Captive Insurance Companies' decision to set up in Malta: A study of the Contributing Factors.

By

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A dissertation submitted in partial fulfillment of the requirements of the Degree of Bachelor of Commerce (Honours) in Insurance at the University of Malta

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Abstract

The Maltese insurance industry has experienced substantial growth over the last 10 years. 10 years ago, the Maltese insurance industry was only made up of local insurance companies. However, over the years Malta has managed to attract a number of insurance vehicles from different countries. The main reason for this growth was Malta becoming a member of the European Union in 2004.

Out of the 57 insurance vehicles, 11 are captive insurance companies. A captive insurance company, also referred to as an “Affiliated Insurance Company” (AIC) is a company which is set up by its parent to insure its risks, rather than insuring them with other third party insurance companies. It is important to note that the insurance managers located in Malta have had an important role in the captive insurance industry’s growth. All the captive insurance companies taking part in this study are managed by insurance managers licensed in Malta. Malta went from having no captive insurance companies 10 years ago, to now having 11 licensed captive insurance companies, some of which include Orlen Insurance Ltd, Falcon Insurance Ltd and Rhenas Insurance Ltd.

This study evaluates the captive insurance industry in Malta. Firstly, some possible reasons for parent companies to create their captive insurance company were determined. Furthermore, the researcher identified the incentives which Malta possesses that attract parent companies into setting up their captive insurance company in Malta.
In order to obtain the captive insurance companies’ views, a number of interviews were conducted with captive insurance companies. It is important to note that all the captives which took part in this study are managed by insurance managers licensed in Malta.

Some of the risks which parent companies have to manage can be quite complex. It was concluded that by creating a captive, the parent company is able to insure these complex risks which would either be uninsured in the traditional market or insured at a high cost. In addition, when there is no claim by the parent company, the premium paid to the captive insurance company would not be lost, as it remains within the company. If the parent company had to insure its risks through a third party, the premium would be lost. This was also considered as an important reason for parent companies to create their captive insurance company.

All the insurance managers interviewed strongly agreed that EU membership is an important incentive in the creation of a captive insurance company. Through EU membership, Malta gained access to the European market and is now able to compete with other countries. Furthermore, the unique Protected Cell Company (PCC) legislation which Malta possesses is also considered by the insurance managers as another important incentive. As explained in the Chapter two, a PCC is made up of a core and a number of cells. The PCC legislation allows a parent company to set up its captive insurance company as one of the cells within the PCC. One advantage for a cell captive is that it is not required to maintain the capital requirements.
The insurance managers interviewed said that Malta’s captive insurance industry has the potential of growing; however, more emphasis must be done on promoting the captive insurance industry. Malta has a good reputation, an approachable and motivated regulator and a strong financial sector. These positive factors can further help Malta in becoming a well-established captive insurance domicile.
Acknowledgements

Firstly, I would like to thank my supervisor Dr. Simon Grima for his help and patience throughout my dissertation and for sharing some of his knowledge, which assisted me during the preparation of this dissertation. I would also like to thank Mr. Andre Farrugia for his opinions and guidance during the early stages of my dissertation and Ms. Jacqueline Micallef Grimaud for her advice and tips. Their guidance helped me during the time of research and writing of this dissertation.

Furthermore, special thanks to my family, especially my brother Mr. Ludwig Vella who supported me throughout the preparation of my dissertation. Lastly, I would like to thank my friends for their continuous support.
# Abbreviations

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<td>AIC</td>
<td>Affiliated Insurance Companies</td>
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<tr>
<td>EEA</td>
<td>European Economic Area</td>
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<td>EST</td>
<td>Eastern Standard Time</td>
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<td>Greenwich Mean Time</td>
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<td>ICC</td>
<td>Incorporated Cell Companies</td>
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<td>IT</td>
<td>Information Technology</td>
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<td>MFSA</td>
<td>Malta Financial Services Authority</td>
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<td>PCC</td>
<td>Protected Cell Companies</td>
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<td>PWC</td>
<td>PricewaterhouseCoopers</td>
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Chapter 1: Introduction
1.1 Introduction

“Malta’s economic stability gives international financial business, valuable and genuine comfort.”

Prof. Joseph.V.Bannister (Curmi & Partners, 2011)

Malta’s geographical position and its contribution as a member of the European Union have played a major role in obtaining one of the best international financial recognition. As a matter of fact, Finance Malta explains how the decision to join the European Union in 2004 and the Eurozone in 2008 have proved to be beneficial for the Maltese economy and Malta’s international relationships. Over the last 10 years, there has been an increase in insurance companies operating in Malta. This can be seen in the graph on the following page. These companies include domestic companies and subsidiaries, whose head office is located in another country. They have recognized the advantages that Malta provides and therefore decided to set up in Malta. (Finance Malta, 2012)
As can be seen in the graph above, before joining the EU there were only 8 domestic insurance companies operating in Malta. However, year after year the insurance industry experienced growth. As at 2012, there were a total of 57 insurance companies operating in Malta. (Finance Malta, 2013)

1.2 The Insurance Sector

The Times of Malta describes the insurance sector as “A unique sector”. This is because of the nature of insurance, where the investment portfolio of insurance companies is based on a long-term risk profile. The management must diversify its investments so as to reduce the
effect of one or two bad investments on the whole investment portfolio. This investment structure helped the insurance industry maintain its growth and survive the financial crisis which hit the world economies. (Galea, 2010)

The Malta Financial Services Authority, which is the single regulator of financial services in Malta, manages Malta's registry of companies. It provides the license for those companies that satisfy the necessary requirements; including insurance managers and insurance companies such as captive insurance companies and protected cell companies. The MFSA serves in the public's and investor's best interest and makes sure that there is compliance with all regulatory standards during their operations. (MFSA, n.d.)

Joining the EU left a positive impact on the Maltese economy. It provided Malta with access to the European market, which introduced further competition that broadened the market for the benefit of customers. Furthermore, the domestic insurance companies had access to other EU member states and could start providing services to other customers in EU member states. This meant a broader customer base for the domestic insurance companies and the ability to widen their market share. Moreover, the increased competition attracted capital towards the Maltese islands, since insurance companies from other EU member states set up their own subsidiaries. (Finance Malta, 2012)

Malta was ranked first by the European Commission in December 2010 for the implementation of EU rules into national law. (Finance Malta, 2012) Once Malta became part of the EU, policies were influenced by the EU regulations and therefore had to be adjusted to cater for the changes. The Maltese legislation had to be modified to be in line with EU
directives. In addition, any developments in the market throughout the last ten years had to be reconciled with the Maltese legislation. This has created the best regulatory framework, which enabled companies to grow and benefit from the opportunities and withstand any economic difficulties that these may encounter. (Finance Malta, 2011)

The following table is a summary of Malta’s rank in the last five years; in terms of how competitive it is, when compared with other countries. This can be found in the Global Competitiveness Reports for the years mentioned below, issued by the World Economic Forum.

*Table 1: Malta’s rank in The Global competitiveness Reports 2009-2013*

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<td>50</td>
<td>51</td>
<td>47</td>
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(World Economic Forum, 2009-2013)

As can be seen, Malta is becoming more and more competitive with other countries, and is heading towards a favourable direction. Furthermore, the diagram below shows the total gross written premium from accession to the EU in 2004 until 2011.
Figure 2: Total Gross Written Premium 2004-2011

As shown in the graph, 2010 experienced a considerable increase in gross written premium, totalling €1.5 billion. In 2011, there was a further increase, with a total of €2.2 billion gross written premium for the year. In fact, Dr Lawrence Gonzi, Malta's Prime Minister at the time, stated that “Malta's financial services sector continues to experience growth even in the midst of the international crisis, and indications show that growth is set to continue.”

