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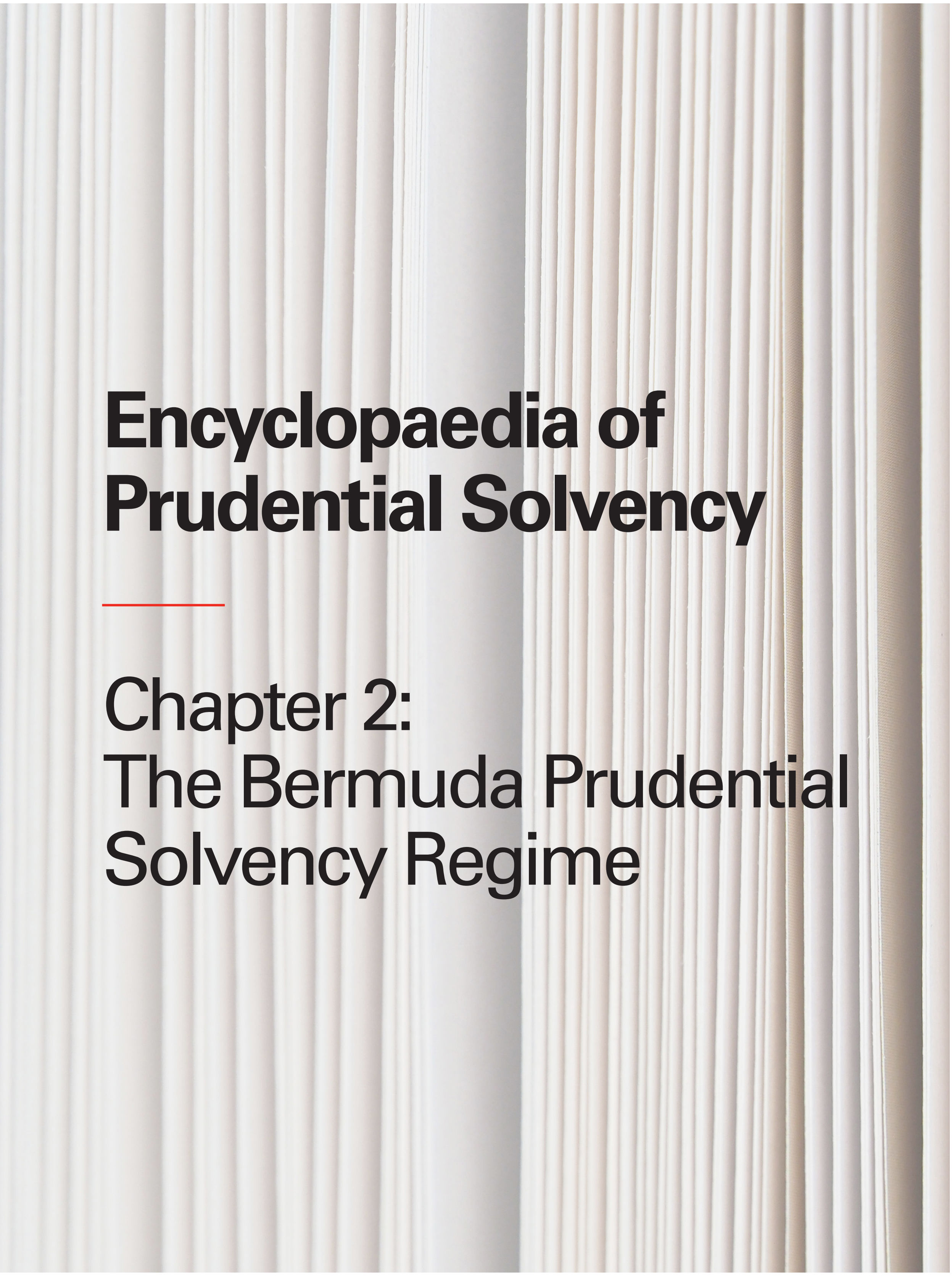

Encyclopaedia of Prudential Solvency

Chapter 2: The Bermuda Prudential Solvency Regime

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Introduction

This chapter discusses the Bermudian prudential solvency regime. Bermuda rose to prominence in the insurance and reinsurance industries in the late 1960s and early 1970s, largely due to its pioneering work in the establishment and regulation of captive insurers. The island's forward-thinking, business-friendly and entrepreneurial atmosphere was instrumental in this progress. For instance, the number of captive insurers in Bermuda grew from approximately 150 in the early 1970s to over 600 in 2024, solidifying Bermuda's status as a significant player in the global market.

