MFSA MALTA FINANCIAL SERVICES AUTHORITY

Feedback Document

Feedback Statement on the Consultation on the Proposed Amendments to the Insurance Distribution Rules

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Contents

1.0 Introduction

On 26 January 2023, the MFSA issued a Consultation Document on the Proposed Amendments to the Insurance Distribution Rules. The Consultation Document proposed to amend a number of Insurance Distribution Rules in line with findings observed during regulatory work as well as other findings observed by the market whilst carrying out their operations. Further to the said Consultation Document, the MFSA is issuing a Feedback Statement on the comments received from interested parties in relation to this Consultation.

In this respect, it is to be noted that the MFSA received comments to amend parts of the Insurance Distribution Rules which were not issued for Consultation. The MFSA will be reviewing such feedback, following which such amendments may be included in the next set of amendments to the Insurance Distribution Rules. A number of market participants also provided drafting suggestions, particularly in relation to Chapter 9 of the Insurance Distribution Rules. It is to be noted that the MFSA has taken on board a number of these drafting suggestions.

2.0 Main Comments Received on the Proposed Amendments to Chapter 1 in Part A of the Insurance Distribution Rules

2.1 Amendments relating to the governing law of the Professional Indemnity Requirements

2.1.1 ***Industry Comment:*** *A market participant suggested to include once again reference to Maltese law as in paragraph 1.9.10 of Chapter 1 of the Insurance Distribution Rules on the governing law of a professional indemnity policy.*

MFSA's Position: The MFSA would like to clarify that reference to EU law in the proposed amendment includes Maltese law and as such, specific reference to Maltese Law is not necessary.

2.1.2 ***Industry Comment:*** *A number of market participants suggested the inclusion of reference to the law of EEA States under paragraph 1.9.10 of Chapter 1 of the Insurance Distribution Rules.*

MFSA's Position: Following a review of the comments received from the market and upon internal discussion, the MFSA remains of the view that the professional indemnity policy shall be governed by the law of a European Union Member State or the law of the United Kingdom. In this respect, the MFSA would like to clarify that "EU Law" refers to the law of a European Union Member State.

2.1.3 ***Industry Comment:*** *A market participant suggested that paragraph 1.9.10 of Chapter 1 of the Insurance Distribution Rules should be amended to read as "The policy shall be governed by EU* ***and/or*** *UK law." as opposed to "The policy shall be governed by EU* ***or*** *UK law.", in order to allow for the extension of professional indemnity insurance cover for enrolled companies that form part of an international group of companies.*

MFSA's Position: Following a review of the comments received, and upon further internal discussions, the MFSA remains of the view that paragraph 1.9.10 of Chapter 1 of the Insurance Distribution Rules should read that the policy shall be governed by the law of a European Union Member State **or** the law of the United Kingdom for clarity purposes.

2.2 Amendments relating to excess in Professional Indemnity Requirements

2.2.1 ***Industry Comment:*** *A number of market participants suggested that the proposed amendments in relation to the professional indemnity insurance policy excess should be revised in order to allow for higher policy excess. In this respect, one market participant proposed the inclusion of a higher deductible above the maximum of €50,000 only by prior approval of the MFSA. Another market participant proposed the introduction of a scale of excesses, where the applicable maximum deductible allowed will be dependent on the entity's limit of indemnity cover in place. Another market participant suggested the application of a capital loading, on a sliding scale, for any excess over and above €50,000.*

MFSA's Position: Following a review of the comments received and further internal discussions, the MFSA remains of the view that the excess under paragraph 1.9.7 of Chapter 1 of the Insurance Distribution Rules should be of a sum not exceeding 1% of the limit of indemnity and subject to a maximum of €50,000. It is to be noted that the proposed suggestion in the Consultation Document emanates from an exercise conducted by the Authority whereby the MFSA analysed the issues encountered by an insurance intermediary when purchasing a professional indemnity policy. The MFSA would like to further clarify that paragraph 1.9.8 of Chapter 1 of the Insurance Distribution Rules already allows for the possibility of having a higher excess, and also contains the procedure as to how a higher excess can be secured.

