

9 July 2024

## Circular Setting the MFSA's Expectations with regards to Outsourcing Arrangements including Delegation of Authority provided by Authorised Undertakings

### **1.0 Introduction**

On 12 August 2020, the MFSA issued a [Circular](#) on the amendments to Chapter 6 of the Insurance Rules issued under the Insurance Business Act (CAP.403). This communication primarily focused on the obligation of authorised insurance undertakings, authorised reinsurance undertakings, captive insurance undertakings and captive reinsurance undertakings (herein referred to as "authorised undertakings") to notify the MFSA of the outsourcing of key and/or critical or important functions or activities as well as of any subsequent material developments with respect to those functions or activities by such authorised undertakings.

The MFSA is now issuing this Circular to set its expectations clearly and formally with regards to the requirements listed in paragraph 6.8 of Chapter 6: System of Governance of the Insurance Rules in circumstances where authorised undertakings:

- a. outsource a key and/or critical/important function to a service provider; and/or
- b. enter into an arrangement with a Managing General Agent ("MGA") and/or an intermediary ("INT") and/or a Third-Party Administrator ("TPA") giving them delegated underwriting and/or claims and/or distribution authority.

### **2.0 Scope**

The primary objectives of this Circular are to:

- i. explain the risk-based approach that will be adopted by the MFSA in relation to 1.a and 1.b above;
- ii. indicate the level of information and documentation required to be submitted by authorised undertakings to the MFSA in addition to the formal notification as required under Chapter 6: System of Governance of the Insurance Rules. This is to ensure alignment between the level of information and documentation to be submitted and the level of risk posed by the specific outsourcing arrangement / delegation of authority;

- iii. launch specific tables containing the information and documentation which authorised undertakings are expected to compile and submit to the MFSA, in addition to the notification in writing which is expected to reach the MFSA sixty (60) days prior to the outsourcing of key and/or critical or important functions or activities including arrangements entered into with MGAs, INTs and/or TPAs giving them delegated underwriting and/or claims and/or distribution authority.

These new tables will seek to achieve:

- a. higher level of convergence across the market;
- b. more clarity on the information and documentation which is to be provided to the Authority; and
- c. increased efficiency and a more timely “no objection” process.

Several authorised undertakings are already familiar with most of the information and documentation outlined in the tables referred to in 2.iii above. This is in view of the fact that most of the information and documentation is already being submitted or requested to be submitted via various interactions with authorised undertakings when notifying the Authority of new outsourcing arrangements (including delegation of authority). The tables are primarily collating all the required information and/or documentation needed in one specific location to make the “no objection” process smoother and more efficient. In this regard, the Authority has also integrated Declarations within the Tables which the Board member responsible for the oversight of the distribution activities (where relevant) and the Compliance Officer need to complete when submitting the notification to the Authority.

The MFSA has already implemented a strong outsourcing supervisory framework as also endorsed by EIOPA in its *‘Final report of the review by peers’* dated 22 June 2022<sup>1</sup>, particularly with the identification of MFSA’s good practices. By means of this Circular, the MFSA intends to continue enhancing its solid outsourcing monitoring framework by addressing the recommendations noted by EIOPA and integrating these into the information and documentation to be submitted by authorised undertakings.

### **3.0 Guidelines applicable to Outsourcing Arrangements including Delegation of Authority**

In line with paragraph 6.8.3 of Chapter 6: System of Governance of the Insurance Rules, an authorised undertaking is to provide the MFSA with:

- a. a notification in writing within sixty (60) days, prior to the outsourcing of key and/or critical or important functions or activities including delegation of authority;
- b. a copy of the draft outsourcing agreement and/or delegation of authority agreement which is to be entered into between the authorised undertaking and the service

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<sup>1</sup> [https://www.eiopa.europa.eu/system/files/2022-07/final\\_report\\_on\\_peer\\_review\\_on\\_outsourcing.pdf](https://www.eiopa.europa.eu/system/files/2022-07/final_report_on_peer_review_on_outsourcing.pdf)

provider, clearly defining the respective duties and responsibilities of the service provider.

Authorised undertakings are also reminded that in addition to paragraphs a. and b. above, they are also expected to submit the following information to allow the MFSA to proceed further with its assessment and eventually provide its “no objection” (or otherwise) in relation to an outsourcing arrangement and/or delegation of authority:

- i. the completed Assessment Form headed “*Annex II – Assessment Form*” forming part of Chapter 2 of the Insurance Rules on Fit and Proper Criteria, Notification and Assessment; and
- ii. additional information with regards to:
  - a. delegation of underwriting and/or claims and/or distribution authority to MGAs and/or INTs (Table 1 and Table 2);
  - b. delegation of claims handling authority to MGAs and/or INTs and /or TPAs (Table 1 and Table 2);
  - c. Outsourcing of Key and/or critical/important functions (Table 1(E) and Table 2); and
  - d. Termination of delegation of authority arrangements entered into with MGAs and/or INTs and /or TPAs (Table 3).