Today, more than 30 major international insurance and reinsurance firms underwrite from Bermuda. The recent growth in long-term life and annuity liabilities is remarkable. The Association of Bermuda Insurers and Reinsurers notes that Bermuda is the largest supplier of catastrophe reinsurance to US insurers. Bermuda therefore plays a vital part in the US and international reinsurance markets.

Along with being highly regarded from a regulatory perspective, Bermuda's favorable tax regime allows reinsurers to operate with greater capital efficiency. The island's history of innovation in the insurance markets, along with the ease of doing business there, also makes it a popular jurisdiction in the insurance and reinsurance markets. Consistent with its commitment to compliance with international standards, Bermuda has recently introduced corporate income tax legislation for businesses meeting certain income thresholds.

1. The Legal Framework

The Bermuda Monetary Authority

Bermuda's insurance and reinsurance industry is overseen by the Bermuda Monetary Authority (BMA). The BMA, is an independent, non-governmental, body established under the Bermuda Monetary Authority Act 1969, and it is responsible under Bermuda's Insurance Act 1978 (Insurance Act) for the licensing and supervision of insurance and reinsurance companies, and insurance related-activities carried on in Bermuda.[1] The Insurance Act sets out the framework for regulating those carrying on insurance business in and from Bermuda. The BMA has the power to make secondary legislation such as rules or regulations which will supplement the primary Insurance Act, as well as create other ancillary regulatory directives such as statements of principle.

The BMA is a member of the International Association of Insurance Supervisors (IAIS) and has demonstrated interest in bringing the Bermudian prudential solvency regime, as it relates to the BMA's supervision of internationally active insurance groups in line with the IAIS's Common Framework.

Insurance Law in Bermuda

The legal framework governing insurance in Bermuda is primarily based on English common law. In recent years, English common law has been modified by legislation such as the Insurance Act 2015 (UK Insurance Act). Legislative changes in the United Kingdom have introduced proportionate remedies, which aim to create a more balanced relationship between insurers and insured parties.

That said, Bermuda has not enacted similar changes. By way of example, section 14 of the UK Insurance Act abolishes avoidance of the contract as a remedy for misrepresentation and non-disclosure (collectively, breaches of the duty of good faith). In contrast, the Bermudian remedy for a breach of the duty of good faith is still avoidance.

[1] Generally, the Insurance Act does not differentiate between insurance and reinsurance businesses or companies. Therefore, unless specified otherwise, any mention of "insurance" and "insurer" in this Chapter also encompasses "reinsurance" and "reinsurer".

Equivalence

Bermuda is one of only two non-EU jurisdictions (the other being Switzerland) whose regulatory regime for commercial insurers has been recognized as being fully equivalent with the Solvency II Directive. Bermuda achieved full equivalency in 2016. Solvency II equivalence for third countries means a non-EU jurisdiction has an insurance regulatory regime that is regarded as achieving the same outcomes as those determined under the Solvency II framework. It enables insurers and insurance groups from third countries (that are not the EU), to do business in the EU in certain respects as if they were EU domiciled entities.

In addition it strengthens the level of trust and cooperation between international insurance supervisors. In turn, this facilitates cross-border transactions. It allows Bermuda-based insurers to access international markets with comparatively less regulatory friction as compared against insurers based in jurisdictions who do not benefit from equivalent status.

Bermuda also benefits from its status as a 'qualified jurisdiction', a status granted by the National Association of Insurance Commissioners (NAIC). The NAIC is the US organization responsible for setting standards and providing regulatory support. The NAIC aids state insurance commissioners in overseeing the insurance industry by establishing standards and best practices, including uniform regulations for multistate insurers. This status allows Bermudian insurers to seek NAIC certification to better access the US insurance market.

2. Bermuda's Prudential Regime

The Class System

There are a number of different types of insurers and reinsurers in Bermuda, who are not all regulated in the same way. Bermuda splits its approach to the regulation of insurers and reinsurers into two. The first approach deals with "limited purpose" insurers. The second deals with commercial insurers. Limited purpose insurers include captives, special purpose insurers and collateralized insurers. The particular requirements that an insurer will have to comply with will vary depending on the classification of that insurer.

These different types of insurers and reinsurers have different prudential requirements. The purpose of the class system is to have lighter regulation for firms such as single captives, who insure only the risks of the parent group, while appropriately increasing the regulatory requirements for firms that underwrite broader risks, with the most stringent requirements imposed on commercial insurers writing more than 50% of unrelated or third-party risk. This topic will be explored in greater detail later in this chapter.

