

MFSA

MALTA FINANCIAL SERVICES AUTHORITY

Circular addressed to Authorised (Re) Insurance Undertakings in relation to the Fitness and Propriety Assessment of persons performing or overseeing Key Functions under the Solvency II Regime

1. Explanatory Note

- 1.1 This Guidance Note is being circulated by the MFSA as a follow up to the MFSA Guidance Notes circulated in April 2010 and January 2012 on the System of Governance requirements under the Solvency II regime.

2. Purpose

- 2.1 This Note is being issued to provide guidance to insurance and reinsurance undertakings in relation to the fitness and propriety assessment of persons performing or overseeing a key function.

The MFSA may update or amend this note, as appropriate

3. Background

- 3.1 The Solvency II Directive 2009/138/EC (“Solvency II”) will apply to (re)insurance undertakings from 1 January 2016. With the adoption of Solvency II, (re)insurance undertakings need to demonstrate strong governance practices that extend to their business decision-making processes at executive management and board levels. Apart from the quantitative requirements in the first pillar and the disclosure obligations in the third, the second pillar contains extensive requirements relating to the way insurers organise their business. Implementation requires (re)insurance undertakings to establish four key functions (i.e. Risk Management, Compliance, Internal Audit and Actuarial Function).

4. Key function Holders

- 4.1 The system of governance of each (re)insurance undertaking should include at a minimum the following key functions: Risk Management, Compliance, Internal Audit and Actuarial Function. However, (re)insurance undertakings may also have additional functions that they consider to be key.
- 4.2 It is not the designation of the role that determines whether a function is key; rather it is the function carried out and the role that the individual or individuals assume/s.

Substance over form should therefore be applied when determining whether or not a role is a key function.

- 4.3 All persons who perform key functions, including persons responsible for key functions, should meet the fit and proper requirements relevant to the function in question.

5. Assessment Process to be carried out by (re)insurance undertaking

- 5.1 Article 42 of Solvency II requires an undertaking to assess the fitness and propriety of persons who effectively run the undertaking or have other key functions. Persons who are effectively running the undertaking or are key function holders (in-house appointed) are subject to formal notification requirements to allow for a fit and proper assessment to be conducted by the MFSA.

- 5.2 In addition, where a key function is outsourced, the MFSA expects the undertaking to be able to demonstrate, at the request of the supervisory authority, how it has conducted its assessment and reached its conclusions that all persons working in that function of the service provider are fit and proper. The undertaking must notify the MFSA prior to designating a person with overall responsibility for the outsourced key function.

- 5.3 The MFSA expects a (re)insurance undertaking to have conducted its own due diligence assessment before appointing a person to perform or to be responsible for a key function.

5A. Fitness - Due diligence assessment to be undertaken by a (re)insurance undertaking to assess a person's fitness to perform or oversee a key function

- 5.4 When assessing 'fit' requirements, account should be taken of the respective duties being performed, to ensure that the individual concerned possesses appropriate qualifications, knowledge and relevant experience to enable sound and prudent management of the undertaking.

- 5.5 In particular, the MFSA expects (re)insurance undertaking to take the following into account when assessing a person's fitness:

- a) The person possesses relevant qualifications and sufficient number of years of experience to perform or to be responsible for the key function.

The person proposed to perform a key function should ideally be in possession of the following relevant qualifications:

Key function	Qualification ¹
Risk Management function	<ul style="list-style-type: none"> • Risk Management qualification from a reputable professional or tertiary education institution; or • Financial services qualification from a reputable professional or tertiary education institution; or • Engineering/Scientific qualification from a reputable professional or tertiary education institution.
Compliance function	<ul style="list-style-type: none"> • Legal qualification from a reputable professional or tertiary education institution; or • Financial services compliance qualification from a reputable professional or tertiary education institution; or • Other financial services qualification from a reputable professional or tertiary education institution.
Internal Audit function	<ul style="list-style-type: none"> • Internal/Quality auditing qualification from a reputable professional or tertiary education institution; or • Financial services (including accounting) qualification from a reputable professional or tertiary education institution; or • Scientific qualification from a reputable professional or tertiary education institution.
<p>Actuarial function, where the insurance undertaking carries on with-profits business and/or life insurance business with guarantees</p> <p>Actuarial function, where the insurance undertaking carries on life insurance business (not writing with-profits business and/or life insurance business with guarantees) and/or non-life companies</p>	<ul style="list-style-type: none"> • Fellow of the Institute and Faculty of Actuaries (UK) or actuarial qualifications of similar standing from a reputable institute • Certified Actuarial Analyst (CAA) offered by the Institute and Faculty of Actuaries (UK) or actuarial qualifications of similar standing from a reputable institute
Additional key functions	Qualification²