3.0 Main Comments Received on the Proposed Amendments to Chapter 2 in Part A of the Insurance Distribution Rules

3.1 Amendments to Remove the Bank Reference Requirement

3.1.1 ***Industry Comment:*** *A market participant commented on the proposed removal of the bank reference requirement and opined that such removal makes it difficult for the insurance undertaking to ensure the fitness and properness of the applicant.*

MFSA's Position: Primarily, the MFSA would like to clarify that Chapter 3 of the Insurance Distribution Rules states that the competent authority must be satisfied that there is nothing in an applicant's present state or past record that would make the applicant unfit for the type of registration or enrolment such person applies for or holds or proposes to hold. The appointing licence holder may test the fitness and properness of such a person in a number of ways. The MFSA would like to clarify that the removal of bank reference does not mean that the appointing licence holder cannot still request the said person to provide a bank reference to be able to conduct the fit and proper test.

3.2 Annex to Chapter 2 of the Insurance Distribution Rules

3.2.1 ***Industry Comment:*** *A market participant stated that they were of the understanding that the Annex to Chapter 2 of the insurance Distribution Rules was going to replicate the requirements of Chapter 6 of the Insurance Distribution Rules and emphasise their importance to pre-enrolment. In this respect, clarification was sought by the same market participant as to the purpose of the Annex to Chapter 2 of the Insurance Distribution Rules.*

MFSA's Position: The MFSA would like to clarify that the minimum requirements that a Tied Insurance Intermediary or Ancillary Insurance Intermediary is required to acquire through the pre-enrolment course are set out in the Annex to Chapter 2 of the Insurance Distribution Rules. These requirements are in line with the knowledge and ability requirements under Chapter 6 of the Insurance Distribution Rules. The purpose of the Annex to Chapter 2 of the Insurance Distribution Rules was to clarify the minimum requirements that need to be included in the pre-enrolment course, in accordance with paragraph 6.4.1 of Chapter 6 of the Insurance Distribution Rules.

3.2.2 ***Industry Comment:*** *Clarification was sought from a market participant who stated that the Insurance Distribution Rules do not specify that a pre-enrolment course for Tied Insurance*

Intermediaries may only be provided subject to approval by the Authority of the course content.

MFSA's Position: The MFSA would like to clarify that, in accordance with paragraph 6.4.1 of Chapter 6 of the Insurance Distribution Rules, all pre-enrolment courses need to be approved by the competent authority. In order to ensure that such pre-enrolment courses are approved by the competent authority, the MFSA requires entities providing a pre-enrolment course to submit a course outline to the competent authority for approval.

3.2.3 ***Industry Comment:*** *A market participant suggested that the Authority publishes a list of approved courses which are not delivered by a licence holder appointing a Tied Insurance Intermediary or appointing an Ancillary Insurance Intermediaries (an appointing licence holder as defined in the Annex to Chapter 2 of the Insurance Distribution Rules). The said market participant stated that without such a list, it would not be clear whether such course has obtained MFSA approval or otherwise.*

MFSA's Position: The MFSA is of the view that the publication of such a list is not necessary. Pre-enrolment courses are approved by the competent authority and therefore a licence holder can ask the course provider to confirm whether the course being offered has been approved by the MFSA or not.

3.2.4 ***Industry Comment:*** *Another market participant sought clarification as to whether the training referred to in paragraph 15 in Part IX of the Annex to Chapter 2 of the Insurance Distribution Rules is considered to be in addition to the pre-enrolment course. The same market participant also sought to confirm that such training is not subject to the assessment referred to in Paragraph 13 of Part VIII of the same Annex.*

