MFSA MALTA FINANCIAL SERVICES AUTHORITY

Consultation Document

Consultation Document on the New Regime regulating Insurance Undertakings carrying on Long-Term Business and the Distribution of Contracts of Insurance as Retirement Products

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1.0 Introduction

1.1 Following a pre-consultation meeting held with the industry on *29 January 2021* and a workshop held at the MFSA premises on *17 April 2023*, the MFSA is issuing this Consultation Document in relation to the introduction of a new regime regulating *insurance undertakings carrying on long term business and the distribution of contracts of insurance as retirement products*.

1.2 The aim behind the proposed new regime is to regulate the retirement provision business of an authorised insurance undertaking carrying on long term business of insurance and the distribution of contracts of insurance as retirement products.

1.3 A number of Maltese life insurance undertakings are already distributing insurance products with a pension element. The popularity of these products increased following the introduction of tax incentives. A regulatory gap was identified by the MFSA since these type of products are neither regulated by Directive 2016/97 (the "Insurance Distribution Directive") nor by Directive 2016/2361 (the "IORP II Directive"). In particular, these products would not fall under the Insurance Distribution Directive, in view of the fact that the definition of "insurance-based investment product" under the said Directive excludes *"pension products which, under national law, are recognised as having the primary purpose of providing the investor with an income in retirement, and which entitle the investor to certain benefit".* Furthermore, these products did not appear to have sufficiently robust characteristics which would make it more appropriate for an insurance retirement product.

1.4 Therefore, in order to mitigate the said regulatory gap, the MFSA is proposing this new regime to effectively regulate insurance undertakings carrying on long term business and the distribution of contracts of insurance as retirement products by insurance undertakings and insurance intermediaries. This new regime will ensure clarity in the manner in which insurance undertakings are operating their retirement provision business and ensure adequate safeguards and consumer protection in the manufacturing and distribution of contracts of insurance as retirement products.

1.5 The regime will provide clarity on the obligations which Maltese life insurers operating this type of business, are to follow. It also lays down obligations on the manner in which this product is manufactured by insurance undertakings and distributed by relevant insurance undertakings and insurance intermediaries.

1.6 In this respect, the documents in draft format circulated by the MFSA for the purpose of this Consultation Document consist of the following:

- **A new Chapter 16 to the Insurance Rules** entitled *"Retirement provision business of an authorised insurance undertaking carrying on long term business of insurance"* which will contain prudential requirements which an insurance undertaking will be required to comply with. The Chapter will also include an Annex entitled *"Programmed withdrawals – Drawdown rates".* The Annex will contain the drawdown rates which Maltese life insurers distributing the products identified above would be guided by. This Annex establishes consistent guidelines in determining the maximum permitted withdrawal benefits when the product reaches the decumulation stage, and the retirement benefits would commence to be withdrawn;

- **An Annex attached to this Consultation Document** and entitled *"Statistical Model Background Information Drawdown Rates".* This Annex will provide an overview of the statistical analysis carried out for the purpose of deriving the maximum pension drawdown rates for personal or occupational retirement products offered by authorised Insurance undertakings carrying on long term business of insurance and and the distribution of contracts of insurance as retirement products;

- **A new Chapter 7 to the Conduct of Business Rules** entitled "*Requirements relating to products which, under Maltese Law are recognised as having the primary purpose of providing the client with an income in retirement, and which entitle the client to certain benefits".* In this respect the MFSA reviewed the Conduct of Business Rulebook and created a new Chapter which would be applicable only to insurance undertakings and insurance intermediaries. For clarification purposes, in order to make certain provisions of the Insurance Distribution Directive and relevant conduct related requirements applicable to relevant Regulated Persons which manufacture and, or distribute Occupational Retirement Products and, or Personal Retirement Products (as defined in the said Chapter 7), this new Chapter lays down certain requirements including provisions on disclosures, product oversight and governance requirements and the sales process with respect to these products.