To unpack how the Bermudian regime applies to each different type of insurer and reinsurer, a good place to start is to explain four of the key concepts of the regime, the Minimum Margin of Solvency, the Bermuda Solvency Capital Requirement, the Enhanced Capital Requirement, and finally the Target Capital Level.

The Minimum Margin of Solvency (MSM)

As its name suggests, the MSM is essentially a regulatory capital floor, which can vary depending on what regulatory class the particular insurer falls under, and its net written premiums. In essence, it is a minimum amount of capital that insurers must always maintain, regardless of the outcome of their more risk-sensitive calculations (such as the BSCR). The requirements for the MSM for limited purpose insurers are set out in the Insurance Returns and Solvency Regulations 1980 and for commercial insurers are set out in the Insurance Accounts Rules 2016.

The Bermuda Solvency Capital Requirement (BSCR)

While the MSM applies to all insurers, in respect of commercial reinsurers, there are a number of other capital requirements that must be considered. The most important of these is the BSCR.[2] The BSCR is the BMA's risk-based capital model, developed specifically to enhance its capital adequacy framework for the insurance sector.

The BSCR takes into account an insurer's risk profile, taking into account the inherent risk and complexity of the different lines of business it underwrites. There are differing BSCR models published by the BMA depending on the class of insurer or reinsurer.[3] For context, the EU and UK equivalent of the BSCR is the Standard Formula Solvency Capital Requirement. Further discussion as to how the BSCR is calculated will be provided later in this chapter.

The Enhanced Capital Requirement (ECR)

The ECR represents the minimum level of economic capital and surplus that an insurer or reinsurer must have. The ECR is calculated either according to the appropriate BSCR model or an internal capital model approved by the BMA. The ECR of an insurer is calculated by reference to the insurer's BSCR and is calculated at the end of the insurer's financial year. The ECR amount *must equal or exceed* the MSM. In practice, the BSCR will almost always be greater than the MSM and will generally drive the ECR.

The Target Capital Level (TCL)

The ECR is important to the BMA as it serves as an early warning indicator of a firm's solvency. The BMA expects insurers and reinsurers to operate *at or above* what is known as a TCL, which exceeds its ECR.

While not a capital requirement as such, as it is not specifically prescribed in legislation, the BMA requires insurers and reinsurers to have a TCL of at least 120% of its ECR. In practice this percentage is usually much higher, for example, 150% or more, often to ensure a sufficiently good credit rating to attract business.[4] This is the equivalent of risk appetite in Europe.

Although this might not, in itself, involve any technical regulatory violation, a failure by an insurer to maintain a level of capital meeting its TCL obligations, may result in increased regulatory oversight, such as additional reporting requirements and enhanced monitoring. Furthermore, the BMA may require the submission of a remediation plan to restore capital above the TCL.

Calculating the BSCR

The BSCR model is a way to determine how much capital an insurance company needs to be financially stable. It does this by looking at different types of risks the company faces and assigning a specific amount of capital to each risk.[5]

Each risk element is assigned a 'capital factor', which is a number that represents how risky that element is. The capital factor is applied to each risk element to calculate the amount of capital needed for that specific risk. This gives a required capital amount for each risk element. This calculation results in a specific amount of capital that the company needs to hold for each risk element. The required capital amounts for all risk elements (except operational risk) are summed together to get a total required capital amount. Further covariance adjustments are made to arrive at the final BSCR figure.

[2] The others being the ECR and the TCL.

[3] Paragraph 4, Insurance (Prudential Standards) (Class C, Class D And Class E Solvency Requirement) Rules 2011.

[4] A1.2, BMA 2024 Instruction Handbook.

[5] A1.3, BMA 2024 Instruction Handbook.

There are a number of different categories of risk charge, these include:

- Fixed income investment risk.
- Equity investment risk.
- Interest and liquidity risk.
- Currency risk.
- Concentration risk.
- Premium risk.
- Reserve risk.
- Credit risk.
- Catastrophe risk.

Capital Ratios

The BSCR and the ECR are used to calculate the BSCR Ratio and the ECR Ratio. Each are calculated as follows:

- **BSCR Ratio:** The ratio of the Available Statutory Economic Capital and Surplus to the BSCR.[6]
- **ECR Ratio:** The ratio of the Available Statutory Economic Capital and Surplus to the ECR.[7]

The BMA uses these ratios to assess the financial strength of an insurer. A higher ratio indicates stronger financial health, meaning the insurer is better equipped to handle financial stress and protect policyholders.

The BSCR was updated as a result of regulatory reform in Bermuda further to the BMA's second consultation paper issued on 28 July 2023 on "Enhancements to the Regulatory Regime for Commercial Insurers" (CP2). CP2 applies to commercial insurers and insurance groups. The reforms came into force on 31 March 2024.