¹ The list provided is not an exhaustive list of relevant qualifications. Applications will be assessed on a case by case basis.

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<p>Underwriting function for undertakings carrying on life business</p> <p>Underwriting function for undertakings carrying on non-life business</p>	<ul style="list-style-type: none"> • Insurance qualification from a reputable professional or tertiary education institution; or • Medical/Paramedical qualification from a reputable professional or tertiary education institution; or • Legal qualification from a reputable professional or tertiary education institution. <ul style="list-style-type: none"> • Insurance qualification from a reputable professional or tertiary education institution; or • Risk Management qualification from a reputable professional or tertiary education institution.
<p>Claims function</p>	<ul style="list-style-type: none"> • Insurance qualifications from a reputable professional or tertiary education institution; or • Legal qualifications from a reputable professional or tertiary education institution; or • Financial services qualifications from a reputable professional or tertiary education institution.
<p>Anti-Money Laundering/Combating the Financing of Terrorism function <i>(where applicable)</i></p>	<ul style="list-style-type: none"> • Financial services qualification from a reputable professional or tertiary education institution; or • Legal qualification from a reputable professional or tertiary education institution; or • Anti-Money Laundering qualification from a reputable professional or tertiary education institution.
<p>Investment function</p>	<ul style="list-style-type: none"> • Financial services qualification from a reputable professional or tertiary education institution.
<p>Finance/Accounting</p>	<ul style="list-style-type: none"> • A university degree with honours in accountancy or accountancy qualification gained from a reputable professional institution. In addition, the applicant must have been awarded the Certified Public Accountant (CPA) certification or its equivalent.
<p>Information Technology function</p>	<ul style="list-style-type: none"> • IT qualification from a reputable professional or tertiary education institution.

- b) The (re)insurance undertaking should satisfy itself that the person has the recognised qualification(s) by, for example, obtaining a copy of the certificate/transcript/records evidencing the qualification. The (re)insurance undertaking should also monitor compliance with ongoing continuing professional development (CPD) requirements.
- c) In the case of a professional qualification, the (re)insurance undertaking should satisfy itself that the person has that specific qualification(s) (e.g., actuary, accountant, lawyer, etc.). This may be achieved by, for example, obtaining a copy of the certificate/transcript/record evidencing the qualification. Where the person is required to be registered with a professional body, the (re)insurance undertaking may consider requiring and maintaining a copy of the person's licence or certificate to practise (howsoever described) and where that licence/certificate is renewed on an annual (or more or less frequent) basis requiring a copy of the most recent renewal.
- d) Where maintenance of a qualification is dependent on completing continuing professional development (CPD), the (re)insurance undertaking may consider requiring the person to self-certify that he or she is compliant with the particular CPD requirements. Where an individual must maintain up-to-date CPD in order to renew his/her practising certificate, evidence of the renewal of that practising certification will be regarded as sufficient to evidence CPD.
- e) Where the (re)insurance undertaking uses the interview process to assess competence and capability (such as skills and experience) it should maintain written notes of the interview to evidence this.
- f) As part of their assessment, (re)insurance undertakings are expected to make all reasonable efforts to obtain adequate references in respect of previous employment and keep these records in their files.
- g) Where a person demonstrates skills and experience gained through a previous role (for example, through the applicant's CV, or the interview process), the (re)insurance undertaking should assess and document how the person's performance in that role equips that person with the expertise and experience necessary for the performance or oversight of the key function.
- h) Competence also includes having the appropriate level of commitment to perform the role. Accordingly, where the person performing or overseeing the key function has other involvements in other entities, the (re)insurance undertaking should seek confirmation from that person that the performance of his/her responsibilities in the other directorships will not adversely impact on his or her ability to perform or oversee the key function from a timing perspective or otherwise.
- i) The (re)insurance undertaking should ensure that the person performing or overseeing the key function does not have other engagements which conflict with the performance or oversight of the key function.

