

SUPERVISION
PRIORITIES 2022

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Table of Abbreviations

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|--------|--|
| ACR | Annual Compliance Returns |
| AIFMD | Alternative Investment Fund Managers Directive |
| AIFM | Alternative Investment Fund Manager |
| AML | Anti-Money Laundering |
| CBDF | Cross-Border Distribution of Funds Directive |
| CFT | Combating the Financing of Terrorism |
| CRD | Capital Requirements Directive |
| CRR | Capital Requirements Regulation |
| CSA | Common Supervisory Action |
| CSDR | Central Securities Depositories Regulation |
| CSP(s) | Company Service Provider(s) |
| DLT | Distributed ledger technology |
| DORA | Digital Operational Resilience Act |
| EBA | European Banking Authority |
| ECB | European Central Bank |
| EFIF | European Forum for Innovation Facilitators |
| EIOPA | European Insurance and Occupational Pensions Authority |
| EMIR | European Market Infrastructure Regulation |
| ESA(s) | European Supervisory Authority(ies) |
| ESMA | European Securities and Markets Authority |
| ESEF | European Single Electronic Format |
| ESEP | European Supervisory Examination Programme |
| ESG | Environment, Social and Corporate Governance |
| ESMA | European Securities and Markets Authority |
| EU | European Union |
| FATF | Financial Action Task Force |
| FCC | Financial Crime Compliance |
| FIAU | Financial Intelligence Analysis Unit |
| ICAAP | Internal Capital Adequacy Assessment Process |
| ICT | Information and Communications Technology |
| ILAAP | Internal Liquidity Adequacy Assessment Process |
| IOSCO | International Organization of Securities Commissions |
| KPI | Key Performance Indicator |
| LIR | Low Interest Rate environment |
| MiCA | Markets in Crypto Assets |
| MiFID | Markets in Financial Instruments Directive |
| MFSA | Malta Financial Services Authority |

| | |
|--------|---|
| MLRO | Money Laundering Reporting Officer |
| MREL | Minimum Requirement of own funds and Eligible Liabilities |
| NCA(s) | National Competent Authority(ies) |
| NED | Non-Executive Director |
| NFDR | Non-Financial Reporting Directive |
| NPE | Non-Performing Exposure |
| OCfR | Office of the Commissioner for Revenue |
| OECD | Organisation for Economic Co-operation and Development |
| PFOF | Payment for Order Flow |
| PIFs | Professional Investor Funds |
| POG | Product Oversight and Governance |
| PSD | Payment Services Directive |
| SFDR | Sustainable Finance Disclosures Regulation |
| SFTR | Securities Financing Transactions Regulation |
| SMB | Sanctions Monitoring Board |
| SRB | Single Resolution Board |
| SREP | Supervisory Review and Evaluation Process |
| TCSPs | Trustees and Company Service Providers |
| TUBOR | Trusts Ultimate Beneficial Ownership Register |
| UCITS | Undertakings for the Collective Investment in Transferable Securities |
| USSP | Union-Wide Strategic Supervisory Priorities |
| VFA | Virtual Financial Assets |

Purpose of the Document

The setting of annual supervisory priorities and their publication in this document provide an overview of the main supervisory and regulatory priority areas that have been identified for the upcoming calendar year. The document also provides updates on certain areas of focus which had been identified for the previous year/s. This exercise is particularly important, internally to guide decision making related to prioritisation, and externally for transparency and accountability purposes.

The MFSA's supervisory priorities for 2022 have been identified following careful consideration of the market environment, regulatory developments, the European Union Strategic Priorities, the work programs of the European System of Financial Supervision, recommendations of international standard setters, and regulatory and supervisory experience.

It is important to note that supervisory priorities outlined in this document should not be considered in isolation, but rather as focus areas of a wider array of work which the Authority will be performing in 2022.

The priorities set out in this document may change during the year as the Authority responds to events which may necessitate reprioritisation. Any such changes will be communicated through further interactions, as may be deemed necessary.

Structure of Document

This document is divided into two main sections: Section I identifies cross-sectoral themes and horizontal priorities; and Section II outlines sector-specific priorities for the Credit & Financial Institutions, Insurance & Pensions, Securities & Markets, and Trustees & Company Service Providers, respectively. Sections I and II will provide an update on the priorities which had been established for 2021 and will subsequently set out those for 2022.

General Context

Background

Following the outbreak of **COVID-19**, the MFSA's priorities shifted towards ensuring business continuity and stability, and mitigating the impact on consumers of financial products and services. The continued uncertainty emanating from this pandemic, coupled with a **prolonged low interest rate environment** and **Brexit** will need to be closely monitored in view of their impact on European and international markets.

Digitalisation and financial innovation continue to evolve, with innovative business models, products, services and distribution channels being increasingly presented to the market. This in turn increases cyber-risk exposures and related operational-resilience risks. Through the adoption of a [Digital Finance Package](#), the European Commission is supporting the EU's ambition for a recovery which embraces the digital transition, while ensuring consumer protection and financial stability. This area will require increased focus from a regulatory standpoint, and from a monitoring and assessment of risks perspective. Europe's push towards the digital transformation of businesses under the strategic priority [A Europe fit for the digital age](#), and the increasing dependence on data, will also require focus on the continuation of MFSA's internal business transformation to ensure that the Authority remains effective in its supervisory methodology. In this regard, continued efforts on MFSA's data management strategy remain key to ensure that the Authority strengthens data-driven supervision through the application of business intelligence and knowledge management tools.

The [European Green Deal](#) and its underlying initiatives including the European Commission's [Sustainable Finance Package](#) form part of the EU's climate and environmental targets in the context of an economic recovery following the impact of COVID-19. The EU's focus on helping improve the flow of money towards sustainable activities across the Member States will, as a result, require more focus on sustainable finance policymaking, regulatory development and resultant supervisory work.

In the context of **Brexit**, the withdrawal of the United Kingdom from the EU continues to impact the evolution of European and global capital markets. In view of the interconnection between the EU and UK markets and ensuring financial stability, ESAs shall continue monitoring developments in the UK framework to enable them to provide advice to EU institutions. ESAs shall furthermore be monitoring the NCAs' handling of relocations to the EU27 and ensuring good supervisory cooperation with third countries. The MFSA shall ensure that it remains aligned with this ESA priority.

Focus on corporate governance, a compliance culture and financial crime compliance remain **national priority focus areas** to continue to shape Malta's reputation as a jurisdiction for serious operators.

The above-mentioned areas of focus, together with other key European and national legislative developments, create competing priorities for the same resources, and impact further the planning of MFSA's activities, which becomes increasingly challenging. The deployment of resources towards key areas of risk and non-negotiable workload has become necessary, subsequently requiring previous areas of focus and targets to be reconsidered.

Supervisory Approach and Engagement

Our supervisory approach and engagement continues to develop to ensure that it remains efficient in the use of the Authority's available resources and effective in achieving the outcomes it sets out to deliver. As part of its Supervisory Plan, referred to under Key Initiatives of the [Supervisory Priorities 2021](#), the MFSA is defining ways to ensure supervisory effectiveness by moving away from compliance-oriented supervision, rather focusing less on the process carried out by firms and more on the outcomes and objectives that the MFSA wishes to achieve.

Risk-based Supervision & Effectiveness

By redefining its approach to increasingly focus on supervisory effectiveness, and keeping the availability of resources in context, the MFSA will be aiming to achieve its supervisory coverage through the different forms of supervisory engagement. Necessarily, supervisory resources will need to be continually prioritised and aligned as the risk landscape evolves, but also taking account of the inherent sectoral risks and the MFSA's internal risk evaluation procedures.

The MFSA shall be refining its KPIs to better measure the effectiveness of its supervisory and regulatory work. These KPIs shall be subsequently reported to stakeholders as part of the Authority's external outreach, in the spirit of accountability and transparency.

Regulatory and Supervisory Toolkit

MFSA's risk-based approach to supervision uses different supervisory tools to specifically address identified risks. The **regulatory and supervisory toolkit** available to the MFSA includes different forms of engagement such as **supervisory interactions** (inspections and meetings), **supervisory reviews**, **thematic reviews**, **SREP** and

mystery shopping. Outputs from the latter deployment of supervisory tools may lead to **enhanced supervision and monitoring, investigations, remediation plans and enforcement action**, where compliance breaches and failures are identified. Thematic findings and identified trends can also lead to the development of **policy, Letters to CEOs, Circulars**, and other forms of **industry guidance**.

