SRS

Strategic Risk Solutions

Cell *Vehicles*

Domicile Differences

Introduction

Let's start at the beginning... sometimes insureds need an alternative risk retention strategy without the costs or capital and complexity of a wholly owned standalone captive. So, depending on where you are in the world or where you'd like to be; you decide to establish a cell vehicle. There are three types of cell vehicles. Those with a single legal identity encompassing a core and multiple cells, known variously as Protected Cell Companies (PCCs), Segregated Account Companies (SACs), or Segregated Portfolio Companies (SPCs); those that house multiple legal entities and multiple cells known as Incorporated Cell Companies; and those that sit in between known as Series LLCs.

Since their invention in Guernsey in 1997, cellular companies have proliferated throughout the world to the extent that they now exist in over 40 different jurisdictions. There are many factors that go into deciding whether a cell vehicle is right for you and your business. Location is one of those factors. We have set out some of the key differences that apply to the principal cellular company jurisdictions throughout the world.

United States

In the U.S., cell companies are referred to by a wide variety of names. Different states have not only different naming conventions, but also different forms of vehicle which are too varied to explore within the confines of this short article. Common benefits that cell vehicles may provide are lower upfront capital, less development time, and less cost due to economies of scale. Protected, incorporated, and Series LLC cells are available depending upon the needs of the insured.

Because of quick establishment and lower upfront capital costs, there has been a huge increase in cell growth during the past 10 years.

At one time, the core capital required for a cell facility was more than a million dollars, whereas now it can be as low as $75,000. Cells are only used for insurance business and once regulatory approval is achieved, establishment of a cell in the U.S. can happen relatively fast, usually between two to four weeks. Looking forward the industry suggests that cells used to support genuinely "entrepreneurial structures" may be established to enable the insured to participate on risk when there are capital constraints. This means cells could help programs getting off the ground by eliminating the need for regulatory capital as that has been addressed by the Core.