(Finance Malta, 2012)

1.3 Captive Insurance Companies

Captive insurance companies, also known as affiliated insurance companies, have also had their share in the Maltese insurance market. A captive insurance company is a company which is set up by its parent to insure its risks, rather than insuring them with other insurance companies. (Finance Malta, 2013) The following graph shows how the total amount of captive insurance companies has increased yearly:
Back in 2004, before Malta joined the EU, there weren’t any captive insurance companies in Malta, but then in 2005, 4 captive insurance companies were formed. In 2012, there were a total of 11 captive insurance companies. (Finance Malta, 2013)

Some of the captive insurance companies located in Malta include:

- Orlen Insurance Limited, which was set up as a subsidiary of Polski Koncern Naftowy Orlen SA in 2006. (Malta Media, 2006) It provides insurance for the company’s risks, which include fire and natural forces, other damage to property, and miscellaneous financial loss. (MFSA, n.d.) Polski Koncern Naftowy Orlen SA, a Polish company, processes crude oil and converts it into unleaded petrol, diesel, heating oil and aviation fuel. (Orlen, n.d.)
• Falcon Insurance Limited, which was set up in 2005 provides insurance cover to its parent company Rio Tinto Limited. (Bloomberg Businessweek, n.d.) Rio Tinto Limited supplies metals and minerals including aluminium, copper, diamonds, thermal and metallurgical coal, uranium, gold, industrial minerals (borax, titanium dioxide and salt) and iron ore. (Rio Tinto, n.d.) Falcon Insurance Limited covers fire and natural forces, other damage to property, general liability and miscellaneous financial loss. (MFSA, n.d.)

• Rhenas Insurance Limited is a subsidiary of RWE AG which is known for its distribution of electricity and gas. (Bloomberg Businessweek, n.d.) (RWE, n.d.) The subsidiary was set up in 2005 and provides insurance and reinsurance covering fire and natural forces, motor vehicle liability, and miscellaneous financial loss. Furthermore, it provides reinsurance, which covers land vehicles, motor vehicle liability and general liability. (MFSA, n.d.)

1.4 Statement of the Problem

Accession to the EU made it easier for international companies to set up in Malta. This helped develop the country’s financial industry into a globalised one. This study looks into the reasons for creating a captive insurance company and the factors that have encouraged international insurance companies to set up their captive in Malta.
1.5 Research Questions

1. What are the main reasons for creating a captive insurance company?
2. Which incentives are considered as being the most important ones, when a parent company decides to locate its captive to Malta?

1.6 Hypothesis

The researcher believes that one of the main reasons for creating a captive insurance company is to allow a parent company to insure its own risk. Some of the risks which a parent company is looking to insure can be complex and are not easily insured in the traditional market. The researcher also believes that insuring risks through a captive could result in a cost reduction for the parent company through lower premiums.

Considering the incentives for setting up a captive in Malta, the author believes that international companies set up their captive insurance company in Malta mainly because of the achievements it has accomplished since it became an EU member state in 2004. This has given Malta an excellent reputation. In addition, Malta’s geographical position is another incentive which the author believes is important.
Furthermore, the tax advantage that Malta offers to both domestic and foreign captive insurance companies is a factor which greatly influences the decision of parent companies. Malta has 64 taxation treaties in place, including all EU member states and the US. The shareholders of the captive insurance companies, whose head office is located in any of the 64 countries, can benefit from the tax system by only being taxed on a small proportion of their income. For this reason, the author believes that the tax system is another main advantage that Malta possesses.

1.7 Thesis Outline

This thesis consists of 5 Chapters which include:

Chapter 1 Introduction – This includes an introduction on the study of this dissertation, together with some statistics of the achievements that Malta has accomplished. Furthermore, the reasons for this study and the researcher’s aims are outlined in this chapter.

Chapter 2 Literature Review – in this chapter a review of the existing literature was carried out. This includes the reasons for international companies locating their captive to Malta and an overview of the benefits for parent companies forming their own captives.

Chapter 3 Methodology – this chapter includes a description of the methodology used throughout this thesis and the procedures followed to collect the data based on the research questions. Furthermore, the tools used in obtaining this data are also found in this chapter.
Chapter 4 Findings and Analyses – this chapter includes the results obtained from the methods used to perform the study and an analysis of the results.

Chapter 5 Conclusions and Recommendations – this chapter includes a highlight of the salient findings and a summary of the methods used to reach these essential findings, an explanation of the answers to the research questions, and whether the hypothesis is correct. Additionally, a brief conclusion and further research recommendations are given in this chapter.
Chapter 2: Literature Review
2.1 Introduction

Malta’s economy has grown over the last 10 years, particularly the insurance sector which has seen increases in insurance business. As a result, Malta now possesses a strong economic structure and a positive international reputation. During an interview with Finance Malta, Dr Lawrence Gonzi said that “Despite the financial and euro crisis, Malta’s diversified economy performs above-average and the country attracts quality business of all sorts”. (Finance Malta, 2012)

This chapter consists of 3 main sections. Firstly, a brief overview of the MFSA is given. Secondly, possible reasons for the creation of captive insurance companies are outlined. Lastly, the existing incentives which parent companies might consider when deciding to set up their captive in Malta are listed.

2.2 The MFSA

The MFSA, which is the single financial services regulator in Malta, was established in 2002. Prior to the formation of the MFSA; the Central Bank, the Malta Stock Exchange and the Malta Financial Services Centre were the financial regulators in Malta. In 2002, a decision was made to have a single regulator for financial services. Five regulatory units were established within the MFSA and these units report to the same board. Therefore, this improved co-ordination and communication within the authority. (PWC, 2012) One of the units which were established was the Insurance and Pensions Supervision Unit, which is
responsible for the supervision of insurance companies, insurance intermediaries, and occupations pensions. (MFSA, 2009)

As Dr. Lawrence Gonzi pointed out during an interview with Finance Malta; “Malta’s regulatory authority has built a strong reputation for attracting quality business and has adopted stringent regulations to safeguard the industry and the country at large.” (Finance Malta, 2012) The MFSA makes sure that there is no abuse in the financial system and that every action taken leads to the improvement in the reputation of Malta and growth in the economy of Malta. The MFSA reconciles together the developments in the market and the rules and regulations to create the best regulatory framework. (MFSA, 2009)

2.3 Reasons for creating captive insurance companies

1. As already mentioned, a parent company would set up a captive insurance company to insure its own risks and for the risks to remain within the company. There are particular risks which are not insured by traditional insurance companies. Traditional insurance companies cover the loss or damage for normal day to day risks, however, other risks such as the loss that a company can incur due to the reputational risk is not insured. To understand this clearly, let’s take an example. A company suffers a major fire and due to the damage, it is forced to stop its operations until the damage on the premises has been repaired and it is safe to resume operations. The company has a business interruption insurance policy in place and can therefore claim for the loss in income that it suffered due to the
temporary pause in operations. However, apart from the loss in income, the pause in operations would also affect the reputation of the company which would in turn affect the sales of the company. Reputational loss is not insured under the traditional insurance and therefore a parent company could set up its own captive insurance company to insure this particular risk;

2. When the parent company and any other associated or group companies pay their premiums to the captive insurance company and no claims arise during the period of insurance, the premiums paid will remain within the group rather than in another third party insurance company;

3. Companies that have big risks can find it unaffordable to insure these risks with traditional insurance companies due to the high premium which they would have to pay every year. If the parent company creates its own captive insurance company, the premium would be lower than when insuring with a third party. Therefore, it would be more affordable for parent companies to insure these risks. In addition, during difficult periods, when the insurance market is going through a tough phase, the insurance premiums charged by traditional insurance companies tend to increase. However, with a captive insurance company the effect on the premium would be minimal since the captive is only insuring its parent;

4. The premium paid by the parent company can be invested and the return would be reserved and used in the event of a major future loss;
5. Since the captive insurance company is owned by its parent and it is insuring its parents’ risks, the parent company can increase its control over the risk and minimise the exposure. (Finance Malta, 2013) (Coverforce, n.d.)