Different forms of supervisory engagement defined:

Supervisory Inspections: A supervisory inspection is defined as an in-depth interaction with an authorised person or otherwise supervised person which inter alia includes reviews and assessments of documentation and information, interviews with officials engaged with the person, walk-throughs, and assessments of systems. A supervisory inspection will lead to the compilation of a formal communication, which outlines the key findings and recommendations. Observations are communicated to the licensed entity for their feedback/action plans to remedy shortcomings. Supervisory inspections are typically held physically at the premises of the supervised person, a service provider of a supervised person, or remotely.

Supervisory inspections have two main forms:

- **Broad-scope:** this is the traditional form of a supervisory inspection, through which the MFSA typically assesses a supervised persons' operations or several aspects of it. The MFSA would typically meet with the board and management separately, and cover a wider range of issues, some of which are delved into in more depth. This form of supervisory inspection is complemented with extensive documentation and information review, and takes several business days to complete. Efforts here are extensive. For credit institutions, this form of supervisory inspection is also carried out in line with ECB procedures, where applicable.
- **Focused-scope or deep dives:** This is a form of supervisory inspection which is ordinarily held at the authorised person's premises in order to discuss key and specific matters. Supervised entities are expected to be represented adequately (i.e., senior management and/or board) and, again, are expected to submit key information and documentation before, during and after the meeting. The level of preparation is also conducted in a way to support the level of detail that can be achieved within this timeframe. For credit institutions, this form of supervisory inspection is also carried out in line with ECB procedures, where applicable.

Supervisory Meetings: A supervisory meeting is defined as an interaction with a supervised person that takes the form of an interview, or a discussion based on a

structured agenda with entity officials. Supervisory meetings are typically held physically at the premises of the supervised person, at the MFSA offices, or remotely.

Supervisory Reviews: Through this form of desk-based supervision, the MFSA applies different techniques to analyse and assess compliance with the applicable regulatory frameworks. The information that is reviewed here includes financial and prudential returns which are periodically submitted by licensed entities and any other documentation, information and data requested on an ad hoc basis, where deemed necessary.

SREP: SREP reviews are currently carried out on credit institutions in accordance with [ECB procedures](#). Through the SREP, the MFSA assesses and measures the risks for each credit institution. This process summarises all the MFSA's findings of a given year and provides recommendations to the bank to address within a specific timeframe. The SREP provides supervisors with a harmonised set of tools to examine a bank's risk profile from four different angles: business model; governance and risk; capital; and liquidity. In line with the new prudential framework for investment firms, SREP reviews will eventually also start being carried out on investment firms.

Thematic Reviews: These reviews are targeted at a representative sample of entities. These studies are used to identify common findings, trends and practices, and to guide further initiatives to urge improvement and avoid common pitfalls. These reviews may take the form of supervisory inspections and supervisory reviews, and may be supported by other forms of supervisory engagement. Findings and related guidance from thematic reviews are communicated to the relevant authorised persons and may also be communicated to the public through various forms of outreach. Firm-specific findings from such reviews may also be directed to the firm should this be considered necessary.

Mystery Shopping: The MFSA considers mystery shopping exercises to be one of the most effective tools or methodologies used to monitor compliance and best practices in the retail space. This tool is also used as a means for identifying potential malpractices and ultimately protecting consumers. Through communicating the findings from the application of this supervisory tool, the MFSA can guide practitioners on best practices, communicate expectations and issue recommendations to address deficiencies.

Outreach

Outreach is a supplementary regulatory and supervisory tool which the MFSA uses to engage with industry practitioners and supervised persons to educate, guide and communicate common findings, failures and best practices. Such engagement also

serves as a mechanism for the MFSA to engage with the financial services industry to understand current issues being faced by practitioners and consider policy and/or supervisory responses.

2021 has seen significant work in this space, including a series of webinars and training events on key topics, publications such as 'The [Nature & Art of Financial Supervision](#)' series and Circulars, as well as bilateral meetings and roundtables with supervised persons, financial services practitioners and their representative associations. The latter were supplemented by engagement through online campaigns and the use of social media. Engagement with stakeholders, industry practitioners and supervised persons will remain firmly on MFSA's agenda.

Section I

Cross-Sectoral Themes and Horizontal Priorities

Introduction

This section identifies cross-sectoral themes and horizontal priorities for 2022. Furthermore, this section provides an update on the cross-sectoral priorities which had been outlined for 2021, particularly the work conducted by the Authority over the past months.

Four cross-sectoral supervisory themes have been identified for 2022, namely: [i] Financial Crime Compliance; [ii] Corporate Governance and Compliance Culture; [iii] Sustainable Finance; and [iv] Digital Finance: Operational Resilience & Innovation. The MFSA has established two other Horizontal Priorities: [i] Monitoring the impact of COVID-19 and [ii] Conduct of Business – Consumer Protection.



Cross-Sectoral Themes for 2022

1.0 Financial Crime Compliance and Corporate Governance & Culture

Corporate Governance & Compliance Culture and **Financial Crime Compliance** remain key MFSA focus areas for the third consecutive year. These two pillars complement each other and support the jurisdiction's objective to raise governance and anti-money laundering and counter-terrorist financing standards. It remains critical for the MFSA and its national counterparts to ensure that market players implement a strong and effective compliance framework which prevents and detects criminal activity, to protect the integrity of Malta's financial system.

The key measure of success will continue to be the improvements observed in the compliance culture, and strengthened governance structures and controls of financial services operators in Malta. In its authorisation and supervisory process, the MFSA will maintain focus on areas that are known to be exposed to risks and vulnerabilities, and where the Authority wants to improve standards.

1.1 Financial Crime Compliance

The ongoing integration of AML/CFT supervision into prudential and conduct supervision continues to shed light on governance and compliance failings and puts the MFSA in a position to take regulatory action in this regard.

During 2021, the MFSA issued a [Status Update on the Implementation of the 2019 MFSA AML/CFT Strategy](#), which outlines the significant improvements made by the MFSA in resources, systems, capabilities and effectiveness.

The MFSA is also contributing towards the implementation of Malta's action plan to exit the FATF's greylist. In this respect, the MFSA continues to assist all agencies throughout Malta to achieve their FATF deliverables and to conduct intrusive supervisory inspections, encompassing AML and compliance with global financial sanctions requirements. The embedding of AML/CFT into prudential supervisory inspections has led to an increase in MLRO interviews and, where necessary, escalations to the relevant agencies have been made. The MFSA also initiated a project to identify aggressive tax structures which may have led to tax evasions. This information has been shared with the OCfR and the MFSA continues to assist the said Office to identify possible tax evasion or aggressive tax structures.

The fight against money laundering and terrorist financing also remains a key priority for the EBA. In this respect, the EBA will continue to coordinate and monitor the fight against financial crime by ensuring policy development and consistent implementation to support AML/CFT supervisors and to ensure effective coordination with prudential, payments and conduct supervisors. In addition, as outlined in the [EBA 2022 Work Programme](#), the EBA also intends to use its database of information obtained from national authorities relating to weaknesses identified in relation to AML/CFT to ensure effective information flows across the EU and that money laundering and terrorist financing risks are addressed in a timely and effective manner. The MFSA continues to engage with the EBA in collaboration with the FIAU to enhance the AML/CFT framework in Malta.

At a national level, the MFSA also contributes extensively to the work on the National Risk Assessment programme. The MFSA has worked closely with the FIAU and the SMB on the assessment of threats and vulnerabilities with regards to the financial sector for AML and proliferation financing.

In 2022, the MFSA shall maintain focus on strengthening effective supervision and fighting financial crime across each sector by continuing to improve the MFSA's collaboration with the FIAU, the SMB and the OCfR. Increased engagement with the SMB on compliance with global sanctions and proliferation finance will also be a key priority.

The MFSA will continue to monitor and assess the compliance of authorised persons with AML/CFT obligations, focusing, in particular, on whether AML/CFT information is adequately exchanged between the different lines of defence of authorised persons, as well as – where applicable – between parent undertakings, subsidiaries and branches. In carrying out its tasks in relation to AML/CFT supervision, the Authority will continue to cooperate closely with the FIAU by acting as their agent and exchange therewith any relevant information.