In this regard at least, there were three main reforms under CP2.

- **First,** increased risk sensitivity related to lapse and expense risks under the BSCR framework.
- **Second,** amendments to the "Property and Casualty" risk category intended to better capture man-made risks.
- **Third,** changes to allow insurers to apply to the BMA to make adjustments to their BSCR.

Lapse and Expense Risks

Before the changes in CP2, lapse and expense risks were grouped under a broad category called "other insurance risk." This category did not explicitly identify or separate these risks. However, the BMA has since revised this approach, segregating the "other insurance risk" charge into distinct "lapse" and "expense" risk components. The BMA has allowed a ten-year transitional period for the implementation of these new lapse and expense risk charges.

6 According to the Insurance (Prudential Standards) Rules 2011, the 'Available Statutory Economic Capital and Surplus' is a figure that is at least, depending on the insurer's classification, equal to its MSM or its ECR.

7 A1.4, BMA 2024 Instruction Handbook.

The capital requirement for lapse risk will be determined by the change in net asset value resulting from applied shocks. This involves calculating the Best Estimate Liability (BEL) before and after the shock. The difference between the pre-shock and post-shock BEL will indicate the impact of the shock and thus the capital requirement.

The new category covering expense risk takes into account both a relative increase in all unit expense assumptions, and an absolute increase in expense inflation rates per annum. As is the case with lapse risk, the difference between the pre-shock and post-shock values will determine the capital requirement associated with expense risk.

Property and Casualty Catastrophe Risk Charges

With respect to Property and Casualty Catastrophe Risk Charges, the BMA amended the BSCR catastrophe risk category to include a dedicated man-made catastrophe risk subcategory. This submodule includes specific scenarios for: terrorism, credit and surety, marine situations and aviation, reflecting market developments.

Adjustments to the BSCR

The third tranche of reform is with respect to insurer requested adjustments to the BSCR. This amended the BMA's Section 6D framework (referring to Section 6D of the Insurance Act). Insurers are allowed to request certain adjustments to the risk parameters relating to their BSCR. These adjustments are necessary when the BSCR framework produces capital requirements that do not accurately reflect an insurer's specific risk profile.

3. Capital Tiers

An insurer's total available capital is not treated as a single homogenous pool. The BMA distinguishes among different 'tiers' of capital based on quality, permanence and loss-absorption capacity. The rules setting out these capital tiers are set out in the Bermuda Insurance Eligible Capital Rules of 2012.

Within each tier, capital can be designated as either 'basic' or 'ancillary'. The highest quality is tier one, followed by tiers two and three. This is similar to the approach under Solvency II. This tiered approach ensures that capital of differing quality is utilized appropriately, so that insurers have sufficient capital to absorb losses and continue operations even in adverse conditions.

Tier One

Tier one is the most reliable and highest form of capital. It is available to absorb losses at any time, including during normal operations, run-off, winding-up and insolvency. Tier one has the following characteristics:

- **Loss Absorption:** Can absorb losses while the company is still operating, either by reducing the principal amount or converting to common stock when losses occur.
- **Subordination in Liquidation:** Has the lowest priority in case the company is wound up.
- **Payment Status:** Fully paid or called.
- **Maturity:** Has no set maturity date or has a maturity date that is at least 10 years from the issuance date.
- **Redemption:** Cannot be redeemed or can only be settled by issuing an instrument of equal or higher quality.
- **No Redemption Incentives:** Does not have any incentives that encourage redemption.
- **Coupon Payment:** The coupon payment can be canceled or deferred indefinitely if it breaches or would cause a breach in the ECR.

- **Unencumbered:** Are free from any encumbrances.
- **Insolvency Terms:** Does not have terms or conditions that could accelerate or induce the insurer's insolvency.
- **Set-Off Rights** No right to set off against an insurer's claims and obligations to an investor or creditor.[8]

Examples of tier one capital include fully paid common equity, share premium and accumulated surplus. The BMA requires a significant portion of an insurer's regulatory capital to be composed of tier one.