2.4 Incentives for setting up in Malta

2.4.1 Law

One of the most important factors that led to Malta developing into a leading financial centre is its legal and regulatory framework. Roman law was the primary law on which Malta’s legal system was based on. However, as time passed and Malta was ruled by the British, Malta’s legal system evolved into Common Law. When Malta became part of the EU, the legal system had to be adjusted to meet the EU requirements. Although the legislative and regulatory framework is geared towards accessibility and flexibility, it still has the capability of safeguarding the interests of investors and strengthening national and international reputation. (MFSA, n.d.)

Furthermore, the insurance industry follows the Insurance Business Act and the Insurance Intermediaries Act. Any person or company carrying on the business of insurance must always follow the provisions found in these acts. The Insurance Business Act regulates insurance companies including captives. The Insurance Intermediaries Act regulates the insurance channels which include insurance agents, insurance brokers, insurance managers and tied insurance intermediaries. These are two important acts which form part of the legislative framework for captives in Malta. (MFSA, 2006) (MFSA, 1998)
2.4.2 Language

Being ruled by the British had a great impact on the language system in Malta. English language is taught from a very young age. Maltese and English are the official primary languages in Malta, however, English is the language used in the business sectors. This is a great advantage since English is considered as the international language. Therefore, most graduates possess well spoken English skills to cater for the international relationships that most insurance companies have. (PWC, 2012)

2.4.3 Education system

Malta has a strong education system which is continuously being improved to provide the best education for those who are willing to learn, especially the younger generation which are the ones who will be managing in the future. Malta’s education system provides a skilled and efficient work force with the motivation to work hard and be successful. The government is continuously investing in the education system so that students will have different options and opportunities. (Finance Malta, 2011)

2.4.4 Geographical Position

Malta’s geographical position has also had an effect on its growth and international reputation. Being in the middle of the Mediterranean Sea provides access to the well-developed and developing European markets such as England, Germany, France and Italy,
and also access to other emerging markets in North Africa and the Middle East. In addition, Malta’s time is an hour ahead of Greenwich Mean Time (GMT) and six hours ahead of US Eastern Standard Time (EST). Although Malta is six hours ahead of one of the biggest economies in the world, this has not had an effect on the international relationships with the US and other close countries. (KPMG, 2011)

2.4.5 Information Technology

Malta possesses a sophisticated IT infrastructure. With the advance in technology and the increased dependency on the internet, an efficient IT system is essential for every insurance company. The internet is a popular distribution channel and setting up a website with updated and complete information and access to online sales has led to success. (Finance Malta, 2011)

2.4.6 Passporting Rights

The biggest benefit that came with accession to the EU was that companies in EU member states can set up their captive in any other EU member state without the need for further authorisation. However, the law requires authorisation to have been given by the competent authority in that specific company’s member state and the competent authority of the country in which the captive will be set up, in this case Malta, will be subject to notification. This is found in the “Single passport” directive which came into force in April 2002 and was introduced in Malta in 2004, when it became an EU member state. Passporting can be of two types, which are passporting by freedom of service and freedom of establishment.
Considering freedom of service; in this type of set up the insurance company will only provide services to other EU member states. However, freedom of establishment is when an insurance company sets up in Malta and sells to the Maltese people. Therefore, a captive whose roots come from an EU member state and is seeking to set up in Malta can benefit from this. In addition, the aim of this directive is to stimulate investment in EU member states and to provide protection to those companies who do decide to set up in other EU member states. (PWC, 2012) (Velentza, 2006)

2.5.7 Insurance Managers Availability

The insurance managers sector is also a growing sector in Malta. There are 15 insurance managers licensed by the MFSA and amongst them there are big international insurance managers such as Marsh, Aon and Willis. Insurance managers offer their services to companies which are interested in starting their operations in Malta such as captive insurance companies. The insurance managers can assist new companies in obtaining their license and they can also offer their experience to help new companies familiarise themselves with the law and regulations. (Finance Malta, 2013)

2.4.8 Tax

Malta’s accession to the EU introduced a number of tax incentives. The primary purpose of such tax incentives is to attract foreign investment. The tax incentive in Malta is the Tax Refund System, also referred to as the Double Tax Treaty. In Malta, the tax rate on the income a company makes is 35%. After the tax is deducted, the balance is distributed as
dividends to the shareholders of a company. Furthermore, the income in the form of dividends of the shareholders is then taxed again and the rate depends on the total income of that particular shareholder. However, shareholders are entitled to claim a refund on the tax initially paid by the company before distributions were made. The general rule is that the tax refund amounts to 6/7 which is equivalent to 30% of the amount paid by the distributing company. So, the tax borne in Malta is equivalent to 1/7 of the 35%. It is vital to point out that not only local captives are able to benefit from this tax incentive but also captives operating in Malta, whose parent company is in another country. Malta is in agreement with 64 countries regarding the Double Taxation Treaty. This can be seen in the table below. Such agreements include all EU member states (in blue), the US (in red) and other countries (in white). Therefore, this is one of the main benefits that could attract parent companies to set up their captive in Malta. In addition, this tax system has been one of the contributors towards the well-developed insurance industry that Malta has developed. (PWC, 2012) (Cap Stone Group, n.d.)
Table 2: Double Taxation Treaties

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(MFSA, n.d.)

2.4.9 PCC Structure

Malta is the only EU Member state that allows the formation of PCCs (Protected Cell Companies) and more recently ICCs (Incorporated Cell Companies). Atlas Insurance, a local underwriter was the first PCC which converted back in 2004. Aseria Life International PCC and AON's White Rock Insurance (Europe) PCC followed Atlas Insurance and registered as a PCC. Malta’s unique legislation allows companies including captive insurance companies to convert into a PCC or an ICC. This important structure makes it attractive for parent
companies from other EU member states to set up their captive insurance company and benefit from the ability of forming a PCC or an ICC locally, as long as the requirements are present. (Finance Malta, 2011)

A PCC is made up of a core and a number of cells. However, the PCC is a single legal entity and all its cells form part of this same legal entity. The PCC as a whole is required to maintain the capital requirements, while the cells of the PCC are not required to maintain the capital requirements but they are required to maintain an amount which enables them to protect their risks. A PCC enables different owners with different interests to be part of the same PCC by establishing a cell. When the captive converts into a cell within a PCC, it would be called a captive cell company. (Deloitte, 2011)