The MFSA will also continue to work collaboratively with the FIAU on improving the local regulatory regime with respect to the expected standards from MLROs and compliance officers, and will continue providing subject matter expertise to all sectoral functions so that AML/CFT elements are further integrated in supervisory inspections and interactions with authorised persons. Building on similar efforts made during 2020 and 2021, the MFSA will continue to ensure that staff members undergo mandatory financial crime training.

The MFSA also plans to increase its engagement with the industry in order to develop local typologies of the access points to financial crime that may arise in Malta and

seek to ensure that Malta is a hostile environment for financial crime. Furthermore, the MFSA will also continue to monitor developments at a European level on the [AML Package](#).

1.2 Corporate Governance & Compliance Culture

With respect to Corporate Governance, during 2021, the MFSA published a [Feedback Statement on the Stakeholder Consultation on Revisiting the Corporate Governance Framework](#). In determining its positions as set out in the Feedback Statement, the MFSA has focused on raising corporate governance standards for authorised persons, ensuring that governance is considered a top priority and is embedded in firms' culture by the governing body and senior management. The MFSA will be issuing a list of principles of good corporate governance applicable to all authorised persons on a 'best effort basis'. The framework will be applicable for authorised persons only, and the current Codes of Governance for Listed Entities and Prospects will be retained.

Findings related to corporate governance and compliance from supervisory activity carried out by the MFSA over the past months were also reported in the series of 'The [Nature and Art of Financial Supervision](#)' publications. These publications provide the industry with the main findings, the risks identified and guidance on the Authority's relevant expectations.

Efforts relating to **Corporate Governance & Compliance Culture** will continue during 2022 through the MFSA's supervisory engagement. In this respect, in 2022, the ESAs will also continue working on the implementation of a system for the exchange of information on fit and proper assessments. This area will remain a key priority for the MFSA, to be in a position to become outcome-focused in its approach and supervisory responses.

2.0 Digital Finance: Operational Resilience & Innovation

Digital Finance: Operational Resilience & Innovation are incumbent 2021 priorities previously referred to as ICT Risk & Cybersecurity, and FinTech & Innovation, separately. Both areas are heavily interlinked and remain high on Europe's agenda especially in the light of the Digital Finance Package, and will be retained as MFSA key focus areas, cutting across sectors.

The ESAs are prioritising this area in the form of monitoring of, and response to, technological innovation, and ICT and cyber-risks emanating from new business models. The ESAs shall be, respectively and collaboratively, focusing on the legislative

proposals by the European Commission. The Joint Committee of the ESAs will also be increasing its efforts in this area. The latter's focus will be on the implementation of the expected mandates that will stem from the Digital Finance Package.

During 2021, the MFSA set up an internal working group specifically established to address the policy changes stemming from the Digital Finance Package as adopted by the European Commission, with the aim of approaching this package in a holistic manner taking into account the needs and specificities of the Maltese financial services industry.

2.1 Digital Finance: Operational Resilience

An Update on the 2021 Priorities

The digital transformation continues to deliver on its promise to bring improved efficiency, value and innovation – including within the financial services industry. Increased dependency on technology, however, as well as ICT risk and cybersecurity, present significant challenges to – and potentially severe consequences for – the resilience, performance and stability of financial systems and economies.

Through the establishment of the Supervisory ICT Risk and Cybersecurity function in February 2020, the Authority embarked on a number of initiatives pertaining to digital operational resilience as one of the industry's cross-sectoral priorities. This function has been supporting the sectoral supervisory functions, for instance on authorisations, and has been conducting various supervisory interactions using a risk-based approach to assess financial entities on their preparedness in this area.

In December 2020, the Authority released its [Guidance on Technology Arrangements, ICT and Security Risk Management, and Outsourcing Arrangements](#) in line with the MFSA Supervisory Priorities for 2021.

In the beginning of 2021, the Authority issued the [third volume](#) of 'The Nature and Art of Financial Supervision' series, focusing on ICT Risk and Cybersecurity Supervision. This document provided detailed insight on the supervisory approach, future developments within the pertinent regulatory framework – emphasising the upcoming DORA – and giving industry feedback regarding the various supervisory interactions carried out. Throughout the year, the MFSA continued with its supervisory inspections from an ICT risk and cybersecurity perspective and in addition conducted various supervisory meetings in the same area.

In 2021, the Authority further designed an ICT and Cybersecurity Risk Model and initiated a cross-sectoral thematic desk-based review on ICT and Cybersecurity Risks

Management. The self-assessment questionnaire, covering a number of sectors, was released and distributed to the respective licence-holders in planned phases.

The Authority processed several incidents through its Major ICT-Related Incident Reporting and Management process. The MFSA, through its Financial Supervisors Academy, organised a webinar on Cybersecurity in Supervision. The Authority also participated in the National Cybersecurity Strategy Committee contributing to the upcoming National Cybersecurity Strategy.

Priorities for 2022

The objective behind the European Commission's new legislative proposal – DORA – is to provide a sound and consistent framework to manage risks associated with ICT. The ESAs will each be working on the implementation of this proposal. The intensity of work required by the ESAs and, subsequently, by the National Competent Authorities will depend on the outcome of the legislative process.

The MFSA will continue participating in the different working groups set up by the ESAs on ICT risk and cybersecurity matters, contributing in their respective work programmes and working in alignment with their focus areas for 2022.

In 2022, the Authority plans to intensify its supervisory activities in this area and plans to expand – and at the same time extend – its outreach to the industry. It will continue to follow closely the developments of the DORA alongside the ESAs while preparing in earnest to meet the supervisory requirements that it will bring. In addition to continuing to strengthen and optimise its core processes, in 2022, the function plans to develop its Major ICT-Related Incident Reporting and Management process further and will start working on the establishment of an Advanced Digital Operational Resilience Testing Framework.

2.2 Digital Finance: Innovation

An Update on the 2021 Priorities

During 2021, the MFSA de-prioritised certain elements of the MFSA's 2019 FinTech Strategy such as the development of a FinTech Innovation Hub (Pillar 2), and focused on the MFSA's commitment outlined in the same strategy to adopt regulatory and supervisory initiatives to support innovation and improve regulatory efficiency (Pillar 1). In this regard, the FinTech & Innovation team led a number of internal business and operational specialists responsible for revising MFSA's application forms and authorisation process, upon which the [Authorisation Process – Service Charter](#) launched in 2021 was based. The new application forms complement the revamped

processes and the Authority's objective to simplify authorisations across all sectors through standardisation, where possible, to drive efficiency.

Further to the launch of the MFSA FinTech Regulatory Sandbox in July 2020, the MFSA received several proposals for consideration under this framework, a number of which are eligible for participation. The MFSA has been working on operationalising the framework while collaborating with the other sectoral and cross-sectoral functions to better understand the underlying innovations of such proposals as well as their benefits, risks and challenges. This initiative enables the FinTech Supervision function to build the necessary capacity in providing internal and external guidance, and enables the industry to discuss matters of innovation and supervision with the regulator.

The Authority also continued to contribute to the discussions at international level through GFIN, while engaging with other EU Member States through different forums to develop a regulatory environment that fosters and enhances the European digital single market for financial services.

With respect to the VFA sector, in the first two quarters of 2021, the MFSA granted the first VFA service providers licences under the Virtual Financial Assets Act. In preparation, the MFSA focused on ramping up its supervisory practices with the formalisation of a VFA service providers risk model, the creation of supervisory processes and procedures, as well as the planning of supervisory interactions. In order to mitigate the inherent risks of the sector and communicate the Authority's expectations, the MFSA is working on assessing all aspects of the operations of all local licensed and active VFA service providers in 2021.

Priorities for 2022

FinTech & Innovation remain a key priority for Europe. Apart from the ESAs' common focus on the policy and supervisory mandates arising from the Digital Finance Package:

- (i) EIOPA – shall be focusing on providing advice on “same activity, same risk, same rules” matters, supporting the establishment of a centralised data hub, contributing to the work on the use of artificial intelligence in finance, conducting preparatory work on open insurance and the impact of platformisation on the insurance value chain;
- (ii) EBA – will similarly be focusing on the notions of platformisation, value chains and artificial intelligence. The EBA will also continue supporting

knowledge-sharing between supervisors to enable common regulatory and supervisory responses, via the EBA FinTech Knowledge Hub; and

- (iii) ESMA – shall also be focusing on furthering its understanding of the impact of financial innovation on financial markets functioning and participants, and shall seek to co-ordinate with national supervisory authorities on the regulatory and supervisory treatment of innovative financial activities and technological innovation. ESMA will also be working on the implementation of the regulation on a pilot regime for market infrastructures based on distributed ledger technology.

