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**BERMUDA MONETARY AUTHORITY**

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***Regulatory Update***  
**June 2006**

*(Incorporating Financial Statistics for the  
Quarter ended December 2005)*



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## **(I) REGULATORY DEVELOPMENTS**

### ***a) Banks and Deposit Companies - Capital Adequacy Framework***

The Authority has completed a first round of consultations with banks and deposit companies on draft amendments to its capital adequacy framework. The amendments, circulated to industry towards the end of 2005, provide a detailed treatment for institutions' market risk that is consistent with the amended Basel Capital Accord. The Authority is reviewing comments received from industry and will be circulating a final set of proposed amendments in due course.

### ***b) Investments***

The Collective Investment Schemes Bill, which amongst other objectives, is intended to introduce a licensing regime for fund administrators, has reached the final drafting stage and will be circulated to industry for consultation shortly.

## **(II) LEGISLATIVE DEVELOPMENTS**

### ***a) Regulations for Banking, Trust and Investment Business***

The Authority has completed preparation of draft Regulations pursuant to the recently enacted Bank and Deposit Companies Amendment Act 2005, Trusts (Regulation of Trust Business) Amendment Act 2005 and Investment Business Amendment Act 2005. The Regulations define the precise circumstances that trigger the duties of reporting accountants and auditors to report certain matters to the Authority.

### ***b) Bermuda Monetary Authority Amendment Act 2006***

The consultation process with industry regarding the latest proposed amendments to the Bermuda Monetary Authority Act has been completed. The current proposals generally seek to refine the Authority's internal corporate governance, as well as providing specific changes connected with the proposed introduction of Regulations pertaining to money service businesses. The Bill has been approved by Cabinet and will be laid in the House shortly.

### ***c) Insurance Amendment Act 2006***

Consultation with industry has also been completed regarding the latest proposed amendments to the legislation governing Bermuda's regulatory framework for insurance. The Authority has subsequently completed the drafting process for the Insurance Amendment Act 2006. The amendments enhance the regulatory framework within the context of international standards while maintaining the practical, risk-based supervision that is appropriate to the business conducted in the Bermuda market. The Bill introducing the amendments is due to be tabled in Parliament shortly.

### (III) OTHER DEVELOPMENTS

#### **a) *Jeremy Cox Named Bermuda's Re-insurance Person of the Year***

Jeremy Cox, Supervisor of Insurance, was presented with the Insurance Industry Award for Re-insurance Person of the Year 2005 at a gala reception held in Bermuda on May 20th. The Bermuda Insurance Institute (BII) established the Insurance Industry Awards in December 1998 to recognize the contributions of outstanding individuals whose work or leadership set them apart from their peers. Commenting on his award, Cheryl-Ann Lister, Chairman of the Authority, said, "It is a reflection of the high level of effectiveness, skill and pragmatism that he brings to his role as Supervisor of Insurance. His professionalism and deep commitment to Bermuda are invaluable assets to the Authority and the jurisdiction." This is the first time that this award has been bestowed on a regulator. Mr. Robert Steinhoff, Deputy Chairman of the Bermuda Monetary Authority, also received the Lifetime Achievement Award.

#### **b) *IAIS Global Reinsurance Market Study 2006***

This International Association of Insurance Supervisors (IAIS) Reinsurance Transparency Group-led study, running for its third year, looks at the workings and performance of reinsurance markets worldwide. The 2006 Study will draw on 2005 financial data and involves a specific group of jurisdictions including France, Germany, Switzerland, Japan, the United Kingdom, the United States and Bermuda. Participating companies from these jurisdictions must meet certain criteria outlined by the IAIS. Participation from Bermuda, which has submitted data for all three studies, has increased over the years, from two companies being eligible in the first year to 10 in the second year, and 11 for the 2006 study.

#### **c) *IAIS Captives Issues Paper***

The Authority continues to participate in the development of the Captive Issues Paper. The Paper was initiated to promote a greater understanding of the nature of captive insurance companies among the IAIS Executive and general membership. The Authority has maintained the position that, using a risk-based approach to supervision, distinction should be made between the regulation of captives and commercial insurers, as the vast majority of the former write little or no third-party risk. Further revisions are being made to the Paper in preparation for its presentation and discussion at the IAIS Annual General Meeting in October 2006.

#### **d) *Seminars, Conferences and Publications***

**Jeremy Cox**, Supervisor of Insurance, attended the IAIS tri-annual meetings from February 14th - 17th in Basel, Switzerland.

**Mr. Cox** was also a participant on a panel as part of the World Insurance Forum held at the Fairmont Southampton Hotel in Bermuda from February 21st - 23rd, as well as the Finite Risk Reinsurance Conference held at the Fairmont Hamilton Hotel on March 29th. He was also the guest speaker at the Intermediaries and Reinsurance Underwriters Association Conference which took place in Bermuda on April 3rd.