Other insurance vehicles which are not that experienced in the market can benefit by establishing a PCC cell and gain from the experience of its cell company. So if for instance, a parent company situated in France wants to set up its captive in Malta, it can purchase a cell within a PCC and set it up as a captive insurance company, instead of a standalone captive insurance company. Furthermore, a cell within a PCC can use the core non-cellular assets of the PCC. For example, if third party claims cannot be satisfied through the cellular assets of the cell, third parties have the right for compensation from the non-cellular assets of the core. In addition, a captive within a PCC can use the skills and expertise of the core which would have been set up in Malta for some years and therefore would be experienced. (Finance Malta, 2012)
There has been an increase in insurance managers in Malta over the years. Some well-known international insurance managers that have located to Malta are AON, Marsh and Willis. This shows how capable the Maltese insurance industry is. Malta offers the opportunity of establishing an insurance manager within a PCC. So, if the core is a Captive Cell Company or a captive cell company is operating through a cell within a PCC, and another cell within a PCC is an insurance manager, the services of the insurance manager could cater for the core and other cell’s specific administrative and operating needs. The existence of an insurance manager cell within the PCC would be essential for parent companies situated in a different country which are setting up their captive in Malta. Parent companies located in other countries could have a different culture, political structure and different rules and regulations. The lack of knowledge regarding a specific country creates risk, which if not handled well could lead to considerable financial loss. Thus, the existence of insurance managers would be useful for the captive insurance companies to fit in. (Finance Malta, 2012) (Finance Malta, 2012)

2.5 Conclusion

The resilience during the financial crisis, which hit a significant number of world-wide economies, shows the strength of the Maltese economy. The financial crisis affected most economies; however, there were minimal effects on the Maltese economy. This highlights the importance of the MFSA as a single regulator, which kept a close eye on the state of the economy at the time to make sure that this would not harm the reputation of Malta and the international relationships that Malta has. This shows how efficient and trustworthy the MFSA is and how it makes sure to make all decisions in the best interest of Malta. Given
Malta’s innovative regulation and presence as an EU member state, this growth is set to remain. (Finance Malta, 2012)
Chapter 3: Methodology
3.1 Introduction

This chapter outlines the research methodology used throughout this study. The purpose of this study is to determine the reasons for the creation of a captive insurance company and the existing incentives for parent companies to set up their captive insurance company in Malta. This chapter outlines the methods used so that any other researcher can replicate the research and test it for viability. This chapter includes:

- The method used to collect data;
- Reasons for choosing this method;
- The limitations of this study; and
- Ethical issues of this study.

3.2 Research Design

The research design can be associated with a set of procedures followed while collecting data. The research design is divided into two approaches, which include the qualitative and quantitative approach. In a qualitative research approach, the researcher performs an in-depth investigation to achieve an understanding of the research questions from the perspective of other parties. This approach uses a small number of participants. On the other hand, in a quantitative approach, the researcher uses statistical techniques to achieve an understanding of the research questions by addressing a large number of participants (Rhodes, 2013).
3.2.1 Multi-methodology approach

For this study, a multi-methodology approach was used, where the quantitative and qualitative approaches were integrated together. This approach was most suitable for collecting data for the research questions of this study. (National Institutes of Health, n.d.) It enabled the researcher to obtain an understanding of the perceptions of captives regarding their setup and licence in Malta. Interviews were conducted with the captive insurance companies, which have located to Malta. A thematic approach was applied to analyse the data collected. This approach included identifying patterns within the data collected and classifying them into categories. The thematic approach was essential in outlining the captive’s opinions in connection with the research questions and enabled the researcher to reach a conclusion. (Braun & Clarke, n.d.)

3.3 Data Collection

The collection of data is divided into 2 forms; the primary data and secondary data. Primary data is data collected through interviews and other original sources. On the other hand, secondary data refers to data which has been published by another party.
3.3.1 Primary Data

For this study, the primary data was collected through interviews with captive insurance companies in Malta. The interviews addressed the reasons for setting up as a captive, and for selecting Malta as the location for their operations.

3.3.2 Secondary Data

The secondary research for this study included information gathered from electronic sources, and books and reports published by Finance Malta. Such information also included published statistics, such as the total number of insurance companies and the number of captive insurance companies in Malta.

3.4 Research Tools

3.4.1 Interviews

Interviews were conducted with a number of captive insurance companies, which have located to Malta, to capture their opinions regarding this study. The interview questions were structured using a Likert scale, which enabled the researcher to easily and accurately analyse the data.
Interview questions can either be open-ended or closed-ended questions. Open-ended questions are those which allow the respondent to express his/her opinion regarding the subject in detail. On the other hand, closed-ended questions are those questions which require only an answer in the form of one sentence or one word. Since a Likert scale was applied to most of the interview questions, closed-ended questions were used. However, there was an open-ended question which allowed the respondent to add any comments regarding the study. This allowed flexibility and enabled the researcher to get a better understanding of the views of captive insurance companies. (Media College, n.d.)

The captive insurance companies which took part in this study are all managed by insurance managers licensed in Malta. Some of the insurance managers manage more than one captive insurance company. Two of the insurance managers manage one captive insurance company each, one of the insurance managers manages two captive insurance companies and another manages six captive insurance companies. The captive insurance companies which took part in this study include:

1. Werla Insurance Company Limited
2. Pembroke International Insurance Company Limited
3. Falcon Insurance Limited
4. AarhusKarshamn Insurance Malta Limited
5. Ergon Insurance Limited
6. Nautilus Indemnity (Europe) Limited
7. Olen Insurance Limited
8. Rhenas Insurance Limited
9. Bluebird Reinsurance (Europe) Limited
10. Palatina Insurance Limited
3.4.2 Pilot Study

A pilot study was carried out with the tutor before conducting the interviews. This was done to ensure that the questions were valid and in connection with the study. Furthermore, a pilot study led the researcher to changing the structure of some of the questions to make them clearer and easier to analyse in the next chapter.

3.4.3 Sampling

For this study, a non-probability sampling approach was used. Since the study is about determining the reasons for the creation of a captive and the existing incentives for parent companies to set up their captive insurance company in Malta, captive insurance companies located in Malta were chosen to take part in this study. Every captive insurance company could have been a part of the study; however the sample size depended on the feedback received by the captives. In addition, the researcher’s aim was to try and maximise the number of respondents to get a better understanding of the captives’ views regarding this study. In non-probability sampling, reliability cannot be measured; however, the comparison between the primary data collected and the secondary data found gave an indication of how reliable the data collected was. (Statistics Canada, n.d.)
3.5 Ethical Considerations

Ethical considerations refer to the steps taken to ensure that the study did not harm any person taking part in it. An informed consent form was sent to the captive insurance companies to inform them about this study and to ask whether they were willing to participate. During the interview, it was also pointed out that their right of privacy was respected.

3.6 Limitations

3.6.1 Interviews

A limitation of this study was that some of the interviewees had limited time allocated towards the interviews. Furthermore, another limitation of this study was that the captive insurance companies which took part in this study were all managed by insurance managers located in Malta. Since all parent companies are not located in Malta, it was not possible for the researcher to conduct interviews with parent companies.

3.7 Conclusion

The research design and research tools, and reasons for choosing such research design and research tools were described in this chapter. The main purpose of this chapter is to give an overview of how the data was collected from captive insurance companies. The data
collected was analysed and discussed in chapter 4, while the results were linked to the literature review, the research questions, and the hypothesis in chapter 5.
Chapter 4: Analysis and Results
4.1 Introduction

The purpose of this study is to determine the reasons for the creation of a captive insurance company, and the existing incentives for parent companies to set up their captive insurance company in Malta. Interviews were conducted with a number of insurance managers located in Malta, which manage the captive insurance companies that took part in this study.

Through this chapter, the researcher was able to analyse the opinions of the insurance managers which manage the captives located in Malta. Every incentive for creating a captive insurance company and for locating the captive to Malta was looked at individually. Firstly, the results of the interview questions were combined into one graph. Then any additional comments made by the insurance managers regarding the importance of such incentives were also compared.
4.2 Interview Results & Analyses

A set of questions were asked and the following results were obtained:

4.2.1 Question 1

How long has the captive insurance company been licensed in Malta?

