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MALTA SPECIAL  
PURPOSE  
REINSURANCE  
VEHICLES

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# Highlights

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- Reinsurance Special Purpose Vehicles Regulations<sup>1</sup> ('RSPV Regulations') came into force on 27 December 2013;
- RSPV Regulations create a regulatory framework for the establishment and supervision in Malta of catastrophe bond issuers and sidecars;
- Malta's insurance regulator – the Malta Financial Services Authority (MFSA) – confirmed it is ready to **fast-track applications** to suit market needs;
- Reinsurance Special Purpose Vehicles (RSPVs) may be structured as **Maltese tax neutral vehicles**;
- Malta currently has a double tax treaty network with 65 countries;
- The MFSA is considering legislating for the use of **protected cell companies (PCCs)** as securitisation vehicles. RSPVs may currently be formed as limited liability companies;
- Malta has developed depth in the insurance industry on the strength of the jurisdiction's reputation as a captive and protected cell company jurisdiction. Service providers including law firms, international audit firms and major insurance managers are present. The Maltese legal framework ensures legal certainty of securitisation transactions.

<sup>1</sup> Legal Notice 452 of 2013

## In More Detail

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The RSPV Regulations enable the Malta Financial Services Authority ('MFSA') to accept and process applications for the authorisation of reinsurance special purpose vehicles. RSPVs may be used as vehicles for a variety of indemnity insurance linked securities deals including catastrophe bonds and sidecars. We analyse the salient provisions of the RSPV Regulations and provide a broad overview of the tax treatment of RSPVs.

# Overview

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## Legal basis

The RSPV Regulations transpose the provisions of the Reinsurance Directive<sup>2</sup> which sets out minimum requirements for special purpose vehicle legal and regulatory regimes.

The content of the RSPV Regulations also reflects the spirit of the Solvency II Directive<sup>3</sup> requirements applicable to special purpose reinsurance vehicles and the content of EIOPA (then CEIOPS) draft Solvency II advice on Level II Implementing Measures published in 2009 for their entry into securitisation transactions.

## Legal form of RSPVs

RSPVs may be formed as limited liability companies. The MFSA has further indicated that it is studying the acceptability of RSPVs established as protected cell companies and incorporated cell companies. This would make Malta the first European Union jurisdiction to make cell structures available for insurance-linked securities transactions.

## Cedants

A RSPV may be established to accept risks from a single (re)insurance undertaking or multiple (re)insurance undertakings forming part of the same group of companies.

## Investors

RSPVs may issue financial instruments in order to fund their exposure under the risk transfer contract only to professional clients, as defined in Annex II of the European Markets in Financial Instruments Directive<sup>4</sup> ("MiFID").

