PART SIX
2000–2001

CHAPTER 49

2000
The End of the Millenium Brings the End of the Soft Market

An end of the soft market

Either the doomsday predictions surrounding the advent of the year 2000 had been overdrawn, or sufficient precautions against disaster had been taken beforehand. Either way, life continued as before. The Great Anxiety was soon forgotten. Yet the fear had not been wholly irrational. It expressed a concern that our support systems were becoming so elaborated and so powerful as to make us subservient to our own technology. Unless we could maintain control over what we ourselves had created, then some day, somewhere, somehow, the Crash might come.

Meanwhile there was a general sense of relief—and no industry was more relieved than insurance. Not even the likes of ACE or XL or Lloyd's could insure against the end of the world. After a substantial rise during the '90s in the scale and number of catastrophes, the industry was in no shape to face an apocalypse. Instead, with the critical moment gone and the year 2000 safely begun, the global insurance industry prepared for rates to harden at last after more than ten years of very low premiums. In light of the recent increase in catastrophes, coupled with low investment income, many believed that for the global industry to survive it must now increase premiums. According to Standard & Poor's analysis—

> '...During the January 1, 2000 renewal season, both the Bermuda insurance and reinsurance markets indicated that prices had stopped falling in most areas, and that in some lines there was marked improvement. Furthermore the decline of the Australian reinsurance and retrocessional markets, coupled with a capacity withdrawal from certain business lines and the large losses incurred from European windstorms Lothar and Martin in late December 1999, should cause pressure for rate improvement throughout 2000.'[823]

The profile of Bermuda's international insurance industry had changed significantly. It now accounted for some 18 per cent of Lloyd's underwriting capacity, in its role as corporate capital provider, while as principal backer of managing agencies it controlled 24 per cent of Lloyd's total capacity.[824] Bermudian insurers were in the forefront of capital provision to Lloyd's. The purpose of such a push by Bermudian insurers was to secure a ready international platform. In addition, it gave the basically monoline catastrophe reinsurers the ability to diversify and provided more distribution points for excess liability carriers.

In a speech to ICAP on 21 June 2001 Brian Duperreault, President, CEO and Chairman of ACE, highlighted the changes prevalent in the global marketplace as a result of the restrictions in the reinsurance industry —

[823] *Bermudian Business*, Summer 2000, Sixth Annual Deloitte & Touche Survey 2000, with analysis by Standard & Poor's, 'Bermuda Reconfiguration Under Pressure'

[824] *AXCO, Market Insight Report*, November 2000, Lloyd's operations', p. 36

'Bermuda companies now account for 81 per cent of the US $21 billion in outstanding market value of the remaining independent publicly traded reinsurance companies. Ten years ago, Bermuda only accounted for 20 per cent of the market value of publicly traded companies. The top four worldwide reinsurers accounted for 57 per cent of the industry reflecting a high degree of concentration. Reinsurers declined from 65 to 33 indicating that the global insurance marketplace was in for a huge shift in the way it operated.'

OIL's corporate history provided the following synopsis of the state of the industry—

'Continuing the trend that emerged in the late 1990s, the commercial insurance industry was witnessing further turmoil and retrenchment. Published reports suggested that the commercial insurance community had been, in general, underwriting energy risks at below loss costs. Results were said to be dire for just about every class of business underwritten. Insurers were being forced to reengineer their entire books of business, cutting out unprofitable lines and returning to rating for an underwriting profit. Cheap and plentiful reinsurance was claimed to be a thing of the past. Even policyholders with good results were facing large increases in premiums and, in many cases, restrictions in overage at renewal, Finally, the ability of capital to flow freely into and out of the insurance sector coupled with investor demands for superior, near-term financial performance were making it increasingly difficult for the commercial market to structure long-term solutions to policyholders current insurance requirements.'[825]

As if the underwriting results were not bad enough for the global insurance industry, on 25 February 2000 nervous investors caused stocks to take a plunge, signalling the beginning of the end of the Technology boom and therewith the end of the bull market, which had lasted much longer than anyone could have anticipated. This stock market devaluation added to the woes of the insurance world.

Not only were changes abundant in the Bermuda insurance industry, the whole of Bermuda seemed to be undergoing another year of upheaval. Examples abounded—

· *The Royal Gazette* described 2000 as 'a year of fireworks', because of the many fires that broke out.

· January was a record-breaking month for cold weather and the Department of Tourism dropped its '68 degree temperature guarantee'.

· The Works Ministry brought in Peugeots 406, larger cars than the average on the island, which sparked another controversy.

· A UK report recommended that the Civil Service be cut and undergo significant changes in the way it was run.

· Illegal Pyramid schemes were found to be rampant on the island.

· More police were to be assigned from overseas

· Chilean dictator General Pinochet was trying to land in Bermuda on his way back from London to Chile.

· January also brought rumours of new work permit rules, which led to the shock announcement by STW Fixed Income Management (an exempted company on the island) that it would relocate its headquarters back to the US, with several Bermudians losing their jobs as a result.

· Over 700 people signed a petition to stop begging in the city of Hamilton. Many argued that this had become more prevalent because the cost of living was rising so much that the average Bermudian now found it hard to make ends meet on his own.

The regulations of the Commission for Unity and Racial Equality (CURE) continued to cause uproar throughout the year as many thought them to be unconstitutional. Though the CURE regulations caused much angst on the island and were not as inclusive of minorities as was hoped, they were unanimously passed by the Senate.

[825] *OIL Corporate History* – Addendum #1, 1996-2000 'Into the New Millennium'

Government issued a Green Paper on long-term residency, a topic that had been avoided in the past and one that sparked major debates across the island. Meanwhile a survey conducted by Total Marketing and Communications did show that 86 per cent of Bermudians believed expatriates made a positive contribution to the island's economy.

The Base Lands abandoned by the US Government again made headlines when UK pollution experts found that the American military had been accustomed to pumping raw sewage into an underground cave in Southampton. This gave added credence to the widespread concern that the pollution problem which Bermuda had inherited would keep out any investors otherwise hoping to redevelop the site as a tourist attraction. Another item of Southampton news that made headlines in 2000 was the protest by Southampton residents over the erection of a cellular tower in close proximity to their residential area.

The state of the marketplace after the 1999 results

On the international insurance scene, the first big news for 2000 came when in January former XL executive Robert Cooney launched Max Re Ltd., a subsidiary of Maximus Capital Holdings. Cooney says he left XL because it had grown into a large company and he was looking for something smaller that he could develop. He also had the idea of forming a company that would focus as much on investment as it did on the underwriting side of the business. The idea had come to him in mid-1994, when stocks went up dramatically while bonds correspondingly fell. The traditional assumption had always been that though stocks might be volatile, bonds were virtually free from risk. Instead, as he watched XL suffer a huge drop in its income, Cooney realised that an effective investment strategy was just as vitally important to an insurance company as was its underwriting strategy. At once he saw an opportunity waiting to be grasped but it was not until some six years later that he could formalise his concept.

Cooney stated that Max Re would pursue a fairly cautious underwriting strategy combined with a more diversified approach to investment—a strategy that he says is unique to the reinsurance industry. Max Re's underwriting strategy was to be based on a structured risk basis, combining finite and traditional underwriting techniques. It was set up to specialise in the structured underwriting of long-tail liability risks with lengthy duration and relatively greater predictability of claim payout patterns, such as annuities, structured settlements, life insurance, disability income, workers' compensation and medical malpractice insurance. This lower volatility in its underwriting strategy would enable the company to support its liabilities through a strategically diversified investment portfolio, that could seek higher risk adjusted returns by allocating between 30 and 50 per cent of its assets in a diversified fund of funds, containing alternative investments, including market neutral hedge funds.

So well received was the newcomer that very soon after its inception Max Re was named 'launch of the year' by *Review* magazine, principally in view of its innovative business plan, its opening of offices in Dublin and London and its success in writing US $300 million in premiums during its first six months of operations.

However not all was good on the Bermuda front. The industry breathed a sigh of relief that none had gone into runoff after the catastrophic 1999 until Terra Nova became Bermuda's first casualty of the year 2000 when it announced it was going into runoff after suffering a net loss of US $81.2 million, this from a combination of the devastating results of the fourth quarter of 1999 and the expenses associated with its restructuring plans.

Closely following Terra Nova's news came that of Trenwick and LaSalle Re merging in order to survive the terrible state of the reinsurance marketplace. Then, in what appeared to be the closing of an era in Bermuda, came the announcement that Odyssey Re was planning to close its Bermuda office. Odyssey Re was once the mighty Sphere Drake operation. For many, Odyssey Re's announcement to close its reinsurance arm came as no surprise because it had been drawn into litigation one year before as a result of the failure of the large US workers' compensation reinsurance pool, Unicover, which contributed significantly to the unravelling of the workers compensation reinsurance marketplace.

Soon the bad news was offset by news of great opportunity when XL Capital announced that it was forming Element Re, to provide weather-risk management insurance, reinsurance and financial products. Element Re's mission statement was to provide its customers with a range of non-catastrophic weather-risk mitigation products, designed to protect against the negative impact that normal weather fluctuation can have on the financial performance of companies operating in a variety of industries.

Then a new wave of reinsurance came to the island. Professing to be the third generation of reinsurance, Imagine Re formed in Bermuda in October 2000. The parent company, Trilon Financial Corporation, owns 90 per cent of the company's stock while the Imagine's management owns the rest. Imagine is a second-generation finite risk reinsurance enterprise, whose goal is to become the leading provider of structured insurance and reinsurance capital to the global marketplace. It was run by Brad Huntington and Tom Gleeson. Says Huntington—

> 'You can actually say that we are a third generation reinsurer, casting Stockton Re and Max Re as the second generation. As the next generation, we have taken what we liked from some of those ideas, but decided that alternative asset strategies did not fit our model with respect to our insurance reserves.' Gleeson adds, 'What differentiates us from other entrants into the market in the past few years is that we are not a hedge fund seeking to be a reinsurer, but a manager of financial assets.'[826]

Despite the furore about Bermuda companies buying United States companies, Overseas Partners Limited (OPL) announced that it was buying Reliance Reinsurance (Reliance Re), including the staff, without any past liabilities attached to the deal. When deciding on the purchase OPL looked at the acquisition as a way to recover the significant premiums it used to receive from the shippers risk policy, which was transferred out of Bermuda after the controversial UPS court case in the United States. The acquisition also served as a springboard for catapulting OPL's position in the United States. Reliance Re is a licensed carrier in 50 States of the US.

OPL's newly appointed President and CEO, Mary Hennessey said of the transaction—

> 'OPL has always been well positioned to create value for our shareowners, given our large capital base, A+(superior) rating from AM Best, Bermuda domicile, and existing profile in the reinsurance market. However, we required additional technical industry expertise in order to further differentiate ourselves in the market. We believe that our acquisition of Reliance Re and its team of reinsurance professionals, together with an infusion of capital, will establish OPL as a significant player in the United States reinsurance market.'[827]

Furthering its bid to diversify, on 17 November 2000, OPL announced that it was acquiring the finite risk team of professionals from Stockton Re. This team, led by Jed Rhoads, was to combine with OPL's existing finite risk underwriters to form OP Finite. In a statement released to the press, OPL said, the acquisition allows OPL to continue its growth strategy, which emphasises a focus on specialised areas of reinsurance where the combination of its Bermuda domicile, strong capital base, and world-class talent will provide a significant competitive advantage.

The life insurance industry in Bermuda also began to diversify when Scottish Annuity & Life Holdings (SALH) announced it was joining forces with Crown World Services of Bermuda, a designer and marketer of variable life insurance products for the high net worth market, to form Scottish Crown (Bermuda) Group. According to the *Bermuda Market Digest*—

[826] *Bermudian Business*, Summer 2001, 'ImaginAre', by Roger Crombie, pp. 101 & 103

[827] *Bermuda Market Digest*, August 2000, Vol.4, 'OPL buys Reliance', pp. 1 & 12

'Scottish Crown will be one of the largest global issuers of offshore variable insurance policies to high net worth world citizens,' said Michael C. French, Chairman and CEO of SAL. 'Combining our underwriting, policy administration and estate planning expertise with Crown's extensive distribution network and product design will produce the premier variable insurance products demanded by the high net worth market.'[828]

Cases settled and suits brought

With all the changes occurring in the Bermuda insurance industry, everyone was relieved to hear that the highly controversial Bermuda Fire and Marine case had been settled. The Directors and Management of BF&M Limited announced that a commercial out-of-court settlement, with no admission of wrongdoing, had been reached between the Liquidators and Creditors of Bermuda Fire and Marine and the defendants, BF&M Limited and several of its subsidiaries, certain shareholders of BF&M Limited, five former directors of Bermuda Fire and Marine, Conyers Dill & Pearman and Coopers & Lines.

The excitement was soon replaced with worry when American International Group (AIG) filed suit against INA, alleging that INA had wrongfully left many policyholders uninsured when it moved its past liabilities, the result of asbestos and pollution claims, into a holding company called Brandywine. AIG was not seeking damages as it was not to be affected by this transfer under California law, but was looking for INA to issue a statement acknowledging ongoing liabilities to policyholders. This caused great alarm within ACE, which had recently purchased the CIGNA Group, ultimate parent of INA, but stated that they knew nothing about the transfer.

US redomestications to Bermuda spark controversy

Bermuda was pulled into yet another scandal when news of company redomestications to the island began to make headlines. Some insurers and reinsurers in the United States say it was the Bermuda players that changed the rules of the global insurance network when they began encroaching on their backyards by acquiring US entities. Some believe that when the large Bermuda based insurers ACE and XL Capital acquired entities in the United States, they created an uneven playing field because, being headquartered in Bermuda, they had the best of both worlds. These US insurers maintained that by acquiring US insurance companies ACE and XL were not only able to gain access to the vast US insurance marketplace; they also had the benefit of operating in an environment (Bermuda) that was less restrictive than the US. Supposing themselves to be at a disadvantage in relation to ACE and XL, some US insurer decided the only way to compete with the Bermuda market was to join it. For that reasons the latest wave of company redomestications to Bermuda began.

One of the major benefits for moving to Bermuda included the ability to offer financial risk products that were not available in the United States. In citing the prime reason for moving to Bermuda, Everest Re said, 'Compared to US state regulatory environments, Bermuda offers insurance companies more flexibility to price their products, develop new products, write additional lines of reinsurance.'

There was further incentive for companies to redomesticate to places like Bermuda when the Glass Steagal Act had been repealed in the US, because it effectively opened the door to the desegregation of the financial services industry. Robert Hartwig, VP and chief economist of the New York based Insurance Information Institute explained the problems for US based companies and why they sought Bermuda as follows—

'In the US, the taxation of captives and alternative forms of risk transfer are bewilderingly complex. There are few people in this country who thoroughly understand it. As the risk-transfer market continues to

[828] *Bermuda Market Digest*, July 2000, Vol 4, 'Bermuda group to market life products', pp.1 & 12

develop, Bermuda can be viewed as a greenhouse for that sort of activity. It attracts the type of talent and companies that want to be involved on the cutting edge of insurance, and the regulatory tax structures make that easy.'[829]

Therefore, it was not the tax benefits alone that attracted companies to Bermuda. As a matter of fact, when Bermuda business people market the benefits of Bermuda to outsiders, they advise companies not to come to Bermuda if they are only interested in tax savings but that if they are interested in finding ways to operate more effectively and efficiently in the global marketplace then Bermuda is the place they need.

According to Jonathan Reiss, partner and senior manager of the insurance group at Ernst & Young's Bermuda office, 'the island appears to have perfected the fine balance between necessary regulation and ease of doing business. The US, on the other hand, is deemed to be overly burdensome with extensive reporting requirements, risk-based capital hurdles and investment restrictions, to name but a few.'[830]

Close the Bermuda loophole

As a result of the extensive coverage Bermuda received, including stories written by *The New York Times*, about several high profile insurance companies choosing to redomesticate to Bermuda and ACE and XL expanding into the United States, four United States insurers and politicians decided to take advantage of the hype and began to make waves about these companies.

Chubb Corp., Hartford Financial Services Group Inc., Kemper and Liberty Mutual were the four United States insurers who took it upon themselves to wage war on Bermuda by going before US Congress to argue that several United States companies were exploiting a loophole in federal tax law. They argued that certain companies, simply by moving their corporate headquarters to Bermuda, or by being acquired by a Bermudian insurer, could save on the 35 per cent US income tax rate and on state rates as high as 5 per cent.

The four companies argued that by remaining in the United States they were being placed at an unfair disadvantage to the Bermuda companies. Ron Panko of *Best Week* reported on the defence statements issued by ACE and XL about the company redomestications controversy as follows—

'...Paul Giordano, general counsel for XL Capital Ltd., said efforts by a few U.S. insurers to subject their competitors to new taxes is "simple protectionism. Longstanding U.S. transfer pricing rules are fair in that U.S. insurers are taxed the same on identical transactions without regard to U.S. or foreign ownership because the transactions have the same effect on the U.S. insurers' tax base," he said in a written response to inquiries. "Under the proposal, a U.S. insurer with a Bermuda parent would be forced to pay higher taxes on reinsurance transactions than their U.S.-owned competitors, even though the transactions had identical terms and identical U.S. tax consequences."