The table below shows the captive insurance companies included in this study, together with the registration date of each captive:

<table>
<thead>
<tr>
<th>Captive Insurance Company</th>
<th>Registration Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Werla Insurance Company Limited</td>
<td>2012</td>
</tr>
<tr>
<td>Falcon Insurance Limited</td>
<td>2005</td>
</tr>
<tr>
<td>AarhusKarlshamn Insurance Malta Limited</td>
<td>2010</td>
</tr>
<tr>
<td>Pembroke International Insurance Company Limited</td>
<td>2009</td>
</tr>
<tr>
<td>Ergon Insurance Limited</td>
<td>2005</td>
</tr>
<tr>
<td>Nautilus Indemnity (Europe) Limited</td>
<td>2005</td>
</tr>
<tr>
<td>Orien Insurance Limited</td>
<td>2006</td>
</tr>
<tr>
<td>Rhenas Insurance Limited</td>
<td>2005</td>
</tr>
<tr>
<td>Bluebird Reinsurance (Europe) Limited</td>
<td>2010</td>
</tr>
<tr>
<td>Palatina Insurance Limited</td>
<td>2008</td>
</tr>
</tbody>
</table>

Table 3: Captive’s registration date
The registration dates show that EU membership had a great impact on the setting up of captive insurance companies in Malta. In the first year of EU membership, there were 4 captives set up in Malta out of the 11 captives which have located to Malta so far.

It was also noted that one of the insurance managers manages more than 50% of the captives located in Malta. This insurance manager was one of the first insurance managers which helped Malta in locating its first captive insurance companies.
4.2.2 Question 2

Do you agree that Malta is an ideal location for setting up captive insurance companies?

Out of the four respondents, three strongly agreed and one agreed that Malta is an ideal location for setting up captive insurance companies. Malta is the fastest growing domicile in the EU. There are other countries which have similar captive legislation such as Dublin and Gibraltar. However, Malta has an advantage over other domiciles since it also provides other incentives which complement the captive legislation; most importantly the PCC legislation and the tax benefits.
One of the respondents added that Malta is reacting slowly to market changes. There was a time when Malta was very efficient, however recently this is not the case. A reason for this possible delay could be the fear of facing unforeseen situations which could lead to bad decisions being made, and a negative effect on the captive industry and possibly the insurance industry as a whole.
4.2.3 Question 3

The following are possible reasons for creating a captive insurance company. In your opinion, please tick according to how important each reason is:

To insure its parent’s risk

Three respondents strongly agreed and one respondent agreed that the creation of a captive insurance company is important to insure its parent's risks. Further comments which highlight the reasons specified in the literature review were that when one creates a captive, the risk is not being transferred as such. It is true that a policy is issued but the risk still
remains within the group. Parent company’s risks could be unique and complex. Therefore, through the creation of a captive, the parent companies can cover their specific risk and avoid certain costs, such as administration costs, which would have been incurred if the risk was transferred to a third party.

*For the premium to remain within the company*

![Bar chart showing the distribution of responses to the question of whether the premium should remain within the company.](image)

*Figure 6: Premium to remain within the company*

Again three strongly agreed and one agreed that the creation of a captive insurance company is important for the premium to remain within the company. Instead of paying the premium to a third party, the premium is paid to the captive insurance company, which means that it is kept within the company. If there aren’t any losses, the premium can then be
invested to make a return. The MFSA, which is always in talk with the parents of the captives and the captives themselves, keeps a close eye on the financial position of the captive, which includes the investment portfolio and the available resources. The MFSA would want the captive to insure its premium in a number of different investments, since if the entire premium is invested in one investment, and that investment performance turns out to be bad, then there will not be a return, and the premium may also be lost. For this reason, diversification is essential so as to minimise the chance of losing the entire premium through a bad investment. Only a part of the investment portfolio would be affected and the rest would receive a healthy return. If money is deposited in a bank, the MFSA would make sure that the money is not only invested in one bank but with more than one bank, say three or four banks. The rating of the bank is also considered because this shows how safe the deposits really are.
Two respondents strongly agreed and two respondents were neutral about whether the creation of a captive insurance company is important for lower premiums. The respondents who were neutral added that lower premiums might be a possible reason but it should not be the main reason. In most cases, lower premium is something which develops with time. When you have an entity starting from scratch, it will use the market rates. With time it will be building history, loss ratios and reserves, and it would be able to lower the premium. In some situations, rather than lower premiums, the cover would be tailor-made according to the company’s needs. If one had to look for the risk in the traditional market, the cost might be higher. In this case, it could be a lower premium.
The respondents who strongly agreed added that the benefits are that premiums are decreased overall for the group, and the premium remains stable year after year to avoid fluctuations. The insurance market is like a cycle, where it softens and hardens. When there are few insurance companies, there tends to be high profits. Other insurance companies are attracted to the market and the prices have to be lowered since there is an increase in competition. After some time, some companies will find difficulties in paying out claims since prices are too low, and therefore would have to shut down. This would again lead to few insurance companies making high profits. Therefore, due to this cycle, there would be fluctuations in the premium charged. Some companies would prefer to set up their own captive insurance company to minimise these fluctuations. Furthermore, with the set up of captive insurance companies, the premium is likely to remain stable, which would allow the parent company to plan an insurance budget.
One respondent strongly agreed, while three respondents agreed that the creation of a captive insurance company is important to reserve the investment returns, which the captive insurance company receives by investing the premium it made. However, it was added that at the moment some companies do not really and truly consider the return. If a company has 10 deposit accounts, the return would be about 0.5%, whereas if it was six or seven years ago, the return would have been about 6% or 7%. So it is a completely different reality today. Furthermore, it was added that the return on investment would be useful for any future big losses such as catastrophes.

*Figure 8: To reserve investment returns*
For the parent company to have an increased control over its risk

Three respondents strongly agreed, while one respondent agreed that the creation of a captive insurance company is important for the parent company to have increased control over its risk. As already mentioned, insuring the parent’s risk through a captive insurance company is not exactly a way of transferring risk, since the risk is still considered to remain within the company. When a parent company insures its risk through a captive insurance company rather than through the traditional market, it is considered to still have control over its risks. Captive management is one of the risk strategies that are in place for a company to cover its risk. When the parent company sets up a captive insurance company, it has to make sure that it sets it up with enough resources to back its liabilities in the case of a big
hit. It has to make sure that the captive can compensate the parent company for any claims which it may incur. To a certain extent, the parent company still has control over the risk since it needs to keep an eye on the captive to make sure that it is being managed well.
4.2.4 Question 4

The following are possible incentives for setting up a captive insurance company in Malta. In your opinion, please tick according to how important each incentive is:

Geographical position

One respondent strongly agreed, while three respondents were neutral on whether Malta’s geographical position is an important incentive in the creation of a captive insurance company. The respondent who strongly agreed added that Malta’s position is an advantage, and captives with a parent company located in the US did not let the distance discourage
them. Malta has good flight connections that also makes it easier for parent companies. On the other hand, the respondent also added that when managers from the parent companies have to attend board meetings in Malta, there is quite a distance between Malta and the US, which is time consuming.