<sup>2</sup> Directive 2005/68/EC

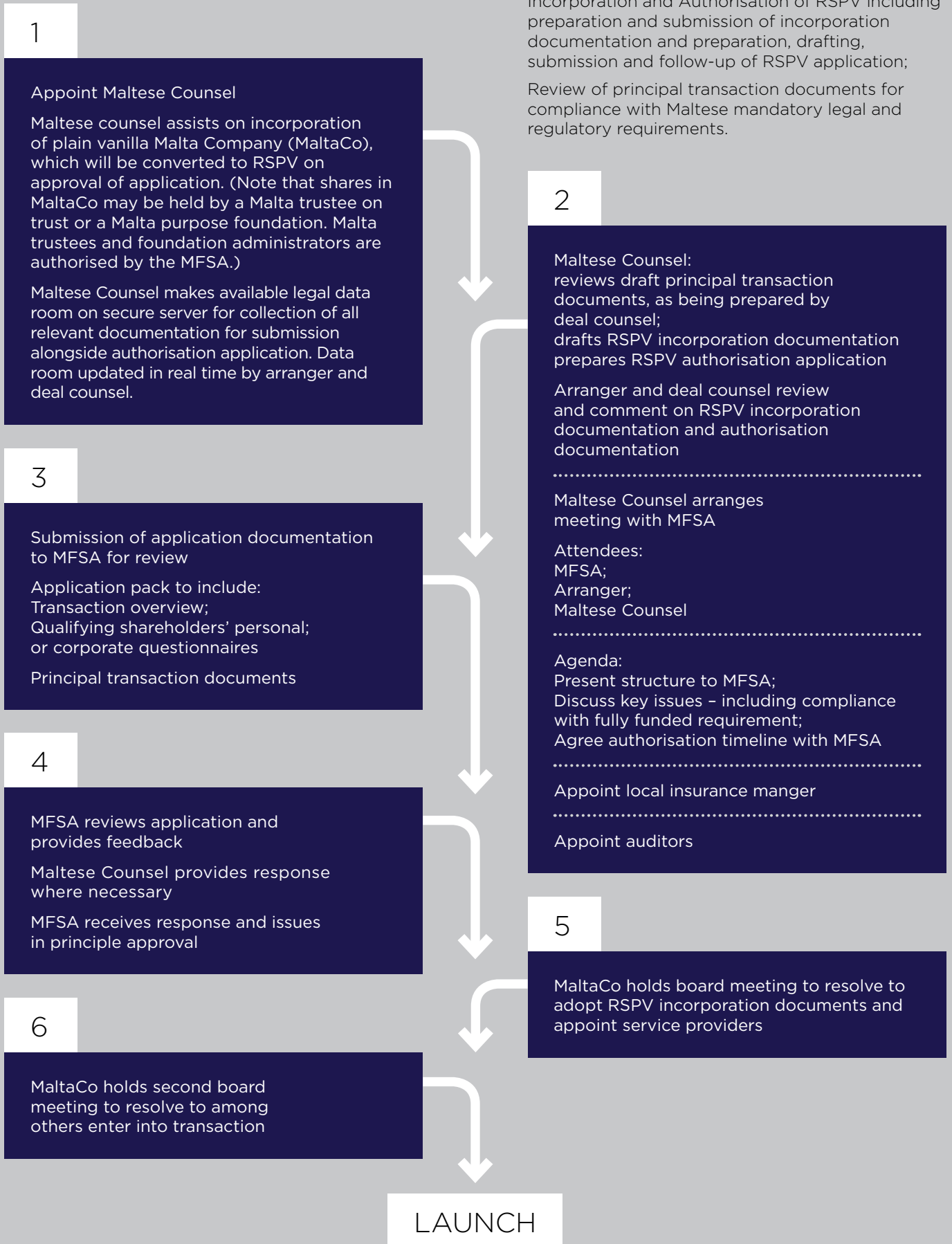
<sup>3</sup> Directive 2009/138/EC

<sup>4</sup> Directive 2004/39/EC

# Deal Timeline – Malta

## SCOPE OF PROJECT

Incorporation and Authorisation of RSPV including preparation and submission of incorporation documentation and preparation, drafting, submission and follow-up of RSPV application;  
 Review of principal transaction documents for compliance with Maltese mandatory legal and regulatory requirements.



# RSPV Application

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## Application for authorisation

The MFSA is the body responsible for the processing of applications for the authorisation of RSPVs. A RSPV will be granted authorisation if:

- the RSPV demonstrates that it will satisfy the fully funded principle and the prudent person principle created under the Solvency II Directive;
- it is formed or constituted in Malta as a limited liability company;
- its objects are restricted to operating as a reinsurance special purpose vehicle;
- it assumes risks from a ceding undertaking through reinsurance contracts, or assumes insurance risks through similar arrangements;
- the contractual arrangements relating to the transfer of risk from a ceding undertaking to RSPV and the investment of the RSPV's assets satisfy the conditions set out in the RSPV Regulations;
- the persons who effectively direct or manage the RSPV satisfy the requirements of the RSPV Regulations;
- the identity of the shareholders or members having a qualifying shareholding in the RSPV<sup>5</sup> is disclosed and such persons satisfy applicable fit and proper criteria; and
- the RSPV has an effective system of governance.

The following documents are required to be submitted alongside an application for authorisation:

- a scheme of operations;
- a copy of the proposed risk transfer contract to be entered into between the ceding undertaking and the RSPV;
- a copy of the memorandum and articles of association of the RSPV;
- details of the trustee (or custodian) holding the investments of the RSPV;
- details of any trustee or administrator of a trustee or foundation established to hold shares in the RSPV;
- details of the identity of any qualifying shareholders, and of the directors, controllers and all persons who will effectively direct or manage the RSPV, including all information needed to assess whether these persons satisfy fitness and probity criteria.

