

Bermuda captive insurers

Briefing Summary: Driven by rising insurance premiums and diminishing property and casualty coverage, beginning in the late 1960s, Bermuda emerged as the domicile of choice for the majority of the world's insurance captives.

Service Area: Corporate, Insurance Law

Sector: Insurance

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At the time, most captive owners (and their advisers) were attracted by Bermuda's perceived economic, social and political stability, its strong infrastructure, its close proximity to New York and a legal system that tended to follow the English common law and provided for an ultimate right of appeal to the Privy Council in the U.K. A series of favourable court rulings, the development of a respected system of financial regulation and the adaptability of the captive concept has contributed to the growth of captives in Bermuda.

A captive insurance company (sometimes also referred to as a limited purpose insurer) is essentially a self-insurance vehicle set up to insure the risks of its parent(s) and/or the affiliates of its parent(s).

The main criteria differentiating a captive insurance company from a commercial insurer is whether the original risks are inwards-facing (that is to say, covering the risks of the company's owner(s), and their affiliates) or outwards-facing (that is, where the company is insuring the risks of unrelated persons with a view to making a profit from its underwriting). Captive insurers cover inwards-facing risks whereas commercial insurers cover outwards-facing risks.

A commercial insurance company that establishes an insurance company to solely reinsure its assumed insurance business is categorised as an "affiliated reinsurer" and is regarded as a commercial reinsurer on the basis that the original risks are outwards-facing.

A captive that insures only the risks of its parent, and its group entities, is known as a "single-parent" captive. To the extent that the single-parent captive insures (or reinsurance – in Bermuda there is no distinction between an insurer and a reinsurer) general business risks (property and casualty), it will be licensed as a Class 1 general business insurer.

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A single-parent captive that writes long-term business (life risks) will be licensed as a Class A long-term insurer.

A captive that is owned by a number of unrelated persons and insures only the risks of those companies and their respective affiliates is known as a "multi-parent" captive. Examples of a multi-parent captives include "agency" captives (which are often formed to enable insurance agents and/or brokers to participate in high-quality business), "association" captives (these insurers are established by industry or trade-associations to meet the insurance needs of their members) and "group" captives (where the captive covers the risks of a group of companies that come together to share risk), among others.

A single-parent captive writing general business consisting of unrelated risks where the premium in respect of which does not exceed 20% of its net written premium, or a multi-parent general business captive that writes no more than 20% unrelated business (by net premium written), is licensed as a Class 2 general business insurer.

A single-parent captive writing long-term business consisting of unrelated risks where the premium in respect of which does not exceed 20% of its net written premium, or a multi-parent long-term business captive that writes no more than 20% unrelated business (by net premium written), is licensed as a Class B long-term insurer.

A single-parent or a multi-parent captive writing general business consisting of less than 20%, and no more than 50%, unrelated business (by net premium written) is licensed as Class 3 general business insurer.

Developing alongside single-parent and multi-parent captives was the rent-a-captive insurer. A rent-a-captive essentially rents its name, underwriting and management expertise and capital to prospective clients in exchange for the payment of an annual fee. Most prospective clients of rent-a-captives do not consider themselves large enough to set up their own captive but wish to avail themselves of the benefits of captive insurance.

Generally, a rent-a-captive carrying out general business will be registered as a Class 3 general business insurer whereas a rent-a-captive carrying on long-term business will be registered as a Class C long-term insurer (note that a long-term rent-a-captive will be licensed as a commercial insurer).

Nowadays, most rent-a-captives operate as segregated, or separate, accounts companies (sometimes also called "cell" companies) where the assets of one segregated account are kept separate and distinct from the liabilities of the rent-a-captive's other clients and the general liabilities of the rent-a-captive company itself (sometimes called the "core"). Should the rent-a-captive, or one of its segregated accounts, become insolvent, an appointed liquidator or receiver is obligated to honour the statutory segregation as between the assets and liabilities linked to the company's segregated accounts and the company's core.

In order to operate segregated, or separate, accounts, the company must either adopt a private act (giving them segregation powers) or be registered under the Segregated Accounts Companies Act 2000 (the "SAC Act"). While originally developed for rent-a-captives, any class of insurer may now register under the SAC Act and operate segregated accounts.

Should you have any questions about setting up an insurance captive in Bermuda, please feel free to contact any member of the insurance team at Carey Olsen Bermuda Limited. We would be glad to answer your questions.

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