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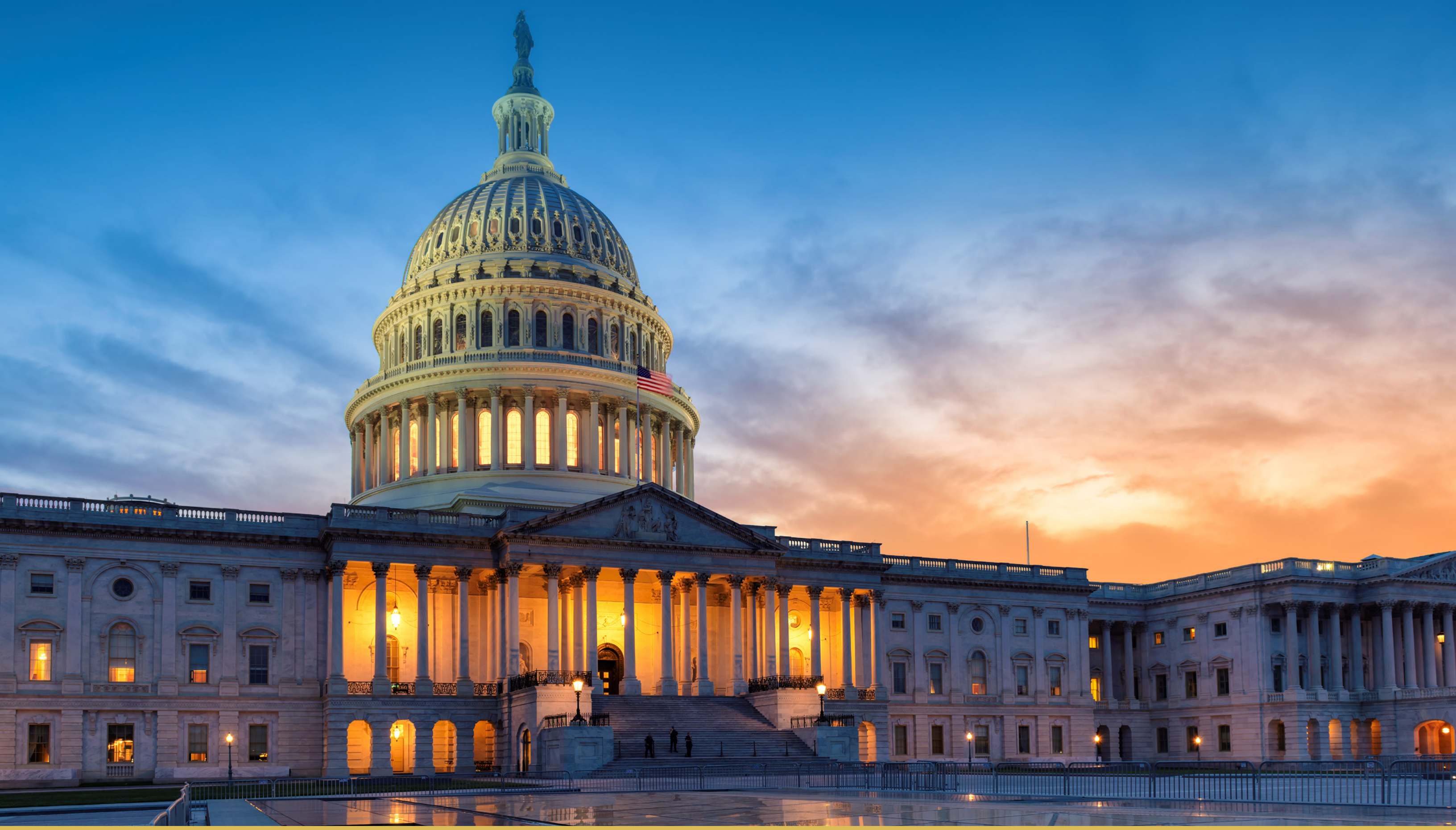
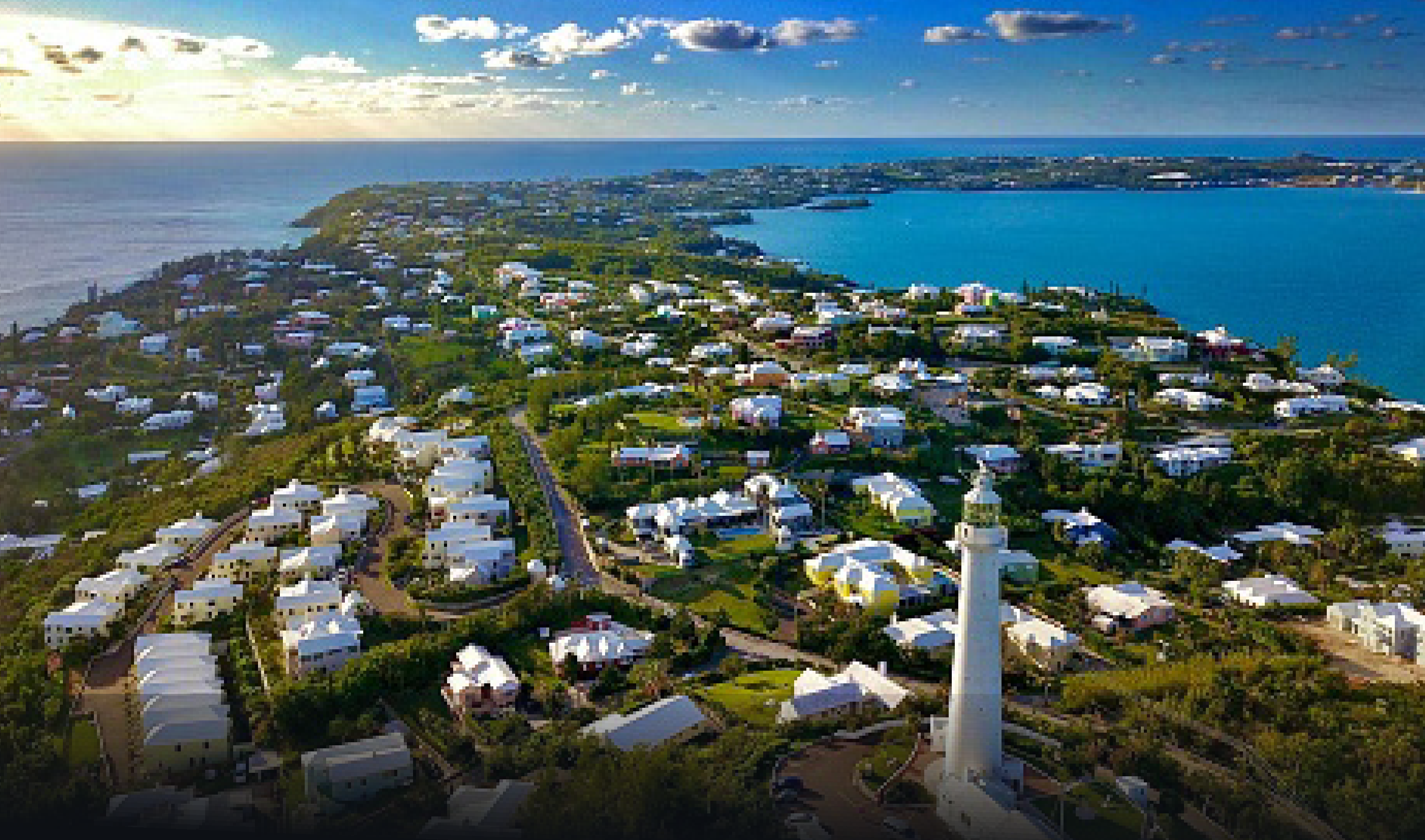