'In addition, the US insurers' proposal seeks to tax income earned by a non-US company outside the United States. "This approach to taxation is contrary to longstanding principles of international tax law and may legitimise similar action against US companies from countries with higher corporate income tax rates than the US," he said. "The principles behind this proposal should be alarming to all non-US based companies with US operations regardless of industry."

'"It's something consumers in the United States should be concerned about, too," Mear (Peter Mear, General Counsel for Bermuda based Ace Ltd.) said. "They benefit from the Bermuda-type business, the fact that pharmaceuticals and oil companies can get insurance at a price they can afford...."'[831]

[829] *Reactions*, February 2000, 'One way trip to paradise island', by Wyn Jenkins, pp. 24-27

[830] ibid.

[831] *Best Week*, Property/casualty Insurance, News and Trends, 13 March 2000, 'Insurers begin to take sides in offshore taxation battle', by Ron Panko, pp. 1 & 3

H.R. 4192

With the arguments put forth by Chubb Corp., Hartford Financial Services Group Inc., Kemper and Liberty Mutual, a bill H.R. 4192 was drawn up. The bill put forth by Reps Nancy Johnson, (R-Conn.), and Richard Neal, (D-Mass) proposed that any United States company that was based in Bermuda should pay additional taxes.

Reps Johnson and Neal felt this bill was necessary to close what they perceived as a tax loophole for United States insurance companies with affiliates in Bermuda. But to those outside the political circle and more involved with globalisation, this bill was too far reaching and could impact not just those in the insurance industry but companies across the spectrum.

Best Week Review reported on the implications of this bill as follows—

> '...By moving their headquarters to Bermuda, or by being acquired by a Bermuda insurer, the companies can escape a 35% US income tax rate and state rates as high as 5%. But the bill's intended impact would affect more than the insurance industry, people in and out of the industry said.
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> 'In a letter to Rep. Bill Archer, R-Texas, Chairman of the House Ways and Means Committee, the Organization for International Investment's executive director, Todd Malan, said, his "members are concerned that this bill sets dangerous policy precedents and violates important international tax policy principles followed by the United States."
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> 'Archer oversees tax issues before the House, including H.R. 4192, which is opposed by Bermuda-based insurers such as ACE Ltd. and XL Capital Ltd.
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> 'The organization, based in Washington, describes itself as the exclusive representative of the largest US subsidiaries of companies based abroad. Part of its mission is to maintain an open environment for international companies in the United States. Its membership includes insurance companies, but they are a minority. Thus, "our concerns are based on considerations much broader than the targeted objectives of the bill regarding the insurance industry," Malan wrote Archer.
>
> 'What Malan doesn't like about the bill is that it "seeks to use the US tax code to address a perceived "unfair competitive advantage" of firms operating in another country."
>
> 'He said that, "as the largest source of foreign direct investment to the rest of the world, the United States should be very careful in the use of tax code to intervene in global competition."'[832]

ACE Chairman, Brian Duperreault was very vocal in his objection to H.R. 4192. *Best Week* reported as follows—

> '..."In a massive and misleading public-relations blitz, they (Chubb Corp., Hartford Financial Services Group Inc., Kemper and Liberty Mutual, Reps Nancy Johnson, R- Conn, and Richard Neal, D-Mass) have lobbied the US Congress to pass a bill attacking the Bermuda insurance market, which is one of the most important suppliers of certain specialty lines of business," Duperreault said in his address to the international council. "They have created a fanciful and utterly ridiculous scenario pursuant to which every US insurance company redomesticates to Bermuda, and according to their misinformation, the US treasury loses US $7 billion in revenue."
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> 'Many US companies have themselves taken advantage of a tax shelter on invested assets provided by municipal bonds and corporate dividends, which aren't available to non-US insurers, said Duperreault, who is also the President and CEO of ACE. Because of this, they had an approximately 19% corporate tax rate, as opposed to the 35% corporate rate paid by most US industrial companies, he added. In addition, rather than the US $7 billion those pushing for the legislation estimate is paid in property/casualty tax revenue, Duperreault said the actual amount is closer to US $5 billion. "Still worse," Duperreault said, "many of the companies accrued taxes on a GAAP basis, but didn't really hand over the money to the US Treasury. In fact, one of the loudest complainers and hardest campaigners for tax equity was actually

[832] ibid. 1 May 2000, 'Bermuda Tax Issue Grows Hotter', by Len Famiglietti, p.16

seeking a refund on a current basis and accruing its taxes on a deferred basis. You know, it's hard for the US government to pay salaries out of 'deferred taxes'."'[833]

The *Bermuda Market Digest* reported that in a further statement, ACE said—

'The Johnson/Neal legislation is pork barrel politics at its worst. It would favour a few Northeastern US insurance companies, but jeopardise the ability of the industry to meet the capacity needs of the domestic market, particularly with respect to coverage for hurricanes, floods and other natural disasters.

'The legislation unfairly singles out Bermuda-based companies which have played a critical role in providing needed capacity for the US market. More outrageous is that this blatant singling out of Bermuda insurers is veiled as a tax equity issue, despite the fact that many countries offer lower effective tax rates on insurers than the United States.

'Further, at a time when the United States is rightly trying to open the insurance markets of China and Japan for US insurers, the Johnson/Neal bill can only be seen as a protectionist measure and a contradictory message to allies and competitors abroad.

'Finally, the sponsors' contention that this alleged problem could cost US $7 billion in lost revenue is not true. Treasury spokesperson Steve Posner said on March 8 that the US $7 billion is not a Treasury estimate. As of this time, there is no Treasury estimate regarding any revenue loss.

'ACE strongly opposes the Johnson/Neal bill and urges Congress to strongly consider tax, trade and capacity issues that would be negatively impacted by passage of this bill.'[834]

Every US company with affiliates in Bermuda and Bermuda based insurers were relieved when HR 4192 failed to progress legislatively. Each moved into 2000 watching to see if the policy would be reintroduced through another bill.

Arch Capital redomesticated to Bermuda

In a rather bold move, Arch Capital became the first company to redomesticate to Bermuda since the attempts in Washington to put an end to company redomestications. Bob Clements, the company chairman, later stated that the reason for redomestication was not primarily for tax reasons. He held that the relevance of Bermuda to the insurance industry is much different from that of companies engaged in manufacturing because Bermuda is a wonderful place in which to own and operate an insurance company and do business, owing to its user-friendly regulatory environment and, most importantly, the very significant role Bermuda plays as a marketplace for insurance placements all over the world. He said from a business perspective it did not make sense for his company to remain headquartered in the United States because its development would have been retarded by the bureaucratic nature of the United States regulatory environment.[835]

Tokio Millennium Re (TMR) forms in Bermuda

Despite US hostility towards the Bermuda marketplace, the Japanese recognised the benefits it offered when Tokio Millennium Re (TMR) became the first Japanese reinsurer to set up operations in Bermuda. TMR's parent, Tokio Marine and Fire Insurance Company Ltd., a domestic Japanese company, with 95 per cent of its income from within Japan, was the largest Japanese non-life insurance company, having net assets of around US $20 billion. Because Japan suffers many large natural catastrophes, such as typhoons, earthquakes and tidal waves, the domestic insurance industry cannot escape from exposures that counter against a fundamental principle of reinsurance, in that

[833] *Best Week*, Property/Casualty Insurance News and Trends, 15 May 2000, ' ACE Chairman blasts offshore-taxation bill', by Caroline Saucer, pp. 1 & 2

[834] *Bermuda Market Digest*, May 2000, Vol.4, 'US insurers cry foul over inability to compete', pp. 1, 15 & 16

[835] Interviews with Robert Clements, 10 December 2002 and 16 April 2003

native insurers and reinsurers are unable to sufficiently spread their risks around domestically.

The decision to form a company in Bermuda was as a result of the need to diversify the geographical spread of Tokio Marine's portfolio. Tokio Marine chose Bermuda as the domicile for TMR because, according to Shin-ichiro Okada, President & CEO of Tokio Millennium Re Ltd, it was by the year 2000 the centre of the cat market. The principal goal behind TMR was to assume non-Japanese natural catastrophe risks, the company decided that in order to generate such business, Bermuda was the best place in which to incorporate. They wanted to use the network established in Bermuda to promote catastrophe reinsurance exchanges with the world's major insurers and reinsurers.

Okada said that before the mid-1980s, Bermuda was considered a domicile for captives and paper companies. After the formation and growth of ACE and XL, and the property catastrophe reinsurance companies established after Hurricane Andrew, Bermuda came to be considered a true reinsurance market. Okada says Bermuda also provided great ground for new companies to do business because of the length of time it takes in other jurisdictions to get a company up and running. Okada also says his company thinks Bermuda's regulatory environment fosters good business.

Bermuda was still unknown in Japan and Okada recalls educating the authorities, as they did not even have a clear idea of Bermuda's location when Tokio Marine sought permission to form a company outside Japan. Tokio Millennium's performance was soon the subject of close study by all other insurance companies in Japan, to see if investment in Bermuda was a wise move.

Okada says his company is happy with their decision to move to Bermuda because their past results have been favourable. In its first nine months of operation, Tokio Millennium showed profits of US $7 million and in its second year of operations profits increased to US $15 million. Although Tokio Millennium keeps a low profile on the island, it provides significant capacity to the reinsurance industry, focusing on top layer of excess of loss contracts covering natural catastrophes. The purpose of TMR's establishment was to 'utilize reinsurance as a tool to make effective use of capital' for the Tokio Marine Group. Furthermore Okada believes that the capacity which TMR provides for natural catastrophes, will eventually benefit consumers around the world.[836]

OECD removes Bermuda from tax haven list

Just after the good news of TMR setting up on the island, the business community had more reason to cheer when the OECD removed Bermuda from its list of tax havens. Along with five other domiciles Bermuda was removed from the list when it agreed to comply with OECD conditions for five years and not to introduce any new legislation that OECD had not first approved.

Some say that Bermuda's agreement with the US, by signing the US/Bermuda Tax Convention in the late 1980s, to an ongoing exchange of information about money laundering, led the OECD to recognise that Bermuda was a much more credible jurisdiction than it had previously believed. Roger Crombie of *Bermudian Business* wrote the following about the OECD's decision to remove Bermuda from its black list—

> 'The decision marks a turning point in the struggle against a series of assaults on the Island's ability to operate as an offshore centre, because the stamp of approval from the OECD says Bermuda is OK, it will be difficult for the European Union, the International Monetary Fund, the G7, the UN or any other group to say that Bermuda is not.'[837]

In a speech to the Bermuda International Business Association (BIBA), Marcus Killick, a United Kingdom advisor, acknowledged that 2000 was a challenging year for offshore jurisdictions. He cited the number of reports, including those by the Financial Stability Forum, Financial

[836] Interview with Mr Shin-ichiro Okada, 4 December 2002

[837] *Bermudian Business*, Fall 2000, 'Is that your final answer', by Roger Crombie, pp. 62-64

Action Task Force and the OECD, that were thought by many to signal the end of offshore jurisdictions, as we had known them. However in his opinion these reports 'are merely evidence that the offshore world is changing, and change itself is nothing new to offshore. Indeed it is upon change that the offshore world flourishes and grows.' He added that he thought Bermuda well suited to meet global changes. 'For the areas that change most threatens are the areas that Bermuda has as its strengths and so is able to deal with those threats'. He gave as example that much of the concern about offshore jurisdictions was prompted by secrecy and a lack of co-operation—

> 'Banking secrecy laws have, whether rightly or wrongly, been the subject of significant criticism and the jurisdictions, which have such laws have suffered (in reputation) as a result. Bermuda has no such specific laws. Bermuda has never relied upon a veil of secrecy to encourage businesses to locate here. Legitimate confidentiality, yes, that is important for both personal, security and commercial reasons. Bermuda provides that, much in the same way as every legitimate centre does, or should provide it. But secrecy as manifested in a failure to cooperate in respect of legitimate criminal and regulatory enquiries, was never a policy followed by Bermuda. This provides a considerable defence to external bodies…'

Killick concluded his talk by saying that he did not believe that there was any world conspiracy against offshore jurisdictions. Instead he thought they were the scapegoats of convenience…

> 'Offshore centres now appear to be asked to apply higher standards than many of their onshore counterparts. Many of the crimes that are in fact committed onshore are having the blame laid at the door of offshore. Clearly this is unfair…. It is always easier to blame someone in a faraway land with little political or economic clout than to accept the fault of oneself and some large jurisdictions are not immune to such thorough processes….'[838]

Segregated Companies Act 2000

In August the Bermuda Legislature passed the Segregated Companies Act with effect from the first of November. Its enactment suggested Bermuda was looking to capture the next generation of insurance. The passage of the Act had been a long time in coming because so many factors had to be taken into account. Those responsible for regulations in Bermuda wanted to make sure that the Act was broader than the ones passed in the Caymans, Guernsey and the United States. The slow passage of the Act was due to the determination of those drafting it to ensure that its provisions extended beyond insurance to include non-insurance uses such as mutual funds for umbrella classes of shares, securitisation, transformer companies, catastrophe bonds, annuity and life and e-commerce.

According to the *Bermuda Insurance Update*—

> 'The purpose of the Segregated Act 2000 is to move Bermuda past Guernsey and the Cayman Islands, where such legislation exists but is restricted in terms of its use, and past the United States, where the NAIC has prepared a draft of the model legislation to permit limited use of such accounts for insurance transactions.
>
> 'The Act provides for any Bermuda company to operate segregated accounts enjoying statutory divisions between accounts. The effect of such statutory division is to protect the assets of one account from the liabilities of other accounts within the same company. Thus, the accounts will be self-dependent, with the result that only the assets of a particular account may be applied to the liabilities of that account. Previously, such a legal effect has only been obtained by private act of Parliament.
>
> Although the concept of Segregated Accounts has been used in Bermuda since 1991, there were no hard and fast rules about how they should be regulated. This Act now establishes a system of registration so that segregated accompanies may be created speedily and with the flexibility necessary to respond to the needs of international business.

[838] *Bermuda Insurance Update*, 12 December 2000, 'UK advisor reveals strong support for Bermuda'

'Many were excited about the passage of the Segregated Companies Accounts Act because they felt it would substantially reduce the time and cost of achieving legal segregation of assets and will therefore clear the way for more securitisation and derivatives deals for insurers, who balked in the past about the cost of a single transaction.

'Michael Burns, Insurance Partner with lawyers Appleby Spurling & Kempe said, "the bill expressly reflects appropriate regulatory safeguards designed to protect Bermuda's reputation as a jurisdiction of high standards and integrity."'[839]

KPMG report on Bermuda

Soon after it had overcome the OECD threat, Bermuda was once again under a spotlight. Back in March 1999 the British Government had published a White Paper entitled 'Partnership for Progress and Prosperity: Britain and the Overseas Territories'. This was supposed to set the tone for ongoing relationships between the United Kingdom and its remaining overseas territories, including Bermuda, the Cayman Islands and the British Virgin Islands. It was widely believed that the report was driven by a desire on the part of Westminster to extend full citizenship to the 190,000 inhabitants of the remaining British overseas territories. However the quid pro quo for this was that the laws of the territories were to be brought into line with so called international standards. One area of review was the regulation of financial services. Ultimately KPMG, a professional services company specialising in audit and consulting services, was selected as the firm to review the financial regulation of these territories.

In their final analysis KPMG stated that Bermuda's financial regulatory systems generally met international standards and were in line with good practice but they thought that the insurance sector could be somewhat improved. The report recommended as follows—

'1.4.2 Regulatory authority

'...Whilst the regulation of insurance also appears to be operated in a generally prudent manner, we do not consider the current structure to be in line with good practice. This is because the current position by which the Registrar is part of the Ministry of Finance means that the regulator is not operationally independent.

'We therefore recommend that the section responsible in the Companies Registry for insurance should become an independent regulatory body and that the current powers exercised by the Minister of Finance are transferred to that new body.

'1.4.4 Insurance

'Whilst Bermuda has an acceptable legislative basis for the regulation of insurance companies, there are a number of areas that should be addressed. The most important of these is in respect of the current reliance by the regulator on third parties such as auditors.

'Whilst such reliance is permitted under international standards, we consider that third parties should be subject to specific guidance and verification. In our opinion, this should involve at least some element of on-site inspection by the regulator. We do not consider that this is currently occurring to the extent necessary.'[840]

The Bermuda government responded to the report on 15 January 2001 with a plan to implement a majority of the changes recommended by the report—

'...The Report contains more than 80 recommendations of varying weight and consequence.

[839] *Bermuda Insurance Update*, Summer 2000, 'SAC legislation to set a new standard', p.1 ff.

