

Regulatory News Alert

BaFin published a new Circular on the Capital Investment Ordinance

26 June 2018

Context

The German Federal Financial Supervisory Authority (BaFin) reviewed the provisions applied to investments in relation to insurance undertakings and published Circular 11/2017 (VA) on 12 December 2017. In broad terms, the Circular is based on the thorough revision of the Investment Ordinance (Anlageverordnung, AnIV) in March 2015 following the introduction of the German Capital Investment Code KAGB, (Kapitalanlagegesetzbuch, KAGB). The circular applies to all companies approved for direct insurance business, to which the regulations for small insurance companies (§§ 212 to 217 VAG) apply, as well as to domestic pension schemes and pension funds.

With the introduction of Solvency II on 1 January 2016, the direct regulation of investments held in the restricted assets has been replaced for primary and reinsurance undertakings by risk-based solvency capital requirements (market risk module, counterparty default risk). However, small insurance undertakings with premium income of under €5 million and gross technical provisions of under €25 million, provident societies and pension funds are still subject to the old supervisory regime, where the investments held in the guarantee assets are directly regulated and thus impacted by the new Circular.

General Requirements

The Circular is presented under the same layout as the old Circular 4/2011 and contains a detailed definition of the investment types that may be included in the guarantee assets, as well as qualitative requirements for investment management, provisions on investment rules, asset mix, and diversification guidelines.

Insurance companies and pension funds must put in place a strong investment risk management system and be able to quantify the impact of an investment on their portfolio at any time. They must continuously monitor their investment activity in terms of compliance with both, defined investment strategy and regulatory requirements.

In the context of investments in funds, this requires comprehensive and regular reporting by the respective asset manager, depending on the type of investment fund.

Regulations on investment funds

The requirements related to investment funds are based on the fund type, as defined in the KAGB. Nevertheless, investment funds are subject to special insurance supervisory requirements concerning their status as restricted assets. As a result, stricter requirements may be placed on the quality of investment funds in some cases, compared to the provisions of the KAGB. Among others, the Circular 11/2017 clarify the treatment of the following investment types for German insurers and pension funds.

- Private equity funds under section 2(1) no. 13b AnIV
- Real estate funds under section 2 (1) no. 14c AnIV
- UCITS funds under section 2(1) no. 15 AnIV
- Open-ended special AIFs with fixed investment rules under section 2(1) no. 16 AnIV
- Units and shares in other AIFs under section 2(1) no. 17 AnIV

Conclusion

The provisions on permissible investment types and investment rules laid down in the Circular 11/2017 (VA) make it easier to invest in funds as existing legal uncertainty in a number of cases has been clarified. However, the circular also stipulates that investments in funds must be included in the insurance undertaking's risk management and the impact of the fund investments on the portfolio must be monitored continuously for compliance with the investment strategy and the regulatory requirements, so new questions may arise.

How can Deloitte help?

Deloitte can help fund managers assess the impacts of the new VAG regulation for the distribution of their products to German institutional investors and help understand key aspects of the regulation to consider to design VAG compliant investment funds. We can assist in the review of your investment fund's offering documents and in the certification of compliance with VAG eligibility rules. We can also assist fund managers with the quarterly production of VAG reporting required by German institutional investors.

All information publicly available from clients or made publicly available by the Firm.

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