Furthermore, the respondents who were neutral added that nowadays, the geographical position of a country such as Malta does not make a lot of difference. For example, if the tax system in Malta is an advantage, a French company seeking to locate its captive in another country because it is more advantageous than setting it up in France wouldn't locate to Luxemburg, but would still consider Malta, even though Malta is not as close to France as Luxemburg is.
One respondent strongly agreed, two respondents agreed and another respondent was neutral on whether Malta’s tax system is an important incentive in the creation of a captive insurance company. The respondent that strongly agreed added that the tax system in Malta is very advantageous since the tax borne is equivalent to $\frac{1}{7}$ of the 35% tax charged on the profit that a company makes. The respondents who agreed that the tax system is an important incentive added that some companies actually stay away because they might be seen trying to get tax arbitrage or tax reduction in the tax bill by setting up in countries with an advantageous tax system.
Furthermore, the respondent that was neutral towards this incentive added that parent companies decision on where to set up their captive insurance company doesn’t primarily depend on the tax system of a country, even though it is advantageous since there are other factors to consider. In addition, even though the tax system is advantageous in a country and a parent company decides to set up in Malta to reduce costs, if careful planning is not done and maintained, the captive would incur other costs.

*IT infrastructure*

![IT Infrastructure Chart]

*Figure 12: IT infrastructure*

One respondent strongly agreed, another respondent agreed and two respondents were neutral on whether Malta’s IT infrastructure is an important incentive in the creation of a captive insurance company. With today’s dependence on IT and the internet, having a strong
IT infrastructure, and having contingency plans in the case of IT being temporarily unavailable is essential for the operation of a captive insurance company. However, there is also the possibility of outsourcing, which makes it easier both for the captives, where IT is not their strong point, and for new inexperienced captives.

**Language**

Two respondents strongly agreed while two respondents were neutral on whether Malta’s language is an important incentive in the creation of a captive insurance company. Additional comments were that Malta is an English speaking society and this is essential given its international relationships. The parent companies are all located in another country so the only way of communication is English. When board meetings or any other communications are held and an employee doesn’t understand English well, this could have an adverse effect
on the parent’s view of the Maltese domicile.

*Regulation*

![Bar Chart: Regulation](chart.png)

*Figure 14: Regulation*

One respondent strongly agreed, two respondents agreed and another respondent was neutral on whether Malta’s regulation is an important incentive in the creation of a captive insurance company. Additional comments were that Malta is a captive domicile and therefore has captive legislation; however, there also is PCC legislation. These two pieces of legislation can be seen as complementing each other since they provide more opportunities for parent companies. Dublin, which is a captive domicile, doesn’t have PCC legislation, while Gibraltar has. So this puts Malta as the only EU member state with both captive and PCC legislation.
Passporting Rights

All respondents strongly agreed that being an EU member state is an important incentive in the creation of a captive insurance company. Additional comments include that the captive success started when Malta became an EU member state. A company with exposures in Europe would prefer a European based captive domicile such as Malta.

Becoming a part of the EU allowed a captive in Malta to sell insurance directly to EEA states. When, say, a Swedish parent company locates its captive in Malta it does not need authorization from the Maltese competent authority, since both Sweden and Malta are EU member states. The captive can provide insurance cover to the parent company and its EU subsidiaries under freedom of services, which is when services are provided to EU member
One respondent strongly agreed, two respondents agreed and another respondent was neutral on whether Malta’s education system is an important incentive in the creation of a captive insurance company. Malta has an education system which is always growing and strengthening, however, when it comes to insurance, more work needs to be done to promote the captive industry. If university students are not given more exposure to this sector, it will be more difficult in the future for this sector to grow and for research to be done which could help this sector grow. If it eventually does grow, there is the possibility of not finding the right people to cater for the opportunities as well as difficulties that this sector may face. Therefore, for the industry to grow, the education related to this sector has to be
improved. Furthermore, the competent authority must be aware of the market needs and make sure that these are being reflected.

**Insurance Managers Availability**

![Insurance Managers Availability](image)

*Figure 17: Insurance Managers Availability*

Two respondents strongly agreed, one respondent agreed and another respondent was neutral on whether the availability of insurance managers is an important incentive in the creation of a captive insurance company. Insurance managers’ legislation can also be one of the factors which complement the captive and PCC legislation. If a parent company decides to set up in Malta as a cell in a PCC, it can benefit from the expertise of the PCC. If one of the cells of the PCC is an insurance manager, the captive could be managed by the insurance manager. New captives have the risk of not being managed well because of being in a new country that might have slightly different legislation and culture, so they can benefit
from the insurance manager’s knowledge and expertise.

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**PCC Structure**

![Bar chart showing PCC Structure](image)

*Figure 18: PCC structure*

All four respondents strongly agreed that the PCC structure is an important incentive in the creation of a captive insurance company. PCC legislation has been a recent competitive tool. With this legislation, Malta has an advantage over other countries since it is the only EU member state which offers this kind of set up. The PCC legislation allows a parent company to set up its captive as a cell in a PCC. When a captive is a cell in a PCC, there is no need for co-operate due diligence, and the parent can benefit from the PCC’s structure.
As already mentioned, the PCC structure can be regarded as complimenting the captive legislation and vice versa. It provides a unique opportunity for parent companies to benefit from, and it is an area which has grown over the last few years and is set to continue strengthening and growing.

**MFSA**

![Graph showing the Malta Financial Services Authority](image)

*Figure 19: MFSA*

One respondent strongly agreed, two respondents agreed and another respondent was neutral on whether the MFSA is an important incentive in the creation of a captive insurance company. The MFSA is very approachable, down to Earth, well-staffed and is looking to grow. In some countries, a meeting with the competent authority could take weeks, however in Malta, one can ask over the phone or set up a meeting a few days later.
The MFSA has a very good reputation, however when it comes to competing with other domiciles, it is regarded as being slow to the market. The MFSA takes a long time to issue a license; it would take Gibraltar about 6 weeks to issue a license while it could take 6 months to issue a license in Malta. If a parent company wants to set up its captive as soon as possible, it would choose Gibraltar over Malta, however if a parent is looking at other factors such as saving costs through taxation, it would consider Malta.
4.2.5 Question 5

*Do you think that the captive insurance industry will continue to grow and attract foreign investment to Malta?*

![Future growth of the captive insurance industry](image)

*Figure 20: Future growth of the captive insurance industry*

Three respondents agreed that the captive insurance industry will continue to grow and attract foreign investment to Malta. Malta has the infrastructure available, the legislation in place, a competent authority with a good reputation, and the economy in place so it is always able to compete with other domiciles such as Luxemburg, Gibraltar, Sweden and Dublin, which are all strong. However, Malta has a very weak starting point since it is very little. Presently, there is a slowdown in growth since the market is soft. However, with the unique PCC legislation and other incentives that Malta has, it is capable of attracting more parent companies to locate their captive to Malta.
One respondent was neutral on whether the captive insurance industry will continue to grow and attract foreign investment to Malta. The main reason was that Malta is not doing enough regarding captive insurance. If one considers Finance Malta, there seems to be more of a push towards other sectors such as hedge funds. When it comes to insurance, initially it had been doing well, however, this has slowed down. The main reasons could be that there has either been piece of mind, since initially the insurance sector was heading towards the right direction, or the long process in obtaining a license has discouraged foreign investors. Comparing insurance with gaming, it takes much less time for a gaming company to obtain a license than for an insurance company. To a certain extent, this is understandable since gaming leaves increased results and increased employment opportunities, however these companies have a higher probability of closing down. Insurance companies’ probability of closing down, such as captives, is less than that of gaming companies. Therefore, in the long run, insurance companies are more beneficial. If more work would be done on the insurance sector especially in the captive industry, it should be able to grow.
4.2.6 Question 6

Additional Comments

Before deciding whether to set up a captive, one must make a feasibility study, which involves looking at the loss ratio and the risk profile. Every risk has what is called a profile and also has its frequency and severity. There are certain risks which occur once every 100 years and there are others such as car collisions which have a higher frequency. When the frequency is high, the risk is more predictable since the captive would know approximately the amount of accidents and their cost based on past experience. However, risks which occur once every 100 years, which are called catastrophic events and the cost related to these events, are likely to be very high and unpredictable. If the risk is predictable, it is likely to be retained, however, if the risk is unpredictable it is less likely to be retained. This depends on the captive’s capacity.

