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Captive domicile growth creates more choice than ever for owners

Regulatory issues, infrastructure scrutinized

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BURLINGTON, Vt. — Prospective captive owners have more choice than ever in terms of available domiciles, but the key factors in their decisions typically remain regulatory quality and available captive infrastructure, according to many captive experts.

While new domiciles continue to form, some wonder whether they'll be able to provide the needed level of regulatory support or be able to achieve a critical mass of captive formations needed to ultimately compete with established domiciles.

Peter Mullen, Pembroke, Bermuda-based CEO of Aon Global Risk Consulting's captive and insurance management operations, suggested keeping a close eye on all the new domiciles. “We would have a concern that they could all support the right level of regulatory infrastructure,” said Mr. Mullen.

Many of the new domiciles, including New Jersey, North Carolina and Texas, are looking to attract the captives formed by businesses that are based in the state, Mr. Mullen said. “But that's finite.”

Established domiciles have a track record prospective captive owners can consider, Mr. Mullen said, something the new domiciles lack. The newer domiciles also potentially face a “dearth of regulatory talent,” Mr. Mullen said, adding that he doesn't think it's a good thing when captive regulation is only a part-time responsibility for a domicile's insurance regulators.

Mr. Mullen offered his thoughts in an interview during the Vermont Captive Insurance Association's annual conference in Burlington, Vt.

“It really is amazing in terms of the number of domiciles,” said James A. Swanke Jr., a director at Towers Watson & Co. in Minneapolis.

Mr. Swanke said he sees clients considering some of the newly formed captive domiciles. “I think some of the new domiciles are getting a look,” he said. “I think people are kicking the tires on them.”

But there's always a tendency to include one of the traditional domiciles in any assessment of forming a captive, Mr. Swanke said. An established captive infrastructure is an important consideration, he said, adding, “What we tell our clients is get on an airplane, visit two or three domiciles, meet the regulators and figure out which is best for your situation.”

In choosing a domicile, it's important that the captive regulation be separate from the politics in a domicile, Mr. Swanke said. “Being comfortable with the regulators and the regulation is very important.”

And from a business reputation perspective, it's important that captive parents make the right domicile choice, Mr. Swanke said, and not find their captive located in a place where changing political winds affect the commitment to captives or political considerations drive captive regulation.

“You just don't want surprises when you're working with a captive,” he said.

Speaking on a panel examining companies' expanding utilization of their captives, Tim East, director of risk management for The Walt Disney Co. in Burbank, Calif., said the regulatory environment was a strong consideration when Disney chose the domicile for its first captive. Disney ultimately chose Vermont for its Buena Vista Insurance Co. property insurance captive in 2002, and chose the domicile again for its Alameda Insurance Co. casualty captive in 2003.

In selecting a domicile, the company wanted a flexible captive environment but also wanted strong regulatory oversight, Mr. East said, because Disney's No. 1 asset is its reputation.

Speaking on the same panel, Anthony A. Benish, general counsel for Cook-Illinois Corp. in Oak Forest, Ill., said his company initially chose Bermuda for its Five Families Insurance Ltd. captive when it formed in 2006 because it was looking for possible tax benefits and easy access to the reinsurance market.

But, he said, “We had some bumps in the road in Bermuda and decided in 2010 to relocate to Vermont.” In fact the company hadn't used the captive to gain access to the reinsurance market and was electing to be taxed as a U.S. company, so the onshore domicile made sense, Mr. Benish said.

One factor that's been driving fewer domicile decisions than some had anticipated is the Nonadmitted and Reinsurance Reform Act of the Dodd-Frank Wall Street Reform and Consumer Protection Act, said Daniel D. Towle, director of financial services in the Vermont Department of Economic Development.

At issue is whether the NRRA subjects insurance business placed in captives operating outside their parent's home states to home state self-procurement taxes, with some in the captive industry saying some states have used the law to drive captives to form or redomicile in their states.

However, said Mr. Towle and David F. Provost, deputy commissioner in the Captive Insurance Division of the Vermont Department of Financial Regulation, there's little current evidence of states using confusion over the law's intent to force captive domicile decisions.

Mr. Towle said he's talked to captive consultants about the issue, “and they've said for the most part it's quieting down.” It remains an important issue, he said, but isn't “on the front burner.”

Many captive experts are seeing considerable interest in captive formations among Latin American companies.

“We've got a strong pipeline of feasibility studies coming out of Latin America,” said Aon's Mr. Mullen. Factors driving the growing captive interest in Latin America include the region's economic growth and the increasing risk management maturity of companies there. “It's also broker-driven,” Mr. Mullen said.

Bermuda has been the biggest recipient of Latin American captives thus far, but Mr. Mullen said he's seeing them look to Luxembourg and Switzerland as well.

Many Latin American captive parents are looking not only for strong captive infrastructures but domiciles where they can have easy access to top-name banking, legal, accounting and other services, Mr. Mullen said.

“One of the things I find about Latin American companies is they want top-quality everything,” Mr. Mullen said.

This year's Vermont Captive Insurance Association conference, held Aug. 13-15 in Burlington, Vt., drew more than 1,100 attendees.

Next year's conference is scheduled for Aug. 12-14, 2014. For additional information about next year's conference, go to *www.vcia.com*.