VERMONT
DEPARTMENT OF FINANCIAL REGULATION
CAPTIVE INSURANCE
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GUIDANCE FOR PROTECTED CELLS

Sponsored Captive Insurance Company and Protected Cells (unincorporated and incorporated)

Sponsored captive insurance companies and associated protected cells must comply with Title 8 V.S.A. § 6001- § 6024 and specifically to § 6031- § 6039. Please refer to the applicable statutes at: https://legislature.vermont.gov/statutes/chapter/08/141. The statute is intended to allow participants to manage their own risks through a protected cell within a licensed sponsored captive insurance company. Any risks meeting requirements set forth in 8 V.S.A. § 6002 may be insured in a protected cell.

A sponsored captive insurance company insures the risks of its participants through separate participant contracts and funds its liability to each participant through one or more protected cells. A protected cell is a separate account established by a sponsored captive in which assets are maintained for one or more participants in accordance with one or more participant contracts to fund the liability of the sponsored captive assumed on behalf of such participants. The assets of each protected cell are segregated from the assets of other protected cells and from the assets of the sponsored captive insurance company's general account. The assets of a protected cell shall not be chargeable with liabilities arising out of any other insurance business the sponsored captive insurance company may conduct. A protected cell can be formed as an *incorporated* protected cell (as any type of entity permissible under Vermont law) separate from the sponsored captive insurance company. An *incorporated* protected cell is allowed to enter into contracts and undertake obligations in its own name and for its own account. As used in this document, the term "protected cell" refers to both cells by contract only (i.e. unincorporated cells) and *incorporated* protected cells, unless specifically designated.

Formation of Sponsored Captive Insurance Company and/or Protected Cells

If seeking a license for a new sponsored captive insurance company with proposed protected cell(s) at the same time, please use the General Application form found on our website. The addition of each new protected cell within an existing licensed sponsored captive insurance company constitutes a change in the business plan, requiring the Vermont Commissioner's prior written approval. When forming a new protected cell(s) within an existing licensed sponsored captive insurance company, please use the Business Plan Change for Protected Cells form found on our website.

Pursuant to 8 V.S.A. § 6002(d), the sponsored captive insurance company shall pay a non-refundable licensing fee of $500 with its application for licensure. There is no licensing fee for a request to add a protected cell to an existing licensed sponsored captive insurance company. However, a $6,000 non-refundable fee for a consulting actuarial review may be required for the sponsored captive insurance company and/or any newly formed protected cell(s) at the discretion of the Department of Financial Regulation (DFR).

Participant/Participant Contract

A sponsored captive insurance company may establish and maintain one or more protected cells to insure the risks of one or more participants, where the losses of the participant are limited through a participant contract to such participant's share of the assets of one or more protected cells identified in such participant contract. The participant contract should specify that the assets of each protected cell will be segregated from the assets of other protected cells and from the assets of the core/sponsored captive insurance company's general account. The assets of a protected cell are not chargeable against the liabilities of any other cell or against any other insurance business the sponsored captive insurance company may conduct. The participant contract should specify that the sponsored captive will account for the loss and expense experience of each protected cell separately and at a sufficient level of detail.

The participant contract should include, at a minimum, information on the following matters, as applicable: required capital, collateral, loss reserves, distributions, taxes, governance/governing body, management, and allocation of expenses. The participant contract should also include an appropriate termination clause describing the liability of respective parties upon termination and a description of transitional services and related fees, if applicable.

No participant contract shall take effect without prior written approval from the DFR. The addition of each new protected cell and withdrawal of any participant or termination of any existing protected cell shall constitute a change in the business plan requiring prior written approval.

The financial statements of the participant(s)/insured(s) shall be submitted with the request for a business plan change to add a protected cell and upon request by the DFR as deemed necessary during analysis and/or examinations.

Capital and Surplus

A sponsored captive insurance company is required to maintain unimpaired paid-in capital and surplus of not less than $100,000. There is no statutorily required minimum capital and surplus for protected cells; however, surplus requirements for protected cells shall be commensurate with the business plan and retained risks as determined by a feasibility study or other evidence deemed acceptable by the DFR. A protected cell shall not begin operations until it possesses and thereafter maintains the unimpaired paid-in capital and surplus as agreed to per approved business plan.

If a Letter of Credit is to be used to satisfy the capital and surplus requirement, the language on the DFR Form E-702 must be used. All Letters of Credit should be issued on bank letterhead. Exceptions will not be considered. The Letter of Credit Form E-702 may be found on our website. The issuing bank must be either a member of the Federal Reserve (note: FDIC membership is not the same as Federal Reserve membership) or appear on the NAIC list of qualified U.S. financial institutions. Other banks may be considered on request.

Vermont Captive Annual Report (VCAR)

[Due on or before March 15 or within 75 days after fiscal year-end.]

8 V.S.A. § 6034(f) requires each sponsored captive insurance company to file an annual report of its financial position, which includes accounting statements detailing the financial position of each protected cell. Protected cells by contract only (i.e., unincorporated protected cells) must use the VCAR Supplemental Form to be filed with the annual report of the sponsored captive insurance company. *Incorporated* protected cells must use the VCAR *Incorporated* Protected Cell (IPC) Form to be filed with the annual report of the sponsored captive insurance company as per the VCAR General Instructions. Note: Separate annual reports of a protected cell may be permitted or required, depending on circumstances. Per the VCAR General Instructions, for each licensed sponsored captive that has one (1) or more cell(s), the Cell Confirmation Exhibit should be included as part of the VCAR filing.

Audited Financial Statements

[Due on or before June 30 or within 180 days after fiscal year-end.]