5B. Probity - Due diligence assessment to be undertaken by a (re)insurance undertaking to assess a person's probity to perform or oversee a key function

5.6 When assessing 'proper' requirements, this requires the undertaking to assess a person's integrity and reputation based on relevant evidence concerning criminal, financial or supervisory aspects. The principle of proportionality does not apply to the 'proper' requirements.

5.7 In particular, the MFSA expects (re)insurance undertaking to undertake the following due diligence when assessing a person's properness:

- a) The (re)insurance undertaking should seek and obtain signed written confirmation from the person proposing to perform or oversee a key function as to whether or not any of the circumstances set out in Section 8 – Declarations and Confirmations in the PQ apply to that person. Where the person confirms that one or more of the circumstances set out in the said Section apply, the person must be in a position to demonstrate that his or her ability to perform or oversee the key function is not adversely affected to a material degree by that matter(s).
- b) The (re)insurance undertaking should require from the person concerned to submit to the (re)insurance undertaking underlying documents relevant to the matter (for example, a final decision or report and/or key correspondence).
- c) The (re)insurance undertaking should make an assessment based on all of the information received as to whether the matter is material to the performance or oversight of the key function. Where it is decided that it is not material, and the (re)insurance undertaking has satisfied itself that the person is a fit and proper person, the matter rests here. The (re)insurance undertaking should document this assessment.
- d) If it is considered that the matter is material, the (re)insurance undertaking should make all reasonable enquiries arising on foot of the information provided by the person, such as, where relevant, contacting third parties for further information, e.g., former employers, regulatory authorities, etc.
- e) A (re)insurance undertaking is not required to remove or suspend a person from performing or overseeing a key function solely on the basis that one or more of the matters listed in Section 8 of the PQ may have occurred.
- f) For example, the fact that a person has been the subject of disciplinary proceedings will not automatically mean that the person fails to meet the level of probity required for the performance or oversight of the key function. In assessing the impact of the proceedings on that person's probity, issues for consideration include the subject matter of the proceedings, the circumstances surrounding the disciplinary proceedings, the length of time passed since the proceedings, the

explanation offered by the person and the relevance of the proceedings to the proposed role.

- g) It is for the person to demonstrate that his or her ability to perform or oversee the relevant function is not adversely affected to a material degree by any of the factors in Section 8 of the PQ.
- h) The question of what is material to a particular key function, however, is a matter for the (re)insurance undertaking. Where a matter may be relevant (for example, where the disciplinary proceedings are in respect of a serious matter), the (re)insurance undertaking may consider it in conjunction with other relevant matters in assessing whether the person is fit and proper to perform or oversee the current or proposed function including:
 - the seriousness of, and surrounding circumstances of the particular set of facts;
 - the relevance of those to the duties that are, or are to be, performed and the responsibilities that are, or are to be, assumed by that person;
 - repetition and duration of the behaviour;
 - the passage of time since the matter under consideration; and
 - evidence of rehabilitation.
- i) A series of matters used to assess fitness and probity may be significant when taken together, even if each matter in isolation might not be significant. The cumulative effect of such matters might determine whether the individual is fit and proper to perform or oversee the key function .
- j) In assessing the impact of a conviction on a person's probity, issues for consideration include the circumstances surrounding the conviction, the length of time since the conviction, the explanation offered by the convicted person, the relevance of the offence to the proposed role and any evidence of the individual's rehabilitation.
- k) The (re)insurance undertaking should refer to the MFSA's website and those of other regulatory authorities (where available) to confirm for their own records that the person has not been the subject of sanction, or other regulatory action.
- l) The (re)insurance undertaking should require those performing or overseeing a key function to confirm whether, to the best of their knowledge, the circumstances set out in Section 8 of the PQ have arisen in relation to matters which may have occurred during the time in which that person held that position of responsibility or influence.
- m) The (re)insurance undertaking should check against publicly available sources whether a judgment debt has been registered against a person.

