


# RISK APPETITE STATEMENT

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# REVISIONS LOG



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## 1. Introduction

The Malta Financial Services Authority (MFSA or the Authority) is the single regulator for financial services in Malta. It was established by law on 23 July 2002 to continue the functions of the Malta Financial Services Centre having taken over regulatory and supervisory functions previously carried out by the Central Bank of Malta, the Malta Stock Exchange and the Ministry of Finance. The Authority is a fully autonomous public institution and reports to Parliament on an annual basis.

The activities and functions undertaken in fulfilment of its responsibilities are overseen by the Board of Governors and the Executive Committee established by the Malta Financial Services Authority Act Cap 330 Laws of Malta.

This Statement considers the most significant risks to which the MFSA is exposed and provides an outline of the approach to managing these risks. All strategic plans and business plans for functional areas need to be consistent with this Statement.

## 2. General Statement of Appetite

The MFSA will act in accordance with its risk appetite statement to achieve its strategic goals and objectives in pursuit of its vision as the single regulator of financial services in Malta. The MFSA must employ sound risk management principles, including identifying, measuring, monitoring, and controlling risk; transparent decision making; effective communication; and prioritisation of risk.

The MFSA faces a broad range of risks reflecting its responsibilities as the single regulator of financial services in Malta. These risks include those resulting from its responsibilities of protecting consumers of financial services and safeguarding the integrity and stability of the financial system as well as from its day-to-day operational activities.

The risks arising from the Authority's regulatory and supervisory policy responsibilities can be significant. These risks are managed through detailed processes that emphasise the importance of integrity, trustworthiness, public accountability, independence and excellence with a constant investment in the nurturing of staff and their knowledge

In terms of supervisory issues, the Authority has a low appetite for risk. The Authority makes resources available to control supervisory and operational risks to acceptable levels. The MFSA recognises that it is not possible to eliminate some of the risks inherent in its activities.

## 3. The Risk Management Framework

The MFSA's risk management framework seeks to ensure that there is an effective process in place to manage risk across the Authority. Risk management is integral to all aspects of the Authority's activities and is the responsibility of all staff. Top management has a responsibility to evaluate the risk environment, put in place appropriate controls and monitor the effectiveness of those controls. The risk management culture emphasises careful analysis and management of risk in all business processes.

These risks are identified, assessed and managed at both an entity level ('top-down') and business level ('bottom-up'). The Risk Committee, which is governed by its Risk Committee Charter approved by the Board of Governors, has oversight of these processes. This Committee meets at least six times a year and provides a report on its activities to the Authority's Board of Governors.

## 4. Overview

### 4.1 About the MFSA's Risk Appetite

#### 4.2 Risk Appetite Definitions

##### Low

- Cautious approach and intentionally conservative.
- Limited tolerance for uncertain outcomes relative to the achievement of the MFSA's mission, vision, or strategic objectives.
- Will tolerate risk if achieving an outcome is especially important to the MFSA's mission, goals, or strategic objectives and there is limited possibility of failure to achieve desired outcomes.
- Prefer to avoid trading off this objective against achievement of other objectives.

##### Moderate

- Measured and deliberative approach.
- A degree of tolerance for uncertain outcomes relative to the achievement of MFSA's mission, goals, or strategic objectives.
- Will tolerate selected risks but must be soundly justified.
- Willing to trade off this objective against achievement of other objectives in certain circumstances.

##### High

- Flexible approach with higher possibility of failure.
- Willing to tolerate uncertain outcomes relative to the achievement of the MFSA's mission, goals, or strategic objectives.
- Willing to tolerate risks when long-term benefits are foreseeable and outweigh risks.
- Willing to trade off this objective against achievement of other objectives.

## 5. Coverage

The MFSA's attitude towards its key risks is described below.