Regulation C-81-2 requires each sponsored captive insurance company to file audited financial statements annually which shall be prepared and presented on the same basis of accounting as the annual report. Therefore, the audited financial statements of a sponsored captive insurance company shall include a separate balance sheet and income statement for each protected cell [on the balance sheet, included in the footnotes, or as a supplemental schedule(s)]. The audited financial statements shall comply with other requirements of Regulation C-81-2. Where the Sponsor/Core and a protected cell(s) are under common ownership/control, GAAP rules of consolidation should be followed. Separate annual audited financial statements of a protected cell may be required at the discretion of the DFR or permitted at the request of management with prior approval from the DFR. Due to variations in cell structures and business plans, the DFR recommends consultation with an approved audit firm to determine the most appropriate presentation. The participant contract should describe the transactional operations of the cell, including whether the audit of the protected cell will be "combined" with the sponsored captive insurance company or prepared on a stand-alone basis, and how related fees will be incurred/paid.

Actuarial Review

[Due on or before June 30 or within 180 days after fiscal year-end.]

Regulation C-81-2 requires each sponsored captive insurance company to file a Statement of Actuarial Opinion (SAO) annually. The DFR does not require separate SAOs for each protected cell; however, an exhibit to support the reserves recorded on the balance sheet of each protected cell is required. The participant contract should describe the transactional operations of the cell, including whether the actuarial opinion of the protected cell will be included/combined with the sponsored captive insurance company or prepared on a stand-alone basis, and how related fees will be incurred/paid. A separate annual SAO of a protected cell may be permitted or required, depending on circumstances.

Examinations

In accordance with 8 V.S.A. § 6008(a), a sponsored captive insurance company is subject to a full scope examination by the DFR whenever the Vermont Commissioner determines it to be prudent, but not less frequently than every five years. Such examination will include the operations of all protected cells within the sponsored captive insurance company as of the date of examination. A separate examination of a protected cell may be permitted or required.

Annual Fees

Annually, each sponsored captive insurance company shall pay a license renewal fee of $500. There is no separate annual fee for protected cells.

Premium Taxes

Each sponsored captive insurance company is required to file a premium tax return annually. The premium tax return includes tax calculation schedules for each protected cell. Refer to 8 V.S.A. § 6014 for premium tax rates, due dates and related information. The annual minimum aggregate tax to be paid by a sponsored captive insurance company is $7,500 and applies to the sponsored captive insurance company as a whole and not to each protected cell. Protected cells are not subject to the minimum tax. The annual maximum tax to be paid by a protected cell is $200,000. The annual tax to be remitted by a sponsored captive insurance company is the aggregate of the tax liabilities of each protected cell. For additional information, refer to the Captive Premium Tax Return (Form CPT) instructions on the Vermont Department of Taxes website.

Insolvency of a Protected Cell

The licensed sponsored captive insurance company is required to formally notify the Commissioner, in writing, within 10 business days of any protected cell becoming insolvent or otherwise unable to meet its claim or expense obligations. Refer to 8 V.S.A. §6038 for additional information. Notification to the DFR shall include a capital remediation plan for the insolvent cell(s).

Closing of a Protected Cell

The termination of any existing protected cell and/or withdrawal of any participant constitutes a business plan change and requires formal notification and prior written approval of the Commissioner.

Incorporated Protected Cells Specifically

Organization of the Business Entity in Vermont & Certificate of Approval to Organize

For purposes of registration of the business entity with the Secretary of State, the Commissioner will issue a Certificate of Approval to Organize/Incorporate upon receipt of a request for such certificate and a complete Business Plan Change for Protected Cells form or a General Application form. The Certificate of Approval to Organize/Incorporate for the *incorporated* protected cell will identify the entity as a protected cell of an existing sponsored captive insurance company. The *incorporated* protected cell will be approved for the limited purposes authorized by the sponsored captive insurance company's license. The sponsored captive insurance company is required to file draft articles and by-laws, or other organizing documents, which will be reviewed in order to issue a Certificate of Approval to Organize/Incorporate.

Board of Directors (BOD) (or equivalent)/Resident Director

An *incorporated* protected cell may have its own BOD, independent of the BOD of the licensed sponsored captive insurance company; or may appoint the same persons as those serving on the BOD of the licensed sponsored captive insurance company. Although not a requirement, it may be considered a best practice for the sponsor to require the BOD consist of representatives of the cell participant(s) and at least 1 representative of the sponsor. "Group" cells should encourage independent member participation on the BOD. There is no resident director (or equivalent) requirement for an *incorporated* protected cell.

BOD Meeting Requirement

Incorporated protected cells should comply with its articles and bylaws and should hold meetings at least annually to address essential items; however, are not required to hold a meeting in Vermont each year as stipulated in 8 V.S.A. § 6002(b)(2). If a cell appoints the BOD of the sponsor as governing board, the cell does not have to hold separate meetings.

Biographical Affidavits

The *incorporated* protected cell is required to file biographical affidavits for directors (or equivalent) only, using either Vermont's prescribed *Biographical Affidavit* form or the NAIC's biographical affidavit. Each affidavit must be filled out in its entirety and no substitute for this form will be accepted. The Vermont form can be found on our website.

Conflict of Interest Statements

There is no requirement to maintain conflict of interest statements; however, the *incorporated* protected cell must follow general corporate law with respect to appropriate standards for its governing body.

Dissolution of an Incorporated Protected Cell

The dissolution of any existing *incorporated* protected cell constitutes a business plan change and requires formal notification and prior written approval of the Commissioner. Dissolution of an *incorporated* protected cell shall be managed in the same manner as the dissolution of another captive insurance company. However, a Tax Clearance Letter issued by the Vermont Department of Taxes is not required for the dissolution of an *incorporated* protected cell.