Bermuda

Segregated Accounts Companies (SAC) are formed in accordance with the Segregated Accounts Companies Act 200 under Bermuda Law. They can also be formed under private acts which may provide more concrete protections to the segregation of assets and liabilities specific to the company. The segregated account structure can be applied across a range of captive and commercial licenses (1, 2, 3, 3A, and 3B). The most common use of Segregated Account Companies refers to a class 3 i.e. captive insurance business.

Bermuda cells are mostly used as an entry point to the captive concept. Sometimes they're used where stand-alone captives would be too expensive. We are increasingly seeing Bermuda cells used to provide Side A Directors and Officers (D&O) insurance which is supported by the active Rhode Island market. The strong Rhode Island market presence in Bermuda certainly helps generate interest as a domicile. Class 3 companies can benefit from the ability to write risks unrelated to the core owner without imposing the Bermuda Solvency Capital Requirement (BSCR) solvency model (SII equivalent).

Bermudan cells are also commonly used as Special Purpose Insurers (SPIs) and Collateralized Insurers (Cis) within the Insurance-Linked Securities (ILS) space. The three most common benefits that a cell vehicle in Bermuda provides are:

1. Cost effective, fast, and efficient access to a captive-like (risk retention) structure
2. Lack of shareholding/corporate consolidation reduces conflicts of interest
3. Avenue for commercial initiatives and fronting without the need to consider the BSCR model

Incorporated Segregated Accounts Companies (ISAC) are available in Bermuda, but less common. Specific regulatory approval is required to establish a cell in Bermuda, but the regulator will typically allow cells to be formed in accordance with the business plan/license restrictions without prior approval and just with notification at year end.

Going forward the SAC act will continue to underpin the ILS industry through CIs and SPI licenses. Cells will also be used within the rent-a-captive model and will continue to provide support to the commercial fronting (non-admitted/non-rated) space and for hard to place coverages such as cyber/D&O as relief from distressed commercial markets.

Cayman Islands

Cell companies are called Segregated Portfolio Companies (SPC) in the Cayman Islands and are mostly used for segregation of assets and liabilities. That can be for a single parent captive that may want to have a certain line of coverage segregated or for a rent-a-captive that allows other parties to set up their own cell(s) within a larger structure. The three most common benefits that a cell vehicle provides are:

- Lower barrier to entry for prospective captive owners/participants.
- Regulators generally approve new cell applications faster than a stand-alone captive.
- Segregation of assets and liabilities.