**Cheryl-Ann Lister**, Chairman and CEO and **Jeremy Cox**, attended the RIMS 2006 conference in Honolulu, Hawaii from April 23rd - 27th.

**William Kattan**, Director, Legal Services and Enforcement, was the guest speaker at the Association of Bermuda Compliance Officers' (ABCO) AGM in February, and the American Bar Association Administrative Law Section Spring Meeting, which took place in Bermuda on April 28th.

**Pat Phillip-Bassett**, Assistant Director, Policy, Research & Communications and **Dianne-Mae Burgess**, Senior Analyst, Insurance, attended the National Association of Insurance Commissioners Annual International Insurance Symposium from February 23rd - 24th.

**Shanna Lespere**, Deputy Director, Insurance and **Afnik Williams-Hyde**, Principal, Insurance, attended the 34th Annual International Captive Insurance Company Association (CICA) Conference in Orlando, Florida from March 8th - 10th.

**Shelby Weldon**, Deputy Director, Insurance and **Suzanne Williams**, Principal, Insurance, attended a conference in Hamburg, Germany entitled Crisis Management, hosted by KPMG Financial Advisory Services from March 16th - 17th.

**Shanna Lespere**, Deputy Director, Insurance and **Dianne-Mae Burgess**, Senior Analyst, Insurance attended the Offshore Group of Insurance Supervisors (OGIS) annual working meeting in St. Lucia from April 30th - May 6th.

**D. Munro Sutherland**, Superintendent of Banking, Trusts & Investments attended a meeting of the Offshore Group of Banking Supervisors in London from March 23rd - 24th.

## **Special Feature – Development of the Capital Adequacy Regime for Bermuda’s Re-Insurance Businesses**

As part of the Authority’s ongoing review of Bermuda’s insurance supervisory framework, consultations are currently underway with the Class 4 re-insurance sector regarding further enhancement of the capital adequacy framework for Class 4 re-insurers.

Such revisions would mark an important refinement in the Authority’s ability to assess the adequacy of capital for its most significant commercial re-insurance sector. However, the minimum solvency margin requirements currently applied to the generality of insurers licensed under the Insurance Act 1978 will continue to apply for all other classes of re-insurers.

The financial stability of several insurers in some of the major markets has been significantly affected over the past few years by deteriorating underwriting results and substantial catastrophe claims. In the coming years leading insurance regulators will be redesigning their insurer capital requirements:

1. The European Union (EU) is replacing its Solvency I regime, where the minimum capital requirement is calculated for general insurers by a formula (expressed as a percentage of gross premium and gross loss reserves, with an allowance for up to 50% for reinsurance). Solvency II is due to come into force in 2010. This regime will be based on a Three Pillar approach comprising: quantitative requirements, supervisory review and disclosure requirements.
2. The United Kingdom has already introduced internal capital assessment standards, where insurers must perform their own individual capital assessment taking into account their risk exposure.
3. The National Association of Insurance Commissioners’ (NAIC) existing risk-based capital model computes a capital adequacy formula used for calculating a company’s minimum capital requirement in the United States.
4. The International Association of Insurance Supervisors (IAIS) will be implementing its own solvency regulation capital standard, a draft to be proposed in mid-2007.

In addition, the recently issued G30 Report has called for the major reinsurance regulatory jurisdictions to further develop requirements for risk disclosure, scenario and stress testing and economic capital analysis as part of a movement towards a harmonized reinsurance regulatory framework.

These worldwide actions will affect regulation in all the major insurance markets. As a significant player in international reinsurance, strengthening Bermuda’s regulation of Class 4 insurers will help to maintain its position in the global marketplace. The regulatory enhancements being proposed for the Bermuda market with respect to capital adequacy are consistent with these global changes in insurance regulation.

When the Authority was last reviewed by the International Monetary Fund in 2003 as part of the assessment of insurance and reinsurance jurisdictions, the Bermuda rules were found to be “observed” with regard to capital adequacy and solvency regulation. It was noted that the solvency margin requirements for large commercial re-insurers were “stringent.”

