Chapter 46

1997
Beyond the Far Horizon

A grim global marketplace

By 1997, the rates in the global insurance industry had softened considerably, particularly in the property catastrophe area. To illustrate the grim marketplace the insurance industry faced, reporter Christopher Adams of *The Financial Times* wrote—

> 'The biggest risk facing the world's insurance companies is possibly the rapid change now taking place within their own ranks. Sluggish growth in core markets and intense price competition, coupled with shifting patterns of customer demand and the rising costs of losses, are threatening to overwhelm those too slow to react.
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> 'An analysis of natural catastrophes by Munich Re, the world's biggest reinsurer, shows that the risks insurers underwrite are as unpredictable as ever: half of last year's losses of US $60 billion were caused by floods. Although 1996 was an exception in that the regions worst affected were in areas such as China where there was relatively little cover, the cost of insured losses will continue to rise over the longer term as a result of the concentration of wealth in the largest cities of developed countries.
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> 'The Kobe earthquake in Japan two years ago set a record of US $180 billion in absolute losses. Insurance companies, still reeling from the damage bill of the 1994 Northridge earthquake in California, have refused to insure citizens living on the San Andreas Fault, forcing the state to set up its own insurance scheme.
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> 'But the risk of another big catastrophe has not deterred companies from entering the insurance business. Competition in the general—or non life—industry in most of the biggest markets has intensified following a huge influx of capital on the back of healthy profits in recent years and breathtaking returns from global bond and equity markets.
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> 'Margins were squeezed savagely last year by fierce price competition in personal and commercial lines of business. The latest renewal season in the London market has seen another decline in marine insurance rates to their lowest levels for more than five years.
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> 'It is not only increased underwriting capital that is driving prices lower, however, patterns of customer demand are shifting rapidly as commercial buyers take on more risk themselves through so-called "captive" insurance subsidiaries. Most multinationals employ professional risk managers to find alternative ways of transferring risk.
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> '...In the US, the world's biggest insurance market, premium income growth is barely keeping pace with the rate of inflation and remains behind the rate of expansion in the economy as a whole. A survey by the New York based Insurance Information Institute found that the mean projected growth for 1997 was 3.1 per cent, marginally higher than the 3 per cent predicted for 1996. This would be the 10th successive year of single-digit percentage increases. "Growth rates in the US are anaemic. Waiting for the cycle to change is like waiting for Godot," says Mr John Kriz, managing director of insurance at Moody's Investors Service.
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> 'Yet, while growth in the world's mature markets remains elusive, insurers are having to protect themselves against the problems of the past. The still largely unquantifiable risks from the threat of court

awards for environmental, industrial health, and personal injury claims have obliged the industry to set aside hundreds of millions of dollars in additional protection. The UK's Royal & Sun Alliance and Eagle Star both took action this month to bring themselves more closely into line with their bigger and better reserved US peers.

'Lloyd's of London put these troubles behind it with the completion of a plan last year to reinsure more than £8 billion of old liabilities into a new company called Equitas. Crucial to its success was a £3.2 billion settlement offer made to the insurance market's 34,000 Names – individuals whose assets have traditionally supported business underwritten at Lloyd's.

'More than 90 per cent of Names accepted this offer for compensation and action groups representing these investors dropped court action against Lloyd's. But hundreds of Names who are refusing to settle continue to embarrass the insurance market as it attempts to restore its reputation internationally. Further upheaval awaits Lloyd's this year as it addresses the rapid restructuring of its capital base and tries to decide how it should be regulated in future.

'A wave of mergers and acquisitions has been one response to these pressures. In France, Axa and UAP merged to create the world's second largest insurer behind Germany's Allianz. Earlier, Royal Insurance and Sun Alliance agreed to merge in the biggest UK insurance deal for more than a decade, promising £175 million in annual cost savings by 1998.

'Three months ago, there were six global brokers, generating more than US $1 billion each in revenues annually. There will soon be four. Marsh & McLennan announced a deal to buy Johnson & Higgins of the US for US $1.8 billion, trumping Aon's acquisition of Alexander & Alexander for US $1.23 billion in January.

'Computers are increasing efficiency, but the industry has been slow to exploit information technology. Lloyd's still has a cumbersome and costly paper-based system where most business is done face to face. Plans by international brokers to introduce electronic trading under a project called World Insurance Network have been dogged by delays. Technology has had the biggest impact in the back office. Insurance companies are using image processing software to speed up claims handling and exploiting weather information that records temperature, wind speed and rainfall in individual postcodes.

'The real gains, however, are to be made outside home markets and in fast growing life assurance, where an aging population and inadequate state welfare provision in the developed economies are creating opportunities. "The potential for growth in the UK is good. The potential for growth overseas is much better," says Mr John Carter, chief executive of UK composite insurer Commercial Union.

'The percentage of people in the European Union aged over 65 will rise from 15 per cent to more than 20 per cent by 2020, according to a recent study by Eurostat.

'Insurers in the US and UK may seek more exciting growth overseas. Deregulation and the advance towards a single European currency is gradually breaking down barriers to competition in continental Europe.

'Further afield, Asia is a strong magnet. With the first steps being taken this year in Japan towards freeing rigid price controls as part of a broader set of measures designed to liberalize the financial service sector, foreign companies are gradually stepping up their involvement. China also offers a largely untapped customer base of 1.2 billion, but operating licenses have so far been difficult to obtain. India promises much, but politics is as much a barrier to proposed liberalization of the state-run industry as bureaucracy.

'Expansion into life assurance and emerging markets will bear fruit over the longer term. Today, meanwhile, is likely to be characterised by consolidation in the US and Europe and, for the next 12 months at least, continued price competition.'[699]

[699] *The Financial Times*, Financial Times Survey, 24 March 1997, 'Insurance Industry, Risks rise as change accelerates', by Christopher Adams

So how was Bermuda shaping up against the deteriorating global insurance marketplace? By 1997, Bermuda had earned its stripes in the global insurance industry arena. While the rest of the world was struggling, the international insurance industry in Bermuda boomed. Captives grew dramatically, while the large companies consolidated to build their might against the continued downturn in the market. There were 1446 insurance companies and 216 insurance brokers/managers registered in Bermuda, a firm indication that Bermuda was faring well as compared to the rest of the world.

The Insurance Accountant quoted Donald Watson, a director with Standard & Poor's, as saying, 'Bermuda is a microcosm of what is going on in the insurance industry in the US and around the world' and went on to add that…'Another theme for Bermuda-based companies is morphing from a monoline company into a diversified multiline insurer, which will soon be a worldwide concern. "The types of changes in Bermuda today are going to happen in property/casualty companies around the world." Further, many of the new ideas and programs around the world have been exported from the tiny island.'[700]

The international insurance industry in Bermuda began to capture the attention of many analysts. Leading rating agency A.M. Best ranked Bermuda among the top three of non-US jurisdictions in the number of insurance/reinsurance entities it rated the other two being the United Kingdom with 78 companies and Canada with about 71 companies.[701]

The Royal Gazette quoted Ted Collins, managing director of Moody's Investor Service, property and casualty reinsurance, as saying that—

> 'The Bermuda insurance/reinsurance market is compromised of companies with good fundamentals, supportive regulation and active managers that make it attractive as a place to locate,' and also pointing out that, 'It's been a very focused, specialised market, but is changing and providing a more broader-based emphasis. It is increasingly not just a specialized market. A number of companies have been quite successful here and are evolving as the market changes.'[702]

Bottom Line wrote of Bermuda's success as follows—

> '…Bermuda is the world leader in finite insurance and reinsurance and has the most significant depth of capital focused on finite reinsurance, and some of the best underwriting brains on the planet. And if Bermuda is the centre of innovation for insurance markets, she is playing a significant role as those markets seek new capacity and alternative risk transfer mechanisms.
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> 'In reinsurance alone, Bermuda companies are writing more than 10 per cent of worldwide premiums. Half a dozen local companies, according to Best, are probably among the top 20 in the world. Eight of them started from nothing this decade writing almost purely property catastrophe business. Today, they are writing a variety of business and attracting global attention.'[703]

While *Bermudian Business* magazine stated that—

> 'Bermuda insurers and reinsurers continue their assault on the global marketplace in terms of both size and lines of coverage offered. Indeed, according to *AM Best*, the Island now ranked third as a reinsurance centre with an estimated US $10 billion in annual reinsurance premiums written, behind only Germany and the US…Bermuda has evolved into a mainstream market that offers lines more traditionally associated with the likes of Lloyd's of London.
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> 'Ironically, some of the more aggressive Bermuda companies have capitalised on the recent troubles at Lloyd's to expand overseas. Bermuda players are now estimated to control £1.89 billion or 18.31 per cent

[700] *Insurance Accountant*, 31 March 1997, 'Bermuda Cat Reinsurers set precedents', by Michelle Clayton, p. 3

[701] *The Royal Gazette*, 9 October 1997, 'Top rating agency eyes up more Bermuda insurers', by David Fox, p. 11

[702] ibid. 15 October 1997, 'Insurance/reinsurance market gets Moody's stamp of approval', by David Fox

[703] *Bottom Line*, October 1997, 'The Feeding Frenzy', by David Fox, pp. 29–34

of Lloyd's market capacity. ACE alone is estimated to manage almost eight per cent of that capacity. Others include EXEL, Mid Ocean, LaSalle Re, Terra Nova, and the Trident Partnership.

'Just as important are the types of coverages that can now be bought in Bermuda. One-stop shopping is truly nearing a reality, at least in the exotic lines of business that the Bermuda companies specialise in. Captives continue to be the bedrock upon which all other sectors of the industry have been built. But to this have been added lines of coverages of truly generational proportions. The industry mantra now goes something like: captives, excess liability, directors and officers, finite risk, property catastrophe. And these include only companies originally set up dedicate(d) to just those lines of business.'[704]

Balance sheet protection

Seizing upon the growing trend toward convergence of financial products with insurance products, Bermuda insurers began to push to provide balance sheet protection coverage for their sophisticated clients. *National Underwriter* wrote of Bermuda's foray into financial products as follows—

'...Of course, the concept of looking at all threats to an insured's bottom line together—including both conventional insurance risks like fires as well as financial risks like changes in oil prices—and funding them on a multi-year, multi-line basis isn't only being promoted in Bermuda. But the island's prominence as a hotbed for reinsurance innovation and its regulatory "flexibility" make it an ideal centre for such approaches, market participants say. Balance sheet protection, which may combine high-level catastrophic coverage along with derivatives or coverage for previously "uninsurable" hazards, typically focuses on "risks that could take the company down," in the words of William M. Thornhill, a senior VP of X.L. Re in Bermuda.'[705]

There were new buzz words floating around the industry including 'second event cover, securitisation, convergence, triggers, options and puts, enterprise risk' and the list went on. Many in the insurance industry were confused by the terms. It came as no surprise that clients could not get their heads around the new jargon.

Bermudian Business commented on Bermuda's expansion into non-traditional products as follows—

'...Following several years in the development phase, 1997 has witnessed the first successful launchings of several different catastrophe securitisations, each with its own unique structure. Several of these transactions, as well as the underlying insurers, have been rated by Moody's. The jury is still out on whether such transactions will generate widespread interest within the insurance and investor communities, and if so, whether the Bermudian property catastrophe insurance community will suffer disintermediation, or perhaps benefit from participating in the underwriting process alongside investors.

'Currently, the BSE (Bermuda Stock Exchange) is working to add to the arsenal of risk transfer and risk financing instruments the world's first electronic risk exchange, the listing of special purpose vehicles such as Act-of-God Bonds, and the design of a new equity index of Bermuda-based insurance and reinsurance companies on which a derivative fund can be based.

'Significantly, as Bermudian insurers expand into these new classes of business, they will most certainly encounter stiff competition from strongly capitalised players in several international markets. However, in contrast with the past, when competition was primarily within-market (ie, between established insurers and reinsurers), the Bermudians are increasingly likely to butt heads with leading global commercial and investment banks, established financial guarantors and other specialty financial firms. Some of these firms, particularly banks and securities firms, may possess substantially more capital and product distribution capabilities—essentials for generating a sustainable and deep securitisation market.

[704] *Bermudian Business*, Summer 1997, 'Bermuda keeps up the assault', pp. 56–62

[705] *National Underwriter*, 17 February 1997, 'Balance-Sheet Protection Buzz Grows', by David M. Katz, pp. 3 & 35

'Whether insurers will lock horns with these firms, or embrace them as partners with different, but complementary, skill set, remains to be seen.