- **Appendices to the said Chapter 7** which primarily specify in a clear and comprehensive manner the contents of the documents which relevant authorised insurance undertakings must provide to their Clients:

  Appendix 1: pre-contractual *Key Information Document* for each product;

  Appendix 2: the personalised *Pension Benefit Statement* for each Client;

Appendix 3: *Inputs, Assumptions and Methodologies* to be followed with respect to both the Key Information Document and Pension Benefit Statement.

1.7 It is to be noted that the proposed new regime will also contain a new Legal Notice (Regulation) entitled the "Insurance Business (Retirement provision business) Regulations, 2023". Following the issuance of this Consultation Document, another Consultation Document will be published in the weeks to follow which will include the new Regulation. The new Regulation will contain high-level requirements on general governance arrangements, investment risk management policy, the own risk and solvency assessment, the transfer of the retirement provision business, the appointment of an approved actuary and the run-off of the retirement provision business of an authorised insurance undertaking.

1.8 The purpose of this Consultation Document is to gather feedback from the market on the documents which will be issued for consultation and referred to in paragraph 1.6. As a result of this, these proposals are not binding and are subject to changes and revisions.

1.9 Any comments and feedback in relation to these proposed amendments are to be addressed to the Insurance and Pensions Supervision function and submitted in writing via email to ips_legal@mfsa.mt, referring to this Consultation Document, by not later than **20 July 2023.**

2.0 New definitions in Chapter 16 of the Insurance Rules

2.1 It is being proposed that Chapter 16 of the Insurance Rules will include new definitions for a retirement product which capture and refer to both occupational retirement products and personal retirement products under the ambit of '*'retirement provision business*''.

2.2 It is also being proposed that two new *terms are introduced* to distinguish between an occupational product and a personal product, these being, *"occupational retirement provision business" and "personal retirement provision business"*

2.3 The term *"occupational retirement product"* will refer to an insurance-based investment product which includes a qualifying scheme as defined in the Voluntary Occupational Pension Scheme Rules, 2017, (S.L 123.175), distributed by an authorised insurance undertaking, the purpose of which is to provide cover for a loss of income due to old age and that:

(a) is based on an agreement or contract:

(i) individually or collectively between the employer(s) and the employee(s) or their respective representatives, or

(ii) with self-employed persons, individually or collectively;

where the occupational retirement product is not a qualifying scheme as defined in the Voluntary Occupational Pension Scheme Rules, 2017, (S.L 123.175), the commencement of payment of Retirement Benefits to a policyholder may not be made on a date that is earlier than that on which such policyholder has attained the age of fifty, or later than that on which the policyholder attains the age of seventy-five.

2.4 Additionally, it is also being proposed that Chapter 16 includes the term ''*personal retirement product*'' which will refer to an insurance-based investment product which includes a qualifying scheme as defined in the *Personal Retirement Scheme Rules, 2014 (S.L 123.163).* The purpose behind the introduction of this definition is to have a personal retirement product which will be distributed by an authorised insurance undertaking to provide cover for loss of income due to old age and that:

- is funded solely by the individual concerned or any other person, including the employer, on behalf of the individual policyholder; and,
- where the personal retirement product is not a qualifying scheme as defined in the Personal Pension Scheme Rules, 2014, (*S.L 123.163*), the commencement of payment of Retirement Benefits to a policyholder may not be made on a date that is earlier than that on which such policyholder has attained the age of fifty, or later than that on which the policyholder attains the age of seventy-five.

2.5 Amongst other definitions, it is also being proposed that a definition for *"retirement benefit"* is introduced and is aligned with the definition found in the Pension Rules. This shall include benefits paid by reference to reaching, or the expectation of reaching, retirement or, where they are supplementary to these benefits and provided on an ancillary basis.

3 Chapter 16 to the Insurance Rules

3.1 The proposed new Chapter 16 to the Insurance Rules will include requirements that an authorised insurance undertaking will be obliged to comply with when effecting and carrying out the retirement provision business.

3.2 The MFSA is proposing the introduction of a provision on the **risk-mitigation techniques** to be adopted by authorised insurance undertakings to ensure that the investment strategy of the retirement product is designed to build a stable and adequate individual future retirement income from the product while ensuring fair treatment of all policyholders. The applicable risk-mitigation techniques may include the life-cycling approach, establishing reserves from contributions or investment returns, and using appropriate guarantees to protect against investment losses.