The current requirements, as imposed by the Insurance Returns and Solvency Regulations, require Class 4 re-insurers to maintain a minimum capital requirement the greater of: 1) \$100 million; 2) 50% of net premium written with a partial deduction for credit for reinsurance; or 3) 15% of loss reserves. The solvency margin requirement applied to Bermuda's Class 4 re-insurers, when originally introduced, compared favourably with the minimum capital requirements for the most significant re-insurance markets. However, although Bermuda re-insurers have shown tremendous resilience and strength there is now a need to incorporate a more progressive method of capital assessment as a function of the particular risk profile of individual companies. The intention is clearly to reinforce further the effectiveness of the Authority's regulatory framework for this business. The Authority's preliminary work therefore took into consideration the following options for introducing new risk-based capital requirements for the Class 4 sector:

1. Adopt a static risk-based based capital formula.
2. Maintain the solvency margin formula but apply an individual company economic capital analysis on top of the solvency margin.
3. Adopt an individual company assessment approach that couples a static risk-based capital formula with a required individual company economic capital analysis, which then becomes subject to regulatory review and adjustment.
4. Create a unique approach that includes a static risk-based capital formula coupled with mandatory stress and scenario testing; a follow on Stage 2 project would be the development of an optional economic capital modeling component that would allow insurers to use internal capital models which they have developed and maintained.

This proposed new measurement framework would continue to represent one facet of the Authority's prudential oversight of the Class 4 sector, supplemented by off-site analysis of financial data and prudential meetings with senior management.

Consequently, the introduction of a risk-based capital approach can be regarded as the next step in the evolution of Bermuda's framework for insurance regulation. Applying this approach, together with the continued roll-out of the Authority's on-site examination programme and the proposed amendments to the Insurance Act 1978 — which include more clearly defined minimum standards for fitness and propriety and new regulatory authority over changes in shareholder control — will serve to establish a more expansive regulatory agenda. The Bermuda Monetary Authority remains fully committed to taking the steps needed to preserve its reputation as a sound insurance regulator, and Bermuda's leadership position as a major jurisdiction in the global re-insurance market.

## STATISTICAL ANNEXE

### BERMUDA MONEY SUPPLY

(BD\$ millions)	2004-Q3	2004-Q4	2005-Q1	2005-Q2	2005-Q3	2005-Q4
Notes & Coins in Circulation*	90	100	93	93	98	93
Deposit liabilities:						
Banks and Deposit Companies (unconsolidated)	3,544	3,558	3,579	3,562	3,510	3,362
	<b>3,635</b>	<b>3,658</b>	<b>3,672</b>	<b>3,655</b>	<b>3,609</b>	<b>3,455</b>
Less: Cash at Banks and Deposit Companies	23	27	26	28	25	40
BD\$ Money Supply	<b>3,612</b>	<b>3,630</b>	<b>3,646</b>	<b>3,628</b>	<b>3,583</b>	<b>3,416</b>
% Growth on Previous Period	<b>1.52%</b>	<b>0.51%</b>	<b>0.43%</b>	<b>-0.50%</b>	<b>-1.22%</b>	<b>-4.67%</b>
% Growth Year on Year	<b>12.14%</b>	<b>10.09%</b>	<b>5.63%</b>	<b>1.97%</b>	<b>-0.79%</b>	<b>-5.91%</b>

\* This table includes the supply of Bermuda dollars only. United States currency is also in circulation in Bermuda but the amount has not been quantified.

### BD\$ DEPOSIT PROFILE - COMBINED BANKS AND DEPOSIT COMPANIES (Unconsolidated)

(BD\$ Millions)	2004-Q3	2004-Q4	2005-Q1	2005-Q2	2005-Q3	2005-Q4
Deposit Liabilities	3,544	3,558	3,579	3,562	3,510	3,362
Less:						
Loans, Advances and Mortgages	(2,752)	(2,865)	(2,942)	(3,079)	(3,281)	(3,368)
Surplus deposits	<b>792</b>	<b>693</b>	<b>637</b>	<b>484</b>	<b>230</b>	<b>(6)</b>
Percentage of Deposit Liabilities Lent	<b>77.6%</b>	<b>80.5%</b>	<b>82.2%</b>	<b>86.4%</b>	<b>93.5%</b>	<b>100.2%</b>



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**COMBINED BANKS AND DEPOSIT COMPANIES FOREIGN CURRENCY**  
**(Consolidated)**

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<u>(BD\$ millions)</u>	2004 - Q3	2004 - Q4	2005 - Q1	2005 - Q2	2005 - Q3	2005 - Q4
Total Foreign Currency Assets	19,252	17,221	19,211	15,621	16,109	18,570
Less: Other Assets	241	284	285	265	285	392
Less: Foreign Currency Loans to Residents	753	850	917	995	1,086	1,154
Net Foreign Currency Assets	18,257	16,087	18,009	14,361	14,739	17,024
Foreign Currency Liabilities	17,324	15,278	17,253	13,517	14,212	16,748
Add: BD\$ Deposits of Non-Residents	161	142	117	124	117	117
Net Foreign Currency Liabilities	17,485	15,420	17,370	13,641	14,328	16,865
<b>Net Foreign Currency Position (consolidated)</b>	<b>772</b>	<b>667</b>	<b>640</b>	<b>720</b>	<b>411</b>	<b>159</b>