'As is characteristic of this business, it will take some time before a general consensus develops in the effectiveness of the range of approaches currently being pursued by the Bermuda insurers. But the combination of the Island's creative intellectual resources and financial capital, together with its excellent geographic placement and business-friendly operating environment, should ensure that the Bermuda insurance and reinsurance market will remain a central resource in the global insurance and financial markets. Stay tuned.[706]

Captive continue to grow and diversify

Faced with many restrictions on coverages, particularly with being forced to increase retentions and exclusions, clients sought their own solutions outside the traditional insurance marketplace. Consequently, the Bermuda captive insurance market continued to grow. Gavin Souter captured the essence of this for *Business Insurance*—

'It's getting to be like old times again in Bermuda. Captive formations are at a 10-year high and, like some of their predecessors, some captives in the domicile today are broadening the spread of risks they cover to include third-party risks.

'While a resurgence in the formation of captives is unequivocally welcomed by regulators and managers in Bermuda, they say a repeat performance of the débâcle of losses that followed the previous surge of third-party risk diversification by captives in the late 1970s and early 1980s is being closely guarded against. While many captives in Bermuda still write little or no third-party business, the pressure to write more unrelated risks will increase if the Clinton administration's tax proposals for captives become law, captive managers say.

'The rise in captives writing third-party business is accompanied by increases in other lines of business not traditionally written in Bermuda. In particular, due to a recent boom in health care captives, about 90 captives on the island now cover health care risks, one manager estimates. And the geographic diversity of captive owners selecting Bermuda continues to expand, with inroads being made into the Southeast Asian markets last year, captive managers say. Anticipated growth from Mexican captives, though, was dealt a blow last year when increased taxation by the Mexican government made captives less attractive for companies seeking a tax break. Although the number of captives is increasing, several managers are reporting a drop in premiums written due to the continued soft market.

'The number of international insurance and reinsurance companies in Bermuda rose 4.9% to 1,470 in 1996 from the 1,401 in 1995. Bermuda had 1,050 active captives in 1996, an increase of 6.5% over its 986 active captives in 1995. Ninety-seven international insurers and reinsurers were formed in 1996 and 28 were wound up, compared with 90 formations and 46 closures in 1995. The record number of new company formations was 158 in 1978. Of the formations, 23 were single-parent captives, which carry Class 1 licenses under the Bermuda regulatory system; 28 were multi-owner captives which have Class 2 licenses; 30 were Class 3, which include non-catastrophe insurers and reinsurers, finite risk insurers and reinsurers, as well as captives writing more than 20% of their premiums for third parties; three were Class 4, which include property catastrophe insurers and excess liability insurers; and 13 were long-term or composite insurers.

'Gross premiums written by Bermuda's international insurers increased 24.5% to US $23.4 billion in 1995, the latest year for which figures are available, compared with US $18.8 billion in 1994. Net premiums rose 23.5% to US $18.4 billion from US $14.9 billion the year before. The total capital and surplus of Bermuda's international insurers increased 23.8% to US $36.9 billion in 1995 from US $29.8 billion in 1994.

[706] *Bermudian Business*, Fall 1997, 'Bermuda plays active role designing coverages', by Allan G. Murray and Ted Collins, pp. 44–46

'The most marked change among the formations in 1996 compared with the prior year was the increase in Class 3 formations and the decrease in Class 1 formations: there were eight more Class 3 formations last year, but 10 fewer Class 1's. The growing popularity of Class 3 formations reflects the increasing number of captives writing third-party business, according to Kymn C. Astwood, Bermuda's registrar of companies. Class 3 insurers can obtain more than 20% of their business from unrelated risks. "What we've seen is that a number of Class 3 companies were formed, as opposed to Class 1, to write third-party business to achieve certain tax objectives," Mr Astwood explained.

'Currently, captives with parents in the United States generally have to derive more than 30% of their premium from unrelated business to tax deduct premiums paid to their captive. However, this has been established by tax case law, not legislation. That could soon change, however. For the second time the Clinton administration is proposing to change tax law to require captives seeking that tax deduction to obtain at least 50% of their premium volume from unrelated business.

'That threat of the increased threshold is likely a factor in the growth of captives seeking to write more unrelated business, Mr Astwood said. However, he stressed, any actions captives take to increase their unrelated business, for tax purposes or other reasons, will be closely watched by regulators. "From a regulatory standpoint, I'll be monitoring the response of captive owners to this proposal, because the last thing we want is a repeat of what happened in the 1980s, when there was reckless writing of third-party business," Mr Astwood said. The new regulations are a check on this issue as single-parent captives will have to seek regulatory approval before they can write a significant amount of third-party business, he said.

'Captive owners generally are interested in writing more third-party risks and, often, it is not to obtain a tax advantage, said Andrew Carr, President of Marsh & McLennan Management Services (Bermuda) Ltd. The third-party risks usually have some connection to the captive owner, he said. For example, the captive owner may use the captive to offer coverage to subcontractors, agents or suppliers. "They are trying to augment their business relationship," Mr Carr said. At the same time, the owners are benefiting from writing controlled business that is well known to them, added Rory Gorman, Senior V.P. at M&M in Bermuda. "People are looking to add an extra dollar onto their bottom line rather than just manage their insurance better," he said. The captives write the business because it is profitable rather than simply to increase the unrelated business premiums for tax reasons, Mr Gorman said. "If the Clinton proposal goes through, it probably won't have a dramatic effect on the captives we manage," he said.

'Many captives would be unaffected if the legislation goes through, agreed Nicholas S. Dove, President of Skandia International Risk Management Ltd. "Very few of our clients are actually taking a tax deduction, so I don't see it having a big affect at the present time," he said.

'If the Clinton proposal does go through, many captives would be hard pressed to find enough third-party business that is in some way connected to the parent to obtain a tax advantage, said Peter J.N. Strong, President and Director of Independent Management Group Ltd. "There is only so much warranty and other connected business out there, and I don't think that writing other third-party business just to reach a certain percentage is a very good idea," he explained.

'Some captive owners welcome the Clinton proposal because it would firmly establish what level of unrelated business has to be met, said Denville C. Reed, President of Sedgwick Management Services (Bermuda) Ltd. "If it goes through, we'll know what you have to do, whereas up to now it's largely been speculation," based on court rulings, he said. The Clinton proposal emphasizes, though, that captives should not be established for tax reasons, said Nigel M. Godfrey, Senior V.P. at Sedgwick. "One always glibly says that you shouldn't form a captive solely for tax reasons, and this illustrates that point," he said.

'Captive owners that want to obtain a tax advantage will likely look to pool more risks with other captives, said Roger C. Gillett, Senior V.P. at Johnson & Higgins (Bermuda) Ltd. Several J&H-managed captives already are pooling more of their risks through the newly formed Green Island Pool. The pool, which was launched with US $60 million in premium, will reinsure member captives' liability risks, Mr Gillett said. "The principal benefit will be the stabilizing of loss costs through a greater spread," he said. The risks covered are at the primary level, so while the volume of claims may vary, there will be little variation in the size of claims, Mr Gillett said. Losses and dividends will be distributed in proportion to the amount of business participants put into the pool, he said. Another trend that is emerging in Bermuda is the growth in the number of captives being formed by health care companies.

'Traditionally, the Cayman Islands has been the preferred domicile for captives covering risks of health care providers, but now Bermuda is home to some 85 to 90 health care captives, estimated Alan C. Cossar, executive director at Alexander Insurance Managers Ltd. and also President of the Bermuda Insurance Management Association. One of the six new formations at A&A in 1996 was a health care captive, and A&A has formed several other health care captives in Bermuda in recent years, Mr Cossar said. Often the formation of health care captives reflects the changes in the health care industry in the United States, he said. "A lot of it is to do with integrated health care delivery systems. You can tie the members of a network together with a captive," Mr Cossar said. And Bermuda is gradually managing to persuade health care organizations interested in setting up a captive that it is a good domicile for the risks, he said. "There is nothing you can do in the Cayman Islands in terms of health care captive business that can't be done here-and to our mind done better-because of our synergy with the commercial market here," Mr Cossar said.

'Four of the five captive formations at Atlantic Security Ltd. were health care captives, said Colin C. James, President and CEO. The opportunity to access the rest of the insurance market in Bermuda is an added attraction to captive owners who previously may have gone to the Cayman Islands, he agreed. "There is no tax or other advantage to either domicile, so the decision often comes down to other issues, like how easy is it to get here and the fact that we do have an actual insurance market here," Mr James said.

'Independent Management Group is currently forming a captive to reinsure the underwriting risk of a workers compensation managed care program for small businesses in Tennessee, said Mr Strong of IMG. The workers comp program is administered by one of the investors in the captive, Provident Assurance Co., an insurer. The hospital providing health care is the other investor. "The hospital and the managed care provider are putting their hands in their pockets to take the risk and the reinsurers have been lining up to reinsure it," Mr Strong said. The reinsurers believe that the combination of the managed care company and a hospital will produce better controlled and more profitable risks, he said. 'The health care captives forming in Bermuda are often covering risks not traditionally associated with captives, said Tracy E. Keill, Senior VP at Aon Risk Services (Bermuda) Ltd. Two of the seven new captives formed by Aon last year for clients were health care captives. Including captives that were transferred from other managers, Aon added 14 new captives in 1996, she said. The health care captives are covering capitation risks and long-term care programs, as well as the medical malpractice risks that are traditionally covered by such captives, Ms Keill said. Three of the other new formations at Aon were agency captives, she said.

'Bermuda generally is seeing more interest from insurance agencies seeking to establish captives, noted regulator Mr Astwood. "A typical example is where a US fronting company would like to reward its best agents by allowing them to obtain an ownership stake in an agency captive so they can receive a small quota share of the business they produce," he said.

'Mr James of Atlantic Security agreed that more insurance agencies in the United States are interested in setting up captives. The agency captives allow insurers to cement a stronger relationship with their best agents or brokers and they allow the agents or brokers the opportunity to profit from their good business, he said.

'Many agency groups are too small to form a captive so they join a rent-a-captive instead, said Mr Dove of Skandia.

'Three of the eight captives taken on by International Advisory Services Ltd. last year were insurance agency captives, said David Ezekiel, President and managing director of IAS. One of the agency captives covers special sports events. The coverage ranges from hole-in-one coverage for golf events to prize free throw competitions at National Basketball Association games, he said. "The loss ratio is excellent," Mr Ezekiel said.

'In addition to writing new risks, captives setting up in Bermuda are coming from a more diverse range of countries, managers report. For example, Yukong Ltd., a South Korean manufacturing group, set up a property insurance captive in Bermuda last year. The captive is one of 12 new ones set up by J&H last year. The formation of the Yukong captive comes after several years of marketing the captive concept in

South Korea, said Mr Gillett of J&H. "Once you get one company in a particular country to set up a captive, usually it is followed fairly quickly by others," he said.

'Another large Southeast Asian company, Petron Corp., an oil company in the Philippines, formed a captive in Bermuda last year. The captive, which will cover property risks, is managed by International Risk Management (Bermuda) Ltd. In general, Southeast Asian companies are becoming a lot more interested in captives, said John R. English, President of IRM in Bermuda. "We get so many questions from Japan and South Korea. They tend to look at things that companies from other countries take for granted about Bermuda like infrastructure and regulatory issues," he said.

'In the future, IRM expects to see more Bermuda captive formations from European companies, said Gareth Bradburn, President and CEO of International Risk Management Group Ltd. Earlier this year, IRMG signed a co-operation agreement with GECALUX, a captive manager in Luxembourg (*BI*, Feb. 3, 1997). The agreement will give IRMG greater access to central European countries, Mr Bradburn said. "We have done very little marketing in that area because of the language barrier," he said. 'Eastern Europe could also begin to generate more captives, but it is likely to be a slow process, said Mr Reed of Sedgwick. "There are a lot of obstacles to overcome, which is often due to the regulatory environment, but there are some opportunities there," he said. A more promising area for Bermuda captive managers is Latin America, Mr Reed said.

'IRM set up captives for Colombian and Venezuelan companies last year, Mr English (see above) said. However, he added, some captive owners in Latin America may opt to set up captives in Panama, which last year set itself up as a domicile targeting Latin American companies…"We have a consultant in Panama, and we are seeing interest in Panama from some clients," Mr English said.

'J&H continues to see interest in Bermuda from Latin American companies, said Shaun A. Reape, Senior VP at the captive manager. J&H now manages 12 captives from Latin America in Bermuda, he said. Six of the Latin American captives are from Mexico. And while J&H formed one of the Mexican captives only last year, there may be a hiatus in new Mexican captive formations due to recent tax changes, said Mr Gillett of J&H. Late last year, the Mexican government introduced controlled foreign corporation legislation that took away many tax advantages of captives, he said. "It will probably cause a pause in the formations because if you were about to form a captive and the tax advantages are taken away, you have to go back and look at the other benefits," Mr Gillett said. But the formations should return as the sound risk management reasons for forming a captive remain unchanged, he added. "In every other country where we've seen this type of legislation introduced, we've seen a pause in formations and then they pick up again."