[840] *KPMG report, Review of Financial Regulation in the Caribbean Overseas Territories and Bermuda*, 1.4.2 Regulatory authority p. 2 and 1.4.4, Insurance, p. 3

Government has undertaken a preliminary assessment of the recommendations against the following criteria: whether the recommendation was based on an international standard or not; the legislative implication; the market impact; the resource requirement for implementation; and whether or not the recommendation added value to Bermuda's regulatory regime. In addition, Government invited and has received written comment on the Report from leaders of financial institutions and organizations of Bermuda's financial services sector. Generally, the Report was positively received by the industry.'[841]

The Government stated that it was already working on many changes to the supervisory statutes and practices identified in the Report. It also agreed with the core recommendations related to improved regulation, independence of the regulator, better international co-operation through enhanced exchange of information between regulators, and extending the provisions against money-laundering to cover the proceeds of all serious crime, and committed to having all amended by September 2001. However Government reserved its right to examine the recommendations made for insurance regulation, corporate governance and licensing of corporate service providers due to the lack of international standards.

Despite the scrutiny Bermuda finds itself under from various regulatory bodies around the world, Bermuda re-confirmed its advanced regulatory and tax framework and took important steps to further enhance the regulations. As a matter of fact, Olga Kalinina, Sovereign ratings at Standard & Poor's, feels it's Bermuda's proactive stance and promptness in addressing these calls that differentiates the sovereign from some other islands. Bermuda has always been very open with what goes on there and that is a feather in its cap.[842]

Millennium comes to an end as does the soft market

By the end of the millennium, many insurers and reinsurers were relieved to see the beginnings of price increases across the board for the first time in over a decade. Many had suffered through a horrific hurricane season.

'...the highest level of North American hurricane activity ever measured was recorded from 1995 to 2000, according to the study conducted by scientists led by Stanley Goldenberg, a meteorologist at the United States National Oceanic and Atmospheric Administration (NOAA) Hurricane Research Division. Compared to the previous quarter century, there were twice as many hurricanes, including two and a half times more major hurricanes (those reaching Category 3 strength with sustained winds reaching more than 110 mph) and more than five times as many hurricanes impacting the Caribbean island.'[843]

Business Insurance reported—

'...2000 was the second year in a row that overall policyholder surplus and capacity declined after an unprecedented multi-year run-up. The regression in 2000 was steeper than in 1999—a signal that underwriters cannot ignore. But the fact remains that the overall commercial insurance market is still extremely over-capitalised. And the competitive landscape for risk management is filled with more alternatives than ever before. Despite unprecedented levels of income in the industry, net premiums up by 5%, net investment income trended upwards reversing a two year decline in 1998, insurers' pretax net income and ROE (Return on Equity) both declined significantly in 2000 because the growth rate of underwriting losses booked by insurers in 2000 outpaced the income growth. Despite the increased NPW (net premiums written) factor, underwriting losses in 2000 are expected to total 32.2 billion, an annual loss level second only to 36.1 billion underwriting loss posted in 1992.'[844]

[841] *Response by the Government of Bermuda to the Review of Financial Regulation in the Caribbean Overseas Territories and Bermuda* by the Ministry of Finance, January 2001

[842] Interview with Alan Levin, Karole Dill Barkley, Olga Kalinina, Standard & Poor's, 30 October 2002

[843] *Bermuda Market Digest*, August 2001, 'Hurricane patterns to change?', pp 1& 2

[844] *Business Insurance*, 13 November 2000, Bermuda Market, 'Exploring the Island's expertise from tip to tip, Charting Bermuda's History', p. 32, by Shirley Henry

Business Insurance also reported—

> 'As the new millennium arrived, risk managers found few if any bargains as they reviewed their property/casualty coverages. Indeed, the soft commercial property/casualty pricing environment had finally bottomed out, which was good news for insurers and brokers that have struggled under a soft market for nearly 15 years.
>
> '...Industry observers agreed that the modest and account-specific rate firming at the beginning of the year was, essentially, a market correction after years of intense price competition and over capacity. By mid year renewals, however, signs of a genuine turn became more evident as insurers reported that they were able to get rate increases—some modest, others substantial—essentially across the board.
>
> '...Buyers, in general have not vehemently resisted the increases. Some accounts particularly those with poor loss histories—and, thus, higher increases—were being shopped to other insurers, but many others remained with incumbent underwriters once the rationale behind rate increases had been adequately explained.
>
> 'Rate increases were even more pronounced in the reinsurance market in 2000. Cedents with losses on property catastrophe reinsurance programs were handed the largest hikes, but loss-free property programs and casualty accounts also saw increases...'[845]

Choppy waters but a steady course

Life for the Progressive Labour Party was far from being roses, hugs and kisses all the way. Premier Jennifer Smith found herself challenged by her own Environmental Minister, Arthur Hodgson, who announced that he would stand against her if his party members so desired. This lent some credence to rumours of divisions within the government. In the end the Premier prevailed and Hodgson was dismissed from Cabinet. Yet the problems rumbled on and the year ended with mixed results as the newly formed government found itself constantly in hot water over actions made and decisions taken, such as large cars for Ministers and lavish travel expenses charged by PLP Members of Parliament, or allegations that Government had misled the public about constitutional change, or the anger of St David's people because one fifth of Bermuda Housing Corporation's 100-home project was to be built on their island.

It also came to light that some 35 per cent of Bermudians were being educated privately. Since this did not include students overseas it could be that the true percentage overall of Bermudians attending private educational institutions was even higher than it seemed. Government acknowledged that the public school system was below standard but promised this would soon change.

The announcement by Finance Minster Eugene Cox that the Bermudian 60/40 rule would be relaxed caused quite a stir among traditional Bermudians. The Bank of Butterfield announced almost immediately thereafter that it would apply for exemption from the 60/40 rule so that it could secure a listing on an overseas stock exchange and the Bank of Bermuda was granted such an exemption.

Crime continued to cause anxiety. The year was marked by an increase in gang violence, prompting police and media to act as mediators in gang 'peace talks'. However not all the news in this respect was bad. Statistics showed that island crime overall had dropped by 28 per cent.

The case of Rebecca Middleton, the Canadian teenager raped and murdered in Bermuda, continued to cause misgivings. It was alleged that the prosecution had made a plea bargain with the first of two defendants prior to a review of critical forensic (DNA) evidence. It was argued accordingly that the plea bargain could have involved a miscarriage of justice. However it would appear that the trial judge saw himself as having in any case no option under the law other than to accept an agreement already made by the Crown. This left him no alternative but to dismiss the case

[845] ibid. 18 December 2000, Year in Review, 'The top risk management stories of 2000, —1, Firmer pricing', by Sally Roberts, p. 12

against the other defendant if his court was not to aggravate an already questionable situation. His ruling was challenged in appellate court but was eventually upheld by the Privy Council in London. The matter was then closed, as far as legal proceedings and judgements were concerned, but the whole history, from beginning to end, left a profound sense of distress, unease, and disillusion within the island.

In the rest of the world, the year 2000 started out with much promise, as many believed new technology would take them to new heights of wealth. Instead they found its allure had worn off. Faltering 'dot.com' companies dragged down the stock market. Microsoft was accused of monopolistic behaviour and was dragged through the US court system, thus ending the honeymoon period Bill Gates had enjoyed with the American public and most of the technological world. It was also in 2000 that the 'dark side of e-commerce' became evident when, as *Business Insurance* reported in mid-January, an extortionist posted on a Web site confidential credit card information pertaining to many customers of an online music store that had ignored the criminal's blackmail demands for US $100,000 of hush money.

A month later, risk managers became familiar with the denial-of-service risk, after several high-profile Web sites were bombarded with so much data that the sites could not function. In May, the Love Bug virus spread globally, crippling business e-mail systems and destroying some computer files. Published estimates placed losses from the virus as high as US $10 billion.... Anti-virus software maker Symantec Corp. reported that approximately 250 viruses had infected the computer systems of multiple organizations.[846] And those were only the highly publicised cases. There were rumoured to be many more that were kept hidden because companies feared just how terrified the general public would become if they knew the true extent of internet hacking.

The world looked upon the United States in wonderment, as their presidential election blossomed into local, whimsical jokes, then broadened into vulgar tragic-comic farce and ended as an appalling indictment of the American electoral system. After weeks of innumerable counts and recounts, charges and counter-charges, threats, innuendoes and uncertainties, it was left to the Supreme Court to decide that Mr George W. Bush was in law and in fact to be the next President of the United States. This seemed a dismal beginning to the first Presidency of the new millennium.

There were plenty of worrisome political, financial and social conditions in the global economy—

- hopes of an early resolution to the Middle East conflict were dashed as negotiations fell apart.
- European unity seemed to come to an impasse, with the various member countries unable to decide either on a currency, on voting rights, or on food safety, and feeling a sense of unease among themselves at the prospect of closer integration in general.
- the Hague summit in November brought forth no decisions on how to address climate changes, despite the floods in Africa, Asia and Europe.
- the global plague of AIDS showed no signs of abatement and no cure in sight.

Despite all these alarms and disquietudes abroad, the Bermuda international insurance industry ended the millennium on a sound note. By celebrating 30 years of operations OIL Insurance Limited proved wrong all those who had said it could never last. Its historical review noted the following—

> 'From meagre beginnings, the Company had grown into a strong and successful enterprise with truly global reach. At December 2000, there were 48 member companies with worldwide assets insured approaching US $1 trillion. In contrast, the 16 original founding shareholders had combined gross assets of only US $50 billion and they were some of the largest oil and gas companies of their day. OIL's capi-

[846] *Business Insurance*, 18 December 2000, Year in Review, 'The top risk management stories of 2000— 4,Internet perils', by Dave Lenckus, pp. 14 & 15

tal and surplus at year-end 2000 was just under US $2 billion, even after paying a US $200 million dividend in April of 2000. This was a far cry from the original founding capital of US $160,000. During the three year period, 1998-2000, (the Company) paid US $700 million in dividends to its shareholders, at a time when the petroleum industry needed additional earnings the most.'[847]

The Registrar of Companies reported the following astonishing results for the Bermuda international insurance industry—

'94 new insurance companies added to the register up from 84 in 1999. Total number of international insurance companies registered in Bermuda rose to 1564. 38% of the 2000 insurance formations came from Class 3 companies. 50% of the formations were captives. Finite Insurers and/or reinsurers and health care captives also showed some positive growth in 2000.'[848]

Bermuda also began to see a change in the type of companies forming, with the larger ones being the most dominant. There were 1538 registered international insurers but their numbers reflected a significant change in the composition of the registry, with fewer Class 1 and 2 (single and multi owner captive) companies. Reductions were offset by growth in long term and composite licenses, reflecting the emergence of Bermuda's life reinsurance market. Fewer redomestications of professional (re) insurers but new registrants included a wide range of captives, (including rent a captives), finite companies and health care captives.[849]

Bermudian Business also gave the following summary of the state of the global insurance market—

'During 2000, the entire market benefited from limited natural catastrophe activity worldwide. According to Swiss Re's "sigma" research, insured catastrophes in 2000 aggregated US $10.6 billion (US $7.5 billion from natural causes), one third of the level of 1999, with US $28.6 billion of insured catastrophe losses (24.4 billion from natural causes). For 2000, only the Tokai flood event is expected to reach US $1 billion. Bermuda was not immune to the adverse developments from prior year losses; some property writers bolstered reserves for the late 1999 storms Lothar and Martin; others corrected deficiencies from broad based property and casualty premium underpricing over 1997-1999 accident years. There were strategic repositionings and joint venture undertakings in an attempt to build organizational strength and market presence while sharing risk, and there were problems, including a US $460 million reserve strengthening recorded by OPL, the placement of Terra Nova (Bermuda) Insurance Co. Ltd. into runoff, continued losses at ESG Re, and the post year-end announcement of changes at Heddington (Texaco's captive), which will cease operations as an independent company.

'Market profitability is significantly lower, with the aggregate underwriting loss increasing to US $740 million for Bermuda up from US $507 in 1999 and relative to strong growth in premium volume and low catastrophe activity. Loss and loss expenses incurred has skyrocketed over the past 2 years up 151% from the level of 1998 with net premium earned up 120%.

'...Finite writings increased by 91% in 2000 with a strong contribution (US $410million) from Max Re as one of the newest companies in the market and a US $170 million increase at Scandinavian Re, a seasoned participant; Overseas Partners also made a splash with US $62 million of finite premium written. Life revenues are up nearly 10-fold from 1997 until 2000 to US $424 million, with Annuity and Life Re, Partner Re and Enterprise Re contributing to the growth over that period. Standard & Poor's cites the favourable regulatory and tax environment in Bermuda (as with other offshore markets) as a factor contributing to the growth of life reinsurance revenues during 2000.

'...The rate of growth of property premium at the three largest writers (ACE, XL, and Renaissance Re) far exceeded that of most other participants.

[847] *OIL Corporate History*, Addendum #1,1996-2000, 'Into the New Millenium'

[848] *Bermuda Insurance Update*, press release, 2 March 2001, 'Bermuda Insurance register grows'

[849] *Bermudian Business*, Summer 2001, 'Bermuda Insurance Survey 2001', Deloitte & Touche, 'Bermuda enters the New Millennium', by Karole Dill Barkley, pp. 59-76

'...Rather than placing the blame on market conditions or Mother Nature, the twin threats of under-priced premium and loosened contractual terms and conditions squeezed profit margins and contributed to higher aggregate underwriting losses. Diversification before establishing in house expertise has been another negative impetus.'[850]

According to *Munich Re*, the world was hit by a record number of natural catastrophes in 2000, with the number of natural disasters rising by more than 100 to 850. Munich Re said the only reason why the insurance industry was spared from significant losses in 2000 compared to 1999 was because the natural disasters in 2000 hit less populated areas. 10,000 people died from natural catastrophes in 2000 as compared to 75,000 in 1999. Material damage from natural catastrophes such as storms, floods, forest fires in the US, dry weather and drought in Europe and cyclone weather in the Pacific and North Atlantic exceeded US $30 billion but was significantly less than the $100 billion of losses in 1999. Of the $30 billion in total damages, only $7.5 billion was covered by the insurance industry. Though the industry was spared in 2000, Munich Re warned that with the continued adverse effects of global warming and increasing global population the effects of the increasing natural catastrophes would be catastrophic to the global insurance industry.[851]

Roger Crombie of *Bermudian Business* gave the following summation of the state of the insurance industry and Bermuda's contribution to it at the end of the millennium—

'...Consolidation has reduced of late the number of players in the global insurance industry, even as its scope and size continue to grow. Bermuda's share of that market continues to increase as the Island becomes recognised as a centre of excellence. Business visitors can achieve in a day in Hamilton what might take weeks in a larger city. A Bermuda posting is now considered all but mandatory for a balanced résumé.

'Bermuda companies insure and reinsure risks as diverse as workers' compensation and earthquakes. What 2001 brings will depend on factors well beyond Bermuda's control. But every indicator suggests that, if Bermuda's insurance sector continues along established lines, continued growth must be the certain outcome.'[852]

Adding to Crombie's summation of Bermuda's place in the global insurance industry, Karole Dill Barkley of Standard & Poor's said—

'Bermuda's place in the global (re)insurance industry continues to grow as its franchises collectively represent a microcosm of the global (re)insurance industry. While the island's fortunes ebbed and flowed with the market during 2000, one could conclude that Bermuda's fundamentals were more robust than the weak global industry conditions. The easy earnings of the low catastrophe mid-1990's have been replaced with expansion and hard won market positions in Lloyd's, global property reinsurance, finite reinsurance, and selective other markets throughout the industry. Bermuda is setting the stage for future growth in life reinsurance and potentially structured products, with the implementation of the Segregated Companies Act of 2000. Bermuda persists as the locus for innovation and creativity, in what those in other segments of financial services might consider a less dynamic sector. Bermuda has helped to make (re)insurance more interesting for investors, underwriters, service providers and other market participants.'[853]

Bearing all these positive factors in mind, the Bermuda insurance industry was set to enter the new millennium with a changed focus and increased optimism that it was on the right track for continuing as a strong force.

[850] *Bermudian Business*, Summer 2001, 'Bermuda Insurance Survey 2001', Deloitte & Touche, 'Bermuda enters the New Millennium', by Karole Dill Barkley, pp. 59-76

[851] *Munich Re*,'Natural disasters at record level in 2000'

[852] *Bermudian Business 2000*, Roger Crombie

[853] *Bermudian Business, Seventh Annual Bermuda Insurance Survey 2001, Deloitte & Touche*, with Analysis by Standard & Poor's, 'Bermuda enters the New Millenium', by Karole Dill Barkley

Somehow or another all the disparate voices seemed to converge into one common point. All indications were that, as so often before, the people of Bermuda felt themselves to be at a crossroads as to where the island was going. This should come as no surprise. Throughout the world the second half of the 20th century had seen change at a speed and on a scale totally unprecedented in all of human history. Nowhere had change, in proportion to size, been more extensive and profound than in Bermuda.

The island that entered the 20th century was then a tiny, insignificant colony of Great Britain, almost inaccessible save to the armed forces of Empire and an elite of well-to-do holiday makers from the American East Coast. But for the naval and military contingents and these few wealthy visitors, Bermuda had no economic resources save fishing and domestic agriculture. The people were relatively poor and their way of life was insular.