3.3 It is also being proposed that additional information in the current **investment risk management policy** of an authorised insurance undertaking is introduced. The new requirements will stipulate the information which an authorised insurance undertaking needs to include in its current investment risk management policy. The new requirements are over and above the requirements already stipulated in paragraph 28 of Annex I of Chapter 6 to the Insurance Rules, and have been included in view of the fact that the undertaking is also conducting retirement provision business. Furthermore, it is also being proposed that the Chapter will also require undertakings to ensure that the investment risk management policy is reviewed on an annual basis and revised without undue delay should any significant changes to the policy occur. Additionally, the requirements identified in this new provision shall also be made publicly available to ensure that transparency is maintained, as much as possible.

3.4 The MFSA is also proposing **additional requirements on the approved actuary**, to ensure that the actuary conducts a separate assessment on the implications for the fair treatment of the policyholder of a retirement product. In this respect, the new provision will require that the findings be included in a separate section in the actuary's report.

3.5 Additional requirements **to the Own Risk and Solvency Assessment (ORSA) of an authorised insurance undertaking** are also being proposed. In this respect, the authorised insurance undertaking shall conduct its ORSA, in line with the requirements of Section 6.4 of Chapter 6 of the Insurance Rules and shall also factor in the retirement provision business it is carrying on. Additional requirements are also being proposed in the Chapter. These new additional requirements are to be included when an authorised insurance undertaking is conducting its ORSA to ensure that it captures this retirement provision business.

3.6 The Chapter will also contain requirements on the **transfer of the assets of the policyholder.** It is being proposed that requirements are added in order to protect policyholders when these opt to transfer their assets to another authorised insurance undertaking. The new requirement will include obligations which an authorised insurance undertaking is required to comply with both **prior to the transfer** of the assets of the policyholder that is being conducted, as well as **prior to the completion** of the said transfer. It is being proposed that the new provisions would include new requirements stating that transfers may only be made in cash. Furthermore, it is also being proposed that prior to the transfer being conducted, the authorised insurance undertaking from which the policyholder will be transferring its assets is also required to provide the said policyholder with:

(a) retirement rights;
(b) retirement choices;
(c) all applicable charges or direct and indirect fees;
(d) any other information as to their pension rights and choices, particularly that the transfer of such assets shall be made only in cash;

which are available to them under the retirement product prior to any transfer. This will be done to enable the policyholders concerned to make an informed decision.

3.7 Further to the above and prior to the completion of any transfer of assets out of the retirement product, it is also being proposed that the authorised insurance undertaking to which the policyholder will be transferring its assets, will need to provide the policyholder with all the information about all the applicable direct and indirect fees and charges imposed by the transferring authorised insurance undertaking relating to the transfer. It also needs to give confirmation that the transfer has been made with another authorised insurance undertaking, including the details of the new authorised insurance undertaking and the new retirement product.

3.8 It is also proposed that the new Chapter 16 contains the detail with respect to **retirement benefits** and the way the retirement benefits are to be paid to the policyholder at the time the policyholder reaches retirement age. The methodology of how retirement benefits are paid is aligned with the current Pension Rules. In this respect, this provision states that authorised insurance undertakings shall ensure that retirement benefits, other than any benefits paid on death or permanent invalidity of the policyholder, shall be paid in the following forms:

(a) Initial cash lump sum (optional);
(b) Programmed Withdrawals and/or Life Annuity (mandatory);
(c) Additional cash lump sum (optional).

3.9 An **initial cash lump sum** will be optional and the policyholder will become entitled to the said sum on the retirement date of the policyholder. It is to be noted that where the retirement product is a qualifying scheme, the retirement date shall be aligned with the Voluntary Occupational Pension Scheme Rules, 2017, (S.L 123.175) and the Personal Retirement Scheme Rules, 2014 (S.L 123.163) as applicable. Where the retirement product is not a qualifying scheme, the retirement date shall be aligned with the pension rules. It is being proposed that the policyholder may elect up to 30 per centum of the assets of the policyholder as a cash lump sum. Additionally, this provision will include that the initial cash lump sum shall be paid either as one lump sum or a series of tranches within one year from retirement date as the policyholder prefers.