Totals may not add due to rounding

**COMPANIES PARTNERSHIPS & PERMITS STATISTICS**

**APPLICATIONS APPROVED  
SUMMARY Q4-2005**

	<b>2004-Q3</b>	<b>2004-Q4</b>	<b>2005-Q1</b>	<b>2005-Q2</b>	<b>2005-Q3</b>	<b>2005-Q4</b>
<b>Exempted Companies</b> (Bermuda companies exempted from the 60% Bermudian ownership requirement)	259	288	248	230	249	279
<b>Exempted Partnerships</b> (partnerships established in Bermuda to carry on business in or from within Bermuda)	13	27	21	32	22	36
<b>Overseas Partnerships</b> (overseas partnerships applying for permits to carry on business in or from within Bermuda)	0	2	3	0	1	8
<b>Overseas Permit Companies</b> (overseas companies applying for permits to carry on business in or from within Bermuda)	5	10	16	7	4	16
<b>Unit Trusts</b>	10	19	11	14	10	46
<b>Continuation Companies</b> (companies from other jurisdictions continuing into Bermuda as exempted companies)	3	11	3	5	7	13
<b>Unlimited Liability Companies</b>	0	1	0	0	0	0
<b>Local Companies</b>	48	53	60	56	50	45
<b>Total Applications Approved *</b>	<b>338</b>	<b>411</b>	<b>362</b>	<b>344</b>	<b>343</b>	<b>443</b>

\* Certain back data have been amended to reflect more up-to-date consent information.

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**COLLECTIVE INVESTMENT SCHEMES STATISTICS**


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	2004-Q3	2004-Q4	2005-Q1	2005-Q2	2005-Q3	2005-Q4
Mutual Funds	785	809	836	849	836	846
Umbrella Funds	72	70	64	67	60	62
Sub-Funds	263	354	378	405	328	315
Segregated Account Companies	26	29	38	45	49	55
Segregated Accounts	137	159	177	247	290	331
<b>Total</b>	<b>1,283</b>	<b>1,421</b>	<b>1,493</b>	<b>1,613</b>	<b>1,563</b>	<b>1,609</b>
Unit Trusts	74	96	100	105	101	105
Umbrella Trusts	69	72	74	81	71	114
Sub-Trusts	82	166	180	227	211	215
<b>Total</b>	<b>225</b>	<b>334</b>	<b>354</b>	<b>413</b>	<b>383</b>	<b>434</b>
<b>TOTAL PORTFOLIOS</b>	<b>1,508</b>	<b>1,755</b>	<b>1,847</b>	<b>2,026</b>	<b>1,946</b>	<b>2,043</b>
<b>TOTAL NUMBER OF SCHEMES</b>	<b>1,026</b>	<b>1,076</b>	<b>1,112</b>	<b>1,147</b>	<b>1,117</b>	<b>1,182</b>
<b>TOTAL NET ASSET VALUE (IN BILLIONS)</b>	<b>\$141.25</b>	<b>\$158.18</b>	<b>\$166.50</b>	<b>\$178.58</b>	<b>\$180.01</b>	<b>\$187.53</b>

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**ADDITIONS TO THE INSURANCE REGISTER**


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	2004 Q3	2004 Q2	2005 Q1	2005 Q2	2005 Q3	2005 Q4
<b>Class 1</b> Single-parent captive insuring only risks of its owners or affiliates of the owners	4	11	2	3	3	4
<b>Class 2</b> (a) a multi-owner captive insuring risks of its owners or affiliates of the owners; (b) a single-parent and multi-owner captive: (i) insuring the risks related to or arising out of the business or operations of the owners and affiliates, and/or (ii) deriving up to 20 percent of its net premiums from unrelated risks	0	4	3	3	3	2
<b>Class 3</b> Insurers not included in Class 1, 2 or 4, such as i) Reinsurers writing third party business; ii) Insurers writing direct policies with third party individuals; iii) Single parent, group, association, or joint venture captives where more than 20% of their net premiums written arises from risks which are unrelated to the business of the owners; iv) Finite reinsurers and rent-a-captives	6	10	6	7	3	15
<b>Class 4</b> Insurers and reinsurers capitalised at a minimum of \$100 million underwriting direct excess liability and/or property catastrophe reinsurance risk	1	0	0	0	0	11
<b>Long-Term Insurers</b> Insurers writing long-term (or life) business	2	5	3	3	1	2
<b>Composites</b> Insurers writing combination of long-term (or life) business and Class 1, 2, 3 or 4 business	1	0	0	0	0	1
<b>Total additions during quarter</b>	14	30	14	16	10	35



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