Tier Two

Tier two includes instruments that are slightly lower in quality than tier one, but still offer loss absorbing capability and policyholder protection. Tier two has the following characteristics:

- **Loss Absorption:** Can handle moderate losses while still operating, including stopping interest payments if the ECR is not met.
- **Subordination in Liquidation:** In case of liquidation, these are paid after policyholder claims.
- **Maturity:** Have no set maturity date or have a maturity date that is at least five years from the issuance date.
- **Redemption:** Cannot be redeemed if the ECR is not met, or can only be settled with an instrument of equal or better quality.
- **No Redemption Incentives:** Does not have any incentives that encourage redemption.
- **Coupon Payment:** Interest payments can be postponed indefinitely if the ECR is not met.
- **Unencumbered:** Does not include terms that could speed up or cause the insurer's bankruptcy.
- **Insolvency Terms:** Does not have terms or conditions that could accelerate or induce the insurer's insolvency.
- **Set-Off Rights:** No right to set off against an insurer's claims and obligations to an investor or creditor.[9]

Examples include qualifying hybrid instruments like preference shares, unpaid callable common shares, and subordinated liabilities. Although it can count towards meeting overall capital requirements, its use is always capped relative to tier one.

Tier Three

Tier three shares some characteristics with tiers one and two, but is generally of lower quality. Tier three has the following characteristics:

- **Subordination in Liquidation:** In case of liquidation, these are paid after policyholder claims.
- **Unencumbered:** Does not include terms that could speed up or cause the insurer's bankruptcy.
- **Maturity:** Has no set maturity date or has a maturity date that is at least three years from the issuance date.
- **Redemption:** Cannot be redeemed if the ECR is not met, or can only be settled with an instrument of equal or better quality.
- **Insolvency Terms:** Does not have terms or conditions that could accelerate or induce the insurer's insolvency.

[8] Paragraphs 2-3, Insurance (Eligible Capital) Rules 2012.
[9] Paragraphs 4-5, Insurance (Eligible Capital) Rules 2012.

- **Set-Off Rights:** No right to set off against an insurer's claims and obligations to an investor or creditor.
- **Coupon Payment:** The coupon payment can be canceled or deferred indefinitely if it breaches or would cause a breach in the MSM.[10]

Examples include short-term approved letters of credit and parental guarantees. Use of tier three capital is generally subject to strict limits so that an insurer's capital base is not overly reliant on instruments that may not be available to absorb losses during stress.

Capital Pools

The BMA permits specific percentages of each capital tier, largely that of tiers one and two, to be included in the capital pool representing an insurer's ECR and TCL. These percentages differ based on the insurer's specific regulatory classification.

For example, class four insurers, which is the category that captures many large commercial insurers, are required to maintain at least 60% of their ECR in the form of tier one capital. The amount of tier two capital is capped at 66.67% of the tier one capital, and the amount of tier three capital is capped at 17.65% of the aggregate sum of tier one and two capital.[11] If an insurer's capital structure is heavily weighted towards lower-quality capital (tier two or three), the BMA may view this is as a sign of weakness and require corrective action.

The hierarchical structure of capital tiers provides a clear framework for the quality and characteristics of capital instruments. This structure helps the BMA assess the financial health of an insurer more accurately. It also ensures that higher-quality capital is prioritized in meeting solvency requirements, providing greater assurance of an insurer's ability to withstand financial shocks.

4. Types of Insurers

The Bermudian prudential regime recognizes a number of different types of insurance companies. The rules organize insurance companies into various classes namely: general insurance company classes (captive and commercial), long-term insurance company classes (captive and commercial), special purpose insurer classes, innovative classes, collateralized insurer classes and intermediaries. The capital requirements of a particular insurer will in part depend on what class it falls under. This section will go over various types of insurers and how their capital requirements vary.

Captive Insurers

Captive insurers are insurance companies established by a parent company to insure its own risks. They are categorised into different classes based on the type of business they conduct:

- **General Business Captives:** The MSM is the greater of net written premiums and discounted loss reserves, subject to a minimum floor of BMD120,000 for Class 1 and Class 2 captives, and BMD1 million for Class 3 captives.
- **Long-Term Business Captives:** The MSM is a proportion of assets reported on the insurer's balance sheet, with a minimum floor of BMD250,000.

[10] Paragraphs 6-7, Insurance (Eligible Capital) Rules 2012.

[11] Paragraph 4, Insurance (Eligible Capital) Rules 2012.

Special Purpose Insurers (SPIs)

The SPI category was developed in 2009 to handle sophisticated, fully funded insurance and reinsurance transactions, recognizing the complexity of the Insurance-Linked Securities market. SPIs benefit from a more relaxed regulatory environment because they pose a lower risk. This is due to their full funding, which ensures they can meet their obligations without needing extra capital. SPIs must maintain a MSM by making sure that their special purpose business assets are at least BMD1 more than their special purpose business liabilities.