'J&H, like several other managers in Bermuda, saw a fall in the gross premiums written despite an increase in the number of captives it manages. "At J&H the reason for the 5.5% fall to US $1.6 billion in 1996 from US $1.7 billion in 1995, is that several large one-time premium payments were made to some reinsurance captives in 1995," Mr Reape said. Other captive managers cite the general soft insurance rates in the market as the reason for downturns in premium volume. At M&M, gross premiums fell 10.2% to US $500 million from US $557 million in 1995. "Rates are soft so captives are paying less premium for risks assumed," said Mr Carr of M&M. "Net premiums for some captives are also down as captives take advantage of soft reinsurance rates to cede more of their risks," he said. "Soft rates also contributed to the fall off in premium at IRM," said Mr English. Gross premiums fell 33.9% to US $240 million from US $363 million.

'The reduction is also attributable to the winding up of the Hopewell captive reinsurance facility formerly managed by IRM, said Mr Bradburn of IRM. The successor facility, Harrington International Insurance Co. Ltd., is being independently managed by its investors, Swiss Reinsurance Co. and Winterthur Swiss Insurance Co. In addition, Mr Bradburn cited a growing trend of US companies setting up a second captive in Vermont to manage high-volume business such as workers comp. "Captive owners say it is easier to manage the investments of the captive when they are closer to home," he said.

'International Advisory Services saw a 12.4% increase in premium volume to US $925 million from US $810 million in 1995, but that was largely due to new business, said Mr Ezekiel of IAS. "Most of the premium volume for existing captives is pretty flat, if not reducing," he said.

'The Mead Corp. in Dayton, Ohio, still receives benefits from its captive despite the soft market, said Terry A. Reiff, director of risk management. "We continue to use the captive because of the ceding commission that we get back from the reinsurers. If we didn't have the captive, that would just be gone, so the captive serves as a cost reduction center," he said. Mead originally set up a captive in Bermuda in 1971, when the island was one of the few captive domiciles available, Mr Reiff said. When Mead closed the original captive and started a new one in 1987, there was no obvious reason to look for another domicile, he said. "There was no tax advantage in going elsewhere, so we decided to stay in Bermuda," Mr Reiff said.

'Meanwhile, the Bermuda market continues to reverberate with rumblings surrounding the controversial redomestication of Electric Mutual Liability Insurance Co., the General Electric Co. liability insurance subsidiary that moved to Bermuda from Massachusetts shortly before it went in to liquidation in 1995 (*BI*, Dec. 11, 1995). While no business has been lost as a result of the episode, Bermuda continues to suffer bad publicity from the incident, captive managers say. Prior to its relocation, EMLICO had reorganized as part of a plan to separate loss-plagued old liability policies from more profitable, unrelated ongoing business. The poor business was included in the company that relocated to Bermuda. The relocation resulted in a contentious dispute between EMLICO and its reinsurers, which argued that the liquidation should take place in Massachusetts. While most managers in Bermuda argue that the relocation was justifiable on business grounds, they acknowledge that the controversy surrounding the relocation may have harmed Bermuda's image. "The discussions going on cast aspersions on Bermuda's liquidation process, which is totally unfair," said Mr Cossar of A&A. Bermuda's liquidation process is largely based on English law, and the liquidators are independent, he noted. Among other things, the reinsurers were critical that GE picked the liquidators for its own failed insurer, which is permitted under Bermuda law. In spite of the controversy, risk managers are not discouraged from using Bermuda as a captive domicile, Mr Cossar said. "It comes up in discussions, but I don't think people are shying away," he said. The EMLICO episode does not reflect badly on Bermuda regulators, said Mr Reiff of Mead. "It is an issue for GE and the way it chose to manage things. It is not a domicile issue," he said.'[707]

Despite the bad press surrounding the EMLICO move to Bermuda, the industry experienced tremendous growth on the captive side, from healthcare to workers compensation to insurance agency captives and from the Far East, which was a feather in Bermuda's cap. The interest was truly remarkable. However, the bad press continued as the EMLICO case began to intensify.

Sovereign Risk

Bermuda received another feather in its cap when ACE and XL decided to combine to form Sovereign Risk, a political risk company. According to Brian Duperreault ACE was looking for ways to get into the political risks business because of the great success that ACE had with the Multilateral Investment Guarantee Agency (MIGA), an organisation formed in 1988 as a member of the World Bank Group to promote foreign direct investments into emerging economies so as to improve people's lives and reduce poverty. MIGA fulfils this mandate and contributes to development by offering political risk insurance (guarantees) against the risks of currency transfers, expropriation, and war and civil disturbances to investors and lenders and by helping developing countries attract and retain private investment. Currently it has a membership of 157 and is open to all World Bank members.

ACE was the first company to reinsure the political risks of this World Bank agency, MIGA. There had never been a significant risk transfer exchange between the public and private sector insurers until ACE underwrote a reinsurance treaty for MIGA. This was a huge coup for Bermuda because it signalled that the World Bank, by virtue of accepting ACE as its partner, also accepted

[707] *Business Insurance*, 14 April 1997, 'Captive Report: Bermuda, Bermuda's Captive Ranks grow, Diversify', by Gavin Souter

Bermuda as a credible place to do business. Now both ACE and XL are reinsurers of MIGA. As a result of this groundbreaking move by ACE to reinsure MIGA several other multilateral and government organisations now reinsure their previously self- insured risks out to the private sector.

Seeing the opportunities available in the very specialised political risk market coming from the huge increases in investment, trade and finance flows into emerging markets, ACE and XL decided to look for an opportunity to enter the private sector political risk market. At the same time as ACE and XL were examining how to enter the private political risk business, Price Lowenstein of Guy Carpenter, the reinsurance arm of Marsh & McLennan, was working on a business plan to start a new political risk company, because he was strongly of the opinion that the market was ready for another insurer. Lowenstein started coming down to Bermuda to talk to companies about his concept. ACE and XL were the most interested and went on to formalise the concept, based on a uniquely Bermudian model, one that sought to form the company as a joint venture rather than have the two companies competing with each other. As a consequence, ACE and XL formed a managing general agency to write political risk insurance. The new company was called Sovereign Risk Insurance Ltd., and it is based in Bermuda. Sovereign's premiums flow through 50-50 to ACE and XL, and any claims payments are made on that same basis.

The new company, Sovereign Risk Insurance Ltd., was formed for the specific purpose of providing financial institutions, export credit agencies, multilateral agencies, and cross-border investors with a new source of highly-rated, long-term political risk insurance capacity.

Lowenstein says one of the biggest challenges Sovereign faced when it first started in 1997 was overcoming the 'Bermuda issue'. Lowenstein and other Sovereign underwriters would call on the big banks in London, New York, Singapore, and Hong Kong to try to solicit their business, only to be faced with questions about the structure of the company, i.e. why it was formed as a 50/50 joint venture and how the counter-party security worked. In addition, they had to overcome the hurdle of Bermuda being confused with other jurisdictions and thought of as a tax haven and money-laundering centre, as well as a general lack of knowledge of what the Bermuda market had to offer. As a consequence, says Lowenstein they spent a lot of time in the early years educating clients about the benefits of doing business in Bermuda and marketing ACE and XL to the major commercial and investment banks.

The first milestone deal Sovereign underwrote was with the French national political risk insurance agency, COFACE. Sovereign underwrote a country-specific reinsurance treaty for COFACE, which helped this agency to better balance its portfolio of risks in China. This groundbreaking transaction opened the door for other major government deals for Sovereign. Within a year of its formation Sovereign was successfully competing against the other major political risk insurers, AIG and Zurich. Sovereign is now one of the top three political risk insurers in the global private market. Because of its 'net line' (no reinsurance purchased) structure, Sovereign has the largest net line of political risk coverage in the private market (US $125 million). Being a net line insurer insulates Sovereign from the highly cyclical reinsurance markets and so provides greater stability to Sovereign's clients.

According to Brian Duperreault, Chairman, President and CEO of ACE, Sovereign is a great success story for Bermuda because it is now one of the very few major players to provide political risks coverage around the world. More importantly, Sovereign had to go into the international marketplace to be accepted and for it to be accepted as a credible political risk insurer the international community had to accept Bermuda as a credible jurisdiction.

Duperreault said Sovereign has very talented people underwriting for it and has managed to establish itself with banks all around the world. When banks think of political risks they think of Sovereign. Its success is largely attributable to the stellar reputation that Price Lowenstein and his team have built up for themselves.

In an interview with the author, on 13 May 2003, the President of Sovereign Risk, Mr Price Lowenstein, said—"Bermuda did not have a single, full time political risk underwriter in 1997, but as of 2003 features ACE and XL with direct ownership of the two largest Lloyd's political risk underwriters, a 50/50 ownership interest in Sovereign Risk and a major reinsurance relationship with MIGA. He says this is an impressive spread of business within the political risk market as it encompasses a multilateral ECA, a private export credit insurer, two Lloyd's syndicates and Sovereign Risk.

"Bermuda's role in the public and private political risk markets is obviously a very positive development for these markets. The increased capacity provided to MIGA by ACE and XL makes it possible for this agency of the World Bank to guarantee a greater number of developmental projects in the emerging market. ACE and XL's creation of Sovereign has added an important source of stable, long-term capacity to the private market, which is making it easier for banks to cover long term project finance transactions and investors to cover long-term debt equity investments. Bermuda has become a major source of political risk insurance which supports socio-economic development in emerging markets globally."

Life Insurance begins to take off in Bermuda

By 1997, many believed that future growth in the insurance industry was going to come from life business and not so much from nonlife insurance. The Swiss Re Sigma World Insurance report for 1997 illustrated the growth of life insurance as follows—

> 'In 1997, worldwide insurance premium volume amounted to US $2129 billion, with 58% of this generated by life business and 42% by non-life business. The growth came entirely from the life business, which expanded by 7.7%, while non-life business was virtually stagnant (+0.2%).
>
> 'Growth in the life insurance was 10.5% in Western Europe and 6.9% in North America after adjustments for inflation, fuelled by growing concerns about the capacity of the pay-as-you-go state systems to provide adequate pension provisions. Growth in Western Europe and in North America was particularly advantageous for unit-linked and index-linked insurance products, as they profited from lower interest rates and higher share prices. In contrast to the Western European and North American markets, Japan's life insurance market—the world's biggest, with 32% of the global market share—only achieved modest growth of 2.1% in 1997, chiefly because of the ongoing recession in the Japanese economy. Emerging markets performed extremely well, with high growth rates in the life business: Latin America expanded by 15.6%, South and East Asia by 21.9%.'[708]

With the growth in life business being at a nine year high, while non-life hit a ten year low, the interest in life business escalated and spurred the interest of many to form life insurance companies or set up life insurance company divisions, thereby signalling the true beginning of a life industry in Bermuda. Accordingly Mutual Risk Management (MRM) spread its wings into life insurance as reported by the *Bermuda Sun*—

> 'On the heels of its acquisition last year of the Hemisphere Group Ltd., Mutual Risk Management plans to branch out into the growing market for offshore variable annuity and life insurance products. MRM announced yesterday it is planning to form a new life insurance exempted company in Bermuda, MRM Life Ltd. From Bermuda, MRM Life will offer variable life insurance products to high net worth individuals and families. It will work in conjunction with major international financial institutions. "It is a very specialized line of business which is just developing in Bermuda to my knowledge," MRM President and CEO Robert Mulderig said. "It is part of our financial services segment expansion, building on our acquisition of Hemisphere."

[708] *Swiss Re, Sigma report No. 3/1999*, 'World insurance in 1997: Booming life business, but stagnating non-life business', Summary p. 3

'Hemisphere provides administrative service to offshore mutual funds and other companies. MRM has also signed with Tremont Advisors of Rye, New York, a specialized investment services company, to jointly market offshore variable life insurance products using investments in offshore hedge funds. MRM will invest US $1 million in this venture. MRM will also buy 20 per cent of Tremont Advisors B shares and it will acquire 51 per cent of Tremont International Insurance Company, a Cayman company recently set up to write offshore variable life insurance products. MRM will invest US $5 million in the company, which will become a subsidiary of MRM Life. Tremont, through its Bermuda subsidiary, has been involved in developing a number of offshore life insurance and annuity programmes.'[709]

Partner Re diversifies

It was also later in the year that Partner Re reversed its view on diversification when it acquired French reinsurer SAFR for US $950 million, thus changing its long term view that cat companies should remain monoline companies. The deal, centred around the minority shares Swiss Reinsurance Co. held in both companies, greatly expanded Partner Re's geographic reach while diversifying its portfolio. *Bermudian Business* magazine reported on the acquisition as follows—

'While the move (to purchase SAFR) surprised some, Partner Re President and chief executive Herbert Haag said the combination was a good fit because each company operates in different markets.'[710]

XL sets up Latin American Re

Shortly after Partner Re's announcement, XL set up a new Latin American reinsurance company, saying it saw a huge opportunity in the Latin American region for growth. The *Bermuda Sun* reported—

'Bermuda's XL Insurance Company is behind a deal to set up a new Latin American reinsurance company whose headquarters will be in Bermuda. Latin American RE (LARe) will be capitalised with some US $100 million, of which XL is putting up US $75 million, while its partner in the venture Connecticut based Risk Capital Re is putting up US $25 million.