Through the EFIF, the Joint Committee of the ESAs will continue focusing on building cooperation amongst innovation facilitators¹ to support the scaling up of innovation in the financial sector. MFSA's contribution to this area has been consistent and is forecasted to grow in view of the extensive work programme of the EFIF in relation to this area.

Building on the MFSA's 2019 FinTech Strategy, the MFSA is committed to continue becoming an enabler of sustainable technology-enabled financial innovation within the financial services market by providing a regulatory environment which is built on global standards, contributes to sustainable growth within the financial services market, and achieves investor protection, market integrity and financial soundness. It is within this context that the MFSA will be focusing on three foundational elements, namely: (i) regulation; (ii) monitoring; and (iii) capacity.

During 2022, the MFSA will be reviewing the Sandbox Framework taking into consideration the lessons learnt over the past year as well as the new regulatory initiatives occurring at a European and global level. Furthermore, the MFSA shall continue monitoring developments at EU level also with respect to the legislative proposal on crypto assets, MiCA. In this respect, the Authority will continue working towards achieving a smooth eventual transition for authorised persons.

Following on the publication of the [FATF's Updated Guidance on a risk-based approach to virtual assets and virtual assets service providers](#), the Authority will also continue working with relevant stakeholders in order to ensure that any new or existing gaps identified by the Updated Guidance are addressed. Furthermore, the Updated Guidance shall inform the ongoing AML/CFT supervision undertaken by the MFSA.

The Authority will also continue to collaborate with the relevant stakeholders in providing feedback on the Transfer of Funds Regulation proposal at EU level, which

¹ Defined as Regulatory Sandboxes and Innovation Hubs

will implement FATF's Recommendation 16 (the Travel Rule) to the Virtual Asset sector. The MFSA will also continue working with the FIAU on the implementation of the Travel Rule locally and ensure that this is fully in line with the FATF's guidance.

The Authority will continue focusing on enhancing its monitoring within the FinTech space, through: (i) its ongoing monitoring; (ii) the MFSA FinTech Regulatory Sandbox; (iii) participation in cross-border knowledge sharing; and (iv) the understanding of the adoption of FinTech and digital finance locally as well as the market's needs, risk, challenges and implications to financial stability. The MFSA shall also be working on realigning the MFSA's 2019 FinTech Strategy with European direction and on establishing an external FinTech and Digital Finance Advisory Committee.

The MFSA shall continue enhancing the MFSA FinTech Regulatory Sandbox as the main tool for reducing supervisory 'blind spots', gaps and risks within the market and shifting towards outward proactive engagement with industry participants to make sure they understand the nature of the risks to the client, the authorised person and the market. Furthermore, through: (i) participation in cross-border sandbox testing frameworks such as the EU Joint Testing Framework and the GFIN cross-border testing initiative; (ii) participation in EU (ESAs & EFIF) and international fora (IOSCO & GFIN) to identify developments in other jurisdictions; and (iii) establishment of FinTech Bridges, the MFSA shall continue increasing focus on cross-border engagement and knowledge sharing. The MFSA will also be contributing to the work carried out by the ESAs in this field.

During 2022, the MFSA aims to continue strengthening its digital finance and innovation capacity and skillset across the supervisory functions through the support of its centralised FinTech Supervision function and the Financial Supervisors Academy. This would enable the MFSA to become increasingly knowledgeable in the area to be able to understand emerging business models that are being presented to the MFSA across sectors. By doing this, the MFSA will be preparing for further integrating FinTech and digital finance within the wider MFSA structures and processes in order to have the necessary supervisory and regulatory requirements to meet the needs of the financial services landscape of tomorrow. In this respect, the Authority will start placing particular emphasis on the integration of digital transformation strategies within authorised persons' overall business strategies. The MFSA shall be looking into the implementation of such strategies, their impact on the business model and risk profile of the same authorised persons, and their approach towards innovative FinTech solutions.

With respect to the VFA sector, the Authority plans to continue with the work it conducted in 2021, supervising both VFA agents and VFA service providers on a risk-based approach by conducting supervisory meetings to follow up the remediation of

findings with respect to 2021 supervisory interactions. In addition, the MFSA also intends to conduct broad scope inspections on newly licensed VFA service providers. Furthermore, the Authority also intends to carry out thematic inspections on ICT and conduct matters. In carrying out its supervisory work in this field, the Authority will be adopting a risk-based approach in terms of assets under custody and the client base.

3.0 Sustainable Finance

The European Commission aims to make Europe the world's first climate neutral continent by 2050. Listed as one of MFSA's key initiatives last year, Sustainable Finance has thus emerged as a supervisory priority focus area for 2022 in the light of the developments happening with the [European Green Deal](#) and its underlying initiatives including the European Commission's [Sustainable Finance Package](#).

An Update on the 2021 Priorities

The MFSA issued [a number of Circulars](#) on the subject of Sustainable Finance, for different legislative instruments, focusing on the requirements emanating from European Frameworks, as well as guidance presented by the ESAs and the MFSA. In addition, in 2021, the MFSA also interacted directly with industry participants with the aim of analysing the current state of play of local market participants with respect to the SFDR.

The MFSA also recently set up a central Sustainable Finance policy team. Through the setting up of a Sustainable Finance platform, this new office aims to support the implementation of the Authority's strategy for the integration of sustainable finance regulation across the sectors. In parallel with the required regulatory and policy development in this space, the MFSA shall be focusing on the integration of this priority into its supervision.

Priorities for 2022

From a European perspective, the ESAs will be working on developing a number of draft technical standards under the SFDR. The ESAs may also contribute to the development of disclosure standards for non-financial information, subject to the review of the NFRD. Additionally:

- (i) EBA – will continue focusing on investigating ESG risks to inform risk assessment and policy making, to eventually incorporate these risks into risk management and supervisory rules. The EBA will also carry out ESG impact assessments with the aim of incorporating ESG considerations in its

policy development, risk analysis and stress testing. Depending on the outcomes from the European Commission's Renewed Sustainable Finance Strategy, EBA mandates may include green securitisation, green bonds, ESG risk management tools and ESG reporting tools.

- (ii) EIOPA – will continue focusing on the integration of ESG risks in the prudential framework of insurers and pension funds, through the development of tools and guidance for the identification and management of sustainability risks. EIOPA will also be working on the promotion of sustainability disclosures and a sustainable conduct of business framework, in order to prevent greenwashing.
- (iii) ESMA – will be focusing on risk assessment and leading the set up of common supervisory practices and approaches related to this area. ESMA will also be developing its risk identification methodology related to ESG factors and continuing to promote transparency by issuers and market participants. ESMA will also contribute to the development of sustainable financial markets and assess how greenwashing can be prevented.

The Authority will be monitoring the above outlined developments at the ESAs. Additionally, the MFSA will be focusing on raising awareness and guiding market participants to address new challenges. The MFSA shall also be working on integrating the new ESG factors in its supervision of regulated entities and ensuring compliance by such entities with the relevant requirements.

In 2022, the MFSA will continue working on creating and fostering a policy framework which provides a clear trajectory for sustainable finance. Concurrently, the MFSA will continue its outreach to ensure that – locally – consumers are aware and informed in this area to ensure that they can make appropriate financial decisions.

Through its Financial Supervisors Academy, the MFSA shall be providing training to its supervisors to upskill its officials in this space.

Horizontal Priorities for 2022

1.0 Monitoring the Impact of COVID-19

Monitoring the impact of COVID-19 remains a focus area in MFSA's ongoing supervision, especially in the banking and insurance sectors. MFSA's key focus areas shall be aligned with the ESAs as follows:

The **EBA** will continue to monitor the impact of COVID-19 by assessing the impact on asset quality and provisioning, and monitoring the effect on moratoria and public guarantees. The MFSA's priorities will be aligned with those of the EBA and with the EBA's [2022 ESEP for Prudential Supervisors](#) in this respect.

ESMA will also continue to focus on the impact of the COVID-19 pandemic on financial markets and financial market participants, while **EIOPA**, as outlined in its [Union-Wide Strategic Supervisory Priorities](#), is expecting National Competent Authorities to focus their supervisory activities on monitoring the impact of the prolonged low-yield environment as well as of the COVID-19 crisis on the business model sustainability, and the development of insurers and institutions for occupational retirement provision.

2.0 Conduct of Business – Consumer Protection & Education

Protecting consumers is a key strategic objective of the MFSA and has been established as a horizontal supervisory priority, cutting across sectors.

