MFSA MALTA FINANCIAL SERVICES AUTHORITY

Guidance Note on the Methodology to Set Administrative Penalties Imposed on Credit Institutions

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DEFINITIONS

Term	Definition
Authority or MFSA	The Malta Financial Services Authority as established by Chapter 330 of the Laws of Malta, the Malta Financial Services Authority Act.
Credit Institution	An undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulations

Section 1 Introduction

The Malta Financial Services Authority (hereinafter referred to as "MFSA" or "the Authority") is publishing a Guidance Note that outlines the methodology for calculating administrative penalties used to sanction Credit Institutions for breaches of regulatory requirements. The publication of this Guidance Note is a further step forward towards enhancing the transparency of the MFSA's regulatory policies, supervisory expectations, and administrative practices. Furthermore, this Guidance Note is intended to provide a clear and consistent framework through which the Authority may ensure that appropriate enforcement measures are applied to Credit Institutions in a proportionate, consistent, and effective manner.

Credit Institutions authorised and supervised by the MFSA should comply with all the relevant regulatory requirements and standards. To foster such compliance, the Authority has a range of enforcement powers emanating from the MFSA Act[1] (Cap. 330 of the Laws of Malta), the Banking Act (Cap. 371 of the Laws of Malta) as complemented by the respective subsidiary legislation, the MFSA Rules[2] in respect of the Banking sector, as well as applicable European Union legislation, especially the CRD/CRR framework.

In terms of Article 35A of the Banking Act, the MFSA may impose an administrative penalty on any person who fails to comply with any condition imposed or where the Authority is satisfied that a person's conduct amounts to a breach of the regulatory requirements applicable to Credit Institutions. While the MFSA is conferred a degree of discretion through the relevant laws in determining the amount of the administrative penalty appropriate in each case, the administrative penalties must be effective, proportionate and dissuasive and must not exceed the limits specified in the respective legislation.

Section 2 Applicability

This Guidance Note provides information on the process followed by the MFSA when setting the appropriate level of an administrative penalty in respect of breaches arising from the actions of Credit Institutions. For the avoidance of doubt, the administrative penalty

[1] https://legislation.mt/eli/cap/330/eng/pdf
[2] https://www.mfsa.mt/our-work/credit-institutions/

methodology described in this Guidance Note shall also apply, where relevant, to breaches arising from the carrying out of unauthorised banking activities by legal persons.

It is important to highlight that the administrative penalty methodology explained in this Guidance Note does not apply to cases relating to submissions of regulatory reporting to the MFSA. In this respect, the Authority issued another Guidance Note in December 2022 (available through this link) which provides information on the process followed by the MFSA when setting the appropriate level of an administrative penalty to be imposed on licence holders following breaches relating to submissions of regulatory reporting to the MFSA.

Similarly, the contents of this Guidance Note shall not apply to natural persons found to have conducted banking activities without the requisite licence or authorisation issued by the MFSA. In such cases, the administrative penalty methodology set out in the guidance document entitled "Guidance Note on the Methodology to Set Administrative Penalties Imposed on Entities and Individuals", published on 7 May 2024, shall apply.

Finally, the contents of this Guidance Note do not apply to prudential breaches attributable to Significant Institutions ("SIs") falling under the direct supervisory remit of the European Central Bank ("ECB") within the framework of the Single Supervisory Mechanism ("SSM"). In such cases, the assessment, investigation, and determination of administrative penalties relating to prudential supervisory matters are conducted directly by the ECB in accordance with the applicable European Union legislative and regulatory framework. Nevertheless, breaches of a conduct-related nature arising from the actions of SIs, insofar as these fall within the supervisory competence of the MFSA, remain subject to the administrative penalty methodology outlined in this Guidance Note. Accordingly, the Authority shall continue to assess and determine administrative penalties for such conduct-related infringements in line with the principles, criteria, and processes described herein.

For the avoidance of doubt, the administrative penalty methodology described in this Guidance Note shall also apply to breaches consisting of the carrying out of unauthorised activities by legal persons.

Section 3 Purpose

The administrative penalty methodology outlined in this Guidance Note seeks to ensure that administrative penalties imposed by the MFSA remain proportionate, effective and dissuasive within the local regulatory context.

The methodology is not intended to provide an automatic mechanism for the calculation of the administrative penalties but to provide general guidance on the process followed by the MFSA and the elements considered when calculating administrative penalties. Essentially, this process should not be regarded as exhaustive, as it serves as a guiding principle for the Authority to ensure that the administrative penalty is proportionate, effective and dissuasive. In the event that the Authority considers that the administrative penalty is not dissuasive enough, the Authority may, at its discretion, amend the quantum of the said administrative penalty.

