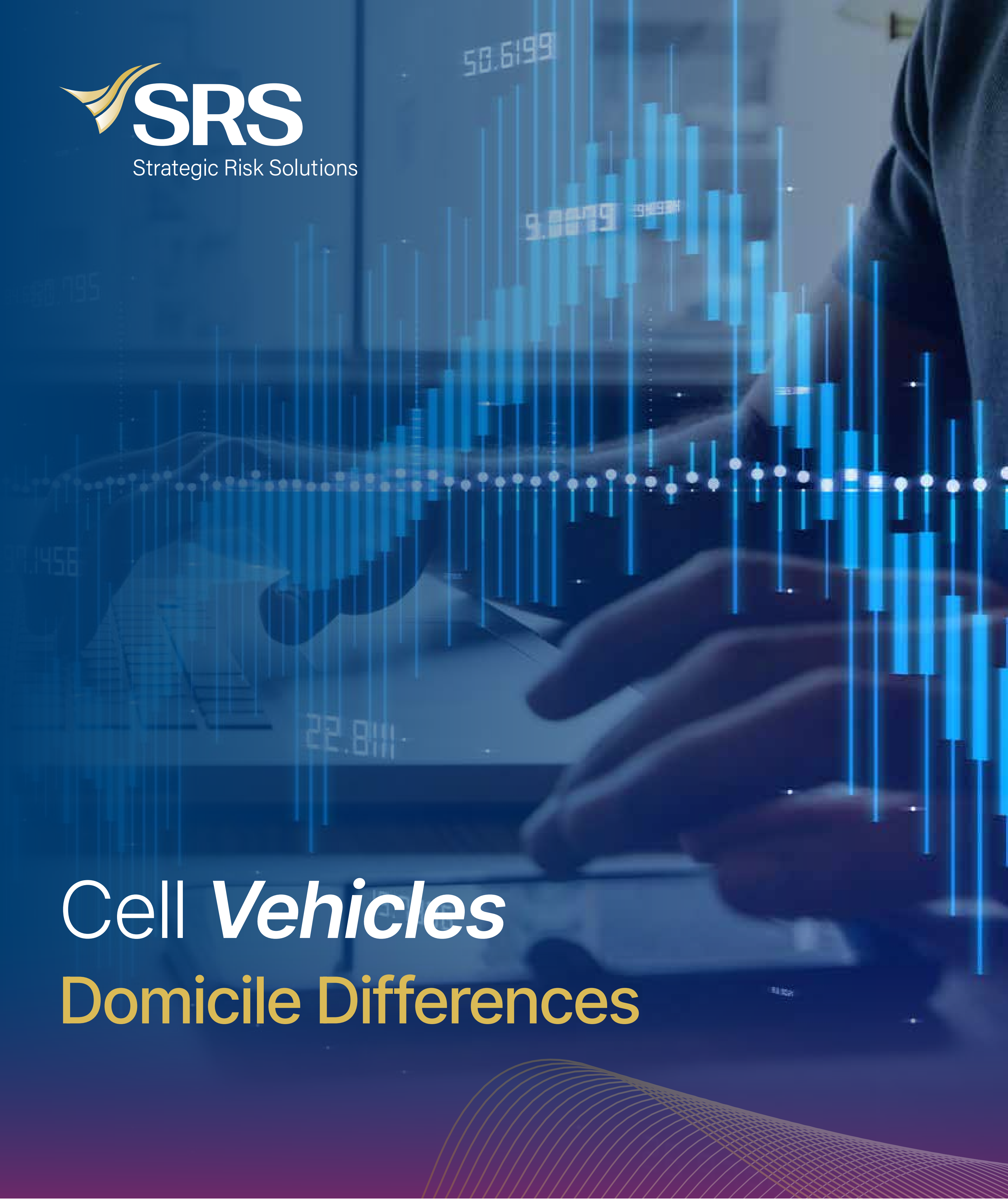

Strategic Risk Solutions

Cell ***Vehicles***

Domicile Differences

Introduction

Let's start at the beginning... Sometimes insureds need an alternative risk retention strategy without the costs/capital and complexity of a wholly owned, standalone captive. So, depending on where they are in the world, or where they'd like to be, they might 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 accounts companies (SACs), or segregated portfolio companies (SPCs); those that house multiple legal entities and multiple cells, known as incorporated cell companies (ICCs); 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 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 across the globe.