Updates on the sector-specific work carried out in relation to Conduct of Business during 2021 is outlined under the sectoral sections further into this document. As an update on 2021's cross-sectoral Conduct of Business work, the MFSA issued its [fifth volume](#) of 'The Nature and Art of Financial Supervision' series, which focused on POG Requirements and published the findings of the cross-sectoral thematic exercise carried out by the Authority in this respect.

2022 will see continued focus on retail investor protection to ensure that the interest of consumers of financial services is placed at the centre of authorised persons' operations. The MFSA shall be focusing on the below ESA priorities on this area:

- From a customer-protection perspective, the **EBA** will continue work started on issues aggravated by the pandemic as highlighted by the consumer trends report 2020/1.
- Unfair and disproportionate costs and fees can impact investors' trust in financial markets. As such, **ESMA** expects NCAs to focus on problems linked to cost and performance, and any associated lack of transparency. Investment firms should ensure that costs and charges are reasonable and disclosed in a transparent and non-complex manner. In this respect, the Authority will also be delving into the applicability of MiFID II requirements on costs and charges in so far as retail clients are concerned.
- Tying with the previous Horizontal Priority and in line with **EIOPA's** expectations, the Authority will focus its supervisory activities on monitoring the impact of the COVID-19 crisis on products and ensuring that Product Oversight and Governance requirements and other relevant consumer protection and conduct of business-related requirements are adequately implemented to address the deficiencies which emerged in the crisis. Products will be reviewed to ensure the sustainability of business models and customer centricity.

Further sector-specific Conduct of Business Priorities for 2022 will be outlined under Section II of this document.

Consumer Education

Consumer protection lies at the heart of conduct supervision. The MFSA seeks to protect consumers of financial services from any detriment caused by the misconduct of firms. Consumer education is a fundamental tool used by the MFSA for the appropriate protection of consumers is consumer education – educating consumers about their rights and duties.

During 2021, the MFSA embarked on numerous consumer education campaigns including those related to [Digital Banking](#) and [Investing Smartly](#). Throughout the year the MFSA also upgraded its [Payment Account Fees Comparison Tool](#), engaged in outreach campaigns held at schools, and issued other warnings and guidance to the public through its website and social media platforms.

From a European landscape, **EIOPA** plans to assume a more co-ordinating role in facilitating how financial education measures are promoted by NCAs at national level. In this respect, EIOPA will be collecting information on national financial education and literacy initiatives, and maintaining an interactive webpage on its website in this respect. Furthermore, **ESMA**, in close co-operation with EBA and EIOPA, will be

supporting targeted financial education and financial literacy initiatives and will contribute to any efforts made within the context of the ESA Joint Committee in this respect.

During 2022, the MFSA will continue carrying out consumer education campaigns to raise awareness on financial services and to enhance consumer confidence in the banking, securities and insurance sectors. This strategy is in line with MFSA's strong commitment to promote the protection and education of consumers of financial services as well as with the ESAs' objectives to promote financial education. The Authority will also continue contributing to the joint initiative as chaired by the European Commission and the OECD, with the aim of developing a financial competence framework for the EU. MFSA is also planning to participate in the next World Investor Week organised by the IOSCO, which is expected to take place in October 2022.

Section II



Sector-Specific Priorities

Introduction

This section provides an update on the MFSA's sector-specific supervisory priorities for 2021 and sets out those for 2022. The priorities outlined in this section build on those having a cross-sectoral nature and should therefore be considered as complementary.

Credit and Financial Institutions

An Update on the 2021 Priorities

In line with the cross-sectoral priorities for 2021, the Authority continued working on the assessment of governance of credit and financial institutions, as a sector-specific priority.

Credit Institutions

The Authority developed and implemented a broader communication channel and training strategy to support the development of boards. The MFSA held a webinar on [Regulatory Expectations of Bank Boards for Non-Executive Directors and Professional Advisors](#) and also a webinar on [Supervisory Reporting Developments brought about by CRR2](#).

Furthermore, during 2021, the MFSA agreed on a SREP Framework with the ECB. As part of the SREP assessment, the MFSA reviewed the structure and quality of boards of directors of less significant institutions and determined that banks should deliver improvements. To support the industry's understanding of the MFSA's expectations, the MFSA ran its first conference for NEDs. In addition, the MFSA imposed qualitative requirements on banks including, but not limited to, the appointment of further independent NEDs, self-assessments or external review exercises and required improvements in the control functions that support board oversight. During 2021, the MFSA also reviewed the adequacy of compliance functions within banks.

The MFSA also reviewed the challenges that the post-pandemic economy present to banking business model viability in Malta. Throughout 2021, the Authority conducted a number of supervisory interactions on credit institutions to examine the quality of banks' controls over the recognition of impaired exposures, board reporting on credit

risk and the operational preparations undertaken for an increase in credit risk profiles. This included a review of banks' capabilities to identify and report credit risk in their balance sheet, and the potential consequences of further credit risk shocks. The MFSA also reviewed the level of overall balance sheet resilience provided by provisioning cover, reliance on collateral and the capital adequacy of banks.

The MFSA initiated its work to assess the preparedness of banks to deal with the impacts of climate change on their business models. To this effect, a questionnaire was used to identify where the main risks lie to an orderly transition in the immediate future. In addition, the Authority also examined the risks to business models from reliance on deposit platforms.

From a conduct perspective, the Authority had plans to launch the Conduct of Business Rulebook for the banking sector in 2021. This had been delayed due to other competing priorities which emerged in 2021.

Financial Institutions

Significant work was also undertaken by the Authority in 2021 with respect to financial institutions from an authorisation and enforcement perspective.

In 2021, the Authority continued with its effort to ensure a higher degree of regulatory compliance in the financial institutions sector. Central to this strategy was closer supervisory scrutiny, an enhanced authorisation process and enforcement.

The Authority conducted a number of supervisory interactions delving into institutions' business models and key risk areas. Through deep dives, thematic reviews and firm-specific engagement, the MFSA examined governance quality at board level, internal governance structures and compliance controls.

As part of its monitoring of firms, the MFSA also required immediate corrective action from a number of institutions that were falling short of key prudential requirements, most notably the safeguarding of clients' funds and the minimum own funds requirement.

The Authority continued its work on revising the Financial Institutions Rulebook and Reporting templates, with a plan for this to be published in 2022.

Priorities for 2022

From a European point of view, the EBA will be working on: (i) monitoring and updating the prudential framework; (ii) revisiting and strengthening the EU-wide stress-testing framework; (iii) leveraging banking and financial data; (iv) deepening its analysis and information-sharing with respect to digital resilience, FinTech and innovation; and (v) fighting money laundering and the funding of terrorism, and contributing to a new EU infrastructure in this respect. In addition, the EBA has also identified ESG risks and the impact of COVID-19 as horizontal priorities for 2022, which have also been identified by the MFSA as a cross-sectoral theme and horizontal priority respectively. The MFSA will continue to work in collaboration with the EBA and to contribute to its work through its participation in various committees and working groups.

Credit Institutions

In 2022, the MFSA will continue to embed the SREP cycle into its supervisory model for banks and will continue to monitor how banks address governance and internal control challenges as part of its SREP reviews and follow up work in 2022. This will continue to be accompanied by Minimum Engagement Level (MEL) supervisory meetings designed to support the ongoing assessment of banks and to improve communication with the sector. The MFSA will use both of these supervisory tools during 2022 to follow up on the governance and risk management findings from its initial SREP reviews of 2020 and 2021, including succession planning at board level. The MFSA will also evaluate the way in which banks are integrating ESG risks into their frameworks.

The MFSA shall also be following up on the questionnaire submitted to credit institutions in 2021 to assess the preparedness of banks to deal with the impacts of climate change on their business models as part of its SREP and MEL supervisory meetings in 2022. The work undertaken by the Authority in 2021 in relation to risks to business models will be expanded in 2022 to look at broader funding risks.

In addition, in 2022, the MFSA will be focusing on the priorities listed below:

Business Model Viability: The MFSA will continue to focus on business model viability through effective budgeting and stress testing, and will ensure that banks' investment in IT contributes to future resilience and cost control by evaluating improvements in ICAAPs and ILAAPs, monitoring business performance against forecasts, and through the quality and understanding of stress testing.

The MFSA will also evaluate the liquidity risk management capabilities of banks and their overall liquidity risk positions.