Through its engagement with various authorised undertakings during the past years, primarily with those undertakings whose business model relies on entering into delegation of underwriting and/or claims arrangements, the MFSA is issuing a set of tables as per Annexes. These tables depict the additional information (referred to in Item 3.ii above) which is expected to be submitted to the MFSA, allowing it to evaluate, grant or otherwise its’ “no objection”.

The Authority would like to clarify that whenever it provides its’ “no objection” in relation to an outsourcing arrangement and/or delegation of authority arrangements, such no objection will be limited to the information provided by the authorised undertaking at the time when the proposed arrangement was notified to the Authority. This implies that in line with paragraph 6.8.3(a) of Chapter 6: System of Governance of the Insurance Rules, authorised undertakings are reminded that any material/significant changes to an outsourcing arrangement (including delegation of authority) which was previously notified to the Authority are to be immediately notified to the Authority sixty (60) days prior to such changes. As guidance, some examples of material/significant changes include but are not limited to the following:

- changes in the original business model;
- changes in the outwards reinsurance arrangements;

- changes/inclusion/ceasing of products, classes and jurisdictions;
- inclusion/removal of parties to the arrangements;
- changes/inclusion of addendums forming part of the delegation of authority agreements;
- new proposed business which is to be distributed by the same MGA/INT for which the no objection would have already been provided;
- entering into delegation of authority arrangement with new MGAs/INTs for a product for which the authorised undertaking had already received a no objection from the Authority under a separate delegation of authority arrangement with another MGA/INT; and
- significant deviations (below/above) the initial projections communicated to the Authority.

**The above is a non-exhaustive list. If in doubt, the authorised undertaking is recommended to discuss its case with the MFSA accordingly.**

The self-explanatory table below provides a summary of the relative tables indicated under Annexes and which of these tables are expected to be compiled by authorised undertakings.

Table Number	Section	To be completed and submitted by:
1	A	<b>ALL</b> authorised undertakings delegating: <ul style="list-style-type: none"> <li>▪ underwriting authority to INTs and/or MGAs;</li> <li>▪ claims handling authority to MGAs/INTs/TPAs</li> </ul>
	B	<b>ALL</b> authorised undertakings delegating: <ul style="list-style-type: none"> <li>▪ underwriting authority to INTs and/or MGAs;</li> <li>▪ claims handling authority to MGAs/INTs/TPAs</li> </ul>
	C1 (in addition to Sections A and B above)	<b>Solely</b> those authorised undertakings which meet the following criteria: <ul style="list-style-type: none"> <li>▪ The insurance cover provided is a <b>compulsory class of business in the jurisdiction where the product will be distributed;</b></li> </ul> <p>and/or</p>

		<ul style="list-style-type: none"> <li>▪ if the <b>aggregated projected gross written premiums over the first 3 consecutive years from the date when the insurance business starts being written exceed 2 million euros.</b></li> </ul>
	<p><b>C2</b> (in addition to Sections A, B, C1 above)</p>	<p><b>Solely</b> those authorised undertakings which will enter into arrangements that meet the following criteria:</p> <ul style="list-style-type: none"> <li>▪ The product type offered is one or more of the following: <ul style="list-style-type: none"> <li>➤ After the Event</li> <li>➤ Cessione del Quinto</li> <li>➤ Construction Liability</li> <li>➤ Directors &amp; Officers</li> <li>➤ Errors &amp; Omissions</li> <li>➤ Health Insurance</li> <li>➤ Medical Malpractice</li> <li>➤ Motor/Motorcycles</li> <li>➤ Professional Indemnity</li> <li>➤ Surety (referring to all products falling under this class)</li> </ul> </li> </ul> <p>and/or</p> <ul style="list-style-type: none"> <li>▪ any of the following are met: <ul style="list-style-type: none"> <li>➤ <b>Current Undertaking Solvency Ratio:</b> MCR% or SCR% is <math>\leq 125\%</math></li> <li>➤ <b>Negative SCR Ratio impact of binder arrangement:</b> impact of the binder on the MCR%/SCR%, with other business assumed frozen, more than a 15 p.p. deterioration vs the current ratio at any point over the next 3 years.</li> <li>➤ <b>Absolute SCR Ratio impact of binder arrangement:</b> impact of the binder on the MCR%/SCR%, with other business assumed frozen, more than a 30 p.p. impact in either direction vs the current ratio at any point over the next 3 years.</li> </ul> </li> </ul>