'A statement from the companies yesterday said LARe was being formed in response to "significant economic growth in Latin America and the lack of specialized reinsurers in the region." LARe will provide multi-line reinsurance to the Latin American reinsurance market, emphasizing short-tail, multi-peril property reinsurance and to a limited extent, casualty, marine, aviation and other lines of reinsurance. Once set up it will also seek to enter other reinsurance niches which may include workers' compensation, directors, officers and financial and finite reinsurance. Executives will include Richard Meyer of J&H as LARe's Chairman and CEO, Keith Shroyer of American Re, Vineet Kalucha of Ernst & Young and Arab Insurance, and John Barger of Bankers Trust who will serve as general counsel.'[711]

Consolidation of the Bermuda property cat market continues

The last breaking news of the year came when XL signalled the changing dynamics of the property cat reinsurance marketplace and bought Global Capital Re, bringing the number of property cat reinsurers from the original seven that had opened in Bermuda during its Capital Summer of 1993 to only four—IPC Re, Renaissance Re, Partner Re and LaSalle Re.

Best's Review reported on the state of the market as follows—

'By 1997, the market was ready to turn again. A rejuvenated Lloyd's market, a lack of major cat losses in the United States, increased competition from American and European reinsurers and plummeting primary property insurance rates led to dramatic cuts in catastrophe pricing. Flat or declining premium

[709] *Bermuda Sun*, 6 June 1997, 'MRM expands into offshore life insurance'
[710] *Bermudian Business*, Summer 1997, 'Bermuda keeps up the assault', p.58
[711] *Bermuda Sun*, 5 September 1997, 'XL Insurance sets up new Latin American reinsurance company'

revenue led many of Bermuda's catastrophe investors and managers to diversify into related property, marine and noncatastrophe lines, and to invest heavily in Lloyd's of London.

'Some original investors decided to exercise exit strategies and line up companies for takeover or merger. The original eight catastrophe reinsurers are now four independent companies: Renaissance Re, Partner Re, LaSalle Re, and IPC Re with year end 1997 capital and surplus of US $2.3 billion. Mid-Ocean, Tempest, Global Capital and Cat Limited have been absorbed by their larger brethren ACE and EXEL.'[712]

Broker consolidation intensifies

The continued soft market and the low premiums in the industry began to have adverse effects as brokers sought ways to show profits despite their reduced incomes. Major consolidations took place to cut costs and redundancies. Along with the consolidations came the need to restructure global organisations, including staff reductions. The first major merger news came with the announcement that Aon was acquiring Alexander & Alexander, thus making it the largest insurance broker in the world. The Bermuda insurance community was especially startled when Aon announced the departure of Bermudian veteran and ambassador, Robin Spencer-Arscott. The *Bermuda Sun* reported on this as follows—

'Local insurance veteran Robin Spencer-Arscott has lost his job amid restructuring arising from the Aon Group's recent US $1.23 billion acquisition of rival broker Alexander & Alexander. Mr Spencer-Arscott was Chairman of Bermuda's Aon Re Ltd. and Aon Risk Services. The company confirmed this week he was no longer employed there. It is expected other jobs will be lost or restructured in the A&A acquisition, part of an overall consolidation trend gripping the insurance brokerage world; Too many large brokers on the international front had led to inefficiency and subsequent loss of clients. Chicago-based Aon Group, one of the US "big six"' insurance brokers, is also still digesting the acquisitions of the Bain Hogg Group and most recently the Minet Group.

'Gregory Springer, who a year ago took up the post of President and CEO of Aon's operating companies in Bermuda, declined to comment "at this stage" on the reasons for Mr Spencer-Arscott's departure. "We will be making a series of announcements concerning structuring and who is running things at a later date," Mr Springer told the *Sun*. "Until then I will reserve all comment." Mr Spencer-Arscott had worked at Aon for almost ten years and played a key role in its Bermuda presence and the local insurance industry. When contacted by the *Sun* Mr Spencer-Arscott declined to comment except to say he was out of Aon and was not working elsewhere in the industry."'[713]

Aon was not able to maintain its position as the world's largest broker for very long because Marsh, its archrival, began to acquire as many brokerage operations as it could; starting with the massive acquisition of Johnson & Higgins. Finally, after negotiating for quite some time, Marsh & McLennan Cos. Inc. completed its US $1.8 billion acquisition of rival Johnson & Higgins after getting early clearance on antitrust filings with the federal government.[714]

This move shook the entire insurance industry because it was something that no one had anticipated and it followed closely on the heels of the large A&A and Aon merger. Moreover for the second time in a year the Bermuda insurance industry lost another veteran executive to broker consolidations. This time it was Brian Hall, long heralded as one of the original founders of the industry and the former head of Johnson & Higgins (Bermuda) Ltd. *The Royal Gazette* described him as 'the Island's most influential insurance man' and reported on his decision as follows—

[712] *Best's Review*, P/C, June 1998, 'The Fourth Wave', by James Wynn pp. 53–57

[713] *Bermuda Sun*, 16 May 1997, 'Spencer-Arscott out of Aon Re', by Marina Esplin-Jones

[714] *Business Insurance Update*, 31 March 1997, 'Giant broker deal completed after government's quick approval'

'In a statement obtained by *The Royal Gazette*, J&H said to staff last week that Mr Hall was electing to retire from the firm but would in future be a "consultant/advisor" to J&H Marsh & McLennan. They look forward to his "continuing counsel". Marsh & McLennan (Bermuda) President Andrew Carr has been named President and CEO of global captive management for the merged company. Mr Carr, who will report to John Deitchman in New York, will remain based in Bermuda. The merger of "Marsh Mac" and J&H brings billions of dollars in captive premiums under him—more than US $two billion in Bermuda alone.

'The announcement said: "Captives continue to be flexible and powerful resources for our clients, and we are committed to further differentiating our capabilities and expanding our activities in this business under Andrew's and John's leadership. Additional management responsibilities within global captive management will be announced shortly." Between the two firms on the broking side, it is estimated that they were responsible for more than half of placements with leading Bermuda-based insurers ACE and XL. "Brian is one of the true pioneers in the world of captive (insurance) management," said the statement, which was circulated to J&H staff on Friday. "He founded his own captive management company in 1969. It later was merged with J&H (Bermuda) Ltd. and Brian subsequently led the company's successful efforts in positioning captives as a key risk management tool."

'Meanwhile, in anticipation of the closing of the March 27 deal for Marsh Mac to buy J&H, filings with the US Securities & Exchange Control show J&H intended to move US $75 million out of its Bermuda operations. The filings state: "US Federal taxes associated with remitting such funds approximate US $26 million of which US $16 million have previously been provided."

'Last week's announcement confirmed months of speculation that the group could find no permanent place for Mr Hall in the new Bermuda structure. Sources close to J&H said Mr Hall informed staff at an emotional meeting on Thursday. Having been a director of the former J&H global empire, he is leaving behind a loyal and shocked group of employees, sources said. And it has led to some confusion among them as to who else may go. Knowledgeable industry people feel certain that more departures are likely as a result of the corporate consolidations. After weeks of uncertainty about personal futures, it is believed by staff that in the wake of Mr Hall's departure, other jobs are not safe.

'The Marsh Mac bosses have made no secret of their desire to effect worldwide redundancies to eliminate duplication in the merged companies. It was estimated that as much as five per cent of the global workforce of the combined companies could be cut. It would go a long way toward excising a half a billion dollars in annual worldwide expenses within two years of the merger. Redundancies have already hit the London market.

'J&H, a huge captive manager and insurance broker, was bought by Marsh Mac for about US $1.8 billion, one third payable in cash (about US $600 million) and two thirds payable in Marsh Mac stock (about 9.8 million shares).

'...At least one industry insider saw this as an opportunity for Mr Hall to devote more time to the IAC and the Bermuda Foundation for Insurance Studies, aimed at encouraging and helping more Bermudian students to enter the insurance business.'[715]

The EMLICO threat continues

Despite making significant inroads into the global insurance marketplace, the ghost of EMLICO's decision to move to Bermuda continued to haunt Bermuda's reputation as being a credible offshore jurisdiction. The first attack came when *Business Insurance*, normally thought of as friend to the Bermuda insurance industry, joined forces with the naysayers about EMLICO's allegedly suspect move to Bermuda. The following editorial, entitled, 'At What Cost Convenience?', cast a negative shadow over Bermuda's regulatory process when it ran in *Business Insurance* on 24 March 1997—

[715] *The Royal Gazette*, 14 July 1997, 'Hall goes in wake of merger', by David Fox, p. 13

'Looking out for policyholders is a regulator's job, but Massachusetts Insurance Commissioner Linda Ruthardt is taking protection of one policyholder—General Electric Co.—to unreasonable extremes. Commissioner Ruthardt has proposed a settlement under which she would become US receiver for GE's hugely insolvent Electric Mutual Liability Insurance Co. In return, she will drop her investigation—and withdraw her support of other investigations—into charges that GE and EMLICO concealed the insurer's insolvency in a scheme to move it to Bermuda to take advantage of the island's favourable liquidation laws. The deal is a bad one and should be rejected by a Massachusetts court.

'GE and EMLICO representatives have repeatedly argued that this case is about greedy reinsurers launching fraud charges to avoid paying valid EMLICO claims. They are wrong. The case is about whether EMLICO lied to regulators to further GE's interests and, if so, whether they will be allowed to get away with it. Documents filed in the case strongly suggest that EMLICO misled regulators and show a concerted effort by GE to stonewall subsequent inquiry. This evidence includes a memo prepared for EMLICO by London law firm Clifford Chance & Co. six months before Commissioner Ruthardt approved EMLICO's redomestication, outlining advantages of a Bermuda runoff.

'When the Insurance Division finally began to investigate, former EMLICO President David St Laurent and another former EMLICO official refused to answer questions under oath, raising among other things the issue of their Fifth Amendment rights. This refusal alone is enough under Massachusetts law to place the insurer they now manage—former EMLICO subsidiary Electric Insurance Co.—into receivership.

'Instead, Commissioner Ruthardt has agreed to a deal in which she will abandon her investigation; absolve GE, EMLICO, EIC and all of their employees and consultants of any liability connected to the redomestication; declare all documents obtained in the investigation confidential; turn over control of all EMLICO material to the insurer's Bermuda liquidators; and withdraw her support of efforts by the US Attorney in Boston-who is still investigating-to obtain the Clifford Chance memorandum.

'This goes beyond any reasonable settlement of disputed issues; Commissioner Ruthardt now appears willing to help GE and EMLICO bury potentially incriminating information. And what does she get in return? An appointment as US receiver that offers severely limited control at best and at worst is a sham. Under the deal, GE's huge environmental claims still will be settled in Bermuda and will only be reviewed in Massachusetts by a special master picked by GE, EMLICO's liquidators and Commissioner Ruthardt. The special master may not "substitute his or her judgment for that of the parties"—GE and EMLICO.

'Commissioner Ruthardt says this settlement avoids the "uncertainty and expense" of trying to regain real control of EMLICO. The cost of this approach, though, is the integrity of the Massachusetts Insurance Division. It isn't worth it.

'Meanwhile, Bermuda's regulatory role in the EMLICO mess also is worth a note. The Bermuda government has steadfastly maintained that this was Massachusetts' problem to solve. While Bermuda authorities could have undertaken their own investigation, they did nothing; they appear instead to agree with EMLICO that this is a mere business dispute and seem content to gain the jobs the EMLICO liquidation will generate. Even if Bermuda regulators didn't believe they were deceived in the redomestication, though, they should not have remained inert when evidence suggested their US counterparts were duped. Bermuda's hands-off attitude in this case should be a concern to all companies—particularly reinsurers—that do business in the domicile.'[716]

Upon reading this editorial in *Business Insurance*, Bermuda's Insurance Information Officer, Roger R. Scotton, took immediate action in a letter to the Editor, written as follows—

'I am writing on behalf of the Bermuda insurance industry with regard to your March 24 editorial "At What Cost Convenience?" on the subject of Electric Mutual Liability Insurance Co. The aim of this letter is to correct misconceptions and challenge assumptions that seem to have arisen as a result of a

[716] *Business Insurance*, 24 March 1997, Editorial, 'At What Cost Convenience?'

decision by the Bermuda insurance domicile not to become publicly embroiled in this dispute, a decision heavily influenced by the dictates of *sub judice*.