3.10 The option of the **programmed withdrawals and/or life annuity** is a mandatory option. In this respect, following the initial cash lump sum, the remaining assets of a policyholder shall either be withdrawn as programmed withdrawals or be used to purchase a life annuity. When opting for the option of programmed withdrawals, the amounts to be withdrawn shall not exceed the maximum amount of drawdown pension rates as calculated on the basis amounts published in the Annex I to this Chapter on programmed withdrawals – drawdown rates.

3.11 Finally, an **additional cash lump sum** is also optional and it can only be pursued if the remaining assets in the retirement product are more than adequate to generate sufficient retirement income throughout the policyholder's lifetime at valuation date. Should this be the case, 50 per centum of the excess value of such assets, as determined by the valuation, may be withdrawn as an additional cash lump sum. This option also includes that the additional lump sum may only be taken after three years from the commencement of the policyholder's retirement benefits, and every year thereafter. In the event that a policyholder is domiciled in Malta, the conditions of this provision shall only apply where the annual retirement benefits from an annuity exceeds €50,000. Furthermore, this value shall be adjusted annually to take into account the changes in the index of inflation as published by the National Statistics Office.

3.12 It is being proposed that the above, in respect to the manner in which retirement benefits are to be paid out, shall be without prejudice to any other limitations on the withdrawal of the retirement assets as may be specified by any other pensions or taxation legislation which a policyholder may be subject to.

3.13 Chapter 16 is also proposing to introduce new requirements in the case of a **run-off of the retirement provision business of an authorised insurance undertaking**. The new paragraphs lay down the requirements that the undertaking would need to comply with should a decision to carry out an orderly run-off of its retirement provision business be reached. In this respect, the provision lays down that the undertaking would be required to formally inform the competent authority within **180 days** before the run-off begins. Furthermore, the provision shall include information which the authorised insurance undertaking would need to provide to the competent authority, in a timely manner. It is to be noted that the list is not exhaustive and that the Authority may ask for any other information it deems necessary.

4.0 Annex I to Chapter 16 of the Insurance Rules on Programmed Withdrawals – Drawdown Rates

4.1 During the pre-consultation stage held with the industry, a number of market players referred to the fact that Malta does not currently have prescribed drawdown rates. The MFSA is therefore proposing a new Annex to Chapter 16 of the Insurance Rules to set consistent guidelines for the market in determining the maximum permitted income withdrawal from 'capped' drawdown retirement benefits. This Annex will provide tables and instructions to determine the maximum income withdrawal rates.

4.2 In order to draft the Annex to Chapter 16, the MFSA's actuarial team assessed the Malta-specific mortality and population data (age and gender specific) for 2001 to 2020, obtained from the National Statistics Office, to estimate the drawdown rates. The Annex contains the necessary tables as well as instructions as to how these drawdown rates are to be used. Furthermore, with the development of this document, harmonisation across the insurance industry will be achieved in the manner in which all Maltese insurers apply the drawdown of retirement benefits, so as to ensure maximum policyholder protection.

4.3 The proposed new annex will determine the maximum rate at which the accumulated funds of the retirement product will be drawdown to yield retirement benefits. The instructions are simple to follow in that to access the correct drawdown figure, one needs to have the policyholder's age at the point of calculation, and to access information on Maltese government bond yields at the same date. This document also includes a step-by-step example on how authorised insurance undertakings are to determine the basis amount and pension drawdown amounts. In this respect, it is to be noted that the document includes a disclaimer that these drawdown rates may need to be amended from time to time as the Authority may deem necessary.

5.0 Annex I to this Consultation Document on Statistical Model Background Information on the Drawdown Rates

5.1 In conjunction with the Annex to Chapter 16 on Programmed Withdrawals – Drawdown rates, the actuarial team also worked on another Annex providing statistical model background information which analyses how the MFSA estimated the projected mortality rates used in drawing up the tables to determine the amounts to be drawn down.

