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Corporate Partner: Bank of Valletta

Position Paper

Consultation Response to the ESMA/EBA Draft Joint Guidelines on the Assessment of the Suitability of Members of the Management Body and Key Function Holders

To: Malta Financial Services Authority
Date: 25th May 2026
Prepared by: Alexia Farrugia, Council Member,
Institute of Financial Services Practitioners (Malta)

Dear Sir / Madam,

We welcome the opportunity to comment on the draft revised Joint Guidelines.

This response is submitted in the context of the work of the Institute of Financial Services Practitioners (IFSP), Malta's leading professional body representing practitioners across the financial services sector. The IFSP brings together professionals from regulatory, legal, accounting, governance, risk, and compliance disciplines, and plays a central role in promoting high standards of conduct, competence, and governance within the industry.

The IFSP's Directors' Chapter comprises individuals who serve as directors, independent non-executive directors, and key function holders across a wide range of licensed entities.

Members of the IFSP and its Directors' Chapter contribute directly to the governance and oversight of regulated entities, including through roles performed both in their personal capacity and within professional governance, risk and compliance (GRC) firms.

This submission reflects the practical experience and insights of practitioners who collectively support the governance frameworks of financial services entities in Malta and across the EU.



General Position

This response focuses on the treatment of key function holders (KFHs) and the need for the Guidelines to explicitly recognise the operational realities and governance benefits of professional governance, risk and compliance (GRC) firms that provide outsourced or co-sourced key functions.

Across multiple Member States, GRC firms have become an integral part of the supervisory ecosystem. They provide regulated entities, particularly small, medium-sized, and newly authorised firms, with access to high-calibre expertise, robust governance structures, and continuity of service that would otherwise be difficult to achieve.

The Guidelines should therefore explicitly acknowledge that key functions may be performed by individuals operating within professional GRC firms, supported by teams, methodologies, and internal quality-assurance frameworks.