MFSA's Position: The MFSA would like to clarify that the training referred to in paragraph 15 in Part IX of the Annex to Chapter 2 of the Insurance Distribution Rules is expected to be given in addition to the pre-enrolment course. The assessment under paragraph 13 of the same Annex is solely required to be undertaken on the knowledge gained during the Tied Insurance Intermediary or Ancillary Insurance Intermediary pre-enrolment course. Where the pre-enrolment course is not being delivered by an appointing licence holder, the applicant is required to undertake an assessment of the knowledge gained during the Tied Insurance Intermediary or Ancillary Insurance Intermediary pre-enrolment course. Following the attendance of this course, the said person shall also be required to attend training delivered by the appointing licence holder in relation to the actual insurance policies to be distributed by the Tied Insurance Intermediary or Ancillary Insurance Intermediary. The said training shall also include an overview of the terms and conditions included in the agreement between the Tied Insurance Intermediary or the Ancillary Insurance Intermediary and the appointing licence holder. In such a case, since the training referred to in paragraph 15 of Part IX of the Annex does not form part of the pre-enrolment course, an assessment is not necessary.

Nevertheless, it is up to the licence holder appointing such person to decide whether or not an assessment is necessary. It is to be noted that the Authority is to be informed that training has been provided.

3.3 Schedules 4 to 8 to Chapter 2 of the Insurance Distribution Rules

3.3.1 ***Industry Comment:*** *A market participant noted that paragraph 3.3.1 of the Consultation Document on the amendments to the Insurance Distribution Rules states that Schedules 4 to 8 to Chapter 2 of the Insurance Distribution Rules, which contain the application forms for enrolment in the Tied Insurance Intermediaries List or the Ancillary Insurance Intermediaries List, state that the* ***applicant*** *must confirm that each of the individuals who is to carry out the tied or ancillary insurance intermediaries' activities is a fit and proper person. In this respect, the same market participant suggested that the word 'applicant' should be replaced by the word 'person'.*

MFSA's Position: The MFSA has taken note of the concerns raised by the market and will be amending Schedules 4 to 8 to refer to the term '**person concerned**' to align it with the definition of the same term indicated in paragraph 2.2.1 of Chapter 2 of the Insurance Distribution Rules.

4.0 Main Comments Received on the Proposed Amendments to Chapter 4 in Part A of the Insurance Distribution Rules

4.1 Amendments to the Capital Requirements of Insurance Intermediaries

4.1.1 ***Industry Comment:*** *A number of market participants opined that the 4% capping at €1,000,000 is excessive and suggested that the MFSA looks into the imposition of a lower capping.*

MFSA's Position: Primarily it is to be noted that the MFSA's priority is the protection of policyholders. Furthermore, it is to be noted that the proposed amendments are a result of an extensive research conducted by the MFSA on the manner in which other Member States regulate the capital requirements of insurance intermediaries. Following a review of the comments received and further internal discussions, the MFSA remains of the view that the imposition of a lower capping may be detrimental to policyholders and as a result, the capping proposed in the Consultation Document is to be retained.

4.1.2 ***Industry Comment:*** *A market participant questioned whether the proposed amendment to the capital requirements of insurance intermediaries is in line with the capital requirements under the Insurance Distribution Directive.*

MFSA's Position: The MFSA notes that Article 10 (6) of the Insurance Distribution Directive states that Member States shall take all necessary measures to protect customers against the inability of the insurance, reinsurance or ancillary insurance intermediary to transfer the premium to the insurance undertaking or to transfer the amount of claim or return premium to the insured. The same Article continues by stating that such measures "shall take any one or more of the following forms". Therefore, it is clear that the Insurance Distribution Directive allows Member States to decide whether to take one or more of the five options available. In view of the fact that Malta has already taken options a, b and c on board, and the fact that a number of Member States have applied paragraph b in a different way, the MFSA is of the view that the proposed amendment should be retained as proposed in the Consultation Document.