If a risk exceeds a certain size and its frequency decreases, it is likely to be transferred. It is more advantageous to retain a risk, when it is predictable. In some situations, companies would be paying, say €1,000 of premium and claiming €1,000 back. This is called money swapping. It would be better if a company in this situation retains the risk since if a claim doesn’t occur, it could retain the premium, hold the investment income, and avoid certain administrative fees.
4.3 Conclusion

Considering the salient points in connection with the reasons for the creation of a captive insurance company; according to the respondents one of the important reasons is for the captive to insure its parent’s risks. Referring to the second chapter and also to a comment which was made by one of the interviewees; some risks are too complex to be transferred to the traditional market, and either no cover exists or the cover would exist but at a very expensive premium rate.

Another reason which the respondents considered as essential is that insuring through a captive would mean that the premium would remain within the company and would not be lost in the case of no claim.

Lastly, when a parent company insures its risk through a captive rather than through the traditional market, the parent company would have control over its risks and would have the ability of keeping an eye on the investment performance of the captive and the financial position of the captive insurance company. If the parent company insures its risks through the traditional market, it would not have access to the investment performance and financial position of the insurance company, or at least it would only get a brief overview through past financial statements and investment records.
Considering the incentives for parent companies to set up their captive insurance company in Malta, there are 3 incentives which the respondents believe are the most important for parent companies.

Firstly, being an EU member state gives Malta an advantage since a parent company can set up its captive by using its passporting rights. In fact, it was noted that Malta’s success as a captive domicile started with EU membership.

Secondly, the unique PCC legislation which Malta offers is also considered as essential. The PCC legislation compliments the captive legislation, and a PCC offers parent companies its expertise and the expertise of its cells. Malta is considered to have an advantage over other countries because it is the only EU member state which offers this set up.

Lastly, the insurance managers’ sector, which is also a growing sector, provides parent companies which have decided to set up in Malta, with the knowledge, experience and expertise about the Maltese captive insurance industry. For this reason, generally the respondents consider this as being another important reason for parent companies to set up their captive insurance company in Malta.

This chapter consisted of an analyses of the results obtained through the interviews conducted. Furthermore, the 3 most important incentives for the creation of captive insurance companies and for the set-up of captives in Malta were noted.
Chapter 5: Discussion, Conclusions and Recommendations
5.1 Introduction

A number of interviews were conducted with insurance managers, which manage the captive insurance companies in Malta. Through these interviews, the researcher was able to collect data, analyse it and reach a conclusion highlighting the salient findings as noted in the previous chapter.

In this chapter, the researcher links the salient findings with the research questions outlined in the first chapter, assesses whether the researcher’s hypothesis is correct or not, and finally recommends any studies linked to the captive insurance sector that could be considered in the future.

5.2 Research Questions

The researcher is now able to consider the research questions which were outlined in the first chapter and link them to the fourth chapter which consisted of results and analyses of results.
Research question 1: What are the main reasons for creating a captive insurance company?

From the conclusions reached in the fourth chapter, it was noted that the main reasons for creating a captive insurance company include:

1. To insure its parent’s risks
2. For the premium to remain within the company
3. For the parent company to have an increased control over its risk

Research question 2: Which incentives do captive insurance companies consider as being the most important ones when a parent company decides to locate its captive to Malta?

It was also noted that the most important incentives which are considered when deciding to locate a captive insurance company to Malta include:

1. EU Membership
2. PCC legislation
3. Insurance Managers’ availability

5.3 Hypothesis

The researcher’s hypothesis regarding the reasons for the creation of a captive insurance company was that creating a captive enables a parent company to insure its own risk at a lower premium. According to the researcher’s findings, insuring risk through a captive is
considered as one of the most important reasons; however, paying a lower premium is not. In fact, only 2 of the respondents strongly agree that premiums would be lower, while the other 2 are indifferent. Therefore, it can be concluded that for the first objective of this study, the researcher’s hypothesis is half correct.

Considering the second objective regarding the existing incentives for parent companies to set up their captive insurance company in Malta, the researcher’s hypothesis included that the three most important incentives are Malta’s geographical position, being an EU member state and Malta’s taxation system. However, the researcher’s findings conclude that being an EU member state, offering a unique PCC set up, and having insurance managers’ legislation in place are considered as the salient incentives which attract parent companies towards the Maltese islands. Therefore, the researcher’s hypothesis is partly correct.

5.4 Further recommended studies

The researcher’s recommendations on possible future studies could include:

1. A comparison between Malta and other captive domiciles which Malta competes with, such as Luxemburg, Gibraltar, Sweden and Dublin. The incentives that each of these countries provide could be compared with each other and this could help the Maltese captive insurance industry operate more efficiently by using any techniques which other domiciles use to attract investment and grow as a captive domicile.
2. Another recommendation would be to look at the benefits and drawbacks of insuring risk with the traditional market compared with the benefits and drawbacks of insuring risk through a captive.

5.5 Conclusion

The insurance market is currently a soft market. Therefore, it wouldn’t be easy to see growth due to lower than average prices and small profits. The financial crisis led to a soft market and some reinsurers closing down. However, big companies are always looking for solutions to mitigate their cost and risk, and the creation of a captive insurance market enables companies to do this. Furthermore, PCC legislation is a big advantage for Malta since it is the only EU member state which provides for this set up.

Through the research and interviews conducted, the researcher believes that Malta is an ideal location for the set-up of captive insurance companies. However, the researcher agrees with a comment made by one of the interviewees, which is that more effort needs to be put into strengthening the captive insurance industry to be able to see more growth. The researcher is of the opinion that promoting Malta's captive insurance industry would positively affect the insurance industry as a whole. In fact, Dr Lawrence Gonzi, stated that “the financial services sector is definitely an industry which will continue to attract foreign investment to our shores.” (Finance Malta, 2012)
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Appendices

Appendices 1: Interview Questions

1. How long has the captive insurance company been licensed in Malta?
   - 1-4 Years
   - 5-8 Years
   - 9-10 Years

2. Do you agree that Malta is an ideal location for setting up captive insurance companies?
   - Strongly Agree
   - Agree
   - Neutral
   - Disagree
   - Strongly Disagree
3. The following are possible reasons for creating a captive insurance company. In your opinion, please tick according to how important each reason is:

<table>
<thead>
<tr>
<th>Reason</th>
<th>Strongly Agree</th>
<th>Agree</th>
<th>Neutral</th>
<th>Disagree</th>
<th>Strongly Disagree</th>
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<tbody>
<tr>
<td>To insure its parent's risk</td>
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<td>For the premium paid for insurance to remain within the company</td>
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<td>For lower premiums</td>
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<td>To reserve investment returns</td>
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<td>For the parent company to have an increased control over its risks</td>
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</table>
4. The following are possible incentives for setting up a captive insurance company in Malta. In your opinion, please tick according to how important each incentive is:

<table>
<thead>
<tr>
<th>Incentive</th>
<th>Strongly Agree</th>
<th>Agree</th>
<th>Neutral</th>
<th>Disagree</th>
<th>Strongly Disagree</th>
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</thead>
<tbody>
<tr>
<td>Geographical Position</td>
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<td>Tax System</td>
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<td>IT Infrastructure</td>
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<td>Language</td>
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<td>Regulation</td>
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<td>Passorting Rights</td>
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<td>Education System</td>
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<td>Insurance Managers Availability</td>
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<td>PCC Structure</td>
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</table>
5. Do you think that the captive insurance industry will continue to grow and attract foreign investment to Malta?