'Before doing so, I should point out that this is not the first time, nor is it likely to be the last, that as a matter of prudent regulation the island has chosen to remain neutral and stay out of what is essentially a disagreement between contracting parties, each of whom has a range of legal and other remedies open to them.

'So what is to be made of Bermuda's public silence on the EMLICO matter? Your answer to that question, as indicated in the editorial, seems based on the assumption that instead of initiating an investigation, Bermuda's authorities did nothing and "remained inert when evidence suggested their US counterparts were duped."

'Our response is that EMLICO's continuance application to move to Bermuda was first subjected to a thorough review by Bermuda's Insurers (Insurance) Admissions Committee. Though this committee's deliberations and findings are, and must remain, confidential, it is clear from an affidavit sworn by Bermuda's registrar of companies that EMLICO's license was issued on condition that it be subject to several key restrictions. More recently, and as a result of allegations emerging from the EMLICO dispute, it became clear from court proceedings that the registrar had conducted an extensive internal review before concluding that an independent investigation would not be appropriate. It would not have been appropriate, in view of the legal actions that had been commenced at that time, for the registrar to have discussed this review in public.

'Furthermore, Bermuda's regulators have maintained close contact with Massachusetts regulators and have monitored relevant information as it was made available. Based on that information, the Bermuda regulators have not been persuaded that the US regulators were duped. As was indicated in the registrar's affidavit, the Bermuda regulators were aware from the outset that the nature and number of adverse developments in the area of environmental claims was such that "EMLICO could be rendered insolvent."

'Against this background, it is quite unreasonable to suggest that an investigation outside the court system should have been commenced. According to a Bermuda Supreme Court judgment on an application for a judicial review, the EMLICO matter does not constitute a case of "clear and manifest fraud." It goes without saying that had this not been the situation, the registrar's position would have been drastically different.

'It is perhaps also worth remembering that the Supreme Court decision allowing an application to set aside leave to begin judicial review proceedings has been appealed and could go before Bermuda's Court of Appeal this summer. If the review is allowed to proceed, matters up for examination will include the Bermuda government's decision to consent to the EMLICO continuation, the registrar's decision to register the EMLICO consent, and the minister of finance's decision to register EMLICO as an insurer.

'The bottom line, as indicated by an earlier judgment on the hearing of a petition for the winding up of EMLICO, is that remedies such as arbitration are available under the terms of valid reinsurance contracts concluded with EMLICO.

'Lastly, I take issue with your contention that "Bermuda's hands-off attitude" should be a concern to all companies doing business in the domicile.

'Bermuda has worked long and hard to strike the right balance between onerous regulation and weak, meaningless controls. One of the reasons the Bermuda market succeeds is because of the spirit of a very real working partnership between the regulated and the regulators, which produces an efficient regulatory environment that does not stifle private-sector innovation.'[717]

This response prompted Richard J. Marcus, Chief Underwriting and Claims Counsel of Kemper Reinsurance Co., one of the most vocal reinsurers in the whole EMLICO saga, to reply as follows in a letter to the Editor of *Business Insurance*—

[717] *Business Insurance*, 14 April 1997, 'Bermuda defends EMLICO Response'

'…I am writing on behalf of one of the several hundred reinsurers intentionally damaged by Electric Mutual Liability Insurance Co.'s redomestication to Bermuda, to respond to the April 14 letter to the editor, "Bermuda Defends EMLICO Response," in which Roger Scotton unfairly criticizes your March 24 editorial about EMLICO. 'Your editorial quite rightly criticized the Massachusetts and Bermuda insurance regulators for their inappropriate actions and inaction in the face of evidence surfacing—despite General Electric Co.'s and the EMLICO liquidators' vigorous efforts to suppress it—that indicates GE and EMLICO engaged in an elaborate scheme to "export" EMLICO from Massachusetts to Bermuda, in violation of both Massachusetts and Bermuda law.

'Mr Scotton asserts that "as a matter of prudent regulation the island has chosen to remain neutral and stay out of what is essentially a disagreement between contracting parties…."

'The fact of the matter is that GE and EMLICO did not simply breach EMLICO's reinsurance contracts; we contend they also violated Bermuda law, which prohibits the incorporation in Bermuda of an insolvent insurer such as EMLICO. When Bermuda law is violated, and its regulatory process is abused, the public interest of Bermuda is implicated, a fact that Bermuda court judge recently pointed out.

'As your editorial justly maintained, it is not in the best interest of Bermuda for its insurance regulators to remain inert in the face of compelling evidence suggesting that GE and EMLICO engaged in serious misconduct against both Bermuda and Massachusetts. GE and its hand-picked EMLICO liquidators have repeatedly relied on Bermuda's inaction as "evidence" that no fraud occurred; hence, Bermuda's "neutrality" in effect is aiding the wrongdoers.

'Mr Scotton also suggests that the reinsurers have a "range of legal and other remedies open to them" to redress the fraud. He conveniently overlooks that:

'Private arbitration can do nothing to reverse the fraudulent redomestication and repatriate EMLICO to Massachusetts.

'Private arbitration can do nothing to punish those individuals responsible for the violations of Bermuda and Massachusetts law and restore the confidence of the industry and the general public in the regulatory process of the two jurisdictions.

'Representatives of the regulators have indicated that the regulators will resist reinsurers' efforts to call their employees and themselves to testify in the private arbitrations, even though they are key witnesses.

'Mr Scotton also makes the amazing claim that "Bermuda's regulators have maintained close contact with Massachusetts' regulators and…have not been persuaded that the US regulators were duped." 'This claim flies in the face of the Massachusetts Insurance Division's statements that they received virtually no cooperation from the Bermuda regulators and that there is strong evidence that deliberate misrepresentations were made to the Massachusetts division by EMLICO during the redomestication application. Mr Scotton must be aware that the two Bermuda judges who reviewed the evidence have both concluded that reinsurers have raised "a serious issue of fraud." In the face of these holdings by Bermuda's own courts, and similar observations by two Massachusetts judges who reviewed evidence of the fraud, *Business Insurance*'s criticism of the inaction of the Bermuda regulators can hardly be challenged.

'Finally, Mr Scotton seems to suggest that the actions of GE and EMLICO and the passivity of the Bermuda regulators reflect "the spirit of a very real working partnership between the regulated and the regulators, which produces an efficient regulatory environment that does not stifle private-sector innovation." With all due respect to Mr Scotton, one cannot condone the clever manipulation of the regulatory process and any violation of Bermuda and Massachusetts law as "private-sector innovation" that deserves immunity from scrutiny and prosecution.

'Unfortunately, when our representatives contacted Mr Scotton to discuss the mistaken assumptions in his letter, he preferred "not to be drawn into" this matter.

'One would have thought that, having voluntarily and publicly interjected himself into the EMLICO affair, Mr Scotton would be anxious to know the actual facts when he professes to speak for the "Bermuda insurance industry."

'The only thing that reinsurers desire—and rightly deserve—from the Bermuda and Massachusetts regulators is a public evidentiary hearing into the highly questionable circumstances surrounding the EMLICO redomestication.

'The Bermuda and Massachusetts regulators are wrong to deny reinsurers this fundamental due process, and they should take no actions that in effect condone this flagrant abuse of the regulatory process.

'*Business Insurance* is to be commended for speaking out against this injustice. I am sure that the reputable, law-abiding insurance companies domiciled in Bermuda, as well as reinsurers that do business in that country, support the views expressed in your editorial.

'The onus now is on the insurance regulators to do the right thing and fully investigate this matter in a public hearing, regardless of any political pressure brought to bear by GE and its allies or any embarrassment a public airing of the evidence may cause them.'[718]

Then in the 1997 summer issue of *Bottom Line* magazine, David Fox wrote the following probing article about the continuing EMLICO scandal, entitled 'EMLICO, The Unanswered Questions'—

'It has the makings of an epic novel: billions of dollars, corporate polluters, a chess game of court battles, international press interest, an exotic island and business giants. However, Bermuda's reputation for light but effective insurance regulation may turn on the resolution of a messy controversy.

'If Bermuda seeks only quality business, then captive insurer EMLICO had the right pedigree. The Electric Mutual Liability Insurance Co. was born of General Electric Co. (GE), a diversified manufacturing, technology and services company, with interests in everything from aircraft operations, appliances and capital services to lighting, plastics, motors and industrial transportation systems. A corporate dynamo, which also owns US TV network NBC, GE posted 1996 assets at more than US $272.4 billion, and profits for the year at US $7.28 billion.

'In February 1995, GE applied to relocate EMLICO to Bermuda. In October that same year, EMLICO declared insolvency and asked Bermuda's Supreme Court to wind the company up. The question is, were American and Bermudian regulators deceived about EMLICO's solvency to begin with.

'There are powerful players with a great deal to lose—potentially billions of dollars in claims. Bermuda's regulatory provisions are being called into question by an insurance press long suspicious that Bermuda may be too good to be true.

'*Reinsurance* magazine wrote in its April issue: "Bermuda has suffered in the past from a perception that the supervision of the Island's companies is lax…The authorities have recently been criticised for their handling of EMLICO, GE's insolvent captive insurer, which relocated to Bermuda from Massachusetts, allegedly to avoid US bankruptcy regulation."

'That same month, *Reactions* commented:" For more than a year now, the EMLICO affair has been calling Bermuda's reputation as an insurance domicile into question." The *Boston Globe* calls Bermuda's insurance laws "lenient".

'*Business Insurance* lectured: "While Bermuda authorities could have undertaken their own investigation, they did nothing; they appear instead to agree with EMLICO that this is a mere business dispute and seem content to gain the jobs the EMLICO liquidation will generate. Even if Bermuda regulators didn't believe they were deceived in the redomestication, though, they should not have remained inert when evidence suggested their US counterparts were duped." It also opined: "Bermuda's hands-off attitude in this case should be a concern to all companies—particularly reinsurers—that do business in the domicile."

'EMLICO informed Bermuda officials of potential insolvency in February 1995. A Price Waterhouse Bermuda report said EMLICO "is exposed to possible losses arising from claims by GE arising from its liability in respect of certain waste disposal sites. The company has denied coverage and, other than a

[718] *Business Insurance*, 28 April 1997, 'Bermuda, Massachusetts deserve EMLICO criticism'

reserve for defence costs of approximately US $20 million, has made no provision for liability in respect of these incidents".

'Amazingly, GE, one of the largest and supposedly smartest corporations in America, suddenly was not covered by their own insurer for hundreds of millions in claims. Yet, they were moving the company to Bermuda. After EMLICO moved, Bermuda Registrar of Companies Kymn Astwood was told that asbestos related law suits against GE had shot up. He was regularly briefed until October 19, when EMLICO announced they would file for bankruptcy the next day. EMLICO's approval was one of the first things Astwood was responsible for when he became the Registrar in June, 1995. It domiciled here a fortnight later.

'Astwood has never believed there was a master plan to gain financial advantage, as alleged by EMLICO's reinsurers. His May, 1996, affidavit states clearly: "I do not consider that I or the Minister of Finance were misled in any way by EMLICO."

'But as late as this year, Astwood had still not seen or considered, what reinsurers felt was their "smoking gun". Allstate Insurance, one of the reinsurers who have now negotiated a private settlement with GE and EMLICO, introduced in a Boston closed court more than a year ago, "whistle-blower" documents they received anonymously. It included a flow chart dealing with a liquidation scheme and a six page memorandum from London law firm, Clifford Chance & Co., which may suggest an intention to liquidate the company six months before it came here. After efforts by EMLICO and GE, the documents have since been sealed.

'GE and EMLICO's Bermudian liquidators, Coopers & Lybrand, have denied the reinsurers' allegations, saying they're trying to avoid their financial obligations. EMLICO supporters have quietly pointed journalists toward the accuser, suggesting Kemper Re, itself, could do with a closer look.

'The Illinois Company is the subsidiary of Lumbermens Mutual Casualty Co., the flagship firm of Kemper Insurance Cos. Kemper Re lost US $228.3 million in the year to December 31, after nearly three quarters of a billion dollars in net premiums. The company was forced to add US $300 million to its environmental and asbestos (E&A) reserves, Later, Lumbermens raised US $400 million through a surplus notes offering and contributed US $300 million to Kemper Re, offsetting the loss and covering more than US $19 million in dividends.

'Kemper Re's 1996 combined ratio had soared to 147.7 per cent, up from an already concerning 107.1 per cent for 1995. Combined ratios measure the performance of received premiums the company has to pay out in losses and expenses. And 46.4 percentage points of it was directly related to E&A. The rumour was that the EMLICO dispute could break Kemper Re, and that's why they are fighting so hard.