4.1.3 ***Industry Comment:*** *A market participant suggested that the own fund requirement under the First Schedule to Chapter 4 of the Insurance Distribution Rules should be calculated on the basis of the insurance broker's earnings, as opposed to the gross premiums. In this respect, the same market participant quoted the approach adopted in the United Kingdom, where the required own funds for an insurance broker are calculated as a percentage of the annual income from its insurance distribution activity.*

MFSA's Position: The MFSA would like to clarify that, from the research conducted on the application of the 4% of written premium solvency requirement, a number of European Union Member States have taken on board this measure to protect customers in line with article 10 (6) (b) of the Insurance Distribution Directive. Such Member States have based the 4% of the sum of annual premiums received requirement on the premiums collected or the annual premiums received, which is also in line with article 10 (6) (b) of the Insurance Distribution Directive. It is to be noted that the United Kingdom is the only jurisdiction which bases the 4% on the intermediary's annual income. Following a review of the comments received and further internal discussions, the MFSA remains of the view that the 4% requirement should be based on the annual gross premium receivable.

4.1.4 ***Industry Comment:*** *Clarification was requested with respect to the applicability of the proposed €1,000,000 cap to the calculation of the Required Own Funds. The said market participant requested a clarification as to whether the proposed €1,000,000 cap is applicable to the calculation of the Required Own Funds as per Row 32 of Form 8A of the Business of Insurance Intermediaries Statements of the First Schedule of Chapter 4 of the Insurance Distribution Rules.*

MFSA's Position: The MFSA would like to confirm that the proposed capping is applicable to the Required Own Funds as per Row 32 of Form 8A of the Business of Insurance Intermediaries Statements of the First Schedule of Chapter 4 of the Insurance Distribution Rules.

4.2 Amendments related to the Credit Risk Transfer Agreement – 10-Working-Day Notification Requirement

4.2.1 ***Industry Comment:*** *A market participant raised its concern on the 10-working-day notification requirement related to the credit risk transfer agreement. The said market participant stated that removing the requirement of having the MFSA's approval before entering into a credit risk transfer agreement, eliminates the certainty that such agreement fully meets the MFSA's expectations and results in no finality to the process. Clarification was also sought as to whether the MFSA might still request changes after the credit risk transfer agreement would have been entered into and whether such a situation put in question the validity of the agreement. Another market participant also suggested that the MFSA should provide clear timelines as to by when the enrolled person should receive any feedback by the MFSA following the submission of the Declaration Form and, unless any such feedback is submitted by the MFSA within the said time period, then the matter is deemed to be closed.*

MFSA's Position: The MFSA notes that the Declaration Form is to accompany the information to be submitted to the competent authority for supervisory purposes pursuant to sub-paragraph (c) of the third proviso to paragraph 4.4.2. Once the MFSA receives the documentation, it will only acknowledge receipt of the documentation. Nevertheless, it is be noted that the MFSA may review the credit risk transfer agreement and the Declaration Form on a case by case basis whilst carrying out a compliance inspection or desk-based reviews, to ensure that such arrangement is aligned with the Second Schedule to Chapter 4 of the Insurance Distribution Rules.

4.2.2 ***Industry Comment:*** *Another market participant raised its concern on the notification requirement related to the credit risk transfer agreement and stated that it is not practical to inform the MFSA of the credit risk transfer agreement on the same date of its execution. In this respect, the same market participant suggested that notification is amended to 5 working days after the execution of the credit risk transfer agreement.*

MFSA's Position: The MFSA has taken note of the concerns raised by the market and will be amending the notification requirement to 5 working days after the execution of the credit risk transfer agreement. Nevertheless it is to be noted that the MFSA expects that the compliance officer ensures that all the requirements in the Schedule are complied with and that the insurance intermediary ensures that all the necessary checks need to be conducted prior to the commencement of the credit risk transfer agreement. This notwithstanding that the

Declaration Form may be submitted to the MFSA up to 5 working days after the execution of the credit risk transfer agreement.

4.3 Amendments related to the Credit Risk Transfer Agreement – New Declaration Requirement under the Newly Proposed Third Schedule

4.3.1 ***Industry Comment:*** *A market participant opined that the Compliance Officer should be signing the Declaration Form in conjunction with the Managing Director/CEO or General Manager. In this respect, the same market participant stated that the wording of the declaration refers to procedures incorporating mitigating action to address conflicts of interests and to an adequate spread of business, which from an operational perspective, falls under the responsibility of the Managing Director/CEO or General Manager.*

MFSA's Position: Following internal discussions, the MFSA has taken note of the concern raised and will be amending the Declaration Form to also include a signature of the Managing Director, CEO or General Manager of the insurance intermediary in line with the suggested feedback.