By the time the 20th century came to an end Bermuda was one of the topmost financial hubs of the global economy. There was an immense concentration of wealth on the island. The standard of living in all classes of society, relative to comparable classes elsewhere, had risen to be amongst the highest in the world. Tremendous progress had been made in all areas, including that of racial interaction and regard. To all intents and purposes, in every way that mattered, Bermuda was an independent nation. That it kept the vestige of an Imperial connection was of its own free will and pragmatic convenience.

All that being said, the fact remains that however beneficial change may be in the long run, change is, by its very nature, unsettling at the time it happens and rapid change can be unnerving to the extent of being traumatic while it lasts. Small wonder, then, that the people of Bermuda worried about the future. Although their worries may have seemed small in relation to the wars, revolutions, tyrannies, famines and epidemics suffered by less fortunate peoples of the world, the worries of Bermudians were real enough and large enough for them in their context of island life.

CHAPTER 50

2001
An End and a New Beginning

Before the Fire

Bermuda saw yet more changes in the first year of the new millennium, politically, socially and financially. Pamela Gordon, who had previously been Bermuda's first woman Premier, resigned from Leadership of the Opposition. Most Bermudians agreed with the hotly debated Constitutional changes, but wished they had been given the chance to vote on them before being presented with them as a done deal by the Progressive Labour Party government. There was a shake up in the PLP Cabinet, in which the ever-popular Paula Cox was moved from the Ministry of Home Affairs to that of Education. This was followed by the introduction of two issues that became controversial, the first being a six-year cap on work permits, except for key employees, and the second being the proposal by the Minister of Transport, Dr Ewart Brown, to introduce Global Positioning Satellite Systems for the taxi industry.

With respect to social and financial developments, tourism continued to decline while international business became ever more essential as Bermuda's financial lifeline. The island was called upon to maintain its own traditions and culture while coming to terms with the influence and the demands of the international business sector. The decline in tourism revenue was offset to some extent by the rise in business revenue. This rise was in part due to significant changes in the insurance industry itself. The hardening of the global insurance market brought benefits to the economy of Bermuda by contributing greatly to its Gross Domestic Product. *AM Best* reported —

> '"Prior to Sept 11, some of the things we thought we were facing included rates that were already increasing," said Ray E. Beane, Vice President of Construction Insurance for Liberty Mutual Insurance Co. "Terms were tightening, some security requirements were enhanced. Some carriers tried to get better cash flow by asking insureds to pay more in advance. From a carrier's and reinsurer's perspective, there was an increase in submissions as the market hardened. There was also a decrease in investment income. That was one of the main drivers of the hardening market prior to Sept. 11—insurers just weren't making investment income..." Beane said combined ratios for both insurers and reinsurers hadn't been below 100 for at least a decade. "So you can see we depend on our investment income," he said. "And in 2001, combined ratios went through the roof." The insurance industry had been making money from 1993 to 2000, said Beane. In 2001, the industry lost money. Return on equity had been adequate for the property/casualty industry since 1987, although 1987 was the last year the property/casualty industry outperformed other sector(s), he said. In 2001, return in equity was in the negative territory. "It used to be that when the combined ratios came in at 100 to 108, that was fine, because the investment income ensured an overall profit," he said. "Well, that investment piece is gone now, so there has to be focus on combined ratio. We have to get better prices, and we have to improve on expenses."

> 'Warren R. Hayward, facultative manager with Swiss Reinsurance America Corp., said that in 2001—before Sept. 11—both insurers and reinsurers took a hard look at their books of business, trying to decide what they wanted to write and at what price. "One of the main concerns going into the third quarter was reserve adequacy," he said. "Other issues included mold—how big a problem would it be? Asbestos was a re-emerging issue, with a number of significant new claims...In 1987, there was a better rate environment

for reinsurers, combined-ratio results were fairly good, and underwriting conditions were favorable," said Hayward. "Policyholders surplus had been rising steadily until 1999, when it began to fall, and it dropped significantly since Sept. 11," he said. "The downward turn came from a host of issues – a previous soft market, rising medical-malpractice losses and more severe claims activity in general. A two year decline in capital historically signals a return to a hard market; it takes the industry some time to understand what it's doing wrong." Hayward said reinsurers were beginning to pay the price for soft-market underwriting well before Sept 11. "Reinsurers got into writing things they didn't really understand, like medical and professional liability and other lines," he said. "So we'd begun to pull back, concentrating on shorter-tail business, imposed exclusions on terrorism and other indeterminate exposures, got away from multiyear treaties. We began to stay with things we felt most comfortable with."'[854]

Thus many buyers of insurance received double digit premium increases and coverage restrictions for the first time in over ten years. The industry was on its way to recuperating the premium it had lost over the years as it tried to find ways to increase its cash flow because of poor investment returns on top of minimal premiums.

ACE sues CIGNA

After much talk about the mega-merger of ACE and CIGNA, which instantly catapulted ACE to become one of the insurance giants in the world, late in 2000, ACE filed suit against CIGNA for breach of contract. ACE sought US $218 million in damages, claiming CIGNA had withheld US $48 million of the funds ACE was entitled to under the Tax Sharing Agreement that formed a part of the Acquisition Agreement. ACE also contended that CIGNA had failed to fairly represent the financial condition of the companies it had acquired. According to the *Bermuda Market Digest*, a monthly newsletter about the insurance industry—

'ACE claims CIGNA has twice breached the acquisition agreement by which ACE acquired the property and casualty operations of CIGNA last summer and seeks restitution....The lawsuit was filed in the United States District Court (Southern District of New York), where ACE is seeking a jury trial.

'ACE confirms that the financial statement impact of the items under dispute has been reflected in its consolidated financial statements prior to September 30, 2000. The financial statement impact included adjustments to goodwill and other balance sheet items and was determined without including any amounts to be recovered from CIGNA as a result of the lawsuit.

'Accordingly, the items included in the lawsuit will not impact the financial results for the quarter ended December 31, 2000.'[855]

The suit arose out of certain balance sheet issues with particular reference to what constituted tangible value as opposed to goodwill. The suit was later settled and all outstanding issues were resolved prior to the case ever going to trial.

US rulings affect the Bermuda international insurance industry

Just when Bermuda thought it had distanced itself from being considered a tax haven, the US Congress took aim against Bermuda yet again. This time by introducing the Reinsurance Tax Equity Act of 2001 (HR 1755), which required United States subsidiaries not subject to United States taxation to defer the deduction of premiums paid for reinsurance until there is a loss recovery. The *Bermuda Market Digest* reported on this new Act as follows—

'A second major industry group opposes moves by American insurers to hobble Bermuda-based companies for their tax advantage.

[854] *A.M. Best, Best Wire Services*, 15 August 2002, 'Little Relief Seen from Battered Market that faces Insurers', by David Pilla

[855] *Bermuda Market Digest*, January 2001, Vol.5 No.1, 'ACE sues CIGNA for US $218 million', pp. 1 & 4

'*National Underwriter* has reported that a major risk managers' group is opposing legislation that would prevent subsidiary insurers from escaping taxation by reinsuring risks with their offshore parent companies.

'The New York-based Risk and Insurance Management Society says it is opposing the proposed Reinsurance Tax Equity Act of 2001 (HR 1755) out of concern that the measure could "adversely affect the reinsurance marketplace and hamper RIMS members' ability to successfully manage their risk exposure."

'...At that time, the Captive Insurance Association, based in Minneapolis, was urging risk managers to join it in speaking out against HR 1755. In CICA's view, risk managers would be the most affected and most capable of helping to defeat the measure.

'..."RIMS members have an inherent interest in maintaining a competitive and innovative global insurance and reinsurance marketplace," says Michael Phillips, RIMS Vice President of external affairs. "We believe HR 1755 would undermine and disrupt this marketplace."

'Additionally, RIMS says that HR 1755 would reduce the pool of global funds that cover losses for organisations and individuals. RIMS has also indicated that it opposed legislation "that encumbers free market movement and the transfer of risk that is vital to a sound global insurance and reinsurance community."

'RIMS also believes that eliminating the deductibility of premiums will lead to increases in insurance rates, which would affect insurance industry solvency and prevent risk managers from correctly gauging the financial health of insurers.'[856]

Todd Malan, Executive Director of the Organization for International Investment (OFII), believes that the insurance industry has done a fantastic job in lobbying this issue by it making clear to members of Congress why it is not sound tax policy. Malan believes that the active education effort by the foreign-based insurance companies has resulted in the failure of HR 1755 (as was the case with HR 4192) to progress in the legislative process. However, he indicated that no revenue raising proposal is ever truly dead in the congressional process. The industry is always at risk that legislation like HR 1755 could be reengerised.[857]

The international insurance industry has been given another reprieve from the draconian bills posed by some in the US but it is imperative that it keeps up the lobbying efforts and makes the right connections in Washington to try to prevent such measures from ever receiving Congressional approval. Issues such as these are never considered dead in the US Congress just resting until someone resurrects them.

Then in a positive development, the captive industry rejoiced with the ruling known as '2001-31' in which the Internal Revenue Services (IRS) reversed its prior 'economic family' theory better known as 'IRS 77-316'. It was this ruling that caused captives to write third party business in Bermuda in the late 1970s and early 1980s, which led to the demise of many of them.

The captive industry received a boost when the IRS also ruled that it would allow premiums paid to captives to be tax-deductible. This decision reversed the ruling of the controversial *Carnation* case in 1979, which essentially said there was no real transfer of risk if the insurance was kept within the control of the parent company because the parent company and the captive all formed one 'economic family'.

The IRS decided that because of the many different types of captives today, it is very difficult to say there is no transfer of risk. Because there are now so many different subsidiaries being insured by captives, and since some captives, such as rent-a-captives and risk retention groups, serve several entities, the IRS concluded that there is true risk shifting or redistribution of risk.

Business Insurance reported the following about why the IRS decided to drop its 'economic family' theory—

[856] *Bermuda Market Digest*, September 2001, 'RIMS opposes tax proposal', pp. 1 & 12

[857] Telephone interview with Todd Malan, Executive Director, Organization for International Investment (OFII), 30 December 2003

'...Other courts declined to accept the IRS' economic family theory, which the IRS recognized in June 2001 when it published Revenue Ruling 2001-31, dropping the theory. "No court, in addressing a captive insurance transaction, has fully accepted the economic family theory," the ruling noted. "Accordingly, the IRS will no longer invoke the economic family theory with respect to captive insurance transactions."'[858]

What was interesting about this ruling is that many more States in the US moved to pass legislation to allow captives to be formed and their uses broadened.

Seen as another victory for the captive insurance industry was the reversal of the ruling that United Parcel Services (UPS) had spun off Overseas Partners Limited (OPL) purely to avoid taxes. A panel of the 11th Circuit Court of Appeals based their decision on the fact that they believed that the programme was a legitimate one and that reducing UPS' taxes was an acceptable aim of the plan. In its 2-1 ruling, the panel also found that the AIG fronting arrangement was not an indication of a sham and that such arrangements still entail risk for the fronting insurers.

Business Insurance reported on the ruling as follows—

'The court found that even if AIG had been merely a conduit for premiums, OPL was an independent entity not under UPS' control, and UPS actually did lose the income from the excess-value charges it collected.'[859]

This decision was believed to have far reaching effects for Bermuda because it signalled another great victory for captives right on the back of the reversal of the 'economic family' theory. Both rulings signalled that it was acceptable for captives to provide fronting arrangements and provide some tax benefits.

Catastrophes continue

2001 was filled with catastrophes for the global insurance industry...

—The first major one for the year was the sinking of a Petrobras oilrig off Rio de Janeiro that cost the industry US $700 million and ultimately drove up offshore energy rates.

—Then storms and tornadoes ripped through the Midwestern and Mid Atlantic states of the United States, causing unexpected damage.

—The third catastrophe took the industry by surprise when in June a slow moving tropical storm called Allison gave rise to unprecedented insurance damages. Rainfall as heavy as 30-40 inches caused severe flooding in coastal parts of Texas and Louisiana, especially in the Houston area, before moving slowly northeast. Fatalities and significant damage were reported in Texas, Louisiana, Mississippi, Florida, Virginia and Pennsylvania. The estimate of total damages/costs was approximately US $5 billion and at least 43 lives were lost.

According to Tom Ross, meteorologist from NOAA/National Climatic Data Centre, one reason why damages were so high may have been societal change rather than increasing frequency of such events. As compared to a few decades previous there is more population in harm's way and property values along the Gulf and East Coast shorelines have risen to astronomic levels. Now it takes only a weak storm to create billions of dollars' worth of damages.[860]

—The fourth major catastrophe came in July with the destruction of 11 aircraft in a terrorist attack at Sri Lanka's International Airport.

All told, the second quarter of 2001 proved to be brutal for the global insurance industry despite fewer catastrophes than in the previous year. *Business Insurance* summarised—

[858] *Business Insurance*, 24 December 2001, 'Year in Review, 8', by Gavin Souter

[859] *Business Insurance*, 24 December 2001, 'Year in Review, 10', by Douglas McLeod

[860] e-mail correspondence with Tom Ross, NOAA, 28 February 2002, website www.ncdc.noaa.gov

'Catastrophes caused an estimated $4.4 billion in insured property damage in the United States during the second quarter of the year, according to the Insurance Services Office Inc.'s Property Claim Services unit... N.J.-based PCS reported that the total makes the second quarter of 2001 the second-worst such quarter in terms of insured property damage in the past 10 years. The worst second quarter was in 1998, with estimated insured damages totalling $4.5 billion. Losses for the same period in 2000 totalled only about $1.4 billion.

'Two catastrophic events each caused more than $1 billion in insured property damage during the second quarter this year. Tropical Storm Allison caused $1.2 billion in damage, and a series of violent storms from Texas to Pennsylvania caused $1.7 billion in losses. In addition, June hailstorms pounded North Dakota and other areas of the upper Midwest along with Colorado. Together, those storms added $415 million to the quarter's catastrophe losses.

'Catastrophe losses for the first half of 2001 now stand at an estimated $5.1 billion, the fourth-costliest six-month period since 1992. Losses in the same period in 2000 totalled $3.4 billion. While producing near-record losses for a second quarter in the last 10 years, this year's second quarter tied the same period of 1997 for the fewest catastrophes-nine. For the second quarter this year, insurers received 1.03 million claims from businesses and homeowners, compared with 550,000 claims in the year-earlier period. The highest number of second-quarter claims filed with insurers was 1.7 million in 1998. Of the 21 affected states, Texas incurred the greatest insured-property losses, with $1.4 billion, followed by Missouri at $1.25 billion, Nebraska at $400 million, Minnesota at $355 million and North Dakota at $160 million.

'Meanwhile, both SAFECO Corp. and Chubb Corp. have warned that, because of catastrophe losses, their second-quarter results will be worse than expected. 'A spokesman from Seattle-based SAFECO said the insurer saw losses of $60 million from hailstorms that hit St Louis in April and losses of $8 million from Hurricane Allison. Warren,-N.J.-based Chubb said it expects catastrophe losses of $80 million for the second quarter.'[861]

Bermuda marketplace continues to respond to the demands of the global insurance industry

In the meantime, the Bermuda government's insurance department implemented significant changes of its own, in response to Bermuda's ever increasing prominence on the insurance industry world stage, and the recommendations made in the KPMG report. Cheryl Lister, head of the Bermuda Monetary Authority (BMA), recalled that as early as the first quarter of 2001 the board of the Bermuda Monetary Authority was given new responsibilities and therefore had to review its structure to ensure the checks and balances were in place to manage the new responsibilities. One such responsibility potentially arising from the KPMG report as discussed in the year 2000 was the newly independent Insurance Division from the Ministry of Finance. Once the board began the review, it looked at various existing structures within the regulatory body to determine if the insurance department should be an independent regulatory and financial authority in its own right or whether it should become a part of the BMA. The purpose of the review was to design an ideal platform to include insurance. It was resolved to place the Insurance Division within the BMA and was so decided.

Cheryl Lister contacted Bob Steinhoff, Chairman of the Insurance Advisory Committee (IAC), to update him about what they were doing. Steinhoff thought the timing was perfect because he felt it would allow the Insurance Division to help shape their future structure within the BMA as opposed to the BMA doing it without their feedback. They had a couple of meetings to discuss the ramifications of the change. At the end of the discussions, it was agreed that the BMA was the best place for the insurance division because it was removed from the control of government.