'By contrast, Kemper Re's executive said unflinchingly in a message to shareholders: "Due to the actions taken in 1996, Kemper Re is now financially stronger, better capitalised and better able to move ahead toward profitable growth than ever before. Indeed, one of the insurance industry's principal rating agencies ...A. M. Best Co., demonstrated its agreement with the assessment by upgrading Kemper Re's rating from A minus to A."

'A US federal grand jury is investigating the fraud allegations against GE and EMLICO. The Massachusetts Senate and House of Representatives each have committees probing when the company was known to be sick, who knew, and why state insurance regulators didn't know. Massachusetts regulators have come under the microscope. An embattled commissioner Linda Ruthardt has been criticised for approving the move. One of her staff said that if he knew in 1995 what he knows today about EMLICO, the company would not have been allowed to move. The commissioner has even conceded EMLICO may not have been totally up front with her office.

'But Ruthardt is proposing a solution. Even though two Bermuda Supreme Court judges conceded the fraud allegations could be tried, she is proposing to drop her own right to investigate the allegations of fraud, through the implementation of a settlement proposal she worked out with GE ad EMLICO.

'Reinsurers were not a party to the proposal, and find it disturbing. The proposal, with the blessing of the Bermuda Supreme Court and EMLICO's Bermuda joint liquidators, would have Ruthardt establish a

US receiver to work in conjunction with the liquidators. It is to be considered by a Massachusetts Court in September or October. Across the Atlantic, Kemper is going to the Privy Council in London seeking judicial review of Bermuda's acceptance of EMLICO.

'Meanwhile, GE, EMLICO's estate and Kemper Re are spending millions of dollars in litigation that has procedurally frustrated Kemper and failed to determine the validity of serious charges against GE and EMLICO.

'Bermuda's regulatory hierarchy, faced with no letup from an unsympathetic press, appears to be waiting to exhale—hoping that the whole thing will simply go away.'[719]

The Bermudiana Site Rehabilitation Act 1997

EMLICO was not the only scandal of 1997. A more localised Bermudian v. non-Bermudian scandal erupted from what one insurance executive thought was going to be an altruistic act. By 1997, ACE and XL had outgrown their office space and found that with offices spread across Hamilton, they needed to consolidate their corporate headquarters and bring their employees together into one large location.

Looking out of his window each day onto prestigious Front Street, Brian Duperreault could see the derelict Bermudiana Hotel deteriorating before his eyes. With cars parked on the property, doors and windows broken, squatters taking over the building—it was becoming more and more of a disgrace and then—He came up with a two-fold solution, both to the space problem that his company was facing and to the question of what should be done with the Bermudiana property before it turned into a slum. Quite simply—ACE would buy it

Duperreault began to think of how ACE would benefit if it in fact did restore and renovate the old Bermudiana building. The only way he could see of making the property cost effective for ACE would be to own it outright. At that time the building was owned by non-Bermudians and though well aware of the conditions for corporate ownership of land, Duperreault thought that this very fact gave him a fighting chance. Confident of his plan, he took it to the Bermuda government. Much to his surprise they were not at all receptive, despite the fact that Argus, the large local insurance company, was about to foreclose on the property. The Bermuda Government was still not interested.

Duperreault realised he might need the support of the one other company on the island with the same expansion problems as his own to help finance the monumental project that lay ahead in redeveloping the site. Duperreault decided to call upon Brian O'Hara, Chairman and CEO of XL. O'Hara was on vacation but Duperreault did not let that deter him. Instead he tracked O'Hara down. O'Hara was just about to go water skiing in the state of Washington, thousands of miles from his corporate giant in Bermuda, when a call was put through to him from Duperreault. Having to switch from water skiing mode to corporate buying mode, especially when he heard the deal that Duperreault was proposing, took all of a few minutes.[720]

Having convinced O'Hara that his deal was more important than water-skiing, Duperreault proceeded to set in motion a *cause célèbre* that made headlines in Bermuda and overseas. The following account of what became known as 'the Bermudiana Deal' is derived from an extensive article written by Kevin Stevenson for *Bermudian Business* in the Summer of 1997—

'ACE and XL decided to use their combined corporate might to convince the Bermuda government that they should be allowed to purchase the five acre Bermudiana site from Argus Insurance Co. Ltd. What the two Brians had not bargained for was the nostalgia the Bermudiana conjured up for many of the old Bermudians. They also did not expect the level of resistance from Bermudians about opening the door

[719] *Bottom Line*, Summer 1997, 'EMLICO: The Unanswered Questions', by David Fox, p. 16

[720] Interviews with Brian Duperreault, 2 December 2002 and Brian O'Hara, 19 November 2002

to foreign investors because of fear of outsiders gaining a stronghold on the already skyrocketing real estate market in Bermuda.

'Unable to get anywhere despite joining forces with XL, Duperreault then decided to contact John Deuss, the oil magnate and recluse who spends a tremendous amount of time on the island, for help. Deuss was a friend of Argus' Chairman, John Sainsbury. Deuss stepped in and told Duperreault and O'Hara that the only way the deal was going to work was if they got the support of the government. Duperreault did not want to lobby for the land nor did he want to get himself involved in a political football. Therefore Deuss stepped in as the lobbyist on behalf of the seller Argus and eventually got the majority of both the UBP and the PLP to accept that the Bermudiana deal was a good deal for Bermuda as well as XL and ACE.

'...In announcing their plan to purchase the property, ACE and EXEL imposed two conditions that had to be met before they could or would buy the property. Existing legislation prohibiting overseas companies from owning Bermuda property outright had to be waived, and planning approval had to be received, both no later than March 31, 1997, or the project would be called off.

'No sooner had the deal been announced, then the directors of BFCL (Bermuda Financial Centre Limited, the original company that defaulted on the loan) mounted a blistering campaign to block it. They argued passage of the private bill to facilitate the deal would set a dangerous precedent leading other exempted companies to follow suit. They "viewed with concern" the public silence surrounding the proposal, and they complained active lobbying was taking place for MPs (Members of Parliament) to vote in favour of the bill.

'It was exactly the type of debate both O'Hara and Duperreault had wanted to avoid. "When we did start running into the usual flak and problems, I was basically ready to say, 'Well, this isn't going to happen,' says O'Hara. Concurs Duperreault: 'I think we both reached the point where we just didn't think it was going to happen. We were offering a solution, but apparently it wasn't acceptable. We wanted unanimous agreement from all sides that this was the right thing for Bermuda. And if it wasn't going to happen—if there was the possibility that it would become divisive—then we didn't want to be a part of it. We were offering a solution, but we wanted everybody to be happy with it."

'The controversy hinged on existing legislation prohibiting overseas companies from owing more than 40 per cent of domestic companies and real estate—a law designed to protect Bermudian interests.

'David L. White, editor of *The Royal Gazette*, Bermuda's only daily newspaper, put it succinctly in an editorial. "The rationale for this (policy) is that Bermudians have a right to the opportunity to own 'a piece of the rock', or build a company without facing severe competition which could come from companies based in much larger countries."

'As White noted, there have been exceptions, which include most of the Island's major hotels, telecommunications company Cable & Wireless, international insurer American International, and spirits purveyor Bacardi. There are others. "In many ways, these are exceptions which make the rule, because Bermuda's greater interest was served by a waiver," wrote White.

'And so the question at the height of the debate was whether a waiver in the Bermudiana case served the greater good. Editor (Tim) Hodgson (of the weekly newspaper, *The Mid Ocean*) argued that while the ownership rule "should probably" be waived in the Bermudiana deal, there was great concern for the future. "If it (the Bermudiana deal) goes ahead, property owners and the offshore community might be tempted to lobby government to waive the 60/40 rule entirely," wrote Hodgson. "Both parties would benefit. Cash strapped landlords would get instant bonanzas; international companies would get their own buildings. A fire sale of Hamilton land would ensue. But Bermuda would suffer in the long-term. Once the property left Bermudian hands, the Island would forfeit ownership of its most valuable asset as well as all future earnings it might accrue. Bermuda Inc. would have effectively auctioned off its future."

'Hodgson conceded this was a worst case scenario, and in the specific circumstance of the Bermudiana site, it was unrealistic to think Bermudian resources could raise sufficient funds to develop the property properly. Indeed, the BFCL had tried and failed, and in the interim, not one single alternative scheme was put forward by Bermudian interests.

'It was against this background that Bermuda Commercial Bank, led by Chairman and major shareholder John Deuss, and newly-installed managing director Peter Roberts, stepped in with an offer to help. The bank's leadership was particularly geared to assist because of its deal-making experience. "When it didn't look like it (the ACE/EXEL deal) was going to happen, I think what John and Bermuda Commercial Bank did was to explain not only the benefits of what we could do—clean up the site—but also the economic realities of the situation," says Duperreault. "Things were unlikely to happen any other way."

'By December, 1996, the ACE/EXEL plan cleared an important hurdle when a special committee of MPs gave it the green light. "It's a big exception to the normal rule," said Joint Select Committee on Private Bills member Trevor Moniz. "We haven't had an outright purchase of land by a non-Bermudian company for many years." It was an admission that the ACE/EXEL plan was the best possible solution for the Bermudiana problem.

'Meanwhile rival developer BFCL also claimed a breakthrough in December when it announced it was negotiating with finance companies in both Boston and New York to raise US $100 million to buy back the property from Argus and develop the property. "I understand we should have finances in effect by the end of the year," said BFCL Chairman Neville Conyers. January 1 came and went without any financing announcement from the BFCL, but that same month Conyers complained, through a letter to shareholders, that Deuss was personally lobbying on behalf of ACE and EXEL and had approached the Planning Department on behalf of the project. "This is an extraordinary situation," said Conyers. "Two companies, albeit important and highly reputable, but nevertheless non-Bermudian, seem to be set to be given permission to own the Bermudiana site and thus defy the 60/40 rule with little apparent debate or dissension."

'Conyers' claims against Deuss were immediately refuted. EXEL spokesman Gavin Arton replied that Deuss was purely a "facilitator", and had no interest in the deal other than to benefit along with the rest of the Island by the clean-up of an eyesore.

'But the BFCL ploughed on, launching its own lobbying efforts at month's end in an effort to get MPs to vote against the ACE/EXEL deal. Shareholders of the BFCL were asked by Conyers to launch a mail-in campaign to MPs asking them to vote against the private members bill. "There's no other way to stop it," said Conyers. "Unless parliament backs us on the 60/40 issue, 140 local shareholders are going to be out of pocket. We'll be insolvent." Conyers was certainly right on the first point, but he was wide of the mark on the second once the dust had settled and the deal was done.

'Meanwhile, sponsor of the Bermudiana Rehabilitation Bill, Progressive Labour Party (PLP) MP Reginald Burrows, expressed surprise over the controversy surrounding the issue. "I knew some people would not be happy with it, but I did not expect all this controversy," he said. "I was asked to introduce it (the private bill), and yes after being briefed on the bill, I was quite satisfied with it."

'So too was the Bermuda public, at least according to an informal survey carried out by *The Royal Gazette*. "Someone has got to take it over," one local woman, Carola Farrell, was quoted as saying. "It's been an eyesore for a long time. If local businesses cannot do it, then a foreign company should. There are tourists who pass there all the time. It's not nice for them to see that."

'Added another local, Stewart Greenslade: "If we could do it ourselves, then by all means I think we should. If it can't be done, then the bottom line is that the Bermudiana site looks like hell."

'By February the tide in favour of the ACE/EXEL deal had turned for good, with the PLP virtually guaranteeing passage of the bill when it threw its collective weight behind the deal. "There comes a time when exceptions have to be made, and this is one of them. Exceptions have been made before," said PLP Shadow Home Affairs Minister Alex Scott. "We've got some real players on board who are willing to invest real money in the Island."

'The PLP's endorsement came in advance of a decision by the ruling United Bermuda Party, a point that wasn't missed by Scott. "The irony here is the PLP may prove to be a better partner to big business," he said, relishing the opportunity to score political points for the Opposition which is at pains to express support for international business, a segment all political platforms in Bermuda realise can heavily influence a general election.

'Emboldened by growing support, Argus soon came out swinging, not only arguing the ACE/EXEL plan would benefit the Island, but also expressing the belief it was the only viable way of ridding the Island of a prominent eyesore.

'Argus released documents attacking BFCL, which it accused of making factual errors in its campaign against the plan to sell to ACE and EXEL. It also laid out reasons why the ACE/EXEL deal should be supported: the Bermudiana site had been in non-Bermudian hands for years, and true ownership would pass from the British hotel chain Trusthouse Forte to ACE and EXEL; BFCL never owned the land, and even if it succeeded in developing the site, it would still be 90 per cent foreign owned; no truly Bermudian entity could afford to develop the site; ACE and EXEL would not be able to sell-on to non-Bermudians without the approval of the Ministry of Finance; a phased development would be ideal for the construction industry; it would anchor key insurance industry businesses solidly to Bermuda, ensuring their long-term presence on the Island; small BFCL shareholders would receive US $525,000 voluntary compensation from ACE/EXEL; and an influx of overseas money financing the development would benefit Bermuda's balance of payments.