The Cayman Islands SPC structure does not on its own create cells that are incorporated as separate legal entities. However, there is specific legislation for Portfolio Insurance Companies (PIC) that allows for an incorporated entity within an SPC structure. PICs allow for contractual relationships to be established between any external party and between any cells of the SPC and also have the advantage of allowing for separate governance within the SPC structure.

They can also be used to streamline a cell's transition into a stand-alone company should that be the desire of the PIC owners.

When it comes to regulatory approval, to establish a SPC, approval from the Cayman Islands Monetary Authority (CIMA) is required.

SPCs can also be created for investment fund purposes or other finance related activities where the segregation of assets and liabilities within a single entity would be desirable, but an SPC can not be utilized for both insurance and investment fund purposes. As a result, there has been a large portion of growth in Cayman related to SPCs. Currently there are 148 SPCs licensed in the Cayman Islands and cell growth within the island has increased.

Q: What do you think cells will be used for most in the future?

A: We see cell usage being generally the same as what has been in the past but for more clients in number and sophistication.

Guernsey

What are the three most common benefits that a cell vehicle provides?

- *Speed of establishment, ongoing expense reduction,and capital reduction*

United States

What are cell vehicles most commonly used for in your jurisdiction?

- *Separately Incorporated Cell Company*

Cayman Islands

Have cells promoted growth in your insurance sector in the past 10 years?

- *Yes, a large portion of the growth in Cayman has been related to SPC's. Currently there are 148 SPC's licensed in the Cayman Islands and cell growth within that sector has grown very quickly.*

Malta

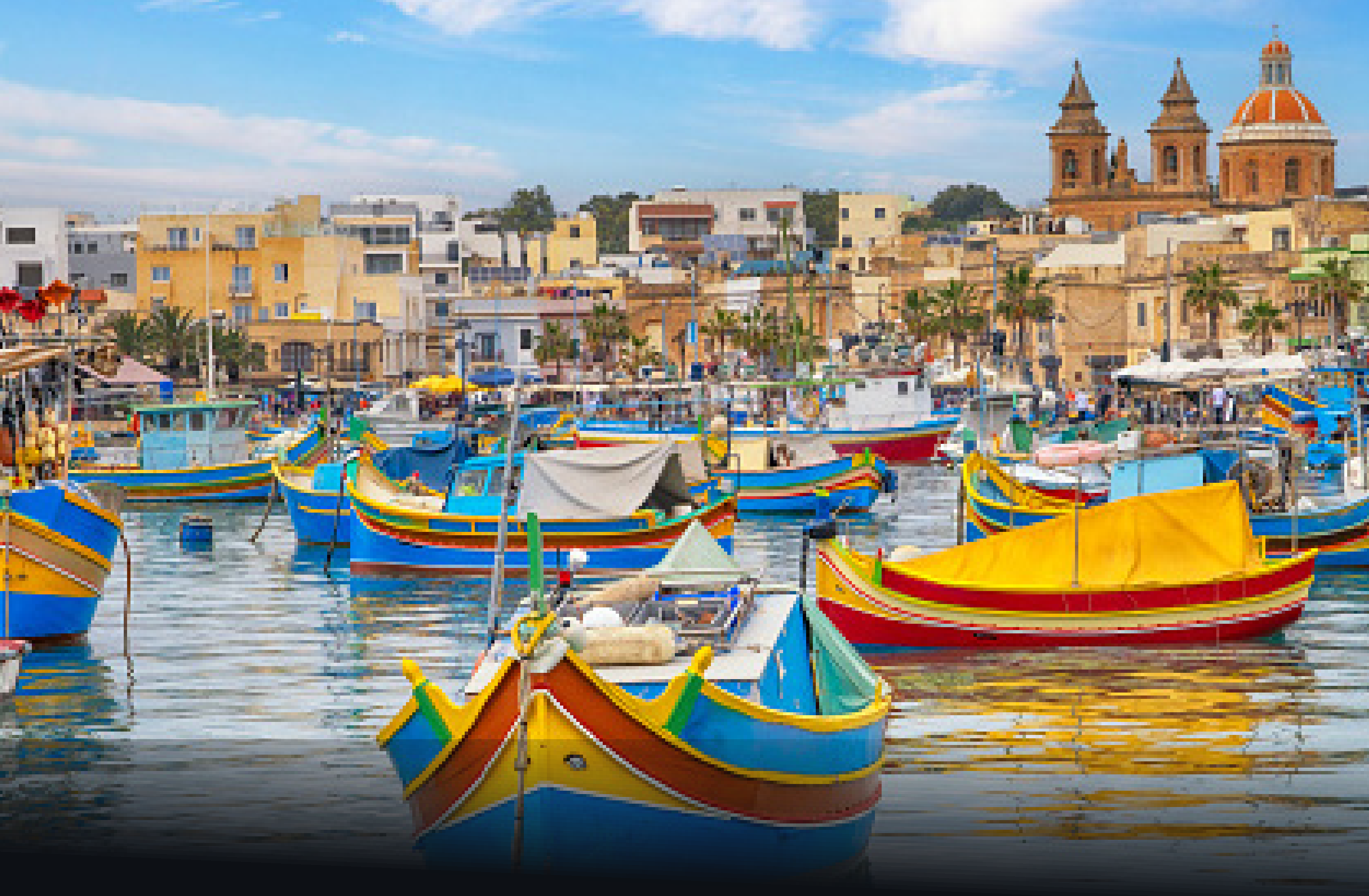
Which is the only EU member state with PCC legislation?