[861] *Business Insurance*, 16 July 2001, 'Second-quarter cat losses at 4.4 billion: PCS', by Mark Hofmann

This move also placated KPMG, the accounting firm responsible for completing the financial report on Bermuda, who considered that for the insurance division to fall under the government would create a conflict of interest. Therefore a subcommittee was formed, jointly between the BMA and the IAC, to look at the future structure of the BMA as an independent regulatory authority responsible for all financial services. The joint committee came up with a joint proposal approved by the BMA board and the IAC and submitted it to the Minister of Finance. And as Cheryl Lister says, 'the rest is history.'[862]

Big news dominated the Bermuda marketplace when in February of 2001 XL Capital Ltd. announced its plans to enter the international primary insurance market with the purchase of Winterthur International from Credit Suisse for US $600 million. *Bottom Line* magazine reported Brian O'Hara, president and chief executive of XL, as saying—

> '... The re-branding of our operations, with XL Re, XL Brockbank, and XL Aerospace presented as part of our global franchise, has now been completed. We are now focussed on growing our more profitable specialty insurance and reinsurance lines. Our acquisition of Winterthur International's large corporate risk management business is a further indication of our focus on selected segments and strong desire to further deliver our products globally. We believe it will provide XL with a significant expanded global franchise and help us to achieve our business objective of becoming one of the world's leading providers of property and casualty insurance. XL is acquiring a high quality underwriting business known for its client servicing capabilities.'[863]

The Life Insurance Industry in Bermuda began to show signs of becoming a true and diversified marketplace when ACE announced it was entering the industry after its agreement not to compete with newly acquired CIGNA expired in 2002. Shortly, thereafter came the news of Hampton Re Holdings, the holding company for a new Bermuda -based life reinsurance company, announcing its formation and initial capitalisation in Bermuda. According to the *Bermuda Market Digest*—

> 'Hampton Re will reinsure in-force blocks of life insurance business, confirming Bermuda's growing strength in the life and annuity market it once eschewed...The company will focus on the assumption of in-force blocks of life insurance business, primarily on a retrocessional basis.
>
> 'Bill Walker formerly of Hannover Life Re, will serve as president and chief executive officer of Hampton Re and head its management team. Kaj Ahlmann, most recently vice chairman of E.W. Blanch and formerly chairman and chief executive of Employer's Reinsurance, will serve as chairman of the board.
>
> 'Hampton Re worked closely with J.P. Morgan in connection with its formation. Morgan serves as the company's exclusive financial and investment advisor and Morgan's lending arm—Morgan Guaranty Trust Company—is providing the company with a multi-year credit facility. Additionally, two senior Morgan officers, one of whom is David Kimmel, head of insurance investment banking for the Americas, serve on Hampton Re's board of directors.
>
> 'Hampton Re's business strategy is to participate in the growing market for reinsurance of in-force blocks of life insurance business that was Walker's strategic focus during his eight year tenure as president and chief executive officer of Hannover Life Re....[864]

At the same time Scottish Annuity & Life announced its intention to move to Bermuda. According to the *Bermuda Market Digest*—

> 'Continuing strife in the Cayman Islands in the wake of the OECD's investigation into the offshore world were not a factor in the move, says management—Bermuda is simply the global capital of the insurance industry.

[862] Interview with Cheryl Lister, 26 November 2002
[863] *Bottom Line*, April 2001, 'Life change', by Roger Crombie, p. 27
[864] Bermuda Market Digest, May 2001, Vol. 5, No.5, 'New Life Reinsurer formed in Bermuda', pp. 1 & 14

'The largest reinsurance company domiciled in the Caymans, Scottish Annuity and Life Holdings, has announced that it is planning to move its corporate and international reinsurance operations to Bermuda. '"Bermuda is the capital of the global insurance industry," said the company's chairman and chief executive officer, Michael C. French. "While the Cayman Islands have provided an excellent home for the company, the long-term growth and success of our business will significantly benefit from being in the global insurance business flow that passes through Bermuda."

'The company is applying to Bermuda authorities for permission to conduct its holding company operations from Bermuda. In addition, the company is applying to redomesticate its flagship subsidiary, Scottish Annuity & Life Insurance (Cayman) to Bermuda.

'...Scottish Annuity & Life Holdings provides reinsurance of life insurance and annuities and is a direct issuer of customised variable life and annuity products for high net worth world citizens.'[865]

Bermuda received an added boost when Hannover Re, the fifth largest reinsurance company in the world, established a new subsidiary, Hannover Re Bermuda (HRB) to write catastrophe business on a worldwide basis. This new addition added to Bermuda's prominence in the global property cat marketplace, despite the consolidations that had occurred. According to the *Bermuda Market Digest*—

'HRB is intended to become the centre of excellence within the Hannover Re Group for property catastrophe excess of loss programmes. Hannover Re will concentrate its underwriting expertise for this particular line of business in this unit. In addition, HRB intends to develop a proprietary catastrophe simulations model. By setting up this new company, the Hannover Re Group will be physically represented in the world's largest catastrophe reinsurance market and will benefit from the Bermudian infrastructure.'[866]

Despite the controversy surrounding redomestications to Bermuda, the world's third largest insurance broker, Willis Group, decided to redomesticate there and to launch an IPO to raise capital. In its filing for the IPO, Willis said it planned to establish an employee stock purchase plan, capitalise on its global reach, expand and cross-sell its employee benefits capabilities and create a single company culture and pursue strategic acquisitions and investments, among other intents and purposes.

Less than two years after its start up, Max Re formed a new reinsurer jointly with HypoVereinsbank and filed for a public issue of stocks.

Then the Bermuda market saw some consolidations when The Imagine Group announced it was buying Enterprise Re. *Bermuda Market Digest* reported Thomas Gleeson, founder and co-chief executive officer of The Imagine Group, as commenting—

'The purchase of Enterprise Re furthers the implementation of our very focused business model and is consistent with our previously-stated goal of providing a unique financial services platform to the global insurance industry. This transaction further enables The Imagine Group to meet the significant demand for structured insurance and reinsurance products that we are seeing in the marketplace today.'[867]

Bermuda also began to develop as the place for weather insurance products. The *Bermuda Market Digest* reported on this new product as follows—

'Bermuda-based insurance companies are marketing a new type of weather insurance, weather index insurance, to local governments and large corporations which have substantial sensitivity to weather fluctuation. Insuring against loss or damage caused by weather is not new business, but has generally been on an indemnity basis that is compensation for actual loss experienced.

[865] ibid. 'Scottish Annuity & Life moves to Bermuda', pp. 1 & 16

[866] *Bermuda Market Digest*, Vol. 5, No.6, June 2001, 'Hannover Re establishes catastrophe reinsurer in Bermuda', pp. 1 & 4

[867] ibid, Vol.5, No. 8, August 2001, 'Imagine Group buys Enterprise Re'

'The new products being marketed by Commercial Risk and Ace Tempest Reinsurance are index- linked, the index used being statistics provided by registered weather stations. Cover is guaranteed to cut in at a level predetermined in the insurance contract and reported by the weather stations, regardless of the degree of loss.

'Christopher Phelan, managing director of Commercial Risk, explains: "In an extreme winter, local government bodies may have to spend more money to heat their buildings or remove snow from the roads, etc. If we can wrap all these eventualities into one insurance product then they can guarantee their budgets instead of having to raise money to pay for them retrospectively."

'As a result of deregulation in the US, utility and energy companies have been able to make use of these index-linked products and Commercial Risk expects this pattern to be followed in the UK and EU as deregulation is applied there.

'...Phelan explains that weather index insurance is sold as a finite contract; there is no open-ended liability. The insurance companies have in-house weather experts and product design and calculations of premium is tailored to suit each individual need and circumstance...'[868]

Following Tempest and Commercial Risk's foray into weather products came Aquila Re as reported by *Bermuda Market Digest*—

'Aquila Re, a Bermuda-based wholly-owned subsidiary of Aquila, and Kemper Insurance have announced that they have formed a strategic alliance to expand the global market for weather derivates and weather risk management products. "The market for weather risk management is large and growing," says Ed Mills, president of Aquila. "We already have a well-established weather derivative business and expect our relationship with Kemper will allow us to reach a broader range of customers," he adds.

'...Aquila is a pioneer in the weather marketplace, having provided the energy industry's first weather hedge in the summer of 1996. Kemper entered the weather business in 1999.'[869]

In addition, Swiss Re and Tokio Millennium Re of Bermuda arranged a US $450 million cat risk swap to cover losses from three natural perils. The cat risk swap is structured in three risk exchanges of US $150 million each—Japan earthquake for California earthquake, Japan typhoon for Florida hurricane and Japan typhoon for France storm. By swapping segments of Japanese catastrophe event exposure with Florida, France and California cat risks, Tokio Marine and Swiss Re are able to significantly improve the diversification of their risk portfolios by transferring 'peak risks' off their balance sheets.

Asbestos returns

Until the events of September 11 pushed most other concerns aside, a surprising upsurge of new claims relating to what had been thought an old problem of the 1950s caused asbestos to arise again as a major headache for insurance personnel around the globe. *Business Insurance* reported—

'...More than three decades after the first asbestos injury lawsuit was filed, the pace of new claims has quickened, defying predictions that the crisis would be nearing its end by now. The number of asbestos cases pending in courts in the United States doubled between 1993 and 1999 despite huge numbers of settlements in the interim, and several defendant companies have reported sharply higher rates of new claims being brought against them.

'The spike in new claims pushed a number of long-time asbestos defendants into bankruptcy. Among these were auto parts maker Federal Mogul Corp., building products makers Armstrong World Industries Inc., Owens Corning, Pittsburgh Corning Corp., USG Corp., W.R. Grace & Co. and a successor to GAF Corp., and engineering firms Babcock & Wilcox Co. and Burns & Roe Enterprises Inc.

[868] *Bermuda Market Digest*, March 2001, Vol.5, No.3, 'New weather insurance products', pp. 3 & 20

[869] ibid. June 2001, Vol.5, No.6, 'Aquila Re, Kemper to offer weather risk cover', pp. 1& 16

'Furthermore, new claims are being aimed at a broadening array of "non-traditional" defendants that face rising liabilities because of the bankruptcies of traditional asbestos defendants. The new defendants range from giants such as IBM Corp., AT&T Corp. and Ford Motor Co. to small regional installers of products that contain asbestos.

'Defendants and their insurers have decried many of these claims, charging that they come from plaintiffs who show no signs of asbestos-related illness. In May, London market insurers announced tougher standards for filing claims, requiring medical evidence of illness and proof of asbestos exposure for which a given defendant is responsible.

'A handful of large insurers, meanwhile, have been funnelling more money into asbestos reserves in light of the trends, including Equitas Ltd.—the runoff reinsurer for Lloyd's of London syndicates' pre-1993 long-tail liabilities—and CNA Financial Corp.

'No one today is discussing the imminent demise of asbestos liabilities.[870]

The first eight months of the year 2001 saw the industry start to firm up its rates, increase its reserves, try to recover from the worst second quarter for catastrophes in over ten years and adopt a more focussed approach to regaining profitability. Then, on September 11, other events and concerns took precedence. Suddenly there was a new order of magnitude to the measurement of man-made catastrophes in a time of nominal peace. To say, as so many commentators have said, that 'nothing would ever be the same again' is to say nothing meaningful. Nothing in human affairs is ever the same from one day to the next. What can be said with little fear of contradiction is that from September 11, 2001 the perceptions, perspectives and priorities of the insurance industry, like those of many others, were suddenly, brutally and radically changed.

'Nine Eleven'

Minoru Yamasaki, designer of the World Trade Center, said when the project was completed, 'I feel this way about it. World trade means world peace and consequently the World Trade Center buildings in New York...had a bigger purpose than just to provide room for tenants. The World Trade Center is a living symbol of man's dedication to world peace...beyond the compelling need to make this monument to world peace, the World Trade Center should, because of its importance, become a representation of man's belief in humanity, his need for individual dignity, his beliefs in the cooperation of men, and through cooperation, his ability to find greatness.' That was in 1970. Such hopes sound bitterly ironic now.

The terrorist attacks of September 11, 2001 have been the subject of so much detailed reporting as to make it needless to recount the history of events yet again. Yet it is appropriate to review their impact on the world of insurance. They struck at the core of its being. Not only was the insurance world devastated financially—it was also devastated emotionally and intellectually. The World Trade Center housed two of the largest insurance brokerage firms on the face of the earth—Marsh & McLennan and Aon—both lost hundreds of employees in a few hours.

For the first time in the history of their industry, insurance companies had to overcome the deaths of their own before even assessing the effects of a catastrophe on their profit lines. Most people in the industry were numbed by shock and in no state even to begin to calculate the damages. There was a perverse, benighted logic in this. An act of terror intended to shatter the outlook on life of an entire society, to threaten and undermine all that society's assumptions as to its strength and stability, had struck deep at the very essence of that to which most people look for security in the event that all else is lost—insurance. The twin towers that stood in New York housed thousands of insurance people, men and women who had all been responsible, in one way and another, for providing some level of confidence, some promise of certainty, some hope of comfort, to those who

870 *Business Insurance*, 24 December 2001, 'Year in Review, 7', by Douglas McLeod

bought insurance products from them. Yet the same men and women were now destroyed in the very buildings that had been envisaged by their architect as symbols of 'World Peace'.

Everybody and every corporation was affected in one way or another. In a report immediately following the events of September 11, *Business Insurance* set out this record—

> 'The many insurance brokers, insurers, reinsurers, and industry related institutions housed in the two 110-story World Trade Center towers suffered widely varying losses in last week's terrorist attacks. Among the most severely damaged are Marsh & McLennan Cos. Inc. which had offices of several units scattered within both trade center towers. MMC units, Marsh Inc and Guy Carpenter & Co., Inc occupied the 93rd through 100th floors of the North Tower. That tower, known as 1 World Trade Center, was the first to be hit. William M. Mercer Cos, LLC Seabury and Smith and Carpenter also had floors on the 49th through 53rd floors of the South Tower. The tower, known as 2 World Trade Center, was the first structure to collapse. MMC had 1700 employees and reported that between 50-100 visitors were scheduled to be in the offices at the time of the attack. Chicago based Aon had 1,100 employees on the 92nd and 98th through 105th floors of 2 World Trade Center along with 250 employees and others visiting at the time of the attack, according to Patrick Ryan, Chairman and Chief Executive Officer. There were other insurance affiliates located in the Center including Empire Blue Cross and Blue Shield, New York's biggest health insurer, corporate headquarters at 1 World Trade Center with 1914 employees in offices from the 17th to the 31st floors, retail insurance broker Frenkel & Co., the 39th largest broker of U.S. business, which had evacuated all 231 of its employees, Kemper Insurance Cos., of Long Grove, Illinois, which had 225 employees on the 35th and 36th floors of 1 World Trade Center, all accounted for, SCOR U.S. Corp which had 120 employees on the 23rd and 24th floors of 2 WTC all evacuated safely, Metropolitan Life Insurance Co., which had 52 employees in a sales office on the 89th floor of 1 World Trade. Several insurers and industry related entities were affected as well.'[871]

That day in September 2001 was the day when insurers were all of a sudden forced to recognise that the unthinkable could 'really' happen. It was the day when for the first time they not only had to imagine the unimaginable—they had to look at it all around them. The seemingly impossible had become that morning's reality. The textbook scenarios for the analysis of loss were no longer useful. All actuarial models were immediately rendered obsolete and so had to be recalculated and redefined. Insurers found it very difficult to differentiate between maximum probable losses and maximum possible losses. They had to face the conundrum that after this there might be no such difference anymore. The perception of risk for the global insurance industry was radically changed. The faith of many in the insurance industry was shaken as to their own ability to price or even to forecast possible future risk exposures. Yet the work had to be done. After days of coming to terms with the immensity of the loss to the industry, insurers began to tally the cost. Early estimates of the total ranged as widely as from US $30 billion to US $70 billion.

It so happened that the World Trade Center was completed in early 1970 at a time when the Bermuda insurance industry was setting forth on the path that would make Bermuda known as the 'insurance innovator of the world'. The World Trade Centre was destroyed at a time when Bermuda had established an infrastructure that would enable it to be a principal point of renewed resources for the world's insurance industry. Thereafter Bermuda made it possible for investors to replace capital that had been lost and to deploy this new capital so as to keep the wheels of the global economy turning. Otherwise many companies would have become uninsured and been incapable of continuing operations.

Following are the thoughts of some key executives about the impact on them and on Bermuda's insurance industry.

Keith Hynes, Executive Vice President & Chief Financial Officer of Max Re told Roger Crombie of *Bermudian Business*—

[871] *Business Insurance*, 12 September 2001, 'Industry reeling amid loss of life', by Douglas McLeod, pp 2 & 21

> 'The tragedy came at a terrible time for the US and world economies. The US was struggling to avoid a recession at the time of the event. The US economy barely grew, with Gross Domestic Product up point three per cent, in the second quarter of 2001. It's clear the impacts from this tragedy will cause a shrinkage in the US economy in the third quarter of 2001, and likely will cause shrinkage in the GDP in the fourth quarter of 2001, resulting in a recession for the US, and probably the world economies. This economic slow down will have negative effects on the capital markets and returns from investments.
>
> '... Insurance organisations cannot look to their assets to support weakened underwriting results, as they have for most of the last ten years.'[872]

Bob Clements, Chairman of Arch Re and the 'father of excess insurance' in Bermuda said September 11, 2001 was very hard to deal with because it was a major tragedy. It looked as if it signalled the beginning of a period of unrest in the world that overshadowed anything pro or con about the industry. Clements said he almost felt guilty talking about its effect on the narrower context of insurance. However, he did recognise that the events had a catalytic effect on the insurance industry.[873]

Robert Newhouse, Chairman of Axis Speciality Bermuda, said September 11 transformed the whole insurance industry because it was the first occasion on which both the insurance and reinsurance businesses were affected so adversely at the same time. When ACE and XL were formed, it was as a result of shortages in the insurance industry. When Mid Ocean Re and the property catastrophe market formed, it was as a result of shortages in the reinsurance market. September 11 brought the shortages forward in both insurance and reinsurance.[874]

Brian Duperreault, Chairman, President and CEO of ACE said it was so poetic to have ACE and XL side by side on that day. Losses were staggering and a surprise to everyone. The combination of events and clash of losses presented a disaster scenario. ACE had even projected a disaster scenario of an airplane crashing into the World Trade Center but they never expected both towers to go down. It shook the industry to the core. However Duperreault felt the industry handled the attacks extremely well. There were no failures. But more importantly the industry stepped up to the plate to honour claims despite the brief erroneous reports that the industry would invoke terrorism exclusion. He was proud to say the industry shouldered its responsibilities and it was the first time that he had witnessed a true coming together of the global insurance industry.