## Mandatory conditions to be included in transaction documentation

The MFSA will seek to ensure that the following mandatory conditions are adhered to in all contractual arrangements relating to the transfer of risk between the ceding undertaking and the RSPV:

- compliance with the fully-funded principle;
- effectiveness of the risk transfer, including clear definition and incontrovertibility of the risk transfer;
- subordination of investors to the ceding entity;
- no right of recourse to the assets of the ceding undertaking; and
- that investors have no rights to petition for the liquidation and winding-up of the RSPV.<sup>6</sup>

## Authorisation Timeline

The MFSA has indicated in a feedback statement published on 11 December 2013 that it will aim to process applications as quickly as possible in accordance with customary market-standard timeframes agreed with applicants prior to submission of application documentation, provided that the authority is provided with accurate and complete information at every stage of the structuring and documentation process together with a complete set of the final documents by an agreed date. This is subject to a statutory maximum period of six months.

<sup>5</sup> We envisage that a number of RSPVs will be established as "orphan" vehicles. Accordingly the RSPV will have a single qualifying shareholder that is either a Maltese purpose foundation or charitable trust overseas, in either case with appropriate authorisation from the MFSA.

<sup>6</sup> We recognise that this is likely to be a rating agency requirement in any case.



## Programme structures and RSPV re-use

Programme issuances will be subject to prior approval of the MFSA. This includes any change of use of the RSPV. Authorisation will only be granted if the RSPV can demonstrate:

- it can maintain adequate bankruptcy remoteness protection for each arrangement at all times;
- it can ensure that the link between the funding leg for a specific arrangement is sufficiently matched to the related risks assumed, and that such links are clearly defined and effectively legally ring-fenced so as to avoid potential contagion from one arrangement to another; and
- how it intends to maintain compliance with the fully-funded requirement at both the aggregate maximum risk exposure level and the individual risk exposure of each separate arrangement assumed.

## Malta: A one-stop-shop capital markets destination

The RSPV Regulations enhance Malta's capital markets offering. The jurisdiction also offers:

- availability of listing on the European Wholesale Securities Market (EWSM);
- legal certainty on matters as bankruptcy remoteness; the validity of non-petition clauses and limited recourse creditor subordination agreements under specialised legislation including the Securitisation Act;
- a dedicated offering of service providers including insurance managers and audit firms of international repute;
- depth of knowledge and expertise in the insurance industry on the strength of the jurisdiction's reputation as a captive and protected cell company jurisdiction; and
- a reputable and responsive regulator.



# Regulation, Capital & Governance

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## Capital Requirements

The RSPV is required to be fully-funded at all times by means of any financing mechanism up to its aggregate maximum risk exposure. Debt or equity used to finance the RSPV is to be fully paid in. The value of the RSPV's assets must be equal to or exceed at all times the aggregate maximum risk exposure assumed and the RSPV must be able to pay the amounts it is liable for as they fall due.

The assets of the RSPV are to be valued in accordance with generally accepted accounting principles.

## RSPV Investments

The assets of RSPVs should be invested in accordance with the prudent person principle.<sup>7</sup> The following criteria should be met:

- the RSPV should only invest in assets and instruments whose risk it can properly identify, measure, monitor, manage, control and report;
- assets are to be invested in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio as a whole. The localisation of assets shall be such as to ensure their viability;
- all assets are to be invested in a manner appropriate to the nature and duration of the liabilities of the RSPV;
- the use of derivative instruments is possible in so far as the derivative instruments contribute to a reduction of risks or facilitate efficient portfolio management;
- investments and assets which are not admitted to trading on a regulated financial market shall be kept to prudent levels;
- assets shall be properly diversified<sup>8</sup> in such a way as to avoid excessive reliance on any particular asset, issuer or group of undertakings, or geographical area and excessive accumulation of risk in the portfolio as a whole; and
- investments in assets issued by issuers belonging to the same group shall not expose the RSPV to excessive risk concentration.