5.2 The Annex which is being attached to this Consultation provides an overview of the statistical analysis carried out so that the details provided will allow a trained user to be able to (closely) replicate the listed rates. It is to be noted that the aim of the Annex is not for the insurance industry to replicate these listed rates.

5.3 The Annex includes past mortality data as provided by the National Statistics Office for the period between 2001-2020 including the number of deaths and mid-year exposure levels for each calendar year, split by age and gender. This serves as input for mortality rate projections. The document also includes the statistical estimation model and statistical analysis results to provide guidance should the licence holder wish to replicate the listed drawdown rates as per the new Annex to the new Chapter 16.

6.0 The new Chapter 7 to the Conduct of Business Rules

6.1 In order to address the regulatory gap (referred to in section 1 above) and to ensure adequate safeguards and consumer protection in the manufacturing and distribution of the retirement products within scope, the MFSA is proposing the publication of a new distinct Chapter 7 within the Conduct of Business Rules which is entitled *"Requirements relating to Products which, under Maltese law are recognised as having the Primary Purpose of providing the Client with an Income in Retirement, and which entitle the Client to certain Benefits."*

6.2 The aim is primarily to ensure the applicability of specific provisions of the Insurance Distribution Directive and relevant conduct related requirements applicable to relevant Regulated Persons which manufacture and, or distribute Occupational Retirement Products and, or Personal Retirement Products (as defined in this new Chapter 7). In this respect, requirements found in the current Chapters of the Conduct of Business Rules have been either made applicable *mutatis mutandis* (via cross-reference) or replicated and adjusted to be made relevant in the context of the retirement products referred to above.

6.3 It is being proposed that the said Chapter 7 contains and makes reference to various conduct-related requirements which are similar to those found in the current Chapters of the Conduct of Business Rulebook, including, amongst other matters, the following subject- matters:

(a) Disclosure requirements and advertising requirements (including relevant risk warnings);
(b) the provision of relevant pre-contractual information;
(c) Product Governance and Oversight requirements;
(d) Complaints management; and
(e) Sales process and sales management.

6.4 Certain requirements, particularly in relation to disclosures and risk warnings, have been adapted or adjusted as considered necessary. It needs to be emphasised that these adaptations include the following:

(a) in order to ensure a high level of consumer protection, in terms of the proviso to R.6.92 of Part A of the Draft Chapter 7, it is specified that, at all times, the Regulated

Person shall, as a minimum, carry out an appropriateness assessment to the Client when distributing and providing services in relation to the Product;

(b) in terms of R.6.45 of Part A of the Draft Chapter 7, a Regulated Person shall ensure that it does not provide any advertisements which indicate past performance, simulated past performance and future performance.

6.5 Moreover, the MFSA is proposing that this new Chapter is also supplemented with further relevant provisions which are not currently found in the current Conduct of Business Rules. For instance:

(a) requirements in relation to certain information to be given to the Client such as, information on the *Accumulation Phase and Decumulation Phase* of a Retirement Product;
(b) information to be given to Clients during *pre-maturity or retirement phase*;
(c) information to be given to the beneficiaries during the *pay-out phase*; and
(d) *other information* to be given to clients and beneficiaries.

6.6 In this respect, this proposed new Chapter 7 is being divided in **three parts**, whereby **Part A** applies to both:

(a) *specific insurance undertakings*: that is, persons who fall under point (iii) of the definition of 'Regulated Person' in the Glossary which carry on long term insurance business and which manufacture and, or distribute occupational retirement products and, or personal retirement products; and

(b) *specific insurance intermediaries*: that is, persons who fall under point (iv) of the definition of 'Regulated Person' in the Glossary (other than ancillary insurance intermediaries) which distribute occupational retirement products and, or personal retirement products.

Whilst **Part B** applies only to persons specified in paragraph (a) above and **Part C** applies only to persons specified in paragraph (b) above.

