PROTECTION FOR CELL STRUCTURES

Angele Galea St John, director at the Malta Financial Services Authority, discusses Solvency II and the legislation affecting Malta-based cell companies

Captive Review (CR): What is the MFSA's opinion on cell companies? What is Malta's current status on legislation on cell structures?

Angele Galea St John (AGS): As part of the process to introduce innovation within the existing EU legislation, the Malta Financial Services Authority has, over the years, been consistently reviewing the insurance regulatory framework. The concept of cell companies was first introduced in Malta in 2004, when specific legislation was put in place to cater for the use of Protected Cell Companies (PCC) by insurance and reinsurance entities (including captives) as well as by insurance management companies and insurance broking companies.

The cell concept has since been developed into a number of different types of cell company structures catering for both the insurance and investment fund sectors. More recently, as part of Malta's drive to introduce capital markets activity, legislation for Re-insurance Special Purpose Vehicles was enacted and the PCC concept was extended to the Reinsurance Special Purpose Vehicles. The new regulations - the Securitisation Cell Companies Regulations (S.L.386.16), continue to build on the Protected Cell concept by adapting and extending the protected cell company structure to cater for securitisation activity.

The legislation leverages on Malta's experience in legislating for cells in other sectors including the investment funds and insurance sectors, where dedicated cell legislation notably contributed to Malta's growth in financial services. These Regulations set out a framework for a new type of Cell Company acting as a reinsurance special purpose vehicle in Malta – the Securitisation Cell Company (SCC) through fusing the highly sophisticated frameworks provided in the Securitisation Act (Cap. 484) and the Reinsurance Special Purpose Vehicle Regulations (L.N. 452 of 2013) with the cell company concept.

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The regulations now provide a legally entrenched framework for segregation of different sets of assets and risk instruments within a single special purpose vehicle, the SCC, thereby allowing for the launch of multiple insurance-linked securities without incurring any risk of cross-contamination between the different sets of creditors and investors. This is a first in securitization vehicle structures as these are normally set up with compartments in other jurisdictions. The SCC is also applicable as a vehicle for all types of securitization transactions

Malta has also always sought to balance the complexity of regulation with efficient supervision – and in this context, over the past three to four years we have seen an increased interest in the use of the Protected Cell Company. Within a PCC structure, the cells may be approved write re-insurance business. The core, or non-cellular part, on the other hand, may or may not be authorised to write re-insurance. The core of the PCC is the provider of capital for solvency purposes and in the event that any of the cells become insolvent, the core should transfer capital to meet the liabilities of the cell. The core also maintains and controls all the activities of the PCC.

In the case of Reinsurance Special Purpose Vehicles structured as Securitisation Cell Companies, no business may be transacted through the core therefore eliminating the risk of insolvency of the core. The Securitisation Cell Company legislation allows an SCC to issue separate tranches, to transact in different currencies and keep accounts in the currency of choice.

CR: How does Malta compare as a domicile for PCCs to other EU domiciles? Do you expect Solvency II to impact the number for cell formations? Why?

AGS: Insurance companies licensed in Malta face the same regulatory challenges as they do in other EU Member States. The concept of proportionality is fundamental to Solvency II and cell structures present a solution for smaller insurance entities which may be concerned that the compliance burden may be too onerous for a stand-alone company. There has been a marked interest in the use of PCC structures over the recent years and to date there are 12 licensed Protected Cell Company structures hosting a total of 27 cells. A number of conversions from licensed standalone companies to protected cell structures have taken place as these latter are viewed as a better risk management tool.

The PCC structure offers various benefits to cell owners; from efficient use of capital, down to cost sharing in respect of governance structures and reporting requirements. Cell structures offer the facility of flexibility, speedier set ups and cost effective solutions while being fully compliant with the Solvency II regulatory framework. The core and cells within the PCC structure are treated as ring fenced funds for the purposes of Solvency II. As a single legal entity, the PCC needs to comply with Solvency II as a whole thereby offering a proportionate facility for cells.