



A captive audience

It's increasingly recognised by big business as the ultimate risk management tool, but the notion of captive insurance has, so far, eluded the Arab world. Mark Johnson reports.

In fact, insurance in general has never been a hot topic in the region. But, as the entire industry gears up for a push across all insurance fronts, the captives sector is already off the starting blocks.

Captive insurance companies operate in the same way as all other insurance companies — they underwrite risks in exchange for premiums. However, there is one key difference in that a captive is directly owned by the insured party rather than a third party, ultimately making them 'captive' to their owners.

Since the captive is effectively a subsidiary company owned by a large corporation, it is able to retain a sizeable portion of its risk exposures, which is why it is seen as a desirable risk management

tool and is looked upon as an important source of alternative risk transfer (ART). There are tax benefits too, and the premiums paid to the captive effectively become protected capital removed from the company and out of reach of creditors. It's so popular more than half of US Fortune 500 companies now have captive insurance vehicles.

It's not a particularly new idea either. Captive insurance companies, or 'captives' as they are more commonly referred to, have been around for more than 40 years. Moreover, they now number over 10,000, and many of them are located in the current global captives hub, Bermuda, with others spread out across equally exotic locations, such as the Bahamas, British Virgin Islands, Cay-

man Islands, Guernsey, St. Vincent and the Netherlands Antilles.

Bermuda was mainly set up to cater to the US market, but has expanded its activities over time to look after other regions such as Europe, Japan and other developed countries. But as the economies of the Arab world continue to grow, so too, is the need for an alternative hub to serve companies and governments in this region.

Robin Harman, md at HSBC Insurance Brokers (UAE), says this presents a real opportunity for the Dubai International Financial Centre (DIFC): "The segment of captive insurance that DIFC is aiming for is one that is not properly exploited in other parts of the world. The location of a hub in the Middle East would certainly make the administration and management of

Ensurion's Tabbara (*below*): companies can see potential of captives. Artist's impression of the main approach to the DIFC (*right*), which hopes to develop a captives hub.



captive insurance companies far easier, both because of the time zone and easy accessibility. The standards offered by DIFC are also equal to those being offered in other international domiciles."

Currently, though, there is precious little captives business being executed in the Gulf, which means much of the insurance premium that is paid there goes out in the form of re-insurance. To many, this is an unacceptable situation, despite the region's flush supply of cash. With a captives industry, a large amount of the premium can be retained in the region and used towards future economic growth.

Aon is the world's second largest insurance broker. It is also the world's largest captives manager, with some 1,850 captive companies under management. The company believes there is a huge

opportunity for a Gulf captive market and has already started making plans to offer captives within the region.

Massoud Shaheem, CEO Aon Middle East, says it was one of the reasons behind the company seeking a licence from the DIFC: "It is very important that captives are started in the region and we are committed to this. We believe the DIFC will provide the perfect platform and venue for it and we are keen to go ahead with it."

This is echoed by Muzaffer Aktas, managing director of London-based insurance group, Willis, who says the fast growing United Arab Emirates (UAE) metropolis, Dubai, is the perfect location to develop a captives hub to serve the Arab world, and beyond: "I am optimistic Dubai will emerge as a captives centre. Bermuda is very far away, and cannot ade-

quately serve the Arab world. Dubai is located right in the middle of Asia, so is a natural hub for the Middle East, as well as places such as Iran, Pakistan and India".

Willis has a joint venture in Dubai with Al Futtaim, which looks after all the company's insurance and reinsurance activities. Aktas says the company is already looking at how it can serve countries beyond the Gulf. "We are paying a lot of attention to our numbers on the ground in the region. We started with Dubai, but now we are looking at how Dubai can serve Iran, Pakistan and India as well, from our base in Dubai. We are keen to expand our activities in these neighbouring countries."

But there are other contenders lining up. In June 2004, Ensurion became the region's first licensed captive insurance management firm. Ensurion's licence was issued by the Bahrain Monetary Agency (BMA), thus allowing it to start marketing the concept of captives man-

agement solutions to large companies across the region.

The firm's management believes there are strong factors supporting the development of a captive hub in the area. "The Gulf is quite promising as a new hub for captive insurance," says Ensurion director, Marwan Tabbara. "Insurance penetration is relatively low when compared with other developing markets, and while this - under-penetration is more pronounced in retail insurance lines, there is also significant room for growth in the regional commercial insurance market, particularly with the boom in several insurance-heavy sectors such as real estate, oil, petrochemicals, energy, and so on."

He explains that captives offer large insurance buyers the potential to reap significant financial benefits rather than treating insurance as a cost-centre. But perhaps more importantly, they also allow regional firms to customise their coverage, for example excluding hail and flood riders

in a region where these phenomena are rare, or purchasing Islamic insurance products such as takaful or re-takaful, instead of traditional insurance.

"Indeed, some large regional enterprises have already recognised the potential of captives and have invested in them overseas because no domicile has been available closer to home. Having a captive hub in the region would make these mechanisms much more accessible to regional firms, and should help promote growth in the commercial insurance market," says Tabbara.