Section 4 Calculation Method

With the aim of ensuring that the amount of an administrative penalty is fair and proportionate, the methodology applied by the MFSA (in determining the amount of an administrative penalty) considers the impact of the breach and the degree of misconduct of the potential breach, as well as the size and financial strength of the Credit Institution, whilst taking into account any aggravating and mitigating factors.

These elements are incorporated in a 3-step process, which is explained below:

Step 1** – **Assessing the Severity of the Breach

The determination of the base amount of the administrative penalty is based on the severity of the breach.

For this purpose, breaches are classified in accordance with a 'severity grid' encompassing five categories of severity, namely; **Minor** (S1), **Moderately Severe** (S2), **Severe** (S3), **Very Severe** (S4) and **Extremely Severe** (S5), on the basis of two main drivers:

(i) the impact of the breach; and

(ii) the degree of misconduct on the part of the Credit Institution.

The impact of a breach is assessed by considering a range of relevant factors and the resulting consequences, including:

- the impact of the breach on the situation of the Credit Institution;
- the duration of the breach;
- profits gained or losses avoided with the breach;
- the extent of any damage caused to third parties;
- the impact of the breach on the effective supervision; and
- the impact of the breach on the reputation and confidence in the banking sector.

Following this assessment, an overall impact rating of **Low**, **Medium**, or **High** is assigned.

A corresponding assessment is carried out to determine the degree of misconduct. This evaluation primarily considers whether the breach was intentionally or negligently, as well as any other relevant circumstances affecting the Credit Institution's level of responsibility. Based on this analysis, a misconduct rating of **Low**, **Medium**, or **High** is likewise assigned.

Using the severity grid below, the overall severity of the breach is determined based on the assessed impact and degree of misconduct.

Severity Grid		Level of Impact			
		Low	Medium	High	+ other significant circumstances
Degree of Misconduct	Low	S1. Minor	S1. Minor	S1. Minor	
	Medium	S1. Minor	S2. Moderately Severe	S3. Severe	
	High	S2. Moderately Severe	S3. Severe	S4. Very Severe	S5. Extremely Severe

Step 2 – Calculation of the Base Amount

Once the severity of the breach has been established, the base amount of the administrative penalty is determined in accordance with the applicable severity category.

For breaches classified as **Minor (S1) to Very Severe (S4)**, the base amount is calculated using one of the following approaches, depending on whether the Authority is able to quantify the profits gained or losses avoided as a result of the breach:

Approach 1: Predefined fixed base amount calibrated primarily by reference to the size of the Credit Institution

As a first step, Credit Institutions are categorised into five clusters based on the total assets as reported in their latest audited annual financial statements, thereby reflecting their size and scale. The classification ranges from the largest credit institutions (Cluster 1: above €15 billion in total assets) to the smallest credit institution (Cluster 5: €2 billion or below).

Cluster	1	2	3	4	5
Ranges of Total Assets	Over €15 billion	Over €10 billion but less than or equal to €15 billion	Over €5 billion but less than or equal to €10 billion	Over €2 billion but less than or equal to €5 billion	€2 billion or under

Once the relevant cluster is identified, the MFSA applies the administrative penalty grid below, which assigns predefined base amounts corresponding to each severity category and cluster. This administrative penalty grid shows the predefined fixed base amount of the administrative penalty that corresponds to the average Credit Institution in each cluster per category of severity:

Amounts (€)		Breach Severity			
		Minor	Moderately Severe	Severe	Very Severe
Degree of Misconduct	1	€62,500	€500,000	€2,500,000	€12,500,000
	2	€37,500	€250,000	€1,250,000	€6,250,000
	3	€25,000	€125,000	€625,000	€3,125,000
	4	€12,500	€62,500	€312,500	€1,562,500
	5	€6,250	€31,250	€156,250	€781,250

As an example, under the administrative penalty methodology as described in this Guidance Note, the application of the administrative penalty grid would result in a sanction of €156,250 for a Severe (S3) breach by a Cluster 5 Credit Institution. However, this amount is calibrated on the basis of the 'average' Credit Institution within Cluster 5, which, according to the Credit Institution clustering table, corresponds to a Credit Institution with €1 billion in total assets (the average amount in cluster 5).