## Administration of RSPVs

Malta RSPVs may be managed by insurance managers authorised by the MFSA. All of the major international names in the insurance management market are present in Malta.

## Fitness and probity criteria

Persons who effectively direct or manage an authorised reinsurance special purpose are required to satisfy fitness and probity criteria. The MFSA will assess the professional qualifications, knowledge and experience of the persons effectively directing or managing an authorised reinsurance special purpose vehicle and their reputation and integrity. The MFSA has indicated in a feedback statement published on 11 December 2013 that this requirement applies to:

- persons having a qualifying shareholding in the RSPV (including the trustee or administrator of foundation holding shares in the RSPV);
- directors;
- senior managers; and
- other key functionaries.

<sup>7</sup> Again, the requirements of capital markets investors and / or credit rating agencies are likely to impose significantly greater restrictions on investment by the RSPV than those set out below.

<sup>8</sup> Adequate diversification of deal collateral structure is a Solvency II requirement. This will be the subject of further discussion with the MFSA



## System of Governance

RSPVs are to have in place a system of governance that is adequate to the nature, scale and complexity of the risks assumed and the intended use of the vehicle. This includes requirements that the RSPV would have in place:

- sound administrative and accounting procedures;
- written policies relating to at least risk management, internal control, administrative and accounting procedures and, where relevant, outsourcing;<sup>9</sup>
- internal controls to ensure that the mandatory conditions to be included in contracts and the prudent person principle are fulfilled on an ongoing basis;<sup>10</sup> and
- an effective risk-management system comprising of processes and reporting procedures necessary to identify, measure, monitor, manage and report, on an ongoing basis the risk to which the RSPV could be exposed.<sup>11</sup>

## Legal Certainty

Securitisation transactions that are structured through the use of Malta special purpose vehicles benefit from provisions confirming the bankruptcy remoteness and insolvency remoteness of securitisation vehicles contained in the Securitisation Act. The same benefit is granted to RSPVs by means of Regulation 16 of the RSPV Regulations applying certain provisions of the Securitisation Act to RSPVs. This includes:

- confirmation of bankruptcy remoteness of RSPVs;
- affirmation that RSPVs are not collective investment schemes; and
- provisions on the privileged position of creditors of an RSPV in respect of the assets held by the RSPV, subject to the terms of a subordination agreement.

<sup>9</sup> We would argue that this would be satisfied by typical restrictions in transaction documents.

<sup>10</sup> We would argue that this would be satisfied by typical restrictions in transaction documents.

<sup>11</sup> We would argue that this would be satisfied by typical restrictions in transaction documents. in combination with market-standard investor reporting as well as ECB reporting requirements under Regulation ECB/2008/30 concerning statistics on the assets and liabilities of financial vehicle corporations engaged in securitisation transactions .

# TAX

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## Tax treatment

RSPVs are deemed to be securitisation vehicles for Maltese tax purposes, and may accordingly benefit from tax rules applicable to such securitisation vehicles. Malta's Securitisation Transactions (Deductions) Rules, 2011 (the 'Tax Deductions Rules') provide for a wide list of deductions which can be claimed by securitisation vehicles over and above any other deductible expenses which may normally be claimed by a Maltese company. These deductions enable a securitisation vehicle to effectively wipe out its chargeable income, thereby resulting in tax neutrality at the Malta level.

The Tax Deductions Rules establish a framework for the determination of (a) the income of securitisation vehicles (b) the applicable deductible expenses, and (c) the originator's deemed income.

The Tax Deductions Rules allow a securitisation vehicle to deduct expenses over and above those which are normally allowed in terms of the Income Tax Act. These additional deductible expenses consist of:

- sums payable by the securitisation vehicle to the originator or assignor of the securitised risk;
- premiums, interest or discounts in relation to the financial instruments issued, or funds borrowed, by the securitisation vehicle;
- any expenditure incurred by the securitisation vehicle in respect of its day to day administration, and collection of receivables; and
- any fees of third party servicer providers (including the originator) to whom the day to day administration is delegated.