- *Malta, allowing Cell owners to write business across all EU/EEA countries.*

Bermuda

Can cells be used for any other business besides insurance business?

- *Yes, cells can be used to issue derivative contracts*



Malta

Malta is the only EU member state with PCC legislation which was passed in 2004. Cell owners setting up a cell vehicle in Malta may avail themselves of Freedom of Service and Freedom of Establishment passporting rights to write business across all EU/EEA countries, whether set up to:

- insure their own risks (captive cell).
- sell insurance to third parties (third party writing cells).
- reduce EEA fronting costs (fronting cell).
- insure risks on a non-admitted basis globally, where allowed.
- reinsure risks outside the EEA.

Because of hardening markets, capacity issues, and access to the EU/EEA markets, establishing a PCC in Europe has multiple benefits such as:

- Low capital requirements
- Substance and Resources share economies of scale
- Direct writing into Europe
- Reinsurance access for smaller insurers

Businesses looking to establish a PCC or create a cell are required to get the approval and authorization of the Malta Financial Services Authority (MFSA). Malta has enacted legislation for both PCCs and Incorporated Cell Companies (ICCs). Within the insurance market the PCCs are sector specific, for example, Insurance PCCs can only have insurance cells, Management PCCs only management cells, and Broker PCCs only broker cells. For the future, Malta should expect to see growth in the PCC market driven by the creation of cells with added interest from FinTech and InsurTech sectors.

Q: Is specific regulatory approval required to establish a cell in your jurisdiction?

A: Yes, approval and authorization of the Malta Financial Services Authority (MFSA) is required.

Guernsey

Just as in Malta and other parts of Europe, cells are referred to as PCCs and are most used for captives, insurance-linked securities, transformers, and commercial insurers. Guernsey was the first jurisdiction to introduce this type of vehicle 28 years ago, therefore they are commonly used for a wide variety of structures. PCCs in Guernsey can be established quickly and provide ongoing expense and capital reduction. Both protected cells and incorporated cell companies are available. Within the insurance sector, ICCs are used mostly for pension longevity risk transfer deals.

In order to establish a cell in Guernsey a business would need regulatory approval. Pre-approval is sometimes available to certain types of Special Purpose Insurer and captive cells. Cells can also be used for other reasons besides insurance business. Investment business and other types of support for regulated financial services activity is permitted. Cells in the past 20 years have been an engine of growth for the insurance sector in Guernsey

Regardless of where you choose to establish a cell vehicle, the overall benefits can be fruitful. Each of these locations is an option to reap the benefits of a captive.

Q: What are cell vehicles most commonly used for in your jurisdiction?

A: Captives, ILS transformers, Commerical Insurers