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Actuaries of the Caribbean

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You say you're tired of the rat race, the long commute, the smog and the weather. Well, why not join the ranks of those actuaries who have left the safety of the shores of the United States, and possibly other homelands, to strike out for a region of the world that was once the habitat of some of history's most colorful characters, including pirates and explorers? Yes, I'm talking about the actuaries of the Caribbean (and Bermuda).

Note that some Bermuda actuaries claim that they are not in the Caribbean. Technically, Bermuda is not in the Caribbean, but since it is an insurance center that has attracted many actuaries, used to attract pirates, has some of the best dark rum I have ever tasted (Goslings) and is subject to devastating hurricanes, for the purposes of this article, Bermuda is in the extended Caribbean. After all, it's one of the pivot points of the Bermuda Triangle.

Who are these adventurers, what have they encountered in this brave new actuarial world, and are they happy in their swashbuckling environment? I am reminded of the Key Largo dive boat operator who wore an earring shaped like a saber running through his ear, a bandanna and a beard; a real pirate. I have obtained one of those earrings but have to figure out how to discreetly get my ear pierced without raising the eyebrows of clients so that I can wear the saber while boating and sailing.

Your author, in search of better diving and sailing locales, has been kicking around the Caribbean for the past several years and also has engaged in some consulting assignments that involved reinsurance companies in the once-dreaded offshore environments. Those of us that have a few years of experience have probably heard horror stories about insurance money disappearing in the Caribbean in the past. We also heard some of the Enron stories about money disappearing in the Caribbean even more recently. In the case of offshore insurance companies, that is no longer the case. We now have

many reputable, highly rated companies ceding their business to likewise reputable, highly rated and highly capitalized offshore companies.

In the process of touring the Caribbean, your author has visited with some of the actuaries of the Caribbean and some offshore insurance regulators in search of the ideal environment for an actuary who likes to play in water.

The actuaries that I visited with were for the most part U.S. expatriates. There are a couple of reasons for these actuaries retaining their U.S. citizenship. One is that they like their U.S. citizenship and the taxes that go with it. The other is that it is extremely difficult for anyone except for the very rich and famous to become a citizen of many of these countries. In one country, the only way, other than being born to existing citizens, was to marry a current citizen and live under the same roof for 10 years. That's a record period of time for many marriages.

What do these actuaries do? For the most part the ones that I met with were busy evaluating

continued on page 38



potential reinsurance deals with U.S. companies. The difference in the methods for accounting for certain liabilities makes it advantageous to cede those liabilities to an offshore environment where the liabilities are accounted for on a GAAP basis in lieu of the statutory methods used for state financial reporting. The assuming company then provides a letter of credit for the reserve credit taken by the ceding company and the ceding company realizes a ceding commission representing part of the difference between the GAAP and the statutory reserves. Two likely candidates for this type of reinsurance are Reduced Paid Up life insurance reserves and Long Term Disability (LTD) reserves. Actually a sizeable portion of the LTD reserves of U.S. companies has already found its way offshore, mostly to Bermuda. Another advantage to ceding the LTD reserves offshore is that U.S. statutory accounting for investments does not make it easy to match assets and liabilities on this business which has extremely long durations. Theoretically, there should be more common stock in the mix. Forget the fact that the market has done poorly recently.

Some of the offshore insurance companies have been set up solely for the purpose of reinsuring U.S. business and earning a profit on the differences in U.S. statutory accounting and international GAAP accounting. Some have been set up to allow wealthy individuals to create self-directed insurance policies with self-directed investments for income tax or estate tax purposes. Others have been established to provide an insurance company structure for a hedge fund or other investment fund. This latter purpose is an outgrowth of some of the tax treaties and allows for the sheltering of hedge fund profits from federal income tax.

The offshore actuary's typical workday begins with a breakfast of the local fruit and maybe a glass of very expensive milk followed by a trip from the company-subsidized dwelling to the downtown office on the motor scooter. The work

attire may be a suit on some of the islands or Bermuda shorts with a white short-sleeve shirt and tie, white socks and dress shoes. Lunch will be at the restaurant with all of the other expatriates, insurance executives, bankers, investment bankers, etc. After a long day at the office, the

actuary might retire to a nearby pub for more quality time with the other expatriates. Often the expatriate actuary will fly back to the states on the weekend since the family did not follow them to the island. The schools are not what we are used to in the states and many expatriates leave the children behind.

As you can imagine, the lifestyles are more limited when it comes to dining and theater. Distance becomes relative since, at times, it only takes 30 minutes to drive as far as you can go on an island.

The pace is a little slower and the temperature a little higher in most of these coun-

tries. The mode of dress is generally casual, but you do find the British influence on a few islands. In at least one of these countries, Cayman, you can find the occasional businessman wandering about on a hot day wearing a full dark suit, which brings to mind the saying about "only mad dogs and Englishmen" going out in the heat of the day. In another country, Bermuda, some actually do wear the Bermuda shorts with the knee socks and, at times, even a tie and a sports jacket along with the combination. Also, in Bermuda, you encounter a stronger British formality in the accepted dress codes in restaurants and on the street. Restaurants are generally casual but they are "smart casual" and the local police will speak to you if you wander around in beach attire while not on the beach. In addition, wearing tennis shoes is a fashion faux pas in Bermuda unless you are actually playing tennis.