Should the securitisation vehicle have any remaining income after the above allowable expenses have been deducted, it may opt to claim a further deduction of an amount which is equal to the said remaining income (the 'Further Deduction'). In this manner, the securitisation vehicle will end up with no chargeable income. Exercise of this option is subject to the irrevocable written consent of the originator or assignor.

## Tax treatment of Ceding Undertaking

The amount of deductions claimed by the securitisation vehicle and relating to:

- the cost of acquisition of the securitisation assets; or
- the cost of the assumption of risk; or
- the Further Deduction referred to above,

are all deemed to be income in the hands of the ceding undertaking, and shall be regarded as income or gains from a business or trade.

The Tax Deductions Rules provide that income so attributable to the ceding undertaking is considered as arising in Malta unless the control and management of the business of the ceding undertaking is exercised outside Malta. Thus, such income would only be liable to Maltese tax in the hands of the ceding undertaking if it is:

- either incorporated in Malta; or
- incorporated outside Malta but is tax resident in Malta by virtue of its control and management in Malta.

Other ceding undertakings will not be liable to Maltese tax in respect of such income.

# Malta fact sheet

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## General



LANGUAGE  
English



CURRENCY  
Euro



DOUBLE TAX TREATY NETWORK  
65 states

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## Regulatory environment



REGULATOR  
Malta Financial Services Authority ('MFSA')



REGULATORY STAFF HEADCOUNT  
300 (2013)



AUTHORISED INSURANCE UNDERTAKINGS  
58 (including 8 PCCs and 21 cells)

INSURANCE MANAGERS IN MALTA  
15

AUTHORISED CREDIT INSTITUTIONS  
26

FUNDS  
650



RSPV APPLICATION AUTHORISATION PERIOD

The MFSA has indicated in a feedback statement published on 11 December 2013 that it will aim to process applications as quickly as possible in accordance with customary market-standard timeframes agreed with applicants prior to submission of application documentation, provided that the authority is provided with accurate and complete information at every stage of the structuring and documentation process together with a complete set of the final documents by an agreed date.

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## Local Note Listing



MARKET  
European Wholesale Securities Market (EWSM)



LISTING AUTHORITY  
MFSA



LISTING DOCUMENTATION REVIEW TIMELINE

The ISELS, in its capacity as listing agent, and the MFSA aim to approve and list securities on the EWSM within 5 - 10 business days from submission of the listing documentation.

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## Indicative regulatory / listing costs



RSPV INCORPORATION FEES  
€250 - €2,250

RSPV AUTHORISATION FEES

€1,800\* (Submission of authorisation application)

€2,500\* (On confirmation of authorisation)

€1,200\* (Continuance of authorisation)

LISTING COSTS (EWSM)

€1,500 (Offering Circular)

€1,000 (Offering Circular Supplement)

\* This is the fee for undertakings authorised to carry on reinsurance business. The MFSA should be in a position to supply the regulatory fees applicable to RFSPVs in the near future.

## Let's connect

GANADO Advocates is a pro-active law firm dedicated to creating value in business transactions.

## Contacts

### **RICHARD AMBERY**

Richard heads the capital markets team at the firm. Recent transactions include advising on the \$234m exchangeable bond issue for Lufthansa Malta Blues, the €403m Grand Harbour I CLO for Mediterranean Bank and a \$150m asset based lending facility for JP Morgan secured over Maltese internet sales receivables.

**[rambery@ganadoadvocates.com](mailto:rambery@ganadoadvocates.com)**

**+356 2123 5406**

### **MATTHEW BIANCHI**

Matthew heads the firm's insurance corporate and regulatory practice. He regularly assists insurance managers, captive owners and (re)insurance companies on corporate and regulatory matters.

**[mbianchi@ganadoadvocates.com](mailto:mbianchi@ganadoadvocates.com)**

**+356 2123 5406**

### **STEPHEN ATTARD**

Stephen leads the tax practice at the firm. Clients include internationally-listed corporate groups, financial institutions, private equity and hedge fund promoters and managers, investment funds, privately-held corporate entities, and high net worth individuals.

**[sattard@ganadoadvocates.com](mailto:sattard@ganadoadvocates.com)**

**+356 2123 5406**

**[www.ganadoadvocates.com](http://www.ganadoadvocates.com)**