Collateralised Insurer (CIs)

An insurer that engages in special purpose business but does not qualify as a 'Special Purpose Insurer' is known as a CI. These insurers write business on a fully collateralized or fully funded basis. CIs must maintain risk-based permanent capital and meet specific paid-up share capital and solvency margin requirements. The risk-based regulatory capital is designed to mitigate operational, market and credit risks, with a minimum threshold of BMD250,000. Additionally, CIs must have a paid-up share capital of at least BMD120,000. The MSM is set at BMD250,000. Furthermore, CIs must maintain total statutory capital and surplus that equals or exceeds the ECR, which is also subject to a minimum of BMD250,000. The ECR is calculated using a bespoke BSCR-collateralized model.

Commercial Insurers

Commercial insurers are traditional insurance companies that provide coverage to the general public or businesses. They must meet a MSM, which varies by class:

- **Class 3A and 3B Insurers:** MSM is based on 25% of the insurer's ECR or BMD1 million.
- **Class 4 Insurers:** MSM is BMD100,000,000.
- **Class C Insurers:** MSM is the greater of BMD500,000; 1.5% of assets under management; or 25% of ECR.
- **Class D Insurers:** MSM is the greater of BMD4,000,000; 2% of the first BMD250,000,000 of assets under management plus 1.5% of the amount by which assets exceed BMD250,000,000; or 25% of ECR.
- **Class E Insurers:** MSM is the greater of BMD8,000,000; 2% of the first BMD500,000,000 of assets under management plus 1.5% of the amount by which assets exceed BMD500,000,000; or 25% of ECR.

Commercial insurers must also maintain available statutory capital and surplus, and available statutory economic capital and surplus of at least the ECR, with a target capital level of 120% of the ECR.

5. Group Capital

As discussed earlier, an individual insurer is required to calculate its BSCR and ECR after taking into consideration certain risk categories and solvency requirements. Groups of insurers have to additionally aggregate the group's capital from all relevant entities. This is not a straightforward task as the designated insurer (the entity responsible for reporting on behalf of the group) must make sure not to double count any intra-group loans or receivables.

Calculating the group's BSCR is similarly complicated. The designated insurer has to determine the group's overall risk exposure by aggregating capital from each risk category before applying a covariance adjustment. The figure is further adjusted to account for other group specific risks.[12] The group's final

[12] BMA 2024 Instruction Handbook, page 338.

solvency ratio is calculated as the group's consolidated available capital divided by the group's BSCR. Under the group supervision framework, the BMA requires that an insurance group's total available capital and surplus be sufficient not only to meet each member's individual requirements but also to cover the group's overall risk profile.[13]

The group supervision rules require that the value of the group's statutory economic capital and surplus exceed the aggregate of the minimum solvency margins of each member.[14] In practice, this means that the capital available at the group level must cover the individual solvency requirements of the various entities within the group, with adjustments made based on the parent company's percentage shareholding in entities where it does not have full control.

6. Ancillary Requirements

Based on an insurer's risk profile, and in addition to the capital requirements, the BMA may also impose additional capital requirements, restrict dividends, require capital maintenance agreements, and mandate liquid contingent capital resources and liquidity management tools.

As is the case with other prudential regimes, the BMA also requires certain information from insurers under its regulatory oversight. Bermudian insurers must file statutory financial statements, financial returns, and a Capital and Solvency Return within four months after the end of the financial year.

Bermudian insurers must also prepare and submit a Financial Condition Report. According to the BMA, the Financial Condition Report "is an opportunity for an insurance group to describe its business to the public in relation to the insurance group's business model, whereby the public may make an informed assessment on whether the business is run in a prudent manner."[15] This report must be published on the insurer's website within 14 days of being filed with the BMA. Unlike the Financial Condition Report, the statutory financial statements, the financial returns, and the Capital and Solvency Return are not available for public inspection.

7. Investment Rules

Bermuda's investment rules are designed with modelling and flexibility in mind, allowing insurers to adapt to a variety of market conditions and business models. Rather than imposing rigid and prescriptive asset allocation strategies, the investment rules encourage investing in assets that allow the insurer to meet its overall solvency and capital requirements.

The Prudent Person Principle (PPP)

One key concept here is the Prudent Person Principle. This is a concept that can be found in other regimes, like Solvency II. The PPP, is outlined in the BMA's Insurance Code of Conduct.

The PPP requires insurers to, when formulating its investment strategy and policy, only take on investment risks that it comprehends and can accurately identify, measure, address, monitor, control and report on. This must be done while also considering its capital requirements and adequacy, as well as its short-term and long-term liquidity needs and obligations to policyholders. Additionally, the insurer must be mindful that investment decisions are made in the best interests of its policyholders and beneficiaries. Market conditions may also require special attention to be given to more risk-sensitive assets, such as real estate equity, concentrated lower investment grade corporate positions, and exposure to highly correlated assets.