Let's not forget the hurricane risk and the more remote volcanic action risk. The hurricane risk has become more well known in the past few years due, in part, to the Weather Channel and

the increased availability of all forms of news and possibly even more as a result of the change in weather patterns caused by El Niño or La Niña which are, in turn, caused by global warming, or so one theory goes. As I was sitting in Bermuda writing my first draft of this article last year, a hurricane was about 400 miles south of me and meandering around. That year's weather pattern caused hurricanes to meander around a lot. The forecasters weren't sure if it was going to hit or not. It was scheduled to hit on the day that I was to leave but, luckily, continued its meandering for another day so I could make it out of town. Hurricanes are such a part of normal life here that one of the local actuaries wasn't even aware that there was a hurricane close by. The previous month I missed Hurricane Debbie by a week when I was in the British Virgin Islands. Debbie may have dispersed over Cuba but it whacked the island that I had been on with 70 mph winds. More recently, when I was in the Caymans, I was caught at the mercy of a hurricane (whose name I forgot) when the airports were shut down. The only option was to sit in the bar and hold a hurricane party as the tidal surge came in and the power flickered on and off. Again, luck spared me the direct onslaught when the hurricane split into two storms, both of which missed the island. The diving was terrible, however, since the fish have more sense and head to deeper water. Some of the underwater stills and video can be seen at my Web site www.sealifepix.com.

So what does the prudent actuary do when weather threatens?

- A) Put your head between your legs.
- B) Head back to the mainland by the fastest route.
- C) Go to the south beach and watch it come in.
- D) Wait it out.

The correct answer, I learned, is D. I've met people who think the correct answer is C. They weren't actuaries, however, and yes, the hurricanes typically approach from the south in the Caribbean and, yes, they did end up in the hospital. Many of the actuaries that I spoke to had not experienced a hurricane. The



recommended approach is to do what people in the Midwest do. During the storm, find the safest place in the house and open the windows facing south to avoid implosion and then after the eye of the storm passes (if this happens in the Midwest, it's too late), close those windows and open the windows to the north. Having spent a bit of time in the Caribbean and the Florida Keys, I raised the question of dealing with the tidal surge, which, we as actuaries know, causes the great majority of deaths in a hurricane. This is an issue that wasn't always well thought out. The risk actually varies with the terrain of the island and the location of your home. For example, the Virgin Islands, which can be visualized as a group of mountainous peaks sticking out of the ocean, are not as subject to tidal surges. Grand Cayman, which is formed on an old coral reef and, where the highest point of the island is about 15 feet, has in the past been literally covered by tidal surges. When you hear about the old disasters that occurred before the current sophistication of storm watching, the large numbers of deaths in the Keys, Galveston and Mississippi were due to tidal surges. However, a few years ago some people stayed around Key West to watch

continued on page 40

a 12-foot tidal surge that occurred during a hurricane. Over 6000 people were killed in the Galveston Hurricane in 1900, most of them by the tidal surge. Camille produced a 25-foot tidal surge in Mississippi and Hugo in 1989 generated a 20-foot tidal surge in South Carolina. A 20- to 25-foot storm surge would completely cover Grand Cayman.

Regarding the volcanic risk, remember, many of these islands were formed by volcanic action. So, if you're on an island that has no hills, you need to worry more about tidal surges. If your island has lumps you need to factor in the volcano risk. One of the islands, Montserrat, was devastated in 1995 by volcanic eruptions.

Another issue is cost of living. When almost everything that we need to survive as 21st-century human beings has to be shipped to the island, you can expect to pay pretty much by weight and volume. Some examples that I was given were \$7.50 for a gallon of milk if you could find it by the gallon and \$12 for a watermelon. Bananas and other island fruit are cheaper, however.

One of the by-products of the higher cost of island living is the higher cost of gasoline and the limitations on the use of automobiles. An example of this is one island where the residents were limited to one car per household. This left other members of the household to either walk or ride around on a scooter. This is not all that bad, unless it is raining. You may also have to take another driver's test and, remember, many of these people drive on the wrong side of the road.

Finding a place to live can also be a problem. In some of the more popular islands, real estate ownership is limited to citizens and, as we now know, that's probably not going to happen for you. This is also an issue in Hawaii. As you can tell, I've been pricing real estate and the prices are actually about the same for Hawaii and the Caribbean—LOTS. So you're typically limited to renting a place that might cost something slightly higher than a place in Manhattan. There are some islands that do allow nonresident purchases of real estate, but there are typically price limits and high taxes or duties associated with this ownership. For example, in

Bermuda, a nonresident can only purchase real estate valued in excess of \$1.7 million and there is a 30 percent or so tax on top of that. The situation in the Caymans is similar except for Cayman Brac, a sister island.

Let's list some of the insurance offices here including Bermuda, Cayman, BVI, Barbados, Turks and Cacos, Grenadine and Panama. Note that Bermuda is apparently a two Letter of Credit (LOC) domicile, which means that you have to buy a LOC to back your reserves in the United States and if you don't have the capital in Bermuda, you need another LOC. This is why some reinsurance companies choose Barbados. Depending on the reigning tax treaties, some islands require two LOCs and some require one. The cost of LOCs has been going up and it is getting more and more difficult to obtain them as banks realize that there is actually a risk associated with these instruments. It is also virtually impossible to obtain one that renews year after year. There are some alternatives to letters of credit including using actual assets, and posting of assets in a U.S. trust equal to statutory reserve credits is becoming more and more common.

These banking and insurance centers were often created initially through tax treaties with Great Britain and have continued through similar tax treaties with the United States and Canada.

The banking lure is the confidentiality of the account holder's identity and information. However, some of this is breaking down in some of the offshore havens. For example, a recently negotiated tax treaty between the United States and the Caymans opens up bank records to the IRS in several years. So, if you have any money there, move it soon. Will this affect the actuaries? Maybe one or two will need to reappropriate assets.

This is just one more example of unusual opportunities for actuaries. You don't have to drink the rum, although I recommend it, and you don't have to wear the saber earring, I'll let you know how that goes, but you do have to know the international GAAP accounting requirements. ☈



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