Furthermore, engagement with senior bank directors will continue in order to understand the manner in which the appropriate oversight of banks' business models is being ensured. This will include discussions on succession planning for key board and management posts that contribute to medium-term viability.

Credit Risk: The MFSA will continue to assess how banks are recognising, calculating and monitoring credit risk in the recovery phase of the pandemic. This includes completion of work to update banking rules on non-performing loans in line with ECB and EU requirements. The MFSA will also evaluate the improvements banks are making to their credit risk management processes.

The Authority will also monitor how banks are assessing credit risk emerging from changes to the economic environment arising from energy price fluctuations, supply chain and trade policy changes, and climate change, as well as from changes to the legislative environment, and seek evidence that banks have documented their overall level of balance sheet resilience in their ICAAPs, including the reliance on – and valuation of – collateral, levels of provision coverage and capital support.

Operational Risk: The MFSA will examine the extent to which boards and management have evaluated their operational risk exposure, with a focus on cyber-resilience and will follow up on the MFSA sector questionnaires that were issued in 2021.

Internal Audit: The MFSA will examine the extent to which banks have an effective three lines of defence model by examining the governance and resources of internal audit functions in banks. This will include the documentation and coverage of the audit universe, the quality of reports and appropriateness of actions to mitigate risks identified by internal audit reviews.

AML/CFT: The MFSA shall continue to monitor the way in which banks evolve their controls to prevent their business models from being used for the purposes of financial crime and the systems that they use to identify and report risks. In addition, in line with the EBA's 2022 ESEP for Prudential Supervisors, in assessing the suitability of board members and senior management, the Authority will continue to take into consideration the level of competence and expertise in AML/CFT.

Conduct of Business: To promote a transparent, simple and fair financial services market, the MFSA will continue its focus on the fees and charges imposed by credit institutions for the provision of retail banking products and services to ensure that the

introduction or changes of such do not lead to consumer detriment. The Authority will monitor the development of fees and charges and establish whether compliance and monitoring costs on the part of the credit institutions are being passed on to the end retail consumers.

The MFSA will strive to ensure that banking services remain accessible to all and will emphasise the importance of financial inclusion, even in the wake of digitalisation – which has accelerated rapidly in the past year.

As COVID-related moratoria and other support measures by credit institutions ceased in 2021, the expectation is that the volume of NPEs will increase during 2022. In response to this, the Authority will initiate supervisory work on NPE management by credit institutions, with a specific focus on consumer protection.

The MFSA will also continue to follow closely any developments related to the [Banking Package 2021](#) and to contribute to discussions at a European level. The aim of this proposal is to ensure banks' resilience to potential future economic shocks, while contributing to Europe's recovery from the COVID-19 pandemic and the transition to climate neutrality.

Finally, the Authority will initiate work to launch and publish the Conduct of Business Rulebook for the Banking Sector.

Financial Institutions

The MFSA intends to change its supervisory approach to the sector and place more responsibility on firms to ensure their own compliance with regulatory requirements. This will include the use of internal audit or externally commissioned reviews that provide assurance to the MFSA in certain areas of its work. Inspections to newly authorised firms will also be introduced to ensure early compliance with key requirements and ensure that licence conditions are being respected as firms grow.

As the sector continues to grow, the MFSA is evolving its supervisory approach to achieve its objectives in an efficient and effective manner.

In addition, the MFSA has identified the following supervisory priorities for this area:

Internal Governance and Culture: The MFSA shall continue to push for good governance practices in financial institutions. Focus shall be on the efficacy of the board of directors, the internal control functions and other key function holders. This will include evaluating how the board of directors ensures that its firm delivers good standards of regulatory compliance.

Business Model: The Authority shall continue to assess how the boards of financial institutions exercise oversight of their business models and determine the appropriate level of controls to mitigate risks to viability. The MFSA's focus will be on the manner in which boards assess the capacity for revenue generation. The MFSA shall also assess the impact on operational resilience of the various external pressures in the current operating environment.

Prudential Obligations: The MFSA shall examine the mechanisms put in place to ensure adherence to key prudential obligations. In particular, the MFSA shall seek assurance that systems and controls in place to safeguard clients' funds are effective in providing the required level of protection. The Authority shall also monitor how the board ensures that their business adheres to their own funds obligations at all times.

Operational Risk: The MFSA shall continue monitoring ICT and cybersecurity risks through the MFSA's Supervisory ICT Risk & Cybersecurity function, with a particular emphasis on ICT governance, outsourcing arrangements and cyber-resilience.

AML/CFT: The MFSA will continue to evaluate how the boards of financial institutions assess the adequacy of their controls to mitigate the risk that their business could be used for the purposes of financial crime and to assess their capacity to detect and report AML/CFT risks.

Insurance and Pensions

An Update on the 2021 Priorities

The Authority continued its work on the monitoring of cross-border activity. In this respect, close collaboration was maintained with other NCAs through meetings and Colleges. In addition, the MFSA acted as a group supervisor and also participated as a college member in a number of other Colleges held throughout 2021.

During 2021, the Authority continued monitoring and engaging with undertakings effected by Brexit and participated in EIOPA Brexit Platforms. The MFSA is also in the final stages of completion of a thematic governance review across the entire insurance market, covering the effectiveness of internal committees and non-executive directors.

The MFSA also continued monitoring prudential requirements relating to capital adequacy, business model profitability, liquidity, data quality and the general financial soundness of regulated entities through ongoing work with EIOPA's Liquidity monitoring, Insurance Stress Tests and Solvency II Reviews. In addition, in 2021, the Authority also carried out supervisory interactions, particularly on outsourcing, including on Managing General Agents arrangements.

From a conduct perspective, the MFSA continued its supervisory work on product oversight and governance arrangements and, in this respect, is working on three main workstreams namely: (i) assessing the state of play of the implementation of such requirements through a cross-sector thematic review exercise; (ii) participating in ongoing supervisory work carried out by ESAs; and (iii) extending the MFSA Conduct of Business Rulebook requirements to other sectors of the financial services industry.

In 2021, the Authority also carried out a number of supervisory interactions with various markets participants with a view to assess their distribution activities and the timeliness of claims handling by insurance undertakings.

The consumer survey on Bancassurance planned for 2021 was postponed to the forthcoming year in view of competing priorities.

Priorities for 2022

In Europe, EIOPA will be focusing on building a safe and sustainable EU for its citizens in times of transformation by ensuring strong and consistent protection of consumer interests across the EU and safeguarding the financial stability of the insurance and pension sectors and the effectiveness of the financial system. In order to achieve these objectives, EIOPA has identified the following strategic activity areas: (i) sustainable finance; (ii) digital transformation; (iii) effective supervision; (iv) technically sound prudential and conduct of business policy; (v) risks to financial stability, preventative policies and mitigating actions; and (vi) its own good governance. In this respect, the MFSA is committed to align itself with EIOPA's priorities, by implementing and transposing legislative amendments and proposals where necessary as well as participating in salient forums, such as project groups and peer review projects spearheaded by EIOPA, to provide its views and obtain a better understanding of EIOPA's objectives.

Insurance

In 2022, the MFSA shall implement the following activities to monitor the impact of the low interest rate environment (LIR) and the COVID-19 crisis on the business model sustainability of insurance undertakings, aligning with the USSP:

- Assessment of long-term sustainability risk related to LIR;
- Assessment of risk associated with LIR in combination with increased uncertainty following COVID-19 on the sustainability of undertakings primarily writing 'with profits' life insurance business;
- Development of a more flexible COVID-19 market stress framework; and
- Assessment of liquidity risk in a risk-based manner.

The MFSA shall continue focusing on how licence-holders are implementing an effective system of governance taking into consideration a number of areas, in particular the collective knowledge, skills and qualifications of the board of directors, the adequacy and effectiveness of the internal control system and oversight arrangements implemented by the licence-holders, and the effective implementation of the internal audit function.

The MFSA shall also continue focusing on how licence-holders are promoting and facilitating a proactive and strong compliance culture within their organisations.

Other priorities include supervisory work in relation to outsourcing which will involve engagement with both licence-holders and third party service providers to assess whether the outsourcing of key and critical/important operational functions and

activities lead to material impairment of the quality of the licence-holders' system of governance, unduly increase operational risk, impair the ability of the MFSA to monitor the licence-holders' compliance with their obligations as well as whether such outsourcing arrangements undermine continuous and satisfactory service to policyholders.

