Reinsurance Special Purpose Vehicles - Why MALTA?

MFSA
MALTA FINANCIAL SERVICES AUTHORITY

Introduction

The current challenging economic environment, together with the need to maximise return on capital, has prompted innovation in alternative forms of risk transfer and financing in reinsurance.

One typical mechanism is the formation and use of Reinsurance Special Purpose Vehicles (RSPVs) which complement traditional (re)insurance arrangements and are a cost effective mechanism to provide an additional pool of capital to (re)insurers while contributing to premium price competitiveness and smoothing against adverse insurance market cycles.

> " a cost effective mechanism to provide an additional pool of capital "

The EU Reinsurance Directive (Directive 2005/68/EC) ("Reinsurance Directive") provides Member States with an authorisation and regulation framework which enables insurance or reinsurance undertakings to transfer risks to RSPVs.

In a typical transaction, an insurance or reinsurance undertaking, uses an RSPV to cede risks through a reinsurance contract or similar arrangement.

The RSPV funds its potential liabilities under that contract through the issuance of financial instruments such as debt instruments to the capital markets.

RSPV Regulations

The Malta Financial Services Authority ("MFSA") has been proactive in aligning the regulatory regime for the authorisation and regulation of RSPVs under the Insurance Business Act (Cap.403) to EIOPA Advice for Level 2 Implementing Measures on Solvency II: Special Purpose Vehicles, published in 2009.

The RSPV Regulations define an RSPV as an undertaking, other than an existing insurance undertaking or reinsurance undertaking, which assumes risks from a ceding undertaking and which fully funds its exposure to such risks through the proceeds of a debt instrument or any other financing mechanism where the repayment right of the providers of the particular debt or financing mechanism are subordinated to the reinsurance obligations of the RSPV.

The regulatory framework for RSPVs provides for the following:

(a) **Authorisation Process** - the detailed procedures to be followed for the grant of an authorisation for an RSVP for a specific use or uses;

(b) **Mandatory Conditions for all Contractual Arrangements** which must ensure that the claims of the providers of capital to the RSPV are at all times subordinated to the reinsurance obligations of the RSPV to the insurance or reinsurance company;

(c) **Governance Requirements** which ensure that qualifying shareholders and all persons who effectively direct or manage an authorised RSPV are fit and proper persons and the RSPV's system of governance is appropriate to the nature, scale and complexity of the risk that the RSPV assumes;

(d) **Supervisory Reporting** which requires the RSPV to report to the MFSA on the value of its assets, its aggregate maximum exposure, any conflicts of interest, as well as any significant transactions entered into within a reporting period; and

(e) **Solvency Requirements** which are particular to RSPVs which must be "fully funded" at all times. "Fully funded" means that an authorised RSPV must have at all times assets, the value of which is equal to or exceeds the aggregate maximum risk exposure, and the RSPV is able to pay the amounts it is liable for as they fall due. It is the fully funded requirement that differentiates a RSPV from a traditional insurance or reinsurance company.

Sponsors and arrangers of financial instruments and debt are therefore able to look to Malta as a potential domicile for the formation of an RSPV and (re)insurers can use the RSPV to transfer their risks to the capital markets in a cost efficient manner.

WHY MALTA?

Malta's regulatory framework is known internationally to be both robust and adaptable, allowing promoters to innovate and develop new products in a stable, proactive and transparent environment. The RSPV Regulations will continue to complement and expand Malta's regulatory framework which already incorporates re-domiciliation legislation applicable to all types of companies including securitisation vehicles under the Continuance of Companies Regulations (S.L.386.05).

"a robust and adaptable regulatory framework"

Malta also offers a legal framework for domestic and cross-border securitisations under the Securitisation Act (Cap.484) as well as a framework for the regulation of Protected Cell Companies (S.L.386.10) and Incorporated Cell Companies (S.L. 386.13) under the Insurance Business Act (Cap. 403).

Furthermore, Malta offers the possibility for the listing of wholesale securities issued by the RSPV. A new regulated market, the European Wholesale Securities Market (EWSM), jointly owned by the Irish Stock Exchange and the Malta Stock Exchange, for the wholesale fixed income securities was set up, registered and domiciled in Malta in 2012. The EWSM is approved as an EU regulated market under MiFID and is a "Recognised Stock Exchange" within the meaning of the UK Income Tax Act, 2007. The regulatory requirements are available in the Guidelines for Listing and Trading on the EWSM [www.ewsm.eu].

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