### 5.1 Information Technology Risk

Information Technology (IT) Risk is the risk that information technology processing, security, stability, capacity, and performance jeopardise core operations of the Authority. These risks

cover both daily operations and ongoing enhancements to the Authority's IT systems. These include:

- Technology Service Availability – Prolonged outage of a core system: The Authority has a very low appetite for risks to the availability of systems which support its critical business functions. Service availability requirements have been identified and agreed with each business area.
- Security – Cyber-attack on systems or networks: The Authority has a very low appetite for damage to Authority assets from threats arising from malicious attacks. To address this risk, the Authority aims for strong internal processes and the development and continuous improvement of robust technology controls.
- Technology Change Management: The implementation of new technologies creates new opportunities, but also new risks. The Authority has a low appetite for IT system-related incidents which are generated by poor change management practices.
- Information Management: The Authority is committed to ensuring that its information is authentic, appropriately classified, properly conserved and managed in accordance with legislative and business requirements. It has a very low appetite for the compromise of processes governing the use of information, its management and publication. The Authority has no appetite for the deliberate misuse of its information.

#### Low Risk Appetite

- Unadaptable or non-agile technology infrastructure and performance (e.g., stability, reliability, capability, capacity, and duplicative systems) to respond to evolving Fintech, legislation and supervisory requirements.
- Unauthorised access, use, or release of personally identifiable information or sensitive data.
- Non-compliance with technology laws, regulations, policies, or procedures.
- Lack of resiliency against cybersecurity threats.
- Non-availability of systems which support its critical business functions.
- Deliberate misuse of information.
- Weaknesses in the information management process.
- Lack of inefficient and ineffective business resiliency planning and execution.
- Untimely analysis and diagnosis of information collected.
- Misalignment of information systems, data, and business practices.

#### Moderate Risk Appetite

- Inability to meet user demands and support a mobile workforce.

## 5.2 People and Culture Risk

People and Culture Risk is the risk that resource use and employment practices do not align with the Authority's mission and strategic objectives.

The Authority's significant people and culture-related risks include:

- Calibre of People – The Authority relies on motivated, diverse and high-quality staff to perform its functions. It aims to create an environment where staff are empowered to the full extent of their abilities.
- Conduct of People – The Authority expects staff to conduct themselves with a high degree of integrity, to respectfully strive for excellence in the work they perform and the outcomes they achieve, and to promote the public interest. The appetite for behaviours which do not meet these standards is very low. The Authority takes any breaches of its Ethics Framework and Code of Conduct very seriously.
- Fraud and Corruption - The Authority has no appetite for any dishonest or fraudulent behaviour and is committed to deterring and preventing such behaviour. It takes a very serious approach to cases, or suspected cases, of fraud or corruption perpetrated by its staff, and responds fully and fairly in accordance with provisions of the Code of Conduct and the Anti-Fraud Policy.
- Health & Safety Environment (HSE) – The Authority is committed to creating a safe working environment for all its staff, where people are protected from physical or psychological harm. The Authority provides a highly secure environment for its people and assets by ensuring its physical security measures meet high standards. The Authority has no appetite for practices or behaviours that could be expected to lead to staff being harmed while at work and for the failure of physical security measures.

#### Low Risk Appetite

- Non-compliance with People and Culture Guidebook, workplace health and safety laws and regulations.
- Non-compliance with equal employment opportunity principles, diversity principles, and ethical standards.
- Non-compliance with Employment and Labour Law, rules, regulation, policy, or procedure, or other matters that could compromise the Authority's integrity.
- Dishonest or fraudulent behaviour.
- Failure of physical security measures.
- Failure to develop talent (developing employees with the necessary skills and competencies, including critical thinking and sound judgment, retention, succession, supervisory competency, leadership development, and training).

#### Moderate Risk Appetite

- Delays in talent acquisition (recruiting and hiring) and work force plan execution when the right candidates/resources are not immediately available.
- Staff empowerment within the appropriate delegation, oversight and reporting parameters.
- Stepping outside historical channels to acquire talent.

### 5.3 External Risk

Risk that political, geopolitical, or external stakeholder events affect the Authority's ability to achieve objectives.

#### Low Risk Appetite

- Lack of commitment to address the recommendations raised by the International Monetary Fund ('IMF'), the European Commission ('EC') and European Supervisory Authorities ('ESAs') and the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism ('MONEYVAL').
- Non-compliance with legislative, regulatory, and industry changes/events.

