A KALEIDOSCOPE OF EVOLVING REGULATION

MFSA's director, Angele Grech, introduces the *Captive Review Malta Insurance Report 2015* which analysis the development of Malta as a financial jurisdiction over the previous year

Financial regulation is designed to achieve key policy goals among which are the safety and soundness of financial institutions, the mitigation of systemic risk, the fairness and efficiency of markets and the protection of the consumer and investor. These goals, which are clearly essential, do not take into account an additional factor that has come to be regarded as critical in any well-functioning regulatory system – achieving regulatory efficiency and cost effectiveness.

The current challenge faced by financial services regulators is to establish and maintain a regulatory framework of high standards and achieve the above mentioned policy goals, and to concurrently create the space for market players to innovate, adjust and flourish to meet changing consumer needs. The approach is geared to positively shape a market that offers consumers alternative choices, products which meet their needs and are delivered in a way which blends in with their lifestyle.

Against this backdrop, the Malta Financial Services Authority (MFSA) is committed to support regulatory innovation. The MFSA operates through a prudent, dynamic and proactive regulatory framework which is based on high standards and promotes sustainable and inclusive growth. The MFSA embraces a culture which values open communication with stakeholders and constantly reviews the delivery of the regulatory framework. The MFSA is responsive to the requirements of existing licence holders, mindful of potential new entrants joining the market and cognisant

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of new operating models which have transformed established markets.

This result is a kaleidoscope of evolving financial regulation.

The MFSA has been reviewing insurance legislation over the recent years as part of its effort to introduce innovation within the existing EU regulatory framework. Specific legislation for re-domiciliation of insurance companies (S.L.403.12) was introduced in 2003 and this was a healthy development which has been instrumental to re/insurance companies intending to move from offshore to onshore. The protected cell company legislation (S.L. 386.10) is a distinctive innovative feature in the Maltese financial regulatory framework and insurance and reinsurance operators have been able to channel their activities through these structures since its introduction in 2004.

In 2013, a Solvency II compliant framework for the authorisation and regulation of reinsurance special purpose vehicles (RSPVs) (LN 452 of 2013) was established to cater for the opportunity to maximise return on capital and enable the efficient management of risk in a sound regulatory environment. This framework offers insurers and reinsurers the possibility to obtain access to capital resources as part of a drive to expand capital markets activity in Malta.

Subsequently, as a result of regular ongoing discussions with stakeholders, the MFSA realised the potential benefits of fusing the cell company concept into the RSPV regulatory framework. This latest addition to Malta's financial legislation – the securitisation cell company regulations (SL 386.16) allows securitisation vehicles to set up cell structures. This is a unique type of legislation not available in any other jurisdiction as it allows an SCC to issue financial instruments in separate tranches through different cells. Accordingly, the SCC regulatory framework allows the issuance of multiple insurance linked securities without incurring any risk of cross-contamination between different sets of creditors or investors. These cells can transact in different currencies and the securitisation cell company (SCC) can keep accounts in the currency of choice. Apart from RSPVs, the SCC is also applicable for all types of securitisation transactions.

In this way, the SCC framework retains the benefits of the Securitisation Act (Cap. 484) and builds on the opportunity of the RSPV regulations providing increased flexibility, enhanced investor protection and economies of scale.

Similarly to a PCC, an SCC is a single legal entity that is structured in two parts, the core and an unlimited number of cells. It is one company with one board of directors and one set of memorandum and articles of association. The key differentiating element between a cell company and the traditional non-cellular company is that the former provides a flexible corporate vehicle within which assets and liabilities can be ring-fenced, or segregated, so as to be only available to the creditors and shareholders (where present) of each particular cell. Therefore, an SCC is able to limit its liability in respect of a particular transaction to a specified pool of assets rather than exposing all of the assets of the SCC, as would be the case with a non-cellular company. A cell of an SCC does not have a separate legal personality, and each cell transacts through the core of the SCC. When an SCC enters in a contract, the directors must specify in the contract which particular pool of assets is to be bound by the obligations under the agreed contract.

An SCC can take either carry on business as a securitisation vehicle in compliance with the Securitisation Act (Cap 484) or carry on business as an RSPV in line with the RSPV regulations.

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Whereas these two categories of SCC vehicles perform different activities, they both enjoy commonalities as far as their setting up and operation is concerned. These are:

- Creation of a cell: an SCC may create cells by means of a resolution of its board of directors. A new cell will be created for the purpose of entering into either securitisation transactions or activities of an RSPV. Each cell of an SCC must have its own distinct name or designation which shall include the word 'cell'.
- Issuance of financial instrument linked to a cell: an SCC may issue financial instruments in one or more tranches, in respect of any of its cells, and the proceeds of the issue are comprised in the cellular assets attributable to the cell in respect of which the financial instruments were issued.
- Cell shares: an SCC may, in respect of any of its cells, create and issue cell shares, the proceeds of the issue of which (cell share capital) are comprised in the cellular assets attributable to the cell in respect of which the cell shares were issued.
- No activities at the core: an SCC may not carry securitisation transactions or activities of an RSPV through its non-cellular assets. Asset-based and risk-based securitisation transactions may therefore only be carried out in respect of specific cells and securitisation assets have to be allocated to a particular cell.
- Duties of directors: the directors of an SCC have the obligation to keep: (a) cellular assets separate and separately identifiable from non-cellular assets; (b) cellular assets attributable to each cell separate and separately identifiable from cellular assets attributable to other cells; and (c) separate records, accounts, statements and other documents as may be necessary to evidence the assets and liabilities of each cell as distinct and separate from the assets and liabilities of other cells in the same company, and as distinct and separate from the non-cellular assets and liabilities of the SCC.
- Choice of cell currency: the directors of an SCC may choose the base currency of a cell which may be different from the currency of the non-cellular share capital.
- Annual accounts: an SCC shall draw up its annual accounts in either the currency of its non-cellular share capital or the base currency of one of its cells.
- Position of creditors: a creditor of a cell has rights to the assets of that particular cell only and has no recourse to the assets of other cells or the non-cellular assets. Apportionments may be made out of the assets attributable to the individual cells towards the costs of the day-to-day administration of the SCC.
- Winding up of individual cells: the SCC regulations provide for the closing of individual cells separately from the SCC as a whole. The winding up proceedings prescribed under the Companies Act (Cap. 386) apply mutatis mutandis to a cell as though it were a distinct legal entity.
- Listing on EWSM: an SCC may list its securities on the European Wholesale Securities Market (EWSM), an EU regulated market [www.ewsm.eu] dedicated to the needs of arrangers and issuers of wholesale debt products.

Innovation

Regulatory innovation is set to continue throughout 2015 and beyond and this will translate into further challenges and opportunities for insurers. The MFSA is committed to enhance sustainability, support stronger governance and promote full transparency. And equally, it will continue to listen and engage with stakeholders to introduce more regulatory innovation to the benefit of market players. The commitment to foster regulatory innovation is continuous.