4.3.2 ***Industry Comment:*** *A market participant commented that confirming the freedom of services and freedom of establishment arrangements of the insurance undertaking is too onerous at the stage when terms of business agreements are entered into. The same market participant stated that this information may change as years pass by, in which respect it was suggested that the responsibility that the Insurance undertaking is authorised to write risks in the territory where the risk is located should remain on the insurance undertaking.*

MFSA's Position: The MFSA expects that the insurance intermediary is fully aware of the business it is entering into and carries out the necessary checks to ensure that the insurance undertaking willing to take the credit risk at the point in time the credit risk is entered into and has the necessary freedom of services and freedom of establishment arrangements. In this respect, the MFSA also expects that the insurance intermediary implements an adequate process to ensure the monitoring on an ongoing basis of any changes to the credit risk transfer agreements. Furthermore, where the insurance undertaking is not authorised in an EU Member State, the MFSA expects the intermediary to carry out the necessary checks and obtain assurances that the said undertaking has the necessary permissions to be able to operate in the jurisdiction it intends to operate. Whilst the information may indeed change as years go by, we would understand that different credit risk transfer agreements would need to be entered into depending on the business the intermediary is entering into.

4.4 Amendment of the Definition of "Insurance Undertaking" in relation to Credit Risk Transfer

4.4.1 ***Industry Comment:*** *A market participant requested clarification as to whether the proposed amendment to the definition of "insurance undertaking" allows enrolled individuals or enrolled companies to enter into credit risk transfer agreements with third country insurance undertakings, specifically UK insurance undertakings.*

MFSA's Position: The MFSA would like to clarify that the enrolled individual or the enrolled company may enter into a credit risk transfer agreement with any third country insurance undertaking which has obtained the necessary authorisations or permissions in the third country where its head office is situated and has the necessary permission to be able to operate in the Member State it intends to operate.

4.4.2 ***Industry Comment:*** *A market participant stated that the proposed amendment to the definition of "insurance undertaking" is in conflict with the EIOPA's paper on Recommendations for the insurance sector. The same market participant also made reference to Article 31 of the Insurance Business Act in stating that, should the enrolled person place insurance business with an unauthorised insurance undertaking, prior to placing that insurance risk the enrolled person should seek the MFSA's written consent.*

MFSA's Position: The MFSA would like to clarify that, when it refers to an insurance undertaking, it is referring to an undertaking which has the necessary permissions or authorisation to operate. The MFSA also expects that such undertaking also has the necessary permissions to be able to operate in other Member States such as the setting up of a branch in line with EIOPA's paper on Recommendations for the insurance sector in the light of the UK withdrawing from the EU. Furthermore, the MFSA would like to clarify that the provision of Article 31 of the Act refers to the entering into of one particular risk with an "unauthorised insurance undertaking". This part of Chapter 4 refers specifically to the instance where an insurance intermediary would like to enter into a credit risk transfer agreement with an insurer which, in this case, is authorised in a jurisdiction outside of the European Union.

4.4.3 ***Industry Comment:*** *A market participant proposed that the definition of 'insurance undertaking' is amended to include reference to a third country insurance undertaking which is authorised* ***under its laws where its head office is situated****. In this respect, the same market participant stated that this suggestion is based on the reasoning that a third country insurance undertaking needs to be licensed by the competent authority where its head office is situated before having the necessary permissions to operate in the jurisdictions where the risk is situated.*

MFSA's Position: Following internal discussions, the MFSA has taken note of the concern raised and will be amending the definition of 'insurance undertaking'.