- Strongly Agree
- Agree
- Neutral
- Disagree
- Strongly Disagree

6. Additional Comments

________________________________________________________________________

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________________________________________________________________________

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Appendices 2: Interview Transcript

The following is a transcript of an interview with a manager of an insurance manager company which took part in this study.

**INTERVIEWEE**: What year are you in?

**INTERVIEWER**: I'm a fourth year student, and my thesis is regarding primarily the reasons why parent companies create captive insurance companies and the reasons for setting up in Malta. Are you the insurance managers of AarhusKarlshamn Insurance Malta Limited and Falcon Insurance Limited?

**INTERVIEWEE**: Yes, we refer to AarhusKarlshamn Insurance Malta Limited as AAK because it is very difficult to pronounce. They are Swedish. Initially, you need to know that there is a small number of captives in Malta compared to other countries where there are hundreds. The reasons are various. But essentially as a domicile Malta is considered to be very small and it hasn't had the success which we thought it would have.

**INTERVIEWER**: Parent companies started allocating their captives after EU membership.

**INTERVIEWEE**: You have a captive because it is a risk mitigating strategy. You have your parent company which looks at risk mitigating strategies, which is keeping your controls tight, making sure your claims history is low but part of that is sometimes you get what has good loss ratio and pass it through a captive, so that you can retain the premiums knowing that the risk is low. But still if you have a captive you need to make sure that you have enough resources to back your liabilities in the case of a big hit. So it is not just a matter of let's have a captive put together, we license it in Malta and become scarce rich, and give it back to the company. So it needs to be managed by people who are knowledgeable about the industry,
and know how to manage the risks which are actually being written. This is very key. Captive management is one of the risk strategies that are in place for big companies. Usually when they do go down the line, if it is managed very well, it is a very profitable business.

INTERVIEWER: Ok. Is the captive insurance company authorised by a parent which is an EU member state?

INTERVIEWEE: AAK Yes. Falcon No.

INTERVIEWER: How long has the captive insurance company been licensed in Malta?

INTERVIEWEE: AAK since 2010 so 4 years and Falcon 2005.

INTERVIEWER: Do you agree that Malta is an ideal location for setting up captive insurance companies?

INTERVIEWEE: Yes I strongly agree.

INTERVIEWER: The following are possible reasons for creating a captive insurance company. In your opinion, please tick according to how important each reason is.

INTERVIEWEE: To insure its parent risk - Strongly Agree. For the premium paid for insurance to remain within the company - Strongly Agree. For lower premium - Neutral. Many times it doesn't mean that they are lower. Usually they try to get market prices and match it. To be able to invest the premium and reserve the returns for the future.

INTERVIEWER: What I mean is for example when you pay an insurance company, you won't get anything back. Do you think that with a captive, the premium will remain within the company and it would be invested?

INTERVIEWEE: Rather than invest the premium I would say retain the premium. When you say invest the premium it means you are putting it in an investment and at the moment
investment returns are so low that we don't even consider it anymore. If you have a deposit account, you can have 0.5% which is nothing, whereas 6 years ago you could get 6/7%. It is a completely different reality today. So I Agree. For the parent company to have an increased control over its risk - Yes strongly agree. For the premium to remain stable within market changes - Agree. To allow the parent company to plan for insurance budget - Agree. The following are possible incentives for setting up a captive insurance company in Malta. In your opinion, please tick according to how important each incentive is. Geographical position - Neutral. Tax System - I would say agree and disagree. Some companies actually stay away because of the tax system, because they don't want to seem as if they are trying to get tax arbitrage or tax reduction in the tax bill. They have prospects to stay away because of that. However, generally I would say agree. IT infrastructure - Neutral. Law - Instead of law I would say regulation. Malta is a captive domicile because it has captive legislation. We also have PCC legislation. Dublin which is a captive domicile doesn't have PCC legislation. Gibraltar has PCC legislation. Sweden doesn't have and it is also regarded as a captive domicile. So I would say yes, law/regulation agree. Passorting rights - Strongly Agree. Education - Agree. Insurance Managers availability - It is important to have it but it is not one of the incentives to set it up. You have to have the law first. If you have the law you have the managers. So Neutral. PCC Structure - Strongly agree. The MFSA - they can be a very big deterrent because they are slow to market. What I mean is that they have a very good reputation but when we come to compete with other domiciles they take long to give us the license even though we have submitted the information on time. Whereas Gibraltar can give a license is 6 weeks, we take 6 months. So if there is a parent who wants a license quickly, they would go to Gibraltar as against Malta. If they want other things such as Double Taxation agreements, they would come to Malta because Gibraltar doesn't have it. So there are these distinctions. The MFSA has a very good reputation but then it can be slow.

INTERVIEWER: Would you say neutral?

INTERVIEWER: What do you think about language?

INTERVIEWEE: Neutral, because everyone is going to speak in English.

INTERVIEWER: Do you think that the captive insurance industry will continue to grow and attract foreign investment to Malta?

INTERVIEWEE: I hope so. I would say agree. Put it this way, the captive business has slowed down. We have the infrastructure in place, we have the people, the MFSA, and we have the economy which is in place. When we make a feasibility study, we are always up against other domiciles such as Luxemburg, Gibraltar, Sweden and Dublin which all are very strong. We are competitive because we have the legislation; we come out cheaper compared to for instance Luxemburg and Dublin. Whether we will see growth, yes I agree but really and truly we have a weak starting point. We have very little captives in Malta. We don't have 300/400 captives, whereas in other domiciles those are the numbers. So I would say yes I agree. Hopefully, we will continue to grow but there is a slowdown even because the market is soft. So if they want to place their property program, they can get a very good deal for the money out there.

INTERVIEWER: Ok, thank you. Do you have any additional comments?

INTERVIEWEE: We would like to see this grow. We are working on other vehicles, not just captives. The MFSA has recently introduced the CSV regulation where we haven't seen anything yet. As I said, it is a difficult market at the moment because it is a soft market.

INTERVIEWER: Do you think that the financial crisis had an impact?
INTERVIEWEE: The financial crisis made two things; got the market soft and some reinsurers disappeared. But no not really, if anything, I think that big companies are always out looking for solution to mitigate their cost/risk, and a captive ticks a lot of boxes. Then it depends on where their exposures are. If they have exposures in the US, they would go for a US based captive domicile. If they have exposures in Europe, they would go for a European captive domicile, and then they look at the domiciles. Depending on what is high in their agenda, they will decide on the domicile. Malta is relatively easy to get to, maybe Gibraltar is more difficult, and Dublin is easier. There are a lot of things to consider. PCC legislation is a big growth area here. PCC regulation is a big plus sign because there is no co-operate due diligence, for instance, when you have a cell, you don't need to come down for board meetings, you don't need to discuss renewals, you can just get your brokers and do it through the phone. It is a quicker way of doing business and having the same structure basically. So you are getting the benefit of having a captive without the actual structure in place. So we see a lot of growth in PCCs rather than standalone captives.