#### Moderate Risk Appetite

- Political, geopolitical, and stakeholder events.
- Court and Tribunal judgments and decisions/judgements that could affect the MFSA's ability to perform its functions or otherwise negatively impinge on its decision-making processes and procedures.
- Domestic and international issues.
- Macroeconomic issues.
- Social issues.

### 5.4 Authorisation Risk

Risk that the MFSA Authorisation process is not robust enough to identify proposed shareholders, directors and other key persons that are not fit and proper and applicants that do not have the funding to trade safely, do not have the appropriate risk controls in place and are inappropriately governed.

In accordance with the Authority's stated aims including under the Malta Financial Services Authority Act and sectoral legislation and rules including at European Union level, the Authority has identified certain key aims (the "Key Objectives") for the MFSA Authorisation process:

- Excluding bad actors from the financial services industry not only to protect their clients or investors but to ensure confidence in the wider financial system.
- Ensuring unfit persons are not able to infiltrate the local market through non-disclosure, false or misleading information being provided to the Authority.
- Excluding actors that, if authorised, risk posing a negative systemic impact and endanger financial stability or the local financial industry's reputation.
- Upholding the Authority's and the local financial services industry's strong reputation and further developing that reputation.
- Ensuring that relationships with ESAs as well as other regulators in foreign jurisdictions are strengthened and not damaged or unduly strained.



The Authority appreciates that not all applicants present the same risks and that requirements should be considered, where regulation permits, based on the European Union law principle of proportionality based on applicant type, clients targeted and size and complexity of the business.

Based on the above general objectives, the Authority's Authorisation risk appetite would be as follows:

#### Low Risk Appetite

- Applicants (including proposed shareholders, directors and other key persons) submitting poor quality applications (directly or indirectly), demonstrating a poor understanding of regulatory expectations and rules as well as a lack of communication, required documentation and general transparency.
- Applicants/promoters from jurisdictions with weak or strategic deficiencies in anti-money laundering / countering the financing of terrorism measures as identified by Financial Action Task Force.
- Applicants/promoters with complex and/or opaque shareholding structures including:
  - Unregulated trusts in shareholding structures;
  - Share capital / own funds financed through external debt that needs to be serviced;
  - Shareholding structures composed of entities that are located in specific jurisdictions that may pose reputational risks.
- Applicants using service providers that do not have robust onboarding systems.
- Applicants that fail to demonstrate appropriate knowledge of relevant European Union and Maltese legislation and rules (whether through key persons or use of external advisors) and which fail to demonstrate a strong compliance culture.
- Applicants/promoters with no track record or experience of operating in a regulated sector and unable to demonstrate commensurate measures to address such gaps and resulting risks.
- Subject to proportionality and/or licence types (e.g. externally managed Alternative Investment Funds or Professional Investor Funds are not expected to have employees), applicants/promoters unwilling to commit human and financial resources.
- Applicants without a demonstrated commitment to ensuring robust onboarding systems and continued adherence to anti-money laundering / countering the financing of terrorism legislation and requirements.
- Subject to proportionality, applicants without stringent Internal Control, Risk Management and Compliance Structures in place and a failure to demonstrate commitment to improve such control functions as the authorised entity increases in size, complexity and resources.
- Subject to proportionality, applicants or licence holders with weak corporate governance structures and a failure to demonstrate commitment to improve governance as the authorised entity increases in size, complexity and resources.
- Applicants or licence holders unable to demonstrate clear responsibility for effective monitoring and oversight of the entity's outsourced functions especially in cases where

these functions are not located locally or, where permitted, are delegated to unregulated entities.

- Applicants that are reasonably considered as posing a high risk to the achievement of the Key Objectives or have strained relationships with other Supervisory Authorities or Regulators.
- Applicants with solvency issues within other jurisdictions particularly where it is a re-domiciliation.
- Licence holders that materially change their business model immediately post-authorisation.
- Applicants with group or operational structures that present unwarranted operational challenges from a cross-border, consolidated supervisory standpoint.
- Applicants that seek to provide high risk or exotic products to retail clients.
- Applicants who:
  - place data servers in hosting facilities that are not ISO certified or other internationally recognised certification acceptable to the Authority;
  - seek to place back-end servers overseas with no replication in Malta; or
  - fail to demonstrate, guarantee or provide unhindered access to the Authority for audit and inspection purposes to their data servers and data.
- Individuals holding directorships and/or occupying approved senior/key positions within regulated entities not committing enough time to be able to perform the functions of their office or role.
- Licence holders with material changes in Senior Management positions, particularly in cases of re-domiciliation.
- Entities trying to enter the market through repeated or different applications (typically where one or more were refused or withdrawn in the past).
- Applicants/promoters with business proposals that present inappropriate conflicts of interest particularly where these are not able to be appropriately mitigated or managed.