'"BFCL has no ownership rights in the site," (said) Argus along with ACE and EXEL in a statement. "It tried for three years, but was unsuccessful in financing and developing the site. And even if it were now to arrange the financing, it would be financing for a site it has no right to own. While it might be nice to consider Bermudian ownership through local companies, like BFCL for example, the economic reality is that more than ample opportunity has been given to "local" investors to finance and develop the site with absolutely no success to date. ACE and EXEL, two significant overseas companies with major financial resources ready to be committed to this project, are here and ready to develop the site. The abandoned and crumbling Bermudiana Hotel is an eyesore totally inconsistent with the image Bermuda wishes to promote at home and abroad. Its dereliction advertises that Bermuda had failed to find a proper economic use for the site."

'Undeterred, BFCL, led by Conyers, appeared to have lined up another backer, with a verbal commitment of US $125 million, and the group tried yet again to get back in the game. But Argus managing director John Sainsbury was having none of it. Sainsbury noted BFCL had for three years tried to raise money for its plans, but in the end commitment to a deal always hinged on various conditions. "I assume the latest one is no different," said Sainsbury, adding that Argus had in principle agreement to sell the property to ACE and EXEL through to the end of March. "We entered the agreement in good faith, and it would be bad faith to negotiate with someone else," he said. "Essentially, it had to play out."

'Finally the landmark bill waiving the 60/40 rule came before the House of Assembly on February 15 and its passage was guaranteed with the UBP imposing a whip for the vote, which meant MPs had to toe the party line. But the controversy that had swirled about the Bermudiana site was not about to go away. Due to different rules that apply to private bills, the Bermudiana Site Rehabilitation Act 1996 was passed without objection 42 seconds after it was moved by MP Burrows. Such swift passage of the bill caused an uproar. At the time the bill was passed, the House of Assembly was half empty. Several MPs admitted they were caught off guard because they were unaware of parliamentary rules on debating private legislation, while Burrows was accused of a "clever parliamentary manoeuvre" that precluded debate.

'At the heart of the uproar was the expectation that the Bermudiana waiver would be given a full airing—which for Bermudian MPs could mean a night-long debate. "A bill of such magnitude should certainly have been debated," said the UBP's John Barritt. "It seems incredible it should go through when only about half the MPs were present. I'm ashamed and embarrassed at what occurred in parliament." Tim Smith was equally outraged: "The silence was deafening if not duplicitous," the UBP MP declared.

'But House of Assembly Speaker Ernest DeCouto was unmoved. He noted at any time during the proceedings an MP could have stood up and moved the bill be committed to the House in Committee, which would have then sparked a debate. But nobody did. "It just went through," said DeCouto. "I think Mr Burrows thought the passage of the bill was a *fait accompli* given that both parties were meant to be supporting it." Ultimately, most of the MPs—and possibly a majority of Bermudians—felt the way former Premier David Saul did: "I think most of the arguments were in the press long before the bill went up to the House."

'But members of Bermuda's other parliamentary body, the Senate, several weeks later took the opportunity to make up for what their House of Assembly colleagues had failed to produce. In a two- and-a half- hour debate senators weighed in with their opinions. Mostly, senators from all sides agreed that the Bermudiana was a derelict eyesore which needed to be demolished before it promoted any more negative messages about Bermuda. Government Senator Noela Haycock summed it up best when she called the site a breeding ground for "termites, rats, winos and druggies" located smack in the middle of Bermuda's bustling capital. What was truly remarkable in the eyes of independent Senator Walwyn Hughes, was that both sides of Bermuda's political landscape were in agreement about something for a change. But even as the Senate was passing the Bermudiana bill, the BFCL was still gasping for air. Company President Conyers announced that Boston-based investment banker Robert Downing had verbally confirmed 100-per cent financing for the US $125 million BFCL project. Downing was scheduled to arrive from the US on February 26, but in a twist of fate was involved in a traffic accident on the way to the airport. The one-day delay soon became indefinite and Downing's name was not heard again. Apparently, he too came to the conclusion the ACE/EXEL deal was the best thing for the Bermudiana site.

'Still the saga continued, for yet another potential investor washed up on Bermuda's shores. This was United Kingdom businessman Peter Clayton, who picked up the BFCL for a nominal sum and launched yet another bid to build on the Bermudiana site. Clayton, who failed to prevent approval for the ACE/EXEL proposal, lodged an appeal that was denied in short order, paving the way for the ACE/EXEL plan to proceed. Bermuda will now finally be rid of its pink elephant.

'Which raises the question which perhaps most interests the average Bermudian: will the Bermudiana Hotel be blasted into history with dynamite in a Hollywood-esque finale? "I've got to tell you that I really wanted to blow it up," says Duperreault. "There'd be a lottery with the winning ticket getting to push the plunger. It would be the greatest thing that ever happened. What a party! But no, we'll tear down the site."

With it, some might lament, will go a chapter in Bermuda's history. But so too will another chapter open, further contributing to the City of Hamilton, and Bermuda in general, well into the next century.'[721]

The *Bermuda Sun* added the following comments about the closing of the Bermudiana deal—

'For Argus the deal ends a long running saga in which the company was forced to seize the land from the Bermuda Financial Centre Ltd. (BFCL) in March last year after the listed company defaulted in a loan. BFCL had failed to raise money to develop the site. Argus had loaned US $7.5 million to BFCL and had invested another US $400,000 when it became clear that the BFCL deal was falling apart.

'The ACE and EXEL price includes paying off a US $7.5 million mortgage the Bank of Bermuda had on the land and about US $10 million to Argus to pay off the loan plus accrued interest.... The proposed project would eventually have four buildings, two housing ACE and two housing EXEL. Construction would be phased over five years.[722]

After months of battling, ACE and EXEL were finally given the go-ahead to purchase the site under a ground-breaking private act called, 'The Bermudiana Site Rehabilitation Act of 1997'. The final purchase price from Argus was US $18 million. Duperreault said it was so poetic for ACE and XL to be housed side by side when they started out as sister companies together in the late 1980s.

Premier Jennifer Smith said the reason why her party elected to support the Bermudiana deal was because they understood what ACE and XL were trying to do. Since 1990, the PLP had adopted as its mandate to attend meetings with the international business sector so as to open dialogue between them in order that all parties could gain an understanding of each other. At one of the many luncheons the PLP had attended the matter of the Bermudiana situation was raised. Everyone in the room agreed that the Bermudiana was an eyesore to the Front Street of Hamilton. After ACE and XL presented their proposal, the PLP went away and thought about the implications for Bermuda.

[721] *Bermudian Business*, Summer 1997, 'The Bermudiana Deal', by Kevin Stevenson, pp 50–55

[722] *Bermuda Sun*, 25 April 1997, 'ACE and EXEL complete hotel site purchase', by Ahmed ElAmin

Premier Smith said that some of the factors her party took into consideration included the massive impact that the two companies, ACE and XL, have had on the flourishing of Bermuda as an international insurance centre and she credits the wave of new insurance companies in Bermuda to the professionalism and success of ACE and XL. She also said these companies provide scholarships and are overall good corporate citizens of Bermuda. By wanting to invest in Bermudian land, ACE and XL demonstrated their commitment to the island and the PLP wanted to capitalise on this generous gesture. The PLP felt that if these companies were allowed to invest in real estate on the island, they would be more loyal to the island. Therefore, they saw no reason to go against the ACE and XL proposal. Premier Smith said that as a result of the party's decision it took a lot of flack from many of its own members but it was felt that it was more important to weigh all options and act in the best interests of all Bermudians. Therefore, they stood behind their decision and they do not regret it to this day.[723]

Local changes to meet international needs

The first big news of local changes was the announcement by the Bermuda Stock Exchange that it was launching a new market index for locally based insurers and reinsurers, as reported by the *Bermuda Sun* newspaper—

> 'Last year when the Bermuda Stock Exchange was in the middle of establishing itself as a leading electronic offshore exchange, the *Financial Post* dubbed it "Bermuda's electronic field of dreams." But the traders and listings came. Since the BSX's implementation of rules to govern secondary listings of international companies and local mutual funds—backed by a major marketing push—its market capitalization has shot up from US $6 billion to more than US $37 billion. Tiny Bermuda now has the world's 34th largest stock market.
>
> 'Total turnover has soared from US $60 million in 1993, shortly after the BSX incorporated as a limited liability company owned by the island's banks, to US $6.6 billion earlier this year. As of this week, it exceeds US $10 billion.... BSX CEO William Woods was quoted as saying, "We understand there is foreign interest in the market right now as well, which is very good for the exchange and Bermuda, as investors outside of Bermuda are starting to look at some of the companies in Bermuda, based on their investment merits. We're pleased that's happening. We're hoping it is a spin-off effect of the work we have done at the BSX to develop and enhance the market and proficiency of its operations as well as the marketing work we've done."
>
> 'The exchange's remarkable success so far has caused it to focus its attention on other areas now—and some that are not so traditional for a stock exchange...Among the most exciting of its new ventures is the new insurance index. BSX CEO William Woods said the exchange had recently linked up with London's FTSE Index on the venture. "We have signed a contract with the FTSE to engage them as consultants in helping us create the Bermuda International Insurance Market Index," Mr Woods said. "It will enable people first of all to track the fortunes of the Bermuda insurance market, and second of all to use it as a way of hedging against a fall in the index. It will be a proxy for the state of the Bermuda insurance market. If the new index catches on, a new insurance mutual fund will be launched enabling investors to buy stock in it."'[724]

Bermuda Commodities Exchange opened

Following closely behind the establishment of the Bermuda Stock Exchange came the Bermuda Commodities Exchange, which indicated that the line between insurance and the financial world had become somewhat blurred. *National Underwriter* reported about the new exchange as follows—

[723] Interview with Premier Jennifer Smith, 26 March 2003

[724] *Bermuda Sun*, 25 July 1997, 'BSX chases its dreams', by Marina Esplin-Jones

'The Bermuda Commodities Exchange, designed to help investors capitalize on and hedge against catastrophe insurance risks, will officially begin trading later this month, with 20 prominent insurance, reinsurance and financial services companies as members.

'...The current members consist of insurer American International Group; reinsurer Transatlantic Holdings, a subsidiary of AIG; reinsurance broker Guy Carpenter; the banking firms of Chase Manhattan and Bankers Trust International; and the investment and securities firms of Goldman Sachs International and Morgan Stanley & Co. All the companies are based in New York.

'Other members are reinsurance brokers Aon Re (Bermuda) Ltd., a subsidiary of Aon Risk Services of Chicago; E.W Blanch Holdings, New York, and General Re Underwriting Services Ltd., a subsidiary of General Reinsurance of Stamford, Connecticut.

'Also on the Exchange are Bermuda Insurers Mid Ocean Reinsurance Ltd., Partner Reinsurance Co., Renaissance Reinsurance Ltd., Cat Ltd., Tempest Reinsurance Co., a subsidiary of ACE Ltd., International Property and Casualty Ltd., and Stockton Reinsurance Investments.

'Other members include Clement S. Dwyer, Jr., & Aaron B. Stern, a partnership firm which will be based in Bermuda; Griffin Trading Co., a New York-based investment firm; and Sedgwick Lane Financial LLC, Chicago, a joint venture of London-based insurance brokers Sedgwick Group and Lane Financial, a consulting and brokerage firm based in Chicago.

'The Bermuda Commodities Exchange was authorized by an act of the Bermuda Parliament in 1996 and is under the supervision of the Bermuda Monetary Authority. The Exchange will offer members the opportunity to conduct trading in option contracts based on an index of insured homeowners losses due to atmospheric perils in particular regions of the United States over specific periods.

'Trading will be in US dollars.

'...Contracts will cover damage from a single event, aggregate damage or second event over the covered period.

'The option buyer will pay a premium to a seller (the writer), and the latter will be liable for payment if a specified amount of losses in the particular region and time period from hurricanes, tornadoes, windstorms, hail and/or freezing temperatures exceed a specified loss-to-value ratio. Prices of particular contracts may fluctuate as trading takes place during the risk period.