5.0 Main Comments Received on the Proposed Amendments to Chapter 8 in Part B of the Insurance Distribution Rules

5.1 Amendments to the Monies to be paid to the Undertaking from the Intermediary within 2 Business Days

5.1.1 ***Industry Comment:*** *A number of market participants opined that the proposed amendment does not protect the policyholders' interest and appears to go against the current trend being adopted by the local insurance market in promoting the use of online payment of premium. In this respect, it was suggested that a more prudent approach should be adopted and therefore consider revising the period to say 5 business days, which effectively means 7 running days, for clients' monies to be deposited.*

MFSA's Position: Following internal discussions, the MFSA remains of the view that all insurance monies are to be paid into the Tied Insurance Intermediaries Account or Ancillary Insurance Intermediaries Account by not later than the next fifteen business days after the day the money is paid to or received by the insurance intermediary as originally proposed in the Consultation Document.

5.1.2 ***Industry Comment:*** *In order to ensure a level playing field for all categories of intermediaries enrolled under the Insurance Distribution Act, market participants suggested that any proposed changes to the period within which clients' monies are to be deposited should also apply to Agents, Managers and Brokers.*

MFSA's Position: Following a review of the comments raised and internal discussions, the MFSA remains of the view that a distinction is to be drawn between Agents, Managers and Brokers and Tied Insurance Intermediaries and Ancillary Insurance Intermediaries. The risk presented by Agents, Managers and Brokers and by Tied Insurance Intermediaries and Ancillary Insurance Intermediaries are different. By drawing a distinction between Agents, Managers and Brokers and Tied Insurance Intermediaries and Ancillary Insurance Intermediaries, the MFSA aims at protecting policyholders.

5.1.3 ***Industry Comment:*** *A market participant suggested the inclusion of an additional proviso which states that the intermediary may pay directly to the insurance undertaking monies received by the enrolled person since a strict interpretation of the current paragraph 8.2.7 may be interpreted to prohibit the deposit of such monies directly with the insurance undertaking.*

MFSA's Position: The MFSA would like to clarify that paragraph 8.2.7 of Chapter 8 of the Insurance Distribution Rules does not prohibit insurance intermediaries from depositing monies directly with insurance undertakings. In fact, there are insurance intermediaries which do not hold clients' monies, in which case such monies are deposited directly with the insurance undertaking. Paragraph 8.2.7 of Chapter 8 of the Insurance Distribution Rules is there to ensure that where an insurance intermediary collects clients' monies and deposits such monies in the specified account, those monies collected are then deposited to the insurer within the timeframe provided in the of Chapter 8 of the Insurance Distribution Rules.

6.0 Main Comments Received on the Proposed Amendments to Chapter 9 in Part B of the Insurance Distribution Rules

6.1 Amendments to Provisions on the Fidelity Bond

6.1.1 ***Industry Comment:*** *A market participant opined that the amendments proposed by the MFSA to the provisions of the fidelity bond are discriminatory towards smaller entities who do not form part of a group and hence cannot refer to their parent companies to provide a guarantee towards any required fidelity bond.*

MFSA's Position: Following a thorough review of all the comments received with respect to the fidelity bond, the MFSA remains of the view that the requirements of the fidelity bond should be retained as suggested in the latest amendments of the Consultation Document.

7.0 Main Comments Received on the Proposed Amendments to Chapter 10 in Part B of the Insurance Distribution Rules

7.1 Amendments in relation to the Auditor's Management Letter

7.1.1 ***Industry Comment:*** *A market participant commented upon the reference made to the enrolled company's or enrolled individual's reply to the auditor's management letter and stated that this is misleading. In this respect, the said market participant suggested that reference should alternatively be made to the enrolled person in view of the fact that Chapter 10 of the Insurance Distribution Rules solely applies to a person enrolled in the Agents List, Managers List or Brokers List.*

MFSA's Position: The MFSA has taken note of the concerns raised by the market and will be amending Chapter 10 of the Insurance Distribution Rules to make reference to the term 'enrolled person'.

8.0 Way Forward

A Circular informing market participants on the applicability of the proposed amendments to the Insurance Distribution Rules will be issued together with this Feedback Statement.

9.0 Contacts

Any queries or requests for clarifications in respect of the above should be addressed by email on ips_legal@mfsa.mt.