However, the industry was still faced with what to do about terrorism in the future. The industry knew that it could not continue to fund terrorism claims without some sort of support but it did not want to leave clients empty handed. As a result an awful lot of effort was put into a search for solutions by the insurance industry, the building and construction industry, banking, and real estate because all of these industries realised that if they did not work together the effects on the economy could be devastating.

Duperreault said September 11, 2001 changed the way the industry looked at all risks, particularly at the way risks were concentrated in one area. Workers' compensation was one line of business that saw massive changes in the way it was underwritten. The industry also became very risk averse as the market had been tightening prior to September 11, 2001 because cash flows had begun to turn negative and because of the sustained investment bear market.

After September 11, 2001 companies started withdrawing from or not covering aviation or reinsurance. Some of the big names in the industry began to scale back or completely withdraw from lines of business in which they had previously specialised. In addition, a whole new breed of reinsurers opened up in Bermuda. There was also accelerated change in the leadership of major companies around the world as all fought to remain profitable. Duperreault was of the opinion that as a result of

[872] *Bermudian Business*, Winter 2001, 'A report on the impact 9/11/2001', by Roger Crombie, p. 23

[873] Interview with Bob Clements, 10 December 2002

[874] Interview with Bob Newhouse, 3 April 2003

the events of September 11 ACE, and XL stepped into leadership positions in the global insurance marketplace, whereas just ten short years previously they were considered to be nothing more than a blip on the radar screen.[875]

Brian O'Hara, President and Chief Executive Officer of XL said that the loss to the industry on September 11, 2001 was so huge as to accelerate a cycle of change that was naturally occurring in the industry anyway. It exposed weaknesses and thereby in effect created many untold opportunities. This was how all the new capital came into the marketplace.[876]

James Stanard, Chairman, President, and CEO of Renaissance Re said September 11 was a shock to the industry because it was the most serious financial loss the industry had ever suffered. The human and psychological impact was enormous. However the financial impact should not have been a surprise because the industry is well aware of the large catastrophes out there, such as earthquakes and other natural catastrophes. What shocked the industry more than anything was the human aspect—an exposure those in the industry had not anticipated or priced for either.[877]

Jim Bryce, President & CEO of IPC Re said he was in Monte Carlo in meetings with clients when he received a call that the towers had been hit. Everyone gathered in the Aon suites at the Hotel Paris to see on the television what was unfolding in the United States. A feeling of foreboding penetrated the conference as the reality of the situation sunk in. The conference was called off. People had difficulty flying back into the United States so they flew to Canada, rented cars and drove to the US.

Bryce felt that the events had more repercussions in terms of Probable Maximum Loss underwriting and correlation of risks. Previously everyone was concerned about earthquakes but now they are concerned about any heavy concentration, in any geospace, because every major class of risk was affected by the tragedy except surety. He doesn't think the amount paid out to ultimate losses will be finalised for decades.[878]

Best Wire Services reported that—

'(Warren R. Hayward, facultative manager with Swiss Reinsurance America Corp., said) "Then came Sept. 11, with implications that threatened the existence of the industry as a whole... Since then, our focus shifted exclusively to the bottom line...Relationships with long-time customers, which had been important in the past, no longer carried the day. Underwriting fundamentals were more important."

'After Andrew in 1992, the maximum disaster loss was projected at US $15.5 billion, said Hayward. "Sept. 11 proved that totally inadequate, with a possible loss of US $40 billion or more...What's worse, worker's compensation and life insurance, for the first time, suffered catastrophe losses—an estimated US $3.5 billion or more for workers comp, and US $2.7 billion for life. The hits were significant for reinsurers," said Hayward. "The hit to the industry was not a funded hit—terrorism was basically a free coverage."

'Compared with the next nine worst catastrophes in insurance history, the destruction of the World Trade Center impacted almost every line, added Beane (Ray E. Beane, vice president of construction insurance for Liberty Mutual Insurance Co). "The rest were mostly property losses," he said. "It was also worth noting that reinsurance accounted for at least 60% of the losses...Sept. 11 showed that the industry has concentrations of exposures throughout the country," he said. "One of the things that risk managers have tried to do since is to spread employees out over a wider area. Things like equipment. Computer systems and records also need a backup to ensure a company can get up and running again if it takes a hit."

'While the loss of the World Trade Center was the main focus for reinsurance losses in the past year, there were US $7.5 billion in natural catastrophic losses over that time as well, Hayward said. And, beyond that, the recovery of the economy in general has been a big issue over the past year.

[875] Interview with Brian Duperreault, 2 December 2002
[876] Interview with Brian O'Hara, 19 November 2002
[877] Interview with Jim Stanard, 4 December 2002
[878] Interview with Jim Bryce, 25 November 2002

'…"How long is the hard market going to last? Some believe another year, but if you look at what's going on in the stock market, it's likely to last at least through 2003," added Beane, referring again to insurance companies' investment losses and eroding stock prices. "We've got to use that to return to profitability."'[879]

Effect on the Bermuda Insurance Industry

The devastating effect of the attacks immediately hit home to Bermuda's local community when it was learned that two of their own—Rhondelle Tankard, of Aon Bermuda, and Boyd Gatton, of Fiduciary Trust—were among the victims, both lost and never to be seen again.

Like that of every similar community around the globe, the first reaction of the Bermuda insurance industry to the news of the World Trade Center was simply one of horror and consternation. After taking a few days to let the enormity of the situation sink in, the industry then scrambled to determine its overall exposure.

Initial reports by the *Bermuda Insurance Update* Autumn 2001, published by the IAC Marketing Committee, indicated that the Bermuda insurance and reinsurance industry was to pay a significant share of the ultimate cost of the World Trade Center damage. Early estimates of property and casualty losses from Bermuda companies suggested that XL Capital, ACE, and Partner Re would pay the largest claims. Life insurers were still to be determined. Early estimates of what insurers would pay were as follows—XL US $700 million, ACE US $500 million, Partner RE US $375-400 million, Trenwick US $75 million, PXRE US $35 million, Annuity & Life US $7 million, Everest Re US $75 million, IPC Holdings US $75 million, ESG Re US $1 million gross, Ren Re US $50 million, Max Re US $5 million gross, Scottish Annuity & Life—minimal exposure.[880]

The Bermuda insurance industry was estimated to bear '10.2 per cent of the gross and 7.8 per cent of the net losses, with US $2.2 billion included in year-end 2001 results. XL, ACE, and Partner Re—the companies most significantly affected—collectively have US $1.7 billion in losses, and Overseas Partners, IPC Re, and Trenwick each have at least US $100 million.'[881]

Within weeks of the attacks, rating agencies such as Standard & Poor's (S&P) and Fitch began to issue warnings and watches on many of the world's largest reinsurance companies considering the magnitude of the loss. Bermuda companies—Centre Solutions (Bermuda); Commercial Risk Reinsurance; Hannover Re; Markel; PartnerRe; PXRE, Trenwick (which was already on a negative watch); and XL Capital, excluding XL Capital Assurance and XL Financial Assurance, were placed on S&P's credit watch negative list along with Lloyd's and companies in the US.

Later on Fitch placed ACE, XL Capital and Markel on rating watch negative.

Initial estimates of exposure were upgraded as time went on because of the complexity of the losses coming in. It will take years before the final numbers are calculated for exposures not just in Bermuda but also across the globe and who will ultimately be responsible for paying what. As a consequence, companies in Bermuda began to commence public offerings of shares or filed shelf registrations with the Securities and Exchange Commission (SEC) in the US to reserve the right for public offerings at later dates in order to raise capital to make up for the significantly larger reserves they established in the wake of September 11.

However, shortly after the ratings watches and warnings, the tides began to change for Bermuda. New company formations escalated and Bermuda began to emerge as the place in which

[879] *A.M. Best, Best Wire Services*, 15 August 2002, 'Little Relief Seen from Battered Market that faces Insurers', by David Pilla

[880] *Bermuda Market Digest*, October 2001, 'US attacks costs Bermuda market US $2 billion plus', pp. 1&3 and various articles throughout

[881] *Bermudian Business*, Summer 2002, Eighth Annual Deloitte & Touche Bermuda Insurance Survey 2002, with analysis by Standard & Poor's, 'The Bermuda Insurance Market, Beyond September 11th', by Karole Dill Barkley

to deploy capital effectively. As such, Karole Dill Barkley from Standard & Poor's stated in the 2002 Deloitte & Touche survey—

> 'When people think of 2001, they will always associate it with the devastation of the September 11th terrorist attacks on the U.S.. For the Bermuda insurance market, 2001—particularly the fourth quarter—also marked the unprecedented entrance of more than US $10 billion of new capital to the market, with 63% of it invested in the establishment of six big new companies that were up and writing business by January 2002. The capital raised in Bermuda constitutes roughly 40% of the new capital raised in the insurance industry worldwide in the last quarter of 2001 and represents a new prominence for the market, notwithstanding the continued decline in market operating performance. Bermuda continues to increase its profile as a market of growing prominence for the insurance and reinsurance industry. With increased exposure and recent concerns about offshore jurisdictions, Standard & Poor's expects that Bermuda will face increased scrutiny in the realm of public opinion. The market is undeniably entering a new sphere of influence.'[882]

Silverstein poised for battle with insurers

The shock of the terrorist attacks was soon replaced by the reality of their impact. And one of the most complicated consequences of the attacks came when real estate developer Larry Silverstein, the leaseholder on New York's World Trade Center (WTC), decided to sue his insurers on the grounds that the attack on the World Trade Center was a double event and that therefore he should be able to collect twice on his insurance policy. His lawyers argued that because two separate aircraft flew into the two towers separately the attack should be viewed as two separate events regardless of whether there was only one underlying plan to terrorise the US. His insurers, on the other hand, led by Swiss Re and Travelers Property Casualty and some 20 others, argued that the attacks had only cause and were therefore only one coordinated event, worth only one claim against Silverstein's US $3.5 million property policy. Adding a twist to the whole suit was the fact that the details of Silverstein's property insurance placements were not completed prior to September 11, 2001. Silverstein had only signed his lease on the World Trade Center some six weeks beforehand and was still in the process of finalising the details of his liabilities.

Further complicating the suit was the fact that two different policy wordings were being put forward as the governing policy wording for Silverstein. One was a policy form written by the Travelers, which did not define the term 'occurrence'. Silverstein's lawyers argued that this was the policy on which they expected coverage to be based. There was, however, another form, devised by Willis Group Holdings Inc., which defined the occurrence of a series of related events as constituting a single event. The insurers arguing that this was the governing policy.

Silverstein's lawyers maintained that although the insurers signed the Willis form, it was the intent of all parties that the Travelers form was to supersede all other forms, because it led the insurance program. They argued that it is common practice in the insurance industry for the lead insurer to sets the terms and conditions of the program and for all other insurers to follow behind.

The insurers argued that Silverstein was clutching at straws to get the maximum limits obtainable because he had failed to purchase enough limits to protect himself in the event of a total loss. At US $3.5 billion the limits he had purchased were insufficient to rebuild the towers and to recoup lost rents. Therefore, said the insurers, Silverstein wanted to collect twice because he had underestimated his exposure and as a result was greatly underinsured.

While Silverstein was set to battle with major European and US insurers, ACE Bermuda Insurance Ltd. and XL Insurance (Bermuda) Ltd., became the first companies to settle with him

[882] *Bermudian Business*, op.cit.

because their policy documentation had been completed. ACE agreed to pay $298 million while XL agreed to pay $67 million in order to remove themselves from litigation. According to the *Insurance Journal*—

> 'Howard Rubenstein, a spokesperson for Silverstein, pointed out that the two Bermuda insurers "were the only participants in the insurance program that had signed binders expressly referencing the so-called 'WilProp' policy form and had never been advised of any different form. Unlike the policies, binders or slips issued by the other insurers, the WilProp form includes a special term that defines an 'occurrence' to mean all losses attributable 'directly or indirectly' to 'one cause or to one series of similar causes'."
>
> 'Rubenstein went on to explain that the policy wording put ACE and XL "in a different posture from the other insurers based on the unique circumstances of the placing of their portions of the coverage." He also indicated that the settlement provided for immediate payment of the "single occurrence limits", avoiding a protracted dispute over when payment should be made.'[883]

ACE establishes fund for victims' families.

In the midst of the sweeping changes that occurred in the Bermuda insurance marketplace, ACE Insurance decided to establish a US $5 million fund for the families of the September 11 victims. Brian Duperreault said his company was moved to offer this gesture of compassion by the outpouring of sympathy for the families. He said the company felt compelled to do something because although they did not lose any of their own employees in the disaster, they did lose a lot of friends and they wanted to do something to help.

In addition, ACE assisted 20 New York firemen and friends or spouses to travel to New Zealand to compete in the firefighter games there because the company thought it would serve to take their minds off the loss of so many colleagues at home.[884]

A Meeting with the President of the United States

The global insurance industry knew it could not withstand another terrorist attack on the same scale and remain whole. This was a far-reaching realisation. Ultimately it could affect the world's economic stability, since insurance underpins the ability of companies to operate. Consequently, the President of the United States invited the largest US insurance companies to meet with him and discuss the fate of the industry. Uppermost in his mind was how the industry was going to handle terrorism coverage in the future. Two of Bermuda's major insurers, ACE and XL, were invited. Because of its expansion into the United States, XL had just at that time been in the process of joining the American Insurance Association. It was XL's newly acquired presence in the US that prompted the President to invite Brian O'Hara, President and Chief Executive Officer of XL. O'Hara recalled that the meeting was held on the morning after President Bush had delivered an address to the nation about the attacks. President Bush was still in the same mood as when he addressed the nation—a feeling of urgency descended on the room. O'Hara said the meeting was very intense, as the President was seeking ways to rebuild the confidence of America as quickly as he could. O'Hara said he still gets emotional about the need for such a meeting because for him it was then, as he sat in the Roosevelt Room of the White House, that the gravity of the danger really began to sink in.

The President thanked all those present for not underestimating the significance of the attacks and sought advice from them about the handling of such attacks in the future. It was from this meeting that the concept of a Terrorist Bill was derived to help the insurance industry from going

[883] *Insurance Journal*, 18 February 2002, 'ACE, XL reach accord with Silverstein on WTC Claims'

[884] Interview with Brian Duperreault, 2 December 2002

bankrupt. The industry explained to President Bush that they were not asking the government to bail them out. To which the President replied that he had wanted to see them because he appreciated that they were looking for solutions beneficial to both private and public sectors as well as to the economy as a whole. He said that the insurance industry had taken the first step towards showing goodwill when it agreed not to invoke terrorism exclusions.

O'Hara was doubly moved by the meeting because he had been on the George Washington Bridge in New York and had watched the collapse of the World Trade Centre as it happened—a sight that he said will forever remain in his memory. After having been a witness to the atrocity, O'Hara felt it was a signal honour that he should be invited to the White House and to meet in conclave with the President himself.[885]

Brian Duperreault, Chairman, President and Chief Executive Officer of ACE, also said that it was a great honour and indeed the highlight of his career to meet with the President of the United States. He recalled that the meeting concentrated on how the industry was going to fulfil its obligations in the wake of terrorist attacks. Duperreault said President Bush was engaged and was well aware of the industry's need for some sort of Terrorism Bill. In Duperreault's opinion the industry might never have seen any such Bill, but for the leadership of President Bush.[886]

Terrorism Protection Act, H. R. 3210

In response to a call for help from the insurance industry in the event of a future terrorist attack, the US government came up with the controversial Terrorism Protection Act, H.R. 3210. This Act provided that insurers were allowed to borrow from the federal government to pay terrorism related losses if industry-wide losses were to exceed US $1 billion, or if the industry-wide losses were such as to exceed US $100 million and some part of the losses was to exceed 10 per cent of the capital and surplus and 10 per cent of the net premium of an individual commercial insurer. Once that threshold had been met, the government would lend 90 per cent of the funds needed to cover the losses. Insurers that did not provide commercial insurance before September 11 would not be eligible except under certain circumstances. Insurers would have to repay any government loans received. If covered losses were to exceed US $20 billion, insurers could recoup part of their costs through a premium surcharge of up to three per cent on commercial policyholders.[887]

Initially many were elated by the passage of this bill but the elation soon gave way to anxiety when it was realised that there were many complicating aspects to the bill, including the fact that no one in the US could specifically exclude terrorism coverage. In the US, rates, terms and conditions must be approved at individual state levels before an insurer may pass them on to their insureds. Therefore insurers would have to come up with a price including terrorism coverage that the insurance department of each state in which they wrote insurance would find acceptable. Trying to develop rates that would be acceptable all rounds proved to be problematic for insurers. In addition, the Act was to cover only those insurers domiciled in the US, which immediately put insurers outside the US at a disadvantage by comparison with their US counterparts as the outsiders had no federal backup to assist them in the event of another terrorist attack.