#### Moderate Risk Appetite

- Entry level consideration for strategically important entities.
- Fintech companies.

#### 5.5 Supervision Risk

Risk that supervisory processes do not identify and mitigate significant risks to the financial services industry or customers and that have an adverse effect on market stability or effective competition.

#### Low Risk Appetite

- Lack of supervisory objectivity, critical thinking, and sound judgment.
- Not proactively identifying emerging or systemic supervisory risks.
- Not developing effective supervisory strategies and not adopting a holistic supervisory approach.

- Supervisory guidance that does not clarify the Authority's supervisory expectations.
- Supervisory processes that fail to ensure supervised institutions adhere to applicable laws and regulations, provide fair access to financial services, and treat customers fairly.
- Supervisory activity that is unable to identify, diagnose and address any instances of harm or potential harm to consumers.
- Lack of internal collaboration and communication between functions.
- Lack of resource expertise and knowledge transfer.
- Inefficient resource allocation and under capacity.
- Not exercising sound judgment and discretion in the execution of supervisory strategies.

#### Moderate Risk Appetite

- Inadequate improvements to the supervision tools and information available to assist reviewers.
- Lack of collaboration with other authorities and other jurisdictions.
- Failure to issue supervisory guidance on a timely basis.

### 5.6 Operational Risk

Risk that people, processes, systems, or external events impede the MFSA's ability to meet its objectives.

#### Low Risk Appetite

- Weaknesses in physical security and workplace safety.
- Employee misconduct.
- Lack of proper business continuity planning.
- Weak internal corporate governance processes.
- Failure to be operationally independent in relation to funding and recruitment.

#### Moderate Risk Appetite

- Outsourcing to third-parties including activities that involve outsourced services and use of independent consultants.

### 5.7 Reputation Risk

Risk that negative perception jeopardises the MFSA's credibility, achievement of mission and strategic objectives.

## Low Risk Appetite

- Failure to perform the Authority's functions as assigned to it by law, including to monitor, supervise and enforce legislation and Rules administered by the MFSA, in a proper and timely manner.
- Breaches in information security.
- Regulatory capture.
- Poor employee conduct.
- Failure to be fiscally responsible.
- Inefficient and ineffective communication strategies (internal and external).
- Lack of issue escalation and response processes.
- Human resource malpractices.
- Inadequate supervision, legal, licensing, and policy decisions.
- Tarnished MFSA culture (external and internal view of MFSA's vision, mission, values, and behaviours).
- Not taking a leadership role in pursuing and/or defending issues supportive of the MFSA's core mission (e.g. MFSA's regulatory powers; interpretation of the applicability of laws, regulations, directives, mandates, and executive orders to the MFSA; defence of the Authority's statutory independence).
- Lack of responsibility and accountability.

## 5.8 Strategic Risk

Strategic Risk is the risk that the MFSA's strategy selection, prioritisation, modification, and implementation jeopardise the achievement of MFSA's goals and objectives.

The Authority aspires to be a leading forward-looking financial services regulator, having the respect and trust of the industry and the general public, contributing towards a strong and dynamic financial sector as measured by the quality and effectiveness of its operations. This requires ongoing development and innovation in its operations through strategic initiatives which often carry significant risk.

The Authority has a low appetite for threats to the effective and efficient delivery of these initiatives. It recognises that the actual or perceived inability to deliver strategic initiatives could have a significant impact on its ability to achieve its objectives as well as its reputation.

The Authority's Executive Committee meets regularly to discuss the major initiatives. A framework is in place to ensure that these initiatives are prioritised appropriately, and that the associated risks are well managed and reported on a consistent basis.

