes long term business and each Class D insurer must along with its respective annual return also submit an actuarial valuation of its assets and liabilities including loss and loss expense provisions certified by an actuary approved by CIMA; and a certification of solvency prepared by a CIMA approved person.

Auditor and Financial Statement Requirements

Along with its annual return, an insurer must submit to CIMA audited financial statements prepared in accordance with internationally recognised accounting standards by an independent auditor approved by CIMA, together with a copy of any prescribed management letter issued by the auditor.

"Auditor" is defined under the Insurance Law as a person who has qualified as an accountant by examination of one of the Institutes of Chartered Accountants in England and Wales, Ireland and Scotland, or the Canadian Institute of Chartered Accountants or the American Institute of Certified Public Accountants, and who is a current member of good standing of one of such institutes or a person of good standing with some other accountancy qualification recognised by CIMA.

Other Requirements

The Insurance Law also includes new provisions related to:

- public disclosure requirements;

- change of control (i.e., CIMA must now approve the issuance of shares totaling more than 10% of the authorised share capital of a licensee and the transfer of more than 10% of the issued shares or total voting rights of a licensee (previously, in both cases, the threshold was 5%));
- enhanced powers for CIMA (e.g., for those insurance companies formed as segregated portfolio companies, CIMA can now take certain actions against a cell and not just the SPC itself);
- increased duties (including whistle-blowing obligations) for auditors and insurance managers; and
- penalties for late filings and non-compliance.

Fees

All insurers will pay registration and thereafter, annual fees to the Registrar of Companies based on the company's authorised share capital which fees generally do not exceed US$3,000.

Furthermore, at present, the licence and later annual fees for Class A insurers is approximately US$91,463.

Previously, Class B insurers (whether licensed on a restricted or unrestricted basis) were required to pay an initial licence and subsequent annual fee of approximately US$10,366. Under the Insurance Law, the licence and annual fees for Class B(i) insurers is approximately US$10,366, US$11,585 for Class B(ii) insurers and US$12,805 for Class B(iii) insurers. As of the date of this memorandum, the licence and annual fees for Class B(iv) insurers had not yet been published. Until they are re-licensed in one of the 4 sub-categories, existing Class B licensees will be required to pay an annual fee of US$10,366.

The licence and annual fees for Class C insurers is US$6,098 and the licence and annual fees for Class D insurers is US$102,440.

Taxation

There are no income, corporation, capital gains or other taxes in effect in the Cayman Islands applicable to a Cayman company conducting offshore business on the basis of present legislation. Certain documents brought into Cayman or presented to a court in Cayman are subject to stamp duty which is generally nominal. All exempted companies are entitled to apply for and receive from the government a "Tax Exemption Undertaking" exempting them from any possible future Cayman taxes for a period of twenty years from the date of the undertaking irrespective of any change in law.

Principal Office and Insurance Manager

Each Class A and Class D insurer shall have a place of business in the Cayman Islands where full and proper business records of the business will be maintained.

The Insurance Law requires every Class B or C insurer, unless it maintains permanently a place of business approved by CIMA to appoint an insurance manager in the Cayman Islands and maintain, at the insurance manager's place of business or at another location approved by CIMA, full and proper records of the business activities of such insurer.

FURTHER INFORMATION

If you would like further information on the subject matter of this memorandum please contact the attorney set forth below for further information.

Cayman Islands

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The foregoing discussion and analysis is for general information purposes only and is not intended to be relied upon for legal advice in any specific or individual situation.

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