The Act was designed specifically to cover United States companies and does not apply to those companies outside the United States despite the significant United States exposures covered by non-United States companies. This development created a huge discrepancy in the global insurance marketplace as far as covering terrorism was concerned.

[885] Interview with Brian O'Hara, 19 November 2002

[886] Interview with Brian Duperreault, 2 December 2002

[887] *Business Insurance*, 3 December 2001, 'Terror bill draws praise, criticism', by Mark Hofmann and Rodd Zolkos

A place of recourse and recovery

While the insurance industry was reeling from the losses, Bermuda was set to become a major new insurance centre to the world. Some say it has even surpassed the London market in terms of its capital base. More than half of the capacity lost by the Bermuda market to the terrorist attacks was replaced by 11 new insurers starting up on the island. Bermuda appeared to be the only world insurance centre in a position to respond to the shortages of cover as a result of September 11, 2001. Several European insurers led by Munich Re declined to write catastrophe insurance or reinsurance at all in the weeks immediately following the attacks. With capital and surplus exceeding US $135 billion, the Bermuda market was thought to be able to meet all likely claims. The Bermuda market is heavily concentrated in the Property & Casualty area and therefore it will escape the huge life insurance claims likely to arise. *The Royal Gazette* reported on the new companies forming in Bermuda as follows—

> 'As many as 74 insurance companies have set up on the Island in the wake of the September 11 tragedy and the void in insurance capacity that followed. Supervisor of Insurance Jeremy Cox told *The Royal Gazette* that during the last two quarters Bermuda had seen "significant companies establishing significant presence here". Mr Cox continued: "Since September 11 there were 74 companies that formed; a large number of which formed in the last quarter of 2001. These however include all classes of insurance companies and captives."
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> 'As such the companies which have formed would range from single parent captive insurers (class one) and multi-owner captives (class two) to class three insurers or reinsurers with a minimum capital and surplus of US $1 million. And the largest insurance and reinsurance companies falling into the class four category with upwards of US $100 million in capital and surplus.
>
> 'Of those 74 companies the most high-profile start-ups have been the highly capitalised ventures including: Arch, Allied World, Axis Specialty, DaVinci Re, Endurance, Goshawk Re, Montpelier, Olympus and Queens Island.
>
> 'The breakdown of new incorporations through the end of March, according to Insurance Division's records, showed that there were 26 class one and two companies formed, and the greatest volume of formations in the class three sector with 29 new companies. In addition the class four—with capitalisation of more than US $100 million per company—and long-term incorporations stood at 12.
>
> 'In tandem with the surge in new insurance companies has come a significant flow of capital with more than half of the US $30 billion of new capital earmarked for the global insurance and reinsurance industry since September 11 headed to Bermuda, according to a breakdown issued by investment firm Morgan Stanley.
>
> 'Mr. Cox indicated that beyond the steady number of incorporations since September 11, last year was overall a bumper year for insurance incorporations with 108 ventures coming to our shores. Mr Cox said: "We have had three straight years of incorporations greater than 85 or 90 per year. And this year, from what I have been told by (Assistant Director of Insurance) Shelby Weldon, through February we have had better incorporation activity than last year at this time. "Last year we had a total of 108 companies form for the total year, which is the highest number of incorporations, by far, in I don't know how long," he said. But the increase in incorporations is something that Mr Cox sees as evidence of the Island's careful planning in years past. Referring to "sweeping changes" made to the Island's insurance legislation in 1995, Mr Cox said: "What has happened following September 11 has magnified the Island's prominence as an insurance sector but the reason that so many companies have formed here is because the prominence was already there."
>
> 'Mr. Cox added that Bermuda also established an important partnership with the industry some 20 years ago in setting up the Insurance Advisory Committee (IAC). Mr Cox said: "The Bermuda Government formed a committee, the IAC, way back—in the early 80s, which is a committee formed to provide advice to the Finance Minister on insurance related matters. And what is great about the IAC is that a number of key insurance professionals—in various areas of expertise—are a part of that committee, whether it be

the main committee, or various sub-committees," Mr Cox said. Mr Cox added: "The Minister appoints these members every year, and chooses people who have the right level of expertise...Around that table you have people that also have a commitment to see Bermuda be successful, to ensure that Bermuda continues to remain credible. We don't however just sit back and say: 'OK guys you do your thing.' We listen to what they have to say and we get their input, but we are the regulators. We still have to do our job, we still have to be the ones to make key decisions to approve or accept something." Mr Cox continued: "The partnership that we have with the industry is a partnership for progress, but it is not necessarily a partnership for regulation. The partnership has helped to progress the legislation, it has helped to progress the regulatory environment. But we are the regulators...There may be the misconception that the tail wags the dog but that is certainly not the case here in Bermuda," he concluded.'[888]

Later on in the year, three Bermudian insurers coinsured with AIG to rescue the troubled US airline industry from the brink of bankruptcy, after insurers reportedly stated that they would not be willing to insure any airlines, as reported by Roger Crombie in *Bermudian Business* magazine—

'American International Group (AIG) announces that it has completed the placement, on behalf of the co-insurance market, of aviation war risk and hijacking liability coverage totalling $1 billion per airline in excess of the $50 million aggregate provided by the primary aviation market. The coverage offers $150 million in excess of $50 million aggregate and up to $850 million in excess of that $150 million. Co-insurers in the AIG-led $850 million master line slip include Bermuda's ACE, Everest Re and XL Capital.'[889]

The new guys in town

With this new wave of companies came a whole new breed of underwriters. Some were pulled out of retirement, while others came from the major underwriting centres around the world, including seasoned underwriters from Lloyd's. Thus Bermuda was no longer looked upon as the dead-end career posting but rather as a great place to show on a résumé. As a result it was no problem for the start-up companies to find qualified candidates for opportunity. However, getting them settled into Bermuda did present major problems for some of the new companies.

The educational resources and career opportunities in Bermuda were of limited appeal to key personnel that might have children of school age and spouses with professional perspectives of their own. The expatriate community was already stretching the private educational system and to add several hundred more families with children was to place an insupportable demand upon Bermuda's infrastructure. Rents and occupancy costs have risen to a level that makes it difficult for the average Bermudian to find affordable housing, while at the same time the spouses of incoming expatriates are told that they cannot work on the island because Bermudians need jobs.

Bermuda cannot accommodate the needs of working spouses and offer private education to the children of every employee coming to the island without taking something away from its own people, who have the right to the same opportunities. Consequently, the government and the insurance industry are looking for ways to ease the strain by introducing measures that will benefit Bermudians as much as the expatriate community.

The infrastructure of Bermuda is under strain at every level. The international insurance industry is booming but the ancient divide between 'have and have not' is broadening once again, with many Bermudians suffering the sense that they, the original people of this island, have been disenfranchised in this, their own constituency, and priced out of this, their own homeland, by the new 'packaging', the new 'brand name', presentation and promotion of Bermuda as 'the place to be' for whomsoever may aspire to the topmost branches of the international financial tree.

[888] *The Royal Gazette*, 'September 11: A silver lining for our insurers', by Lila Zuill, 30 April 2002

[889] *Bermudian Business*, Summer 2002, 'The Capital Gang, 100 days, 20 billion dollars. How?' by Roger Crombie, pp. 35-51

In only three years, between 1998 and 2001, more than one million square feet of office space was built. The city of Hamilton is no longer distinctively 'Bermudian'. The traditional architecture of the island, in a style that the islanders took for granted, because it was their own creation, and because it was all that they knew—though recognised for generations past by visiting painters of international fame as being unique—has now been replaced by modern office structures, the majority, as usual, being nondescript and of no account, although a few, by the grace and nobility of their design, may last as examples beyond the reach of functionality and passing fashion.

Despite the infrastructural strains in Bermuda, as can be seen from the descriptions given below, those who were recruited from afar to run the new companies on the island after September 11, 2001 were all industry veterans, with extensive worldwide contacts, which enabled them to hit the ground running, so that their companies would be in positions to start underwriting risks immediately. The following descriptions and accounts bear witness that the Bermuda market can no longer be downgraded as attracting unseasoned underwriters. For further details the reader is referred to an article by Roger Crombie in the Summer 2002 issue of *Bermudian Business* magazine, by whose courtesy these extracts are included—

John Charman: A veteran Lloyd's underwriter, Charman began his underwriting career with Sturge Marine in 1971, where he later became an underwriting member in 1979. Since then he held various senior positions at Lloyd's. He was elected to the Council of Lloyd's in November 1995 and was a Deputy Chairman from January 1996 until December 1997. He was also a member of Lloyd's Core Management Group during its reconstruction and renewal, while also serving on Lloyd's Market Board. He first came on the Bermuda scene in 1998 as Chief Executive Officer of ACE Global Markets, when ACE Limited purchased Tarquin PLC. Charman left the island in March of 2001 but his leave did not last long. He was invited back to run Axis Specialty, as described by Roger Crombie—

> 'Friends at MMC Capital track down John Charman, who was in Bangkok when the planes hit the World Trade Center. "We had been talking about setting up a company in mid-2002," Charman says, "but I felt before September 11 that the industry needed one more financial reporting season before we started. You might say we had been meandering towards 2002."
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> '...In New York, Charman shakes hands with Jeff Greenberg and Chuck Davies of MMC and sits down to map out plans to jump-start their meandering idea. "We first set about determining how to raise the capital," Charman says. "It was clear it would take a huge effort, but Bob Newhouse (chairman of MMC and the man who co-founded ACE, XL Capital and Mid Ocean Reinsurance during earlier capacity shortages) and I set about it."
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> '...Axis Specialty announces that it has raised more than $1.6 billion through a private placement of its equity securities and has been licensed in Bermuda to underwrite specialty lines of insurance and reinsurance. "We could have raised much, much more, but had a regard for the best interests of our shareholders," Charman says.
>
> 'The company takes offices on Pitts Bay Road, which it sets up largely as a single space. The internal walls of Charman's office are glass. "Our compelling combination of a substantial, unencumbered capital base aligned with a proven, strong and capable management and underwriting team will quickly position the company as a market leader," Charman says.
>
> '..."It never occurred to me to go any place (other than Bermuda) when we were forming this company," says Newhouse. "Our original target was $1 billion. We began to see the size of the displacement of the business, and the opportunities that would be created as a result of that, and the fact that we had a great number of friends wanting to invest in the company. We then went to a target of $1.5 billion and will close out a little in excess of $1.6 billion."

'Terrorism cover is included by Axis on particular risks. Charman has good experience writing such cover. His goals for Axis include making the company a leading underwriter of terrorism insurance.'[890]

Ken LeStrange: Over 25 years ago Ken LeStrange began his career in the insurance industry at the Hartford Insurance Group. He then moved to Swiss Re as a treaty underwriter. He later became president and CEO of Am-Re Managers Inc., the alternative market operation of American Re, where he worked for 12 years. He then left there to become Chairman and CEO of Aon Corporation's retail brokerage operations for the Americas. Roger Crombie describes how LeStrange came to Bermuda to head up Endurance Specialty—

'…"I was working for Aon," says Kenneth LeStrange. "My business unit was profoundly affected on September 11. We lost 180 employees. We spent the first couple of weeks dealing with trauma, getting the business back up and running." The idea of a start-up was not discussed in those first two weeks. The following week, however, the matter was raised. "There was a healthy scepticism," LeStrange says. "People were interested in what would be unique." A decision was made to develop a business plan for the company that would become Endurance Specialty.

'… The business plan drawn up for Endurance Specialty is approved. Le Strange will head the Bermuda operation. "As events unfolded, it was a good fit with my business background," he says. "The company I worked for before September 11, Aon, was going to be one of the sponsors of the new company."

'Endurance moves to raise its capital. A billion dollars was the minimum threshold at which the business plan would work "in terms of our knowledge of clients and the likely perceptions of the ratings agencies," LeStrange says. " We were aware that many others were out there raising money, too."

'…Aon and Zurich Financial Services sponsor the formation of Endurance Specialty Insurance, a new Bermuda-based insurance and reinsurance company. Plans include capitalisation of approximately $1.2 billion with investments from several parties. LeStrange is named the chief executive officer.'[891]

Anthony Taylor: A Fellow of the Chartered Insurance Institute, Anthony Taylor has over 25 years experience as a recognised lead reinsurance underwriter globally. In 1983 he set up his own nonmarine Lloyd's syndicate, Number 51-A Taylor & Others, with Willis Faber Agencies as his main manager initially. There was later a management buyout by Wellington Underwriting Agencies of which Taylor was a director. Taylor became underwriting director and later chairman of Wellington Underwriting Agencies Limited and deputy chairman of Wellington Underwriting PLC. Roger Crombie described Taylor's decision to come to Bermuda as follows—

'…Anthony Taylor receives a phone call from Benfields. A visit to Taylor's office follows, at which Benfields say they are "thinking about setting up a billion dollar reinsurance company in Bermuda," Taylor recalls, adding: "They had a long list of just one for who would run it." At home that evening, he discusses the idea with his wife, Sandra. The next day, Taylor speaks to Jack Byrne, chairman of White Mountains Group, and the two men agree on a course of action. Taylor then departs on a two-week cruise with his wife and friends, a trip that had been arranged earlier in the year.

'…Meanwhile, half way around the world, Taylor's cruise has taken on a less than relaxing aspect: the creation of a business plan for the company that would become Montpelier Re. "Faxing business plans from Albania was a little unusual," Taylor says, adding as an aside that in the process he racked up the largest mobile phone bill he'd ever heard of. He flies back to London from Venice with his wife and friends. They go home and he flies to New York to present his business plan to the main investor the following day.

'…"We took a decision that meeting to proceed," Taylor says. "White Mountains subscribed for $200 million and we set about raising the rest."

[890] *Bermudian Business*, Summer 2002, 'The Capital Gang, 100 days, 20 billion dollars. How?' by Roger Crombie, pp. 35-51

[891] ibid.

'...On the same day: Montpelier Re announces that it has raised the $1 billion of capital it targeted. "We stand ready to bring the King of Lloyd's to Bermuda," says Byrne, who becomes chairman of the new company, adding: "*The Wall Street Journal* last week called (Taylor) one of the three kings of Lloyd's and we can't figure out who the other two are." Byrne cites Taylor's track record as an underwriter at Lloyd's with the Wellington Management Group, a publicly traded Lloyd's underwriting vehicle. Taylor is to join Montpelier Re in January. The company sets up in the original ACE Building on Woodbourne Avenue.

'...On his birthday, (December 12) Taylor is notified that Montpelier Re's $1 billion has been put in place.'[892]

Michael Morrison: Michael Morrison had worked for over 40 years at American Home Assurance in many different positions, among them President of Commerce & Industry, a subsidiary of AIG, from 1976 to 1978, President of American Home Assurance Company, from 1978 to 1983, and was director of domestic branch operations from 1983 to 1988. He then held the position of Vice Chairman of American Home Assurance, AIG Senior Executive for broker relations and General Manager of AIG's China Division in Shanghai. Since his retirement from AIG in July 1997, Morrison had acted as a consultant to the company. However in 2001 all that changed. He received a call at his home in Maine from Maurice (Hank) Greenberg, the Chairman of AIG. Roger Crombie recounts what happened next—

'...Greenberg explains that AIG intends to start a new insurance and reinsurance company, and that he wants Morrison to head it up. Morrison writes "Bermuda" on a piece of paper and shows it to his wife, Eileen. She smiles, he smiles, and Morrison is on board to lead the $1.5 billion dollar venture that will become Allied World Assurance Company. Morrison had been to Bermuda before—as a child travelling with his British father in 1934, the year before Bermudians formed the first offshore company in Bermuda.'[893]

Paul Ingrey: After spending 36 years in the industry and eventually becoming Chairman and Chief Executive of F&G Re, Paul Ingrey decided to retire in 1996. He enjoyed his retired years but knew that the industry was about to undergo a significant change after the catastrophic events of September 11, so when Bob Clements called him up to offer him the position of Chairman and CEO of Arch Re Ltd., Ingrey did not hesitate in accepting the new challenge. Ingrey said in an interview with Roger Crombie—

'..."I think he had a game plan which included several people and I hope I was the first person on his list... I loved being retired but it just seemed to all come together, A lot of it is that I love to compete, no matter what it is, and I love working with people in this business, and the chance to do both at the same time is just very appealing. The chance to be in Bermuda is a real plus too."