'Trading will be done via an automated, electronic system that connects members in a "virtual open outcry" arrangement. The prices and quantities of all bids and offers will be displayed without disclosing the identity of any particular trading member of customer.'[725]

The Bermuda Stock Exchange's CEO William Woods did not see the Commodities Exchange as a threat, as reported by the *Bermuda Sun*—

'We see it as complementary and indeed the President of BCE, Mr Tom Heise, has made the same point,' he said. 'The BCE is a more specialty catastrophe risk option for investors. CATEX will open up the reinsurance market more. The main thing is it is all happening in Bermuda, making it an innovative centre for new insurance products and services.'[726]

Bermuda Scholars Programme

Another initiative on behalf of the Bermuda insurance industry to help those overseas to understand the Bermuda insurance marketplace came when the Bermuda Foundation for Insurance Studies (BFIS) offered the Bermuda Scholars Programme—

[725] *National Underwriter*, 3 November 1997, 'Bermuda Commodities Exchange set to Open'

[726] *Bermuda Sun*, 25 July 1997, 'BSX chases its Dreams, Catastrophe Index', by Marina Esplin-Jones

'BFIS begins offering a programme called the Bermuda Scholars Programme, which allows students the opportunity to combine classroom study with practical training.

'The inaugural six-week, six-credit Bermuda Scholars Programme was offered in conjunction with the College of Insurance in New York and took place this summer (1997). While other BFIS initiatives are designed to provide academic and professional education for Bermudians, the scholars programme is directed towards overseas students.

'The course places Bermuda firmly in the real world for people training to be tomorrow's insurance leaders. They gain a deep understanding of the Bermuda industry's scope, its significance, its products and its people. Presumably, it's an understanding that will endure, and they'll spread the good news about Bermuda to both the university community and the working world.

'The scholars' programme works are follows. Take 10 outstanding insurance students. Bring them to Bermuda for six weeks of meetings and classes. Introduce them to a broad spectrum of people in business, government administration and politics. Challenge them to explore issues likely to affect Bermuda's insurance industry in the coming years. Then ask them to present their findings and recommend ways for Bermuda to respond.

'...The programme was divided between classroom instruction and a research project. With local business leaders as guest speakers, instructors from the College of Insurance in New York led a three-week course, Global Insurance and Risk Management at the Bermuda College.'[727]

The first Programme seemed to go down with resounding success. Only time will tell if those university students do retain their knowledge of Bermuda when they join the real world as insurance workers and help to bring business to the Island.

International Commercial Arbitration

One of the greatest announcements made on the local scene came as a result of Bermuda establishing a dedicated international commercial arbitration centre at The Bermuda College.

After enacting the International Conciliation and Arbitration Act 1993 (the Act), Bermuda went on to "establish a register of internationally-recognised arbitrators in the insurance and reinsurance sector as well as other recognised commercial sectors. The Bermuda Chapter of the Chartered Institute of Arbitrators has almost 30 members, of whom a third are fellows of the Chartered Institute of Arbitrators.

Having hosted several meetings, Bermuda saw itself as a viable centre for arbitrators and as such established a separate centre dedicated to international commercial arbitration at the Bermuda College. *Bottom Line* magazine gave the following details and background—

'The LCIA Arbitration International (LCIA) has held conferences in Bermuda and, as a result of the recognition given by a number of international arbitration institutions, including the LCIA, Bermuda has been able to establish a dedicated international commercial arbitration centre at the Bermuda College. The US $50 million campus was completed in 1996, and is located in a 22 acre site. There are numerous rooms of various sizes available for arbitrations, including two separate video conferencing rooms—one of which uses Picturetel technology...

'In 1993, Bermuda enacted the Bermuda International Conciliation and Arbitration Act 1993 (the Act) which incorporates the United Nations Commission on International Trade (UNCITRAL) Model Law. Not only does this legislation provide a much easier framework within which to conduct arbitrations, but it also limits the involvement of the courts, leaving the arbitrator(s) and the participants in the arbitration with a clear understanding of what its expected of them.

[727] *Bermudian Business*, Fall 1997, 'Business class – Scholars programmer offers insight into Bermuda's scope', by Sue Johnson, pp. 20–22

'Recognising that Bermuda was in a unique position with its rapidly emerging insurance and reinsurance business, 1993 was an opportune time to adopt an internationally recognised set of rules which would enable major international commercial disputes to be resolved by arbitration. The UNCITRAL Model Law is internationally recognized, and, additionally, Bermuda is a party to the New York Convention, thus giving mutual recognition to other Convention countries in respect of the enforcement of foreign arbitral awards. As such, it would seem that any remaining hurdle to a primary position in international arbitration has been overcome.

'The act has also made it easier for parties to arbitrate in Bermuda by not requiring work permits for arbitrators or parties to arbitrations coming to Bermuda. At the same time, there is no requirement that any arbitrator of a dispute should be a local arbitrator, and the Government of Bermuda, through its various ministries, has recognised the importance of international commercial arbitration to Bermuda and is willing to assist in the smooth running of arbitrations.

'...Since 1993, the UNCITRAL (United National Commission on International Trade Law) Model Law, as incorporated in the Act, has encouraged greater use of Bermuda, and there is increasing reliance by the insurance industry on Bermuda as an arbitration jurisdiction of substance.

'The arbitration rooms and "break out" rooms of the Bermuda College readily lend themselves to the work of complex arbitrations, with abundant space for books, binders and arbitration materials. Fax and computer modems and every modern communication facility are also available.

'In September 1996, Appleby Spurling & Kempe was involved in the formation of a Bermuda chapter of the AIDA (*Association Internationale de Droit d'Assurances*— in English the "International Insurance Law Association"). The aim of the Bermuda chapter is to provide a forum for the discussion and debate of legal issues affecting the insurance and reinsurance industry in Bermuda, and to promote arbitration and dispute resolution by forming a chapter in Bermuda of ARIAS, which is the AIDA Reinsurance and Insurance Arbitration Society.

'The aim of those most closely connected with arbitration in Bermuda is no less than to complement Bermuda's sophisticated insurance market with a world class reputation as an arbitration centre. The necessary infrastructure is now firmly in place and the number of arbitrations taking place in Bermuda is steadily increasing.'[728]

A year of change

1997 was a time of political comings and goings. Sir John Swan resigned from the House of Assembly and Dr David Saul resigned from the Premiership after holding office for only 18 months. Saul's decision was based on the fact that he thought things had settled down after the Referendum and the McDonalds controversy. The island was functioning tranquilly again, his party was well organised and therefore his job was done. After much political back and forth, and indeed to the surprise of many, history was made when Pamela Gordon, daughter of political activist Dr E.F. Gordon, was chosen to be the next Premier of Bermuda, not only the youngest person but also the first woman ever to hold that position.

By the summer, the economic front in Bermuda began to show signs of improving as inflation dropped below two per cent for the first time on record. However, shortly after this good news, the island was brought to a near standstill when ferry workers threatened to strike over wage negotiations. An overtime ban was imposed and other Government workers, including bus drivers, threatened to strike. However a strike was averted after a favourable compromise was reached. Then, just when everyone thought things had cooled down despite the summer heat, teachers threatened to work to rule because they had been left out of the educational restructuring process. The temper of the island rose as people began to feel they were no longer a part of the growth of Bermuda.

[728] *Bottom Line*, Spring 1998, 'Corporate Brief, Offshore Arbitration', by Warren Cabral, p. 30

Then, in September, Police Commissioner Colin Coxall announced that he was resigning as Police Commissioner in view of the contention and controversy aroused by 'Operation Cleansweep', an initiative whereby he had hoped to rid Bermuda's streets of drugs. September also marked the official opening of Bermuda's state-of-the-art 'mega' school CedarBridge, and the beginning of a new way to educate Bermudians. Initial reports from the school were discouraging. The hooliganism of an unruly few detracted from the reputation of the entire school and was a cause of concern to the many Bermudians who had questioned the need for such a school in the first place.

From the global insurance industry's perspective, after three consecutive years of soft insurance pricing, 1997 was the year of consolidations in the marketplace, including some in Bermuda. It also marked the year when, because of the continued soft market, several of Bermuda's insurers began diversifying overseas. Every insurer was looking for a profitable means to expand its market share. *Bermudian Business* reported on the state of affairs—

'...Pricing pressures remain extraordinarily intense, fuelled among other things by a recent scarcity of large natural catastrophe losses, by excess underwriting capacity in most primary and reinsurance markets, and by the re-emergence of an aggressive Lloyd's market following the latter's Reconstruction and Renewal.

'Responding to these fundamental market forces, several major Bermudian insurers and reinsurers have redeployed their financial resources in various ways, seeking to improve efficiency of capital utilisation, to ensure survival of their franchises, and to enhance shareholder returns.

'These strategies have included returning capital to controlling shareholders through share repurchases and/or heightened dividend payments; mergers and acquisitions; joint ventures; and substantial investing abroad.'[729]

Only time will tell if the decisions made by the Bermuda insurance marketplace to diversify will pan out but clearly 1997 was a redefining time for the industry as it struggled to maintain its place in a continuing soft market and for Bermuda socially as it fought to regain a sense of stability. David Fox of the *Bottom Line* reported on the changing scene—

'While many Bermudians have become blasé about Bermuda's success in the insurance business, few truly comprehend the astonishing scale of corporate growth in a short period of time. Few really understand the prestige insurance success has added to the Bermuda name and its real contribution to tourism and the public purse. And few appreciate that increasingly, observers of the global market place are acknowledging that something really special has happened here with the emergence, development and diversification of a commercial insurance market. In one decade, it has flourished from simply the world's dominant force in captive insurance, to what respected ratings agency A.M. Best Co. last June called " A Growing Global Powerhouse."

'Bermuda, they reported had evolved into a world reinsurance centre of insurance and reinsurance. It is an indication of how impressed A.M. Best is with what Bermuda has achieved, how surprising such speedy, broad industry development is, and how satisfied Best is that Bermuda has fully arrived. This idyllic mid-Atlantic jurisdiction has gone from being an "alternative" insurance provider to more of a mainstream market, from a jurisdiction criticised for "naïve capital" to one hailed for creativity and innovation.[730]

According to the *Bermuda Market Digest*—

'The Bermuda economy has grown on average 4.2 per cent per year in real terms since 1993, double the 1993 five year plan target rate of two per cent, according to Finance Minister Grant Gibbons...The international business sector continues its expansion and diversification.... Expenditures by international

[729] *Bermudian Business*, Fall 1997, 'Breaking the Mould, Bermudian insurers lock horns in a competitive world', by Alan G. Murray and Ted Collins, pp. 44–46

[730] *Bottom Line*, October 1997, 'Feeding frenzy', by David Fox, pp. 29, 30, 31, 32 & 33

business increased at an average annual rate of nearly 21 per cent between 1994 and 1996, and the government annual survey of international companies, currently underway, will show a similar pattern of expansion for 1997. International companies added 247 jobs in 1997, a 10 per cent increase over 1996, which saw 157 people added to their payrolls…"The real good news in these figures is that Bermudians are progressively moving into higher-paid positions in the international companies," says Gibbons. "In 1995 28 per cent of Bermudians in international companies were working as either managers, accountants or book-keepers, but in 1996 39 per cent of Bermudians working for international companies were in these higher-skill, higher-paid categories."

'...Bermuda's balance of payments position is extremely strong, with the current account surplus reaching US $174 million in 1997. There has been a strong and consistent build-up in the current account surplus over the past five years—1993, US $21 million; 1994, US $45 million; 1995, US $96 million; 1996 US $135 million; 1997, US $174 million. The surplus is growing primarily due to the international business sector's increasing amount of foreign exchange earnings, which pumped an additional US $239.3 million of expenditures into the economy in 1996 compared to 1993.'[731]

The 'Millennium Bug'

The global insurance industry also began to undergo major retrenchment in advance of the year 2000, as the new buzzwords in the insurance industry became 'the Millennium Bug' or 'Y2K'. Every risk manager and underwriter began checking and rechecking to make sure the proper procedures were put into place for all computer systems against the moment when the date of the year would change from 1999 to 2000. The major concerns centred on the potential of losses arising out of the failure of electronic equipment to correctly read and process the change. The petroleum industry was said to have spent the most, with some individual companies spending in excess of US $2 billion to ensure their computer systems were Y2K compliant.

Clients began to spend hundreds of millions of dollars to make sure their systems were upgraded to handle the change. Underwriters were using a benchmark minimum of US $200 million as an appropriate capital expenditure for the correction of a client's software. Software companies made millions writing programmes to eliminate the Y2K 'threat'. There was talk of Armageddon. Only the turn of the fateful year would tell if this had been hysterical hyperbole—but no one wanted to take a chance on finding out it was not.

Globally, these closing years of the century seemed in many ways to be a time of farewells—especially to familiar faces and to age-old assumptions. It was also a time of onrushing new developments. 1997 would be remembered as the year when it was suddenly obvious to all just how interdependent global economies had become. It was the year when the 'East Asian Tiger' economies collapsed. Stock markets plunged across the globe. If there was ever truth in the saying that the 'market is driven by greed on the one hand and fear on the other' this was a time when that would be put to the test.

[731] *Bermuda Market Digest*, August 1998, Vol. 2, No.8, 'Booming Bermuda doubles growth forecast', p. 11