Moreover, setting up a captives market in the region could lead to greater diversification of Islamic finance within the insurance arena, with sharia compliant or takaful captives emerging.

The insurance industry believes there

are two over-riding factors that make a regional hub — its legal and regulatory infrastructure and its proximity to markets possessing relatively large and developed commercial and/or industrial infrastructures.

According to Ensurion, despite the rapid industrial and commercial development of the region during the past few decades, no comparable insurance centre had begun to evolve until recently. However, that is now changing, and, with international-calibre regulatory frameworks taking shape in the region, many believe the opportunity is ripe.

Tabbara believes there is definitely room for a captive insurance hub in the region, and that many other factors are making it an attractive option. "The current abundance of capital in the Gulf suggests an alternative approach to using internation-

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al re-insurers to finance local and regional risk. Today, only a small portion of insurance premiums paid by firms in the region are retained by their local insurance companies; most are passed along to international re-insurers, most of which are outside the region. Cash-rich firms can instead choose to capitalise local captives, retain more risk in the region, and capture the significant benefits that result. This should help spur the rise of a captive hub in the Gulf."

In addition, he says the current surge in regional growth is driving a need for regionally tailored expertise in enterprise risk management, and this also suggests the need for a regional captive hub. "Several major initiatives in the region in energy, petrochemicals, aluminium, real estate, construction, hotels and leisure, and air and sea transportation have not only come of age, but now also rank among international leaders in their field. Their international profile requires risk management solutions that are harmonised, capable of being centrally controlled, and globally executed. As regulatory frameworks for insurance in the region are being finalised the region is becoming increasingly ready for a captive insurance centre. Furthermore, the emergence of new firms such as Ensurion, the region's first dedicated insurance



Shaheem (**left**): CEO, Aon Middle East - Gulf region needs its own captives market.

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manager specialising in captive insurance, reinforces the fact that the commercial opportunity is indeed a real one."

Just as Bermuda is complemented by a raft of other captive centres clustered off the coast of the US, both Bahrain and Dubai could emerge as complementary centres better able to serve the entire Gulf region and further across the Arab world. To this end, both Bahrain and Dubai have taken positive steps that should help develop the regional market for captives.

The BMA in Manama has invested heavily in the development of a new insurance rulebook, with specific regulations addressing the niche captive market. And the Bahrain Financial Harbour project, with its purpose-built insurance centre should further supplement its captive-

friendly regulatory structure and existing insurance infrastructure with a world-class physical environment.

At the same time, Dubai has seen rapid infrastructure development and international investment, in addition to making a concerted effort to create a financial services hub in the shape of the rapidly growing DIFC.

Because heavy investment has already positioned Dubai as a regional leader in various other sectors (tourism, real estate, aviation and so on), it seems well positioned (next to Saudi Arabia) to be the largest market for organic captive growth.

Moreover, DIFC and the Dubai Financial Services Authority (DFSA) have worked hard to create the legal and regulatory environment necessary to attract a host of financial service segments, including the world's insurance market.

Besides building regulations and promoting investment, a captive insurance domicile will also need to offer a skilled, insurance-specialised labour force. The two contenders for captive hub status in the region have taken different approaches on this front, also.

Bahrain has invested heavily in "home-grown" human capital through institutions such as the Bahrain Institute of Banking and Finance (BIBF). Similarly, Dubai, by attracting human resources from around the world, has now acquired an impressive cadre of financial services professionals, and more are arriving with each month that passes.

Tabbara says there are other conditions that are necessary for captive promotion. "These include liberal exchange controls, relatively free capital flows, anti-money-laundering regulations and a business-friendly tax environment. Since captive insurance companies will need to receive premium payments across borders, pay claims, even to their parent's overseas subsidiaries, will need to adopt local, regional and/or international investment strategies, and repatriate dividends to the parent. Both Dubai and Bahrain have similarly conducive environments on these fronts."

However, there are some issues that the market still needs to overcome. One of the main challenges is to develop an awareness of captive insurance, and communicating the benefits to executives and company boards across the region.

"Today, insurance is viewed by most insurance buyers as a cost-centre. Conveying the message that investing in a captive can turn insurance into a profit-centre instead will not be an easy task," admits Tabbara.

"But we believe it will only be difficult until the first success stories become known. From a nascent form of insurance a few decades ago, captives are now used by over 4,500 enterprises globally. Also, two of the leading international re-insurers active in the London market today started as captive insurance companies in Bermuda some two decades ago. Once regional firms are aware of all that captives have to offer, many of them are bound to find them quite compelling."

Aon, aims to market to the region's largest, most successful companies and government groups, and it, too, realises that awareness is a challenge to be overcome. "You need to go through the process of education, offering seminars, lectures and just getting together with potential clients," says Shaheem. "Eventually they will begin to understand the benefits and will move towards captives, just as it has happened elsewhere."