'He adds that Arch has previously formed new companies, and had already gained the necessary approvals. Arch had established a Bermuda company in June, in anticipation of an opportunity following market hardening in the reinsurance sector. "And as smart as some people might think the board of Arch Capital Group are," Ingrey says, "they certainly didn't have this in mind. The market was limping along. It was still a little bit underwater, price wise, in general. Rates were coming up a bit and then we had the worst tragedy that any of us have lived through."'[894]

Adding to the depth of his team, Ingrey brought with him Dwight Evans, formerly Executive Vice President, North American property, for St Paul and F&G Re, Marc Grandisson, Vice President and Actuary of the reinsurance division of Berkshire Hathaway. Later in the year, they also brought on board, Constantine (Dinos) Iordanou from Zurich Financial Services to become

[892] *Bermudian Business*, Summer 2002, 'The Capital Gang, 100 days, 20 billion dollars. How?' by Roger Crombie

[893] ibid.

[894] ibid.

President of Arch Worldwide Insurance and Reinsurance Group (Arch Worldwide)

Sheila Nicoll: The only female and the only Bermudian recruited to run one of the Bermuda companies was Sheila Nicoll. Roger Crombie describes how Nicoll landed the position of President and Chief Underwriting Officer of Olympus Re—

> '…Sheila Nicoll, a Bermudian with extensive industry experience, receives a phone call from Gill & Roeser, financial advisors to the group of investors that is considering forming a Bermuda-based company to write property catastrophe and other short-tail reinsurance lines. Within three weeks, Nicoll will be announced as President and Chief Underwriting Officer of Olympus Re, a $500 million start-up backed by Leucadia National, Gilbert Global Equity and other investors.'[895]

Outsider's view on capital coming into Bermuda after September 11, 2001

According to Robert Hartwig, Senior Vice President and Chief Economist at the Insurance Information Institute in New York, a negative view was cast over Bermuda by the ease with which so much capital flowed there. Many looked askance at the seeming frivolity with which it was possible to deploy such capital into Bermuda and therefore concluded that Bermuda lacked adequate regulation. However it is generally accepted that this capital was as vital to the global and United States industry as it was to the world at large. Were it not for this new capital flowing into Bermuda, the problem of the hard market would have been much worse than it became after September 11, 2001.

The fact that people were willing to invest money in the industry after the worst year ever was a good thing, regardless of where that money was invested. However Hartwig continues that where most insurers failed was in public relations. He says that when major Chief Executives made statements immediately after the catastrophe that the market presented great opportunities to make large sums of money this neither spoke well nor did it bode well for the industry.

Prior to September 11, 2001, there were tremendous underwriting losses as a result of under pricing in the 1990s, of the resurgence of some adverse trends, such as the rapidly rising costs of medical care, workers' compensation, casualty lines, and the increasing proclivity of consumers toward litigation. Many lines of business, such as medical malpractice, were being driven into ruin. Investment income was already slipping prior to September 11, 2001, as the global economy was already one and a half years into a bear market. Rates fell in accordance.

In addition, catastrophe activities were high through the 1990s, combined with the aforementioned trends and, in Hartwig's view, by adding the events of September 11, 2001 a total storm was created. Insurers were left bleeding money and had no way to stop the downward spiral. The global insurance industry was in its worst troubles and Bermuda was able to provide a place in which to regroup.[896]

So what now for Bermuda?

Long before the events of September 11, Maurice R. (Hank) Greenberg, Chairman of the American International Group, gave the following advice on the key to the continued success of the Bermuda market:

> 'The future of the Island depends upon professionalism of the institutions here. Markets have existed for hundreds of years and are always going up and down. There's a market on another island about 4,000 miles from here that came close to losing its identity. Duration of time is not a guarantee of continuation. Professionalism is the only thing that will make a market survive. I think in every market you have those who practice professionally and those who have a ways to go. Bermuda is no exception…

[895] ibid.

[896] Interview with Robert Hartwig, 31 October 2001

'...I think the (Bermuda) market is still new. It's still really untested during periods of great adversity and they will happen just as sure as we're sitting here and talking. Things don't go in a straight line, trees don't always grow to the sky, the laws of gravity have not yet been defied. There will be times of adversity and when they occur, then you test how well that market has behaved.'[897]

Allan G. Murray, Vice President and Senior Credit Officer in the Property & Casualty Insurance Group at Moody's Investors Service, based in New York, and Ted Collins, Managing Director in the Finance, Securities and Insurance Group of Moody's Investors Service, also gave the following advice for the continued success of the Bermuda international insurance industry in an article they wrote for *Bermudian Business* magazine—

'...The challenge for commercial insurers and reinsurers, including those specialty companies operating out of Bermuda, is to resist chasing rates downward, and to maintain reasonable pricing integrity in their core lines while simultaneously refining and developing their strategies. The Bermudian insurance market has historically capitalised on its flexibility and adaptive skills to serve the changing needs of international insurance clients and to navigate market turbulence, as evidenced by its role in the birth of entirely new industries on recent decades: captive insurers in the 1960s and 1970s; finite risk and excess liability insurers in the 1980s; and during the mid-1990— the mono-line property catastrophe reinsurance market.

'These skills will be necessary ingredients to continued success of the market as Bermudian companies look to thrive and expand their horizons despite stressful conditions in traditional markets....'[898]

Following the events of September 11, at the World Insurance Forum on 20 February 2002, Tom Tizzio, President of American International Group, said that the regulation in Bermuda must be viewed in perspective as to how it stabilises the world economy. Bermuda must avoid tying itself to low tax jurisdictions because as it stands it is very proactive and can react quickly to trends happening in the world.[899]

Jim Stanard, Chairman, President, and Chief Executive Officer of Renaissance Re, said that because Bermuda has risen so high on the radar screen in the global insurance industry it faces many external and internal threats. The external threats come from the United States, attacking companies that redomesticate to Bermuda and also tax harmonisation. Even though Bermuda is on the right side of the intellectual argument for companies choosing to domicile here, because of the changing landscape for competition, as a result of the free market, it still faces stiff opposition.

Stanard thinks that the internal threats to Bermuda's dominance in the international insurance arena are far more dangerous than the external threats. He holds that the local community needs to have a better understanding of how important international business is to Bermuda's economy and to its continued prosperity. He thinks that Bermuda does a good job in dealing with the external threats but sees it as falling short when dealing with internal threats that could ultimately damage the island because these will continue to foster a sense of displacement among Bermudians as compared to non-Bermudians.[900]

Bob Clements, 'Father of the Excess Carriers' and Chairman of Arch Re, also stated that Bermuda has the potential to become the keystone of the whole insurance business. However he believes the biggest risks that Bermuda faces are—first, complacency and—second, space. He said that if he was a part of Bermuda's government, he would be working on landfill, to deal with the space problem. And to deal with the complacency issue, he would educate the public in Bermuda

[897] *Bermudian Business*, Fall 1997, 'Greenberg forecasts bright future', by Roger Crombie, pp. 30-34

[898] op. cit., 'Breaking the Mould, Bermudian insurers lock horns in a competitive world', by Allan G. Murray and Ted Collins, p. 44

[899] Tom Tizzio, Speech at the World Insurance Forum held at the Southampton Princess, 20 February 2002

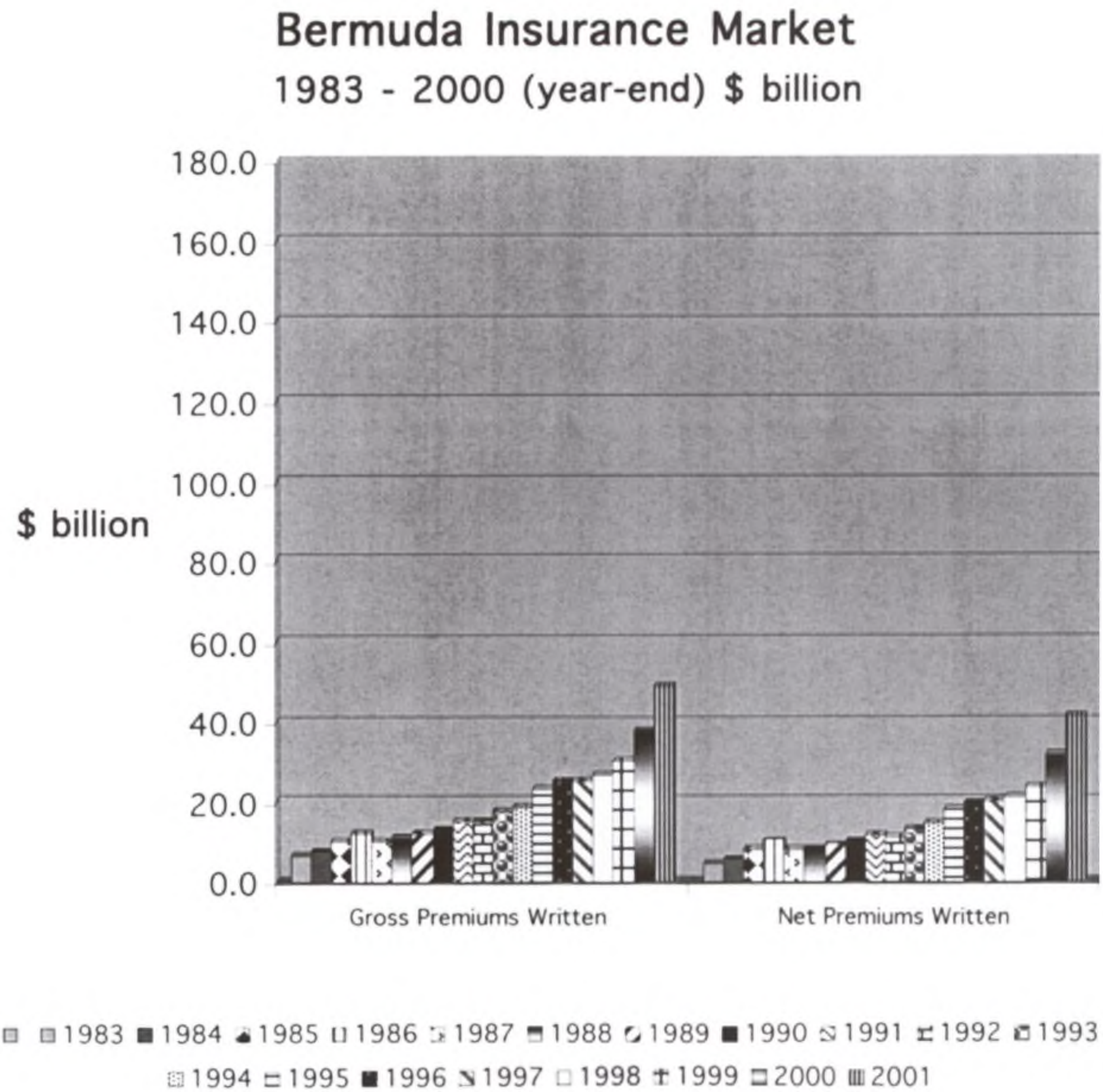
[900] Interview with James Stanard, 4 December 2002

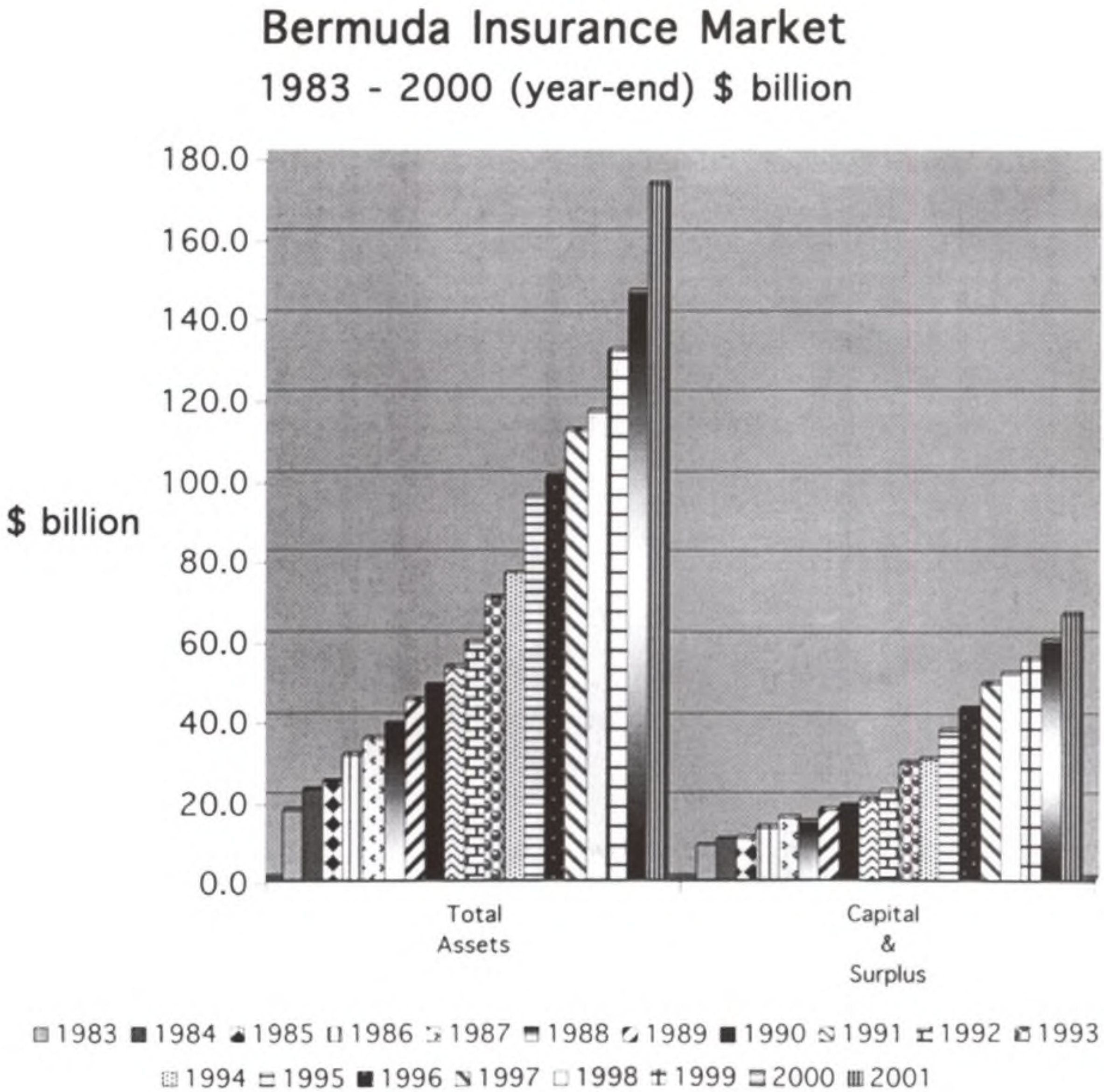
to understand and to value the presence of international business on the island and not to take it for granted.[901]

'9/11', the eleventh day of September 2001, was a turning point in the history of insurance in Bermuda and so it is the appropriate point at which to end this volume. It signifies an end to the way insurance was bought and seen by everyone involved in it; yet sets the stage for the next generation of insurance. The events of that day demonstrated to the world just how interrelated all industries have become, just how interrelated everyone is and just how delicate is the balance of the world's economy.

Bermuda—the island that saw the whole history, from its first exempted company, the Elbon Company, incorporated in 1935, and then the first international insurance company, American International Company incorporated in 1947, to the first "captive" company with Shell International in 1956, to the booming captive industry in the 1970s, to the excess and finite risk carriers in the 1980s, to the property/cat reinsurers in the 1990s, and finally to in excess of US $11 billion in new capital finding its way to Bermuda in 2001—Bermuda has found itself to be the cockpit and testing ground of prototypes throughout every decade of international insurance. As such Bermuda has come to be known as "the microcosm of the global insurance industry", because of the diversity it has been able to assimilate in such a short period of time. Success does not come without challenges. Bermuda is now left to ponder how, if indeed whether, it can continue to accommodate each new change in the international insurance industry without cost unacceptable in the eyes of its people to their heritage, their infrastructure, their culture and their identity. Bermuda is not alone in facing this conundrum. The same dilemma faces every community and every culture in the word, as humanity enters this new millennium. Bermuda is to that extent an archetype of the human story. People came here by accident. They survived by the skin of their teeth. They built something wonderful…

[901] Interview with Bob Clements, 10 December 2002


Bermuda Insurance Market
1983 - 2000 (year-end) $ billion
180.0
160.0
140.0
120.0
100.0
$ billion
80.0
60.0
40.0
20.0
0.0
Gross Premiums Written
Net Premiums Written
1983 1984 1985 1986 1987 1988 1989 1990 1991 1992 1993
1994 1995 1996 1997 1998 1999 2000 2001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Total Assets
Capital & Surplus
1983 1984 1985 1986 1987 1988 1989 1990 1991 1992 1993
1994 1995 1996 1997 1998 1999 2000 2001