## Low Risk Appetite

- Execution and achievement of the Authority's strategy and outcomes not aligning with MFSA's goals and objectives.

- Inability to safeguard the stability and sustainability of the local financial market through an ineffective macroprudential policy, and lack of collaboration and cooperation with international institutions.
- Ineffective or inefficient decision-making and execution.
- Inability to evolve, adapt, and remain relevant.
- Non-responsiveness to changes in the internal and external operating environment.

## 5.9 Legal and Compliance Risk

Legal and Compliance Risk is the Risk that the Authority does not fulfil its functions and obligations under applicable laws, has gaps in mission-critical functions to license, supervise, take the necessary enforcement action, and ensure high standards of conduct, integrity and management throughout the financial system.

The Authority is committed to a high level of compliance with relevant legislation and international standards as well as internal policies and sound corporate governance principles.

### Low Risk Appetite

- Non-compliance with applicable laws and other requirements as imposed by international regulatory bodies.
- Failure to abide by contractual obligations.
- Loss or reduction of the MFSA's statutory independence.
- Poor employee conduct.
- Gaps in mission-critical functions to license, supervise, take the necessary enforcement action, and ensure high standards of conduct, integrity and management throughout the financial services.
- Inadequate supervisory follow-up subsequent to issuing of licences and authorisations.
- Weaknesses in People and Culture guidance and practices.

### Moderate Risk Appetite

- Unpreparedness for changes in legislation and other regulatory standards.

## 5.10 Financial Risk

Financial Risk is the risk that the MFSA's financial resources will be impaired because of adverse economic conditions, inefficient resource utilisation, the potential award of damages against the MFSA or increasing expenditures reducing the ability to successfully complete the Authority's mission.

The Authority holds risks associated with financial controls and systems. The Authority does not aim to eliminate this risk as this would significantly impair its ability to achieve its policy

objectives. Instead, the risks are managed to an acceptable level through a framework of controls. The Authority acknowledges that there will be circumstances where the risks carried on its balance sheet will have a material impact on its financial accounts. The Authority regards it as desirable to hold sufficient reserves to absorb potential losses.

#### Low Risk Appetite

- Weak internal controls and reporting.
- Inefficient resource utilisation.
- Not using sound financial stewardship to operate more efficiently and invest in projects, technologies, and personnel that enhance the Authority's ability to meet its mission.
- Failure to collect due supervisory fees and administrative penalties.

#### Moderate Risk Appetite

- Inability to impact financial resources due to adverse economic conditions.

### 6. Implementation of the Authority's Risk Appetite

All Heads of Functions are responsible for the implementation of, and compliance with, this Statement.

#### 6.1 Communication

The Authority's Risk Appetite Statement is published on the Authority's intranet and the Authority's website.

#### 6.2 Risk Assessments

Each function maintains a Risk Register of the business risks it faces in its day-to-day operations and the control framework which is in place to mitigate risks. These Registers take into account risks from within the Authority and external sources and are reviewed regularly. Risk Registers are also updated where necessary when there are key changes in policies, structures or functions and in response to incidents.

All risks which are judged as unacceptable at functional level are reported to the Risk Committee and remedial action plans to reduce these risks to acceptable levels are reported, where appropriate, to the Executive Committee.

All risks which are judged as having a residual risk equal to medium or above are reported to the Risk Committee annually.

Functions are required to manage their specific operational risks in a manner which is consistent with this Statement, and to manage and address any risks outside appetite or agreed tolerance levels. Function risk appetite settings in their Risk Registers for groups of risks with a similar nature must also be consistent with this Statement.

### 6.3 Reporting & Monitoring

This Statement is complemented by several specific risk metrics which assist management in assessing whether outcomes are consistent with the Authority's risk appetite.

Performance against these metrics is tracked and reported to the Risk Committee on a regular basis.

Reporting systems are maintained to provide assurance that the risk appetite is effectively incorporated into management decisions.

### 7. Review

This Risk Appetite Statement is reviewed annually, or whenever there is a significant change to the Authority's operating environment. This review is coordinated by the Risk Management Function. Changes to the Risk Appetite Statement must be endorsed by the Risk Committee, approved by the Board of Governors and promptly and effectively communicated to staff.

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