	<b>D</b>	<b>ALL</b> authorised undertakings delegating: <ul style="list-style-type: none"> <li>▪ underwriting authority to INTs and/or MGAs;</li> <li>▪ claims handling authority to MGAs/INTs/TPAs</li> </ul>
	<b>E</b>	<b>Solely</b> those authorised undertakings which will delegate outsourced activities which in turn be sub-outsourced.
<b>2</b>	<b>A</b>	<b>ALL</b> authorised undertakings: <ul style="list-style-type: none"> <li>▪ <b>entering into an Outsourcing arrangement with a service provider to carry out a Key and/or Critical or important function(s) or activity(ies) on its behalf</b></li> <li>▪ <b>which will be delegating</b> underwriting authority and/or distribution activities to MGAs/INTs</li> <li>▪ <b>which will be delegating</b> claims handlings authority to MGAs/INTs/TPAs respectively.</li> </ul>
	<b>B</b>	
	<b>C</b>	
<b>3</b>	-	<b>ALL</b> authorised undertakings which have terminated a delegating underwriting authority with an INT/MGA.

#### **4.0 General MFSA Expectations**

The Authority would like to reiterate that it is the primary responsibility of the Compliance Officers to bring the contents of this Circular to the attention of the Board of Directors of their respective authorised undertakings in a timely manner.

The Board of Directors must ensure that senior management take note of the MFSA's expectations and adequately implement the requirements mentioned in this Circular in the processes and procedures of the authorised undertaking in the shortest possible time from the date of this Circular. Furthermore, the Board of Directors is reminded that they are ultimately responsible for ensuring that the authorised undertaking has implemented adequate ongoing monitoring and due diligence processes in relation to third-party service providers, as well as implemented robust processes in relation to the ongoing monitoring of general good provisions of the host member state where the business is being distributed.

The completion of the tables noted in the Annexes is to come in force with effect from **9 September 2024**.

All authorised undertakings should endeavour to meet the MFSA's expectations in full, immediately after the issuance of this Circular. However, the MFSA also understands that there may be some initial challenges or queries until the authorised undertakings familiarise themselves with the process and implement it seamlessly. In light of this, the MFSA intends to adopt a light supervisory approach in the initial stages until all authorised undertakings become familiar with the tables and the additional information that is expected to be submitted.

The Insurance and Pensions Supervision function will be closely monitoring the quality of the submission of the information being requested and will engage with problematic authorised undertakings expecting them to achieve improvement within a reasonable timeframe. Repeated observations might lead the Authority to take regulatory action in respect of those authorised undertakings which are consistently providing submissions that are not in line with the Authority's expectations. This may also create a time lag to the MFSA issuing its "no objection" due to inappropriate information being provided to the Authority.

The Authority would also like to point out that notwithstanding the tables being rolled out, the MFSA still reserves the right to request further additional information from authorised undertakings as may be required on a case-by-case basis. However, such requests are expected to be minimal.

The Authority would like to make it very clear that the MFSA will **not commence** the assessment leading to providing its "no objection" until such time all information and documentation noted in Section 3.0 is submitted by the authorised undertaking and is to the satisfaction of the MFSA.

As part of the "no objection" provided by the Authority in relation to delegation of authority agreements, it is quite common that this is accompanied by a number of conditions which authorised undertakings are expected to meet. From supervisory monitoring work carried out by the Authority in the past years, it has been noted that not all authorised undertakings were adhering to the conditions issued, in particular those relating to obligations to notify the Authority when certain parameters or metrics are exceeded. Authorised undertakings are reminded that it is their responsibility to ensure that they implement an adequate tracking/monitoring process to ensure that the conditions set by the Authority when giving its "no objection" are abided to at all times. Furthermore, all authorised undertakings are expected to notify the MFSA immediately but by no later than fourteen (14) days in cases where the authorised Undertaking identifies that it was not adhering to the conditions attaching to the "no objection" communication issued by the Authority.

## **5.0 Conclusion**

Any queries or requests for clarifications in respect of the above should be sent by email on [ipsu@mfsa.mt](mailto:ipsu@mfsa.mt).

## **6.0 Annexes**

- [Table 1 - Information on Delegated Authority Arrangements](#)
- [Table 2 - Terms and Conditions of Outsourcing Agreements](#)
- [Table 3 - Termination of Agreements](#)