[13] Paragraph 4(2) Insurance (Group Supervision) Rules 2011.

[14] Paragraph 19(1) Insurance (Group Supervision) Rules 2011.

[15] B4.2, BMA 2024 Instruction Handbook.

The Insurance Code of Conduct (Code) and the Insurance (Group Supervision) Rules 2011, require insurers to implement the PPP as an integral part of their risk management framework. Compliance with the PPP shall continue to be considered on a case-by-case basis notwithstanding the provisions of the rules.

The BMA has recognized that what may be prudent for one insurer may not be prudent for another, and that the application of the PPP is likely to give rise to a range of reasonable investment strategies. The BMA places responsibility on senior management to ensure the insurer complies with the PPP.

Updates to the PPP

The BMA has been actively updating its guidance on the PPP, in respect of commercial insurers, most recently publishing a consultation paper on 4 December 2024, entitled the Proposed Instructions and Guidance on the Application of the Prudent Person Principle (PPP Paper). These proposals are intended to come into effect on 1 July 2025.[16]

The PPP Paper offers further guidance on several application areas pertinent to the PPP, including:

- Expanded considerations within an investment strategy that align with the PPP.
- Governance-related recommendations.
- Compliance with the PPP in the context of outsourcing investment-related services.
- Matching assets to liabilities.
- Management of risk concentration, accumulation and diversification.
- Handling of complex and non-publicly traded assets.
- Management of affiliated, related, and connected party assets.
- The Commercial Insurer Solvency Self-Assessment and Group Solvency Self-Assessment; and use of derivatives and other financial instruments.

8. Discounting Liabilities

In Bermuda, life and annuity insurers may discount their insurance liabilities (which are inherently more asset-intensive and long-term) using the discount curves prescribed by the BMA or an alternative Asset-Liability Management (ALM) approach called the Scenario-Based Approach (SBA). The SBA, like the Solvency II matching adjustment, allows the usually higher credit adjusted return on the actual assets held to be used to discount particular types of liability. This is crucial for life companies.

To be approved to use and continue to use the SBA, firms must meet specific conditions, such as demonstrating that their liquidity risk management plans align with BMA specifications and conducting detailed liquidity stress tests. At a minimum, liabilities should be matched with suitable assets that produce predictable and stable cash flows. Where a mismatch exists, the SBA assigns an explicit cost by running the calculation through eight alternative interest rate scenarios and selecting the worst of the eight scenarios to determine the BEL.

To mitigate the consequences of lapse risk, the BMA has implemented a more intrusive supervisory approach and standard. The BMA has noted that the recent enhancements to the SBA, which approach is commonly used by PE firms, will likely have a significant quantitative impact on the Bermuda market.

[16] Paragraph 1.58, Proposed Instructions and Guidance on the Application of the Prudent Person Principle.

The BMA has introduced new requirements for insurers to seek approval to use non-publicly traded assets and affiliated investments in the SBA. The BMA is bolstering SBA supervision with additional resources to analyze reported data, ensuring the adequacy of technical provisions set up by supervised firms.

9. Private Equity Insurers

The Bermudian market has experienced significant involvement from private equity and alternative asset manager-backed insurers. This trend is expected to continue. Bermuda has emerged as a favored jurisdiction for so called private equity (PE) owned insurers (PE Insurers) due to a combination of regulatory flexibility, strategic location and a robust financial ecosystem.

There are onshore regulatory concerns about this model, which have been echoed in Bermuda. The BMA has recognized what are perceived to be the unique risks associated with PE-owned insurers, such as complex structures, conflicts of interest, and higher proportions of illiquid assets.

As is the case with other components of the Bermudian prudential regime, the rules relating to PE owned insurers are also subject to some change. The practical effect of CP2 depends on the specific company concerned, but for many PE Insurers writing life insurance liabilities, the reforms have significant effects. Additionally, the BMA published a now much-discussed paper in December 2023, "Supervision and Regulation of PE Insurers in Bermuda", clarifying the Authority's position on oversight of insurers operating and licensed in Bermuda that are owned or supported by private equity or alternative asset managers. This paper may be seen as a response to the concern with the model, while also supporting and protecting the Bermudian insurance industry.

The BMA's regulatory focus on PE Insurers is notable due to the potential impact on transaction timelines, deal and group structures, capital and collateral requirements, costs and potentially increased administrative responsibilities, such as the requirement to get approval for block trades. The market's growth, pressure from onshore regulators and increasing sophistication will likely lead to further regulatory evolution as the BMA adapts to new challenges and considers industry feedback.