6.7 The MFSA is also proposing that the new Chapter 7 of the Conduct of Business Rules also contains certain specific definitions which shall apply in the context of this new Chapter, such as definitions of "*Beneficiary*", "*Retirement Benefit*", "*Occupational Retirement Product*" and "*Personal Retirement Product*", as well as definitions of "*Accumulation Phase*" and "*Decumulation Phase*". However, other terms used, which are not defined therein, shall be construed in terms of the Glossary to the Conduct of Business Rules.

7.0 Three new Appendices to the said Chapter 7 of the Conduct of Business Rules

7.1 The proposed new Chapter 7 of the Conduct of Business Rules also contains the following three Appendices.

Appendix 1 - The Key Information Document

7.2 The MFSA is proposing the publication of Appendix 1 to this proposed new Chapter 7. Appendix 1 contains information on the Key Information Document ("KID"), a pre-contractual document which needs to be drawn up by the Manufacturers for each retirement product and which is to be provided to clients prior to the conclusion of the contract in order to enable clients to understand and compare the key features and risks of occupational retirement products and/or personal retirement products.

7.3 The KID has been drafted with the intention to provide a clear and comprehensive picture of the retirement product enabling the policyholder to have a better understanding of the retirement product they would be purchasing. In fact, in order to enhance the requirements included in the KID, Part II of this Appendix contains user-friendly picture templates which have been developed within this Appendix to enhance the requirements that the KID needs to contain.

7.4 In drafting the KID and its contents, the MFSA also took into account, amongst others, the main requirements emanating from Regulation (EU) 2019/1238 (the "PEPP Regulation"), Directive (EU) 2016/2341 (the "IORP Directive"), as well as Regulation (EU) 1286/2014 (the "PRIIPs Regulation").

Appendix 2 - The Pension Benefit Statement

7.5 The MFSA is also proposing a new Appendix 2 to the new Chapter 7 which will contain information on the Pension Benefit Statement ("PBS"). This is a concise, personalised document drawn up by the Manufacturers and provided to each Client, at least annually, containing key information for the Client in relation to occupational retirement products and, or personal retirement products.

Provided that, during the Decumulation Phase, where the Client has chosen not to opt for an annuity, the insurance undertaking shall provide a Pension Benefit Statement to every Client at least annually, including the information laid down in Appendix 2 to this Chapter, specifically within the section titled *"How have my savings under the retirement product changed in the last 12 months?" of the said Appendix.* The said Pension Benefit Statement should also include information on the maximum annual withdrawals for the next 12 months.

7.6 This Appendix outlines the information contained in the Pension Benefit Statement, which information shall be accurate, updated and made available to each client free of charge and on an annual basis, as a minimum. In addition, any material changes to the information, when compared to the information provided in the previous year, shall be clearly indicated to the Client.

7.7 The PBS has been carefully developed with the key purpose of providing a clear picture of the evolution of the product to the policyholder who acquired the product. In fact, in order to enhance the requirements included in the PBS, Part II of this Appendix contains picture templates which have been created to enable a better understanding of the requirements contained in the PBS by the policyholder.

7.8 In drafting this Appendix, the MFSA has also taken into account the salient features of the Pension Benefit Statement as outlined in Directive (EU) 2016/2341 (the "IORP II Directive").

Appendix 3 – Inputs, Assumptions and Methodologies for the purposes of Appendix 1 and Appendix 2 to this Chapter

7.9 The aim of Appendix 3 is to set out further guidance on the inputs, assumptions and methodologies to be followed by Manufacturers when drawing up certain elements of the pre-contractual KID and the personalised PBS set out in Appendix 1 and Appendix 2, respectively.

8.0 Transitional Period

8.1 The MFSA is proposing that, in light of the intricacies of this proposed new regime and in view of the fact that retirement products are already being manufactured and distributed on the market, there should be a transition period. In this respect, the MFSA is of the view that a transition period of one (1) year from the day the law is published should be provided to the industry. This will enable Maltese insurers which are already carrying out and effecting retirement provision business and distributing these products ample time to come in line with the requirements of the legislation.

9.0 The Way Forward

9.1 Any comments and feedback in relation to the Consultation are to be addressed to the Insurance and Pensions Supervision function and submitted via email on ips_legal@mfsa.mt by not later than **20 July 2023.**