6. Notification for Key function Holders - *General Considerations*

- 6.1 When an authorised undertaking appoints a person to perform a key function or to be responsible for a key function, the MFSA must be notified in writing without undue delay.
- 6.2 A person performing or being responsible for a key function on 31 December 2015, will not be required to notify the Authority to continue the performance of, or be responsible for, that key function. Should that person change to a 'new' key function within the same undertaking, or to the same key function in a different undertaking, the MFSA must be informed in writing without undue delay.
- 6A. Notification for Key function Holders -Key functions (other than the risk management function) which are carried out in-house.**
- 6.3 If an individual is appointed to perform a key function, this person has to be notified to the MFSA and a fit and proper assessment has to be undertaken on the individual. If a group of persons or a committee or the Board of Directors are appointed to perform a key function, the person who holds the ultimate responsibility i.e leading this team of people, must be notified to the MFSA to allow for a fit and proper assessment to be undertaken.
- 6B. Notification for Key function Holders -Key functions (other than the risk management function) which are outsourced to third parties or group entities.**
- 6.4 A group of persons being a committee or the Board of Directors collectively may assume the responsibility to oversee the outsourced function. The person or group of persons being a committee or the Board of Directors appointed to oversee a key function from within the undertaking has/have to be notified to the MFSA and a fit and proper assessment has to be undertaken on the individual or collectively (in the case of a number of individuals overseeing the function). It is the undertaking's responsibility to check the fitness and properness of the service provider.
- 6C. Notification for Key function Holders -Risk management function (RMF) which is carried out in-house.**
- 6.5 The RMF may be carried out by an individual, a group of persons or a committee or a Board member or number of Board members (but not the entire board). Where more than one person is carrying out the RMF, an individual must be identified as the person with the ultimate responsibility for the function to be notified to the MFSA, to allow for a fit and proper assessment to be undertaken.
- 6.6 While it is acceptable that members of the board may carry out the RMF, it is not acceptable that the entire board carries out the RMF, as this would effectively mean that no oversight of the function can be carried out. If a member or a number of members of the board opt to carry out the RMF (but not the entire board), a different member or members of the board shall be designated to oversee the RMF and the risk management system.

6D. Notification for Key function Holders -Risk management function (RMF) which is outsourced to third parties or group entities.

6.7 The person or persons overseeing the RMF has/have to be notified to the MFSA and a fit and proper assessment has to be undertaken on the individual or collectively (in the case of a number of individuals overseeing the function).

6.8 It is the undertaking's responsibility to check the fitness and properness of the service provider. If the identified person or persons responsible for the oversight of the RMF is not a member of the Board, the undertaking must designate at least one director to oversee the risk management system on the board's behalf. If the identified person or persons responsible for the oversight of the RMF is/are a member of the board, this person/persons may also satisfy the role of overseeing the risk management system on the board's behalf.

7. Assessment by MFSA at appointment

7.1 The MFSA assessment will require the submission of:

- a) a personal questionnaire ("PQ") and a competency form of the person within the (re)insurance undertaking responsible for a key function if the latter is outsourced and of the person performing a key function if the latter is undertaken in-house;
- b) Assessment form to be completed by the (re)insurance undertaking in cases where a key function is going to be outsourced.

7.2 The 'fit' assessment of the proposed appointee may be complemented by an interview to ascertain the person's competences in relation to the key function's expectations under Solvency II.

7.3 In line with the proportionality principle, the nature, scale and complexity of the risks inherent in the business of the (re)insurance undertaking would be taken into account as an overarching consideration during the assessment process.

7.4 In addition, when assessing the key function holder, the level of support, resources and expertise provided by other functions, persons and/or committees should be duly taken into consideration by the MFSA to ascertain the person's overall ability to effectively carry out the duties of the function concerned.

7.5 Following the assessment, the MFSA will provide feedback in writing. If the MFSA concludes that the person already appointed does not comply with the fit and proper requirements, it shall require the undertaking to replace the person in question. The MFSA may reassess the fitness and properness of an individual if facts, circumstances or actions give rise to such a measure.