10. Undertakings in Difficulty

The prudential solvency rules are under continuous revision by the BMA to ensure that best market practices are being observed by insurers in the Bermudian market. On 25 April 2024, the BMA issued the Insurance (Prudential Standards) (Recovery Plan) Rules 2024 (Recovery Rules), which are set to take effect on 1 May 2025.

In September 2024, the BMA held a workshop with industry members to discuss its expectations in relation to recovery planning. In a follow up letter released on 22 November 2024, the BMA summarized its expectations for recovery planning and provided practical examples of the challenges insurers face when drafting and implementing a recovery plan. The Recovery Rules provide guidance as to whether an insurer has to prepare a recovery plan. The BMA will consider the following:

- **First:** whether the insurer carries on domestic business;
- **Second:** whether the insurer has a three-year rolling average total assets of at least $10 billion;
- **Third:** whether the insurer has a three-year rolling average total gross written premiums of at least $5 billion; and
- **Fourth:** whether the insurer is subject to enhanced supervisory monitoring by the BMA or any relevant supervisory authority.

If the BMA does decide that an insurer needs to have a recovery plan in place, the BMA will determine the scope and requirements of the plan taking into account, among other things, the size or market share of the insurer; business model; and risk profile of the insurer.

Any recovery plan must contain, among other things, a description of the insurer, the nature of the insurer's business, a description of the insurer's governance policies, and the various methods to be used to recover from stressed situations.

These recovery plans must be reviewed at least once every three years, or when there is a material change to the insurer's strategy, business or risk profile, or in its financial position. Additionally, the recovery plan must be filed with the BMA within 30 days of its update.[17]

11. Public Disclosure

The BMA issued a consultation paper in December 2024 on Proposed Enhancements to the Public Disclosure Regime: "Public Disclosure of Assets and Liabilities for Commercial Long-Term Insurers" (December Paper). This consultation proposes to, among other things, publicly disclose the assets and liabilities of all Bermudian insurers caught by the paper. This is in response to a global trend where the life and annuity insurance sector has increased its exposure to illiquid, hard-to-value assets that are non-publicly traded. To address the risks involved, the BMA has intensified its oversight of Bermuda's long-term insurers, ensuring these risks are well-understood, managed and governed appropriately. The application of the PPP plays a critical role in this context. For example, long-term insurers must ensure that investment decisions have been executed in the best interests of their policyholders under both normal and stressed conditions.

For assets, the December Paper proposes to publicly publish the asset portfolios of Bermudian insurers. The disclosed information will be presented on a consolidated basis. It will encompass all assets held by the long-term insurers, including, but not limited to, equities, fixed-income securities, mortgage loans, derivatives, alternative investments, structured assets and other assets such as deferred tax assets. For liabilities, the BMA proposes publicly disclosing the reserves held by long-term insurers at a product-type level. The disclosed information would encompass currency, gross and net reserves, reinsurance recoverables, average duration, and year-on-year changes in reserves.

As part of the same consultation, the BMA also proposes to introduce new rules requiring long-term insurers to disclose their asset liability management practices, including disclosures that offer insights into the appropriateness of their investment strategies, liquidity adequacy, investment risk management practices and an assessment of how market conditions will impact their portfolios.

Long-term insurers will be required to submit public disclosures on an annual basis as part of the Capital and Solvency Requirements filing. The BMA has provided a proposed standardized reporting template which will be used for the public disclosure of both assets and liabilities. This will ensure uniformity, in the presentation of data across the sector, thereby facilitating comparisons and ensuring consistent and reliable disclosures.

The BMA's intention is that the detailed disclosure of assets and liabilities will facilitate more informed decision-making by policyholders and other relevant stakeholders by providing insights into the composition and risk profile of insurers' investment and liability portfolios. By providing greater transparency into insurers' investment activities, these requirements are intended to enhance market discipline and incrementally contribute to the overall stability of the global insurance sector.

[17] Section 9(2), Insurance (Prudential Standards) (Recovery Plan) Rules 2024.

12. Conclusion

It is evident that the regulatory framework in Bermuda is designed to balance the protection of policyholders and regulatory equivalence, with the need for insurers, and Bermuda, to remain competitive. However, the rapid growth in Bermuda, especially in the life segment, has forced greater scrutiny from onshore regulators.

In summary, we expect that consideration of the market's growth and increasing sophistication will lead to further regulatory evolution as the BMA adapts to new challenges. Bermuda is rapidly adapting its regime to be more equivalent and sympathetic to onshore regulation in order to preserve its position within the global reinsurance market. Its desire to be equivalent with the IAIS's ICS will only push this further.

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