It follows that the uniform application of this administrative penalty across all Credit Institution within the same cluster would not achieve a proportionate outcome. In particular, credit institutions with lower total assets than the cluster average would be subject to a disproportionate sanction, if the €156,250 figure were applied without adjustment. Conversely, Credit Institutions whose assets are above the average of Cluster 5, would not be adequately penalised if confined to the same baseline amount. Accordingly, the €156,250 figure should be understood not as a fixed or final administrative penalty, but rather as a reference starting point within the calculation methodology, from which further adjustments are necessary to ensure that the resulting sanction is proportionate to the size of the Credit Institution.

To address this limitation, an additional adjustment step is applied to ensure that the base amount reflects better the actual size of the sanctioned Credit Institution. This adjustment preserves the table above as a reference framework while refining the administrative penalty through a size-sensitive approach.

Approach 2: Calculation on the Basis of Profits Gained / Losses Avoided

Where the profits gained or losses avoided as a result of the breach can be determined, the base amount of the administrative penalty shall be calculated by applying a predefined percentage, determined according to the severity of the breach, to the amount of the profits gained or losses avoided.

This method shall be used only where such profits or losses can be reliably quantified and the resulting administrative penalty is proportionate, otherwise the methodology described in the section above will apply.

In any event, the base amount of the administrative penalty shall be no less than the total profits gained or losses avoided.

For breaches classified as **Extremely Severe (S5)**, the base amount is determined as a percentage of the total annual turnover of the supervised entity, reflecting the heightened seriousness and potential systemic impact of such infringements. In such cases, the base amount of the administrative penalty is determined by applying predefined percentages on the total annual turnover ('TAT') of the sanctioned Credit Institution.

The calculation starts from a minimum threshold, which shall be no less than:

- the profits gained or losses avoided as a result of the breach, where these can be reliably quantified; or
- the administrative penalty that would otherwise be applicable under the methodology for Very Severe (S4) breaches

The applicable minimum threshold may then be increased by applying a percentage of the Credit Institution's TAT. The applicable percentage shall be determined by reference to all relevant circumstances indicating that the breach is Extremely Severe, including, amongst other factors, the nature, scale, duration and impact of the breach, as well as whether the breach resulted in, or had the potential to result in, systemic consequences.

In assessing the appropriate percentage to be applied, the Authority shall consider the following:

- whether the breach involved a significant duration or was persistent in nature;
- whether the breach resulted in significant turnover, financial gain or other advantages for the supervised entity or enabled it to avoid significant losses or disadvantages;
- whether the breach caused significant losses or other detriment to third parties;
- the extent to which the breach adversely affected the financial soundness, prudential position or regulatory compliance of the Credit Institution;
- the extent to which the breach undermined confidence in, or the reputation of, the financial sector; and
- whether the breach resulted in, or had the potential to result in, systemic consequences affecting the wider financial system.

Step 3 – **Base Amount Adjustment**

In this final step, the base amount determined in Step 2 is adjusted to: (i) reflect any mitigating or aggravating circumstances, ii) account for multiple breaches arising from the same set of facts, and (iii) ensure that the administrative penalty is proportionate, effective and dissuasive.

The following factors may be taken into account as mitigating or aggravating circumstances:

- **Pro-Active Breach Disclosure:** whether the supervised entity voluntarily disclosed the breach before investigative actions, or admitted it after the initiation of investigative or sanctioning proceedings;
- **Pro-Active Cooperation:** the degree of proactive cooperation with supervisory and investigative teams, or conversely, any obstruction or misleading conduct;
- **Remedial Actions:** measures taken to address the breach, mitigate its impact, and prevent recurrence. Consideration is given to whether these actions were taken on the entity’s own initiative or in response to supervisory requests; and
- **Financial Situation:** the financial situation of the supervised entity, liquidity and capital adequacy.

Step 4 – Capping Limit

In line with the proportionality principle, the final administrative penalty amount shall be subject to a capping limit to ensure that it does not jeopardise the financial viability of the Credit Institution. In particular, the administrative penalty must not result in insolvency or cause serious financial distress, must remain proportionate relative to the Credit Institution's total annual turnover and shall in no circumstances exceed 10% of its total annual net turnover.

Section 5 Conclusion

By way of conclusion, before a decision is communicated to the Credit Institution, the Authority will consider any representations received from the Credit Institution, which representations may justify a reconsideration of the proposed administrative penalty.

In conclusion, the information presented in this document should not be regarded as binding and the process followed by the MFSA in determining the amount of an administrative penalty is essentially a guideline for the Authority to ensure that administrative penalties are proportionate, effective and dissuasive.