United States

In the US, cell companies are referred to by a wide variety of names. Different states not only have different naming conventions, but also different forms of vehicle, which are too varied to explore within the confines of this brochure. Common benefits US 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 US cell growth over the past 10 years.

At one time, the core capital required for a US cell facility was more than $1M, 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 US can happen relatively fast—usually between two to four weeks. Looking forward, the industry suggests cells used to support genuinely "entrepreneurial structures" may be established to enable the insured to participate in risk when there are capital constraints. This means cells could help those programs just getting off the ground by eliminating the need for regulatory capital (as this would be addressed by the core).

> *...cells could help those programs just getting off the ground by eliminating the need for regulatory capital..."*

Bermuda

Segregated accounts companies (SACs) are formed in accordance with the Segregated Accounts Companies Act of 2000 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 a company. The segregated account structure can be applied across a range of captive and commercial licenses (Classes 1, 2, 3, 3A, and 3B). The most common use of "SAC" refers to a Class 3 (i.e., captive insurance) business.

Bermuda cells are mostly used as an entry point into the captive concept. Sometimes they're used in instances in which standalone 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 the island nation 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 (the SII equivalent).

Bermudian 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 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, which reduces conflicts of interest.
3. Avenue for commercial initiatives and fronting, without the need to consider the BSCR model.

Incorporated segregated accounts companies (ISACs) are available in Bermuda, but these are 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 simply 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 (SPCs) in the Cayman Islands and are mostly used for segregation of assets and liabilities. These SPCs can be for a single-parent captive that may want to segregate a certain line of coverage. They can also be 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 a Cayman cell vehicle provides are:

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

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

PICs can also be used to streamline a cell's transition into a standalone company, should that be the desire of the PIC owners.

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

SPCs can also be created for investment fund purposes or for other finance-related activities in which the segregation of assets and liabilities within a single entity would be desirable. However, an SPC cannot 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 nation 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 it has been in the past, but for more clients (in number and sophistication).

Guernsey

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

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

Cayman Islands

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

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

Bermuda

Can cells be used for any other business besides insurance?

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

United States

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

- *Separately incorporated cell companies.*

Malta

Which is the only EU member state with PCC legislation?

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

Barbados

What does the licensing process require?

- *To establish a cell in Barbados you must complete an application, feasibility study, and compliance review.*

Malta

Malta is the only EU member state with protected cell company (PCC) legislation, which the country passed in 2004. Owners setting up a cell vehicle in Malta may avail themselves of freedom to provide 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. In 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

Guernsey was the first jurisdiction to introduce protected cell company (PCC) legislation back in 1997. Therefore, PCCs in Guernsey are commonly used for a wide variety of structures, including insurance-linked securities (ILS) transformers and commercial insurance products. These PCCs can be established quickly and provide ongoing expense and capital reduction. In 2006, Guernsey introduced PCC legislation allowing for both protected cell and incorporated cell companies (ICCs). Within the insurance sector, ICCs are used mostly for pension longevity risk transfer deals.

To establish a cell in Guernsey, a business needs regulatory approval. Pre-approval is sometimes available to certain types of special purpose insurer (SPI) 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. Over the past 20 years, cells have been an engine of growth for the insurance sector in Guernsey.

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

A: Captives, ILS transformers, and commercial insurers.

Barbados

In Barbados, cell companies can either be segregated cell companies (SCCs) or incorporated cell companies (ICCs). SCCs are often utilized in a rent-a- captive format that allows businesses to reap the benefits of a captive insurance company without having to form their own single/pure captive. SCCs have historically been the more popular form of cell company due to their ease of setup. ICC legislation was introduced more recently in Barbados and is gaining popularity because each cell acts as a separate legal entity, offering stronger legal separation and governance flexibility.

Barbados is considered a favorable location for captive insurance companies for many reasons. As a domicile, Barbados has a simple, strong, and flexible regulatory framework for captive insurance companies. It includes reasonable solvency requirements and streamlined licensing procedures, with an ability to write all major lines of insurance. Barbados also has an extensive tax treaty network within many major markets.

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 rewards of a captive.

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

A: Reinsurance, private placement life insurance, and estate planning, with Latin American entities being more interested in the ICC structure.