The MFSA will also continue with the integration of financial crime assessments in prudential assessments and engage with licence-holders to assess the level and quality of controls implemented in relation to AML/CFT risks posed by their respective business models.

The MFSA shall also be conducting thematic reviews into:

- **Reserving:** continuing from 2021, with a special focus on life insurance in 2022, assessing the appropriateness of forward-looking assumptions including lapse and mortality rates, expenses, changes in investment profile, how guarantees affect the calculations and future management actions; and
- **Reinsurance:** assessing the balance between the risk effectively transferred and the capital relief in the Solvency Capital Requirement, in line with [EIOPA recommendations issued in July 2021](#), while also assessing counterparty default risk calculations and risks associated with use of non-EU jurisdictions.

The Authority will also assess prudential and conduct aspects relating to 'with profits' products.

On the regulatory front, the MFSA will start the implementation of the amendments to the Motor Insurance Directive in close coordination with the Ministry for Finance and Employment, and Transport Malta. Throughout this process, extensive consultation will be held with the industry and all stakeholders.

Following the [proposals](#) issued by the Commission on the Solvency II 2020 Review and the new Insurance Recovery and Resolution Directive, the MFSA will be actively participating in discussions at a European level in coordination with the MFSA's Resolution Team and the Ministry for Finance and Employment.

From a **Conduct of Business** perspective, the Authority considers that insurance products should always provide value for money to their policyholders, by meeting the policyholder's expectation of risk cover for the premium paid. In this context, the Authority will be focusing on:

- (i) monitoring whether manufacturers assess the design of the products to ensure that they are easily understood and offer value by/to the relevant target market;
- (ii) assessing whether insurance manufacturers have adequately performed product monitoring and review activities, focusing on the products whose features and target markets' needs, objectives and characteristics have been impacted by the COVID-19 crisis, leading to a significant change to the risk profile; and
- (iii) carrying out supervisory work relating to the exclusions forming part of certain types of policies and their impact on the value for money for consumers.

Furthermore, the Authority will also focus on the distribution activities of insurance agents and will particularly focus on their sales processes to assess their alignment with the applicable regulatory requirements.

Pensions

With respect to the pensions sector, in 2022, the MFSA will be primarily targeting the effectiveness of compliance activities in relation to suitability and conduct undertaken by retirement scheme administrators, which includes an assessment of how they are promoting and facilitating **a proactive and strong compliance culture** within their organisations.

The MFSA will be also focusing on how retirement scheme administrators are implementing an **effective system of governance** to ensure sound and prudent management of the business.

Furthermore, the MFSA will be also assessing the potential abuse of double taxation treaties by complex pension structures as part of the **financial crime assessments** integrated in its prudential assessments.

Securities and Markets

An Update on the 2021 Priorities

Capital Markets and Market Infrastructures

During 2021, the Authority continued with the supervision and enforcement of financial and non-financial information, as well as with market oversight in relation to EMIR and Market abuse carrying out a number of supervisory inspections, supervisory meetings and transaction reviews, as necessary. In addition, MFSA continued its efforts to monitor the impact of the COVID-19 pandemic.

The Authority continued work in relation to the implementation of the Covered Bonds Directive. Further efforts were focused on the regulatory review of legal texts which impacted the market infrastructures' space, such as MiFID II and the CSDR.

Throughout 2021, the MFSA focused on improving data quality, and all entities falling within the scope of reporting data in terms of MiFID II, EMIR, SFTR and CSDR, among others, were required to report details accurately and up to the standards required by European bodies.

The Authority also processed an increasing number of applications for admissibility to listing of securities throughout 2021 and continued working on its Capital Markets Strategy.

Funds and Service Providers

In 2021, the Authority published the fourth volume of the publication 'The Nature and Art of Financial Supervision'. The [document](#) provided an overview of the Authority's approach to the supervision of fund managers, collective investment schemes, recognised persons and depositaries of collective investment schemes. It also highlighted the main observations made by the MFSA through the supervisory engagements conducted in 2020, sets out the Authority's findings, and identifies the best practices which are expected of licence-holders.

MFSA also provided [updates](#) on its website to the regulatory framework in relation to the supervision of ESG Funds in 2021.

During 2021, the MFSA carried out an assessment on the adequacy of controls of licence-holders over outsourced functions, including portfolio managers, risk managers and compliance officers, through a number of remote inspections, including on the initial and ongoing monitoring, and on the due diligence carried out by asset managers and collective investment schemes on service providers to whom activities have been outsourced.

The Authority also carried out substantial work with respect to ESMA's CSA on Fees and Costs on UCITS management companies and UCITS. This deliverable was conducted in two phases: (a) a desk-based questionnaire on costs and fees covering the entire population of UCITS fund managers; and (b) focused inspections on a selected number of UCITS and UCITS management companies. The main scope of the exercise was to determine the adequacy of fees being charged to UCITS investors, governance practices relating to the initial setting up of fee structures as well as the ongoing review thereof. A data aggregation exercise has been set in motion to assess the adequacy of the fee charges when compared to industry peers. The outcome of this exercise will be reported to ESMA.

Follow-up work was also carried out on liquidity risk management during 2021. The function [published](#), inter alia, its liquidity risk management findings and best practices in relation to the thematic liquidity risk exercise carried out in 2019 as well as the CSA on UCITS liquidity risk carried out in 2020. The MFSA also carried out a number of remote supervisory inspections on depositaries, reviewing governance, compliance and operational aspects including cash flow monitoring, investment restriction verifications and reconciliations, with specific focus on the Notified AIF regime.

The MFSA carried out other work in relation to this sub-sector, including the launch of the Fund Return for Collective Investment Schemes and the transposition of the CBDF Directive. The Authority also published a [discussion paper](#) on its Asset Management Strategy. The initiatives identified in this document are in line with the MFSA's risk-based approach and are directed at streamlining the regulatory framework in key areas and optimising the level of effectiveness from a supervisory perspective.

Investment Firms

The implementation of the Investment Firm Regulatory Package including revisions to the regulatory framework and the Investment Services Rules applicable to investment services providers, and industry engagement to raise awareness thereon remained a priority for 2021. Moreover, the Authority continued working on the implementation of the revised Capital Requirements Directive Package – CRD V and CRR II.

Throughout 2021, the Authority continued its focus on the assessment of governance and the three lines of defence of investment firms, governance models and the effectiveness of control functions, such as the compliance function.

Thematic supervisory interactions on safeguarding of clients' assets and thematic engagements on outsourcing were conducted throughout the year as per supervisory priorities. In addition, capital adequacy verifications were carried out on an ongoing basis by way of desk-based reviews from the financial information submitted.

From a conduct of business perspective, the MFSA followed up on supervisory work which was being undertaken vis-à-vis the MIFID II suitability assessments and examined the selling processes of a sample number of investment firms with respect to the distribution aspect of locally issued financial instruments to the general public, focusing particularly on high-risk customers groups, also supported with a data-driven approach.

The Authority also continued working on the application of MiFID II Product Governance requirements. Furthermore, building on the cross-sectoral priority for 2020, further supervisory work on cross-border investment services was also conducted by integrating it as part of the Authority's supervisory inspections.

Priorities for 2022

From a European viewpoint, ESMA will be focusing on the development of the Capital Markets Union in order to develop capital markets that can contribute to financing the economy and ensure economic growth and job creation. Furthermore, ESMA will, inter alia, continue working on its Sustainable Finance Strategy, assess the opportunities and risks of innovation and digitalisation, promote supervisory convergence, strengthen its risk identification as well as increase its co-operation with national competent authorities and other public authorities at EU and international level.

The Authority will continue to contribute to the work carried out by ESMA through its participation in various committees and working groups. The Authority will also follow any developments related to the [Capital Markets Union Package](#) and contribute to the discussions at a European level.

Capital Markets and Market Infrastructures

The Authority will continue with the supervision and enforcement of financial and non-financial information, as well as with market oversight in relation to EMIR, market abuse and SFTR, carrying out several supervisory interactions and transaction

reviews, prioritising investigations of any alleged breaches and taking the necessary supervisory actions.

In so far as the enforcement of financial information is concerned, the Authority will be conducting its work in line with the European Common Enforcement Priorities of Annual Reports for financial years 2021, which shall focus on:

- (i) Impact of COVID-19 pandemic;
- (ii) Climate related matters – Consistency between IFRS financial statements and non-financial information; and
- (iii) Expected credit loss disclosures of credit institutions.

2022 will be the first year of ESEF implementation, where the Authority will ensure that all annual financial reports prepared by issuers are in compliance with the European Single Electronic Format. The Authority will continue supporting issuers for the smooth transition into the ESEF format.

The MFSA will continue reviewing applications for admissibility to listing of securities on the Malta Stock Exchange.

The MFSA will continue its efforts on improving data quality as required in terms of inter alia MiFID II/ MiFIR and the CSDR. In fact, as of 1 February 2022, the MFSA will be commissioning the commencement of reporting items related to settlement discipline.

The Authority will continue its work on the implementation of the Covered Bonds Directive, will continue to follow closely updates on the European Green Bond Standard and will be participating in the regulatory review of the Prospectus Regulation and the Market Abuse Regulation.

Furthermore, a push on policy will be one of the main focuses of the Market Infrastructures team, with legislative proposals like the DLT Pilot Regime, CSDR review and MiFID II review eventually materialising. Lastly, the MFSA will be looking more closely at two areas: crowdfunding and securitisation. The Regulation on European Crowdfunding Service Providers came into force on 10 November 2021, and the MFSA will be gradually introducing local rules which will seek to smoothen the process for accepting such business. Similarly, in the securitisation area, the MFSA intends to review the local regime to come up with amendments which make securitisation vehicles workable while taking into consideration risk mitigating factors.

The MFSA shall carry out supervisory interactions on trading venues, member firms, central securities depositories, benchmark administrators, and clearing members, to review the arrangements, strategies, processes and mechanisms implemented and ensure compliance with all relevant regulations.

The MFSA shall continue its work on implementing the Capital Markets Strategy, with the aim of providing equal opportunities to market players, safeguarding the stability and integrity of financial markets, and protecting investors, while focussing on transparency and efficiency.

Funds and Service Providers

The MFSA will continue incorporating liquidity risk management and outsourcing topics in its onsite and offsite engagements, in addition to governance and compliance work which will remain core to the routine supervisory interactions held. In addition, building on the work done during 2021, AML will continue to be integrated in most supervisory interactions. Follow-up work will also be conducted with respect to ESMA's CSA on fees and costs charged by UCITS.

Based on the data collection exercise undertaken in the year 2021, tapping into the level of preparedness and compliance of licence-holders with the SFDR and Taxonomy Regulation, the MFSA will continue monitoring licence-holders in relation to the SFDR and to address compliance with the said Regulations. Furthermore, a separate self-assessment request for information covering de minimis AIFMs/PIFs is expected to be issued in Q1 2022.

The MFSA will be conducting reviews on valuation practices being adopted by fund management companies, with a particular focus on whether such valuation principles and methodologies comply with the requirements set out in the respective regulatory frameworks and with a particular view to assess the governance principles that are embedded by funds and fund managers in their valuation functions.

Finally, the Authority will continue to strengthen its focus on enhanced supervision cases in this sub-sector.

Further work will be carried out with respect to depositories, with a review of the rulebook of such licence-holders being underway. The MFSA also remains committed to review depositories of collective investment schemes and their compliance with Part BIV of the Investment Services Rules for investment services providers. In continuation with the work carried out during 2021, the Authority will monitor closely and participate in European forums involving the review of the AIFMD.

Following the entry into force of the CBDF Directive and Regulation, the MFSA also intends to review sample marketing communications of AIFMs to assess how these are compliant with the CBDF Regulation and with ESMA's guidelines on marketing communications. Attention will also be given to the governance and oversight elements present within such fund management companies in relation to such marketing communications.

Furthermore, the Authority will also pursue the initiatives identified in the discussion paper on its Asset Management Strategy. Feedback collected in the course of this consultation will be taken into consideration in the process of implementation and identification of new issues requiring attention.

Investment Firms

The MFSA will continue engaging with the industry to ensure good governance and that overall internal functions and controls are in place, while endeavouring to minimise AML/CFT shortcomings. Through the risk-based model to supervision, the Authority will continue focusing its resources towards entities which require heightened supervision based on inter alia their operational model, size and compliance culture.

Building on the cross-sectoral priority for 2021, the MFSA will continue assessing the type and level of cross-border investment services undertaken in terms of the investment firms' business model.

Furthermore, as the Investment Firms Regulatory Package is now in place, the MFSA will carry out initiatives, through supervisory engagement, to ensure the industry's preparedness and compliance with the regime, including capital and liquidity requirements, firms' classification, prudential consolidation, internal capital adequacy risk assessment as well as reporting and disclosure requirements.

The MFSA will also continue to keep the industry informed about any changes and approvals in relation to regulatory and implementing technical standards that are yet to be approved by the European Commission and will provide the necessary support that may be required.

From a **Conduct of Business** perspective, the MFSA plans to follow up on the supervisory work which is currently being undertaken in relation to the MiFID II Product Governance requirements. Follow-up supervisory work is also planned with respect to the examination of the investment firms' selling processes in so far as the retail distribution of locally issued financial instruments is concerned.

The Authority will also be delving into the applicability of MiFID II requirements on costs and charges in so far as retail clients are concerned. Furthermore, MFSA will also be examining PFOF practices in relevant business models and in this respect will be considering the investor protection issues as detailed in the ESMA Public Statement.

Trustees and Company Service Providers

An Update on the 2021 Priorities

Work on verifying the accuracy of data reported in the TUBOR continued throughout the year, in line with expectations set for 2021. Complementing this is the monitoring of business models and the level of risk acceptance through supervisory inspections and other supervisory reviews including but not limited to the ACRs, financial statements and managements letters. The Authority also completed the plan of reclassification of CSPs in 2021 of approximately 185 subject persons.

In line with the cross-sectoral priority in 2021 on 'Corporate Governance and Culture', the Authority continued with its assessment of governance structures of TCSPs as one of the supervisory areas of focus through the previously mentioned inspections and reviews. This was done also through interviews with the proposed MLROs and compliance officers, as well as – in some cases – with the proposed persons to hold directorship positions in TCSPs, to better assess their competency.

Furthermore, 2021 saw the implementation of the reform to the CSP framework which is currently being undertaken. The Authority processed 276 applications that were received through the new CSP regime transitory period. MFSA is conducting the necessary checks in line with the provisions and timeframes set out by the Company Service Providers Act as amended. By 16 November 2021, CSP applicants whose business is limited within specific parameters set out in the CSP Rulebook (Under Thresholds) were granted full authorisation subject to the satisfactory outcome of the necessary pre-authorisation checks, while those exceeding such thresholds (Over Thresholds) and Class C CSPs will be provisionally authorised and proceed to the next phase of processing – which will continue throughout 2022.

A revamp of the rules for trustees and other fiduciaries was also being undertaken by the MFSA as per plan for 2021, but this will feature as a continued workstream in 2022 due to other priorities this year.

Priorities for 2022

Given the continued focus on the availability of accurate beneficial ownership information at an international level, and also in the light of EU-wide efforts for the implementation of the interconnection of beneficial ownership registers across the EU, the MFSA will continue with its work to verify the accuracy of reported beneficial information of trusts as reported on the TUBOR. In view of the interconnection of

registers project, the MFSA will engage in significant contribution to this initiative to ensure compliance with international obligations. Moreover, the MFSA will also be focusing on ensuring that TCSPs in general have adequate systems and controls in place to obtain and maintain accurate beneficial ownership information of all corporate structures serviced by TCSPs, including coordination and alignment with other relevant competent authorities in respect of supervisory approach strategy and engagement with this sector.

In view of the overhaul of the CSP legislative and regulatory framework which came into force in 2021, focus will also be placed on the CSP population which was previously exempt from licensing (similarly subject to coordination with other relevant competent authorities) while also verifying the implementation of newly introduced requirements such as professional indemnity insurance and the risk management function.

Conclusion

This document provides an update on the MFSA's supervisory priority areas that had been identified for 2021 and an overview of the cross-sectoral themes, horizontal priorities and sectoral priorities set for 2022. The document also provides an overview of the 2022 focus areas being prioritised in the European landscape.

In this document, the MFSA further explains its approach to supervisory engagement and its regulatory and supervisory toolkit. While the document aims to provide visibility on the key areas of supervisory focus for the upcoming calendar year, the priorities outlined in this document should be construed as forming part of a wider array of activities that the Authority will be performing during 2022.

Regulated entities are expected to discuss the contents of this document within their board of directors, or equivalent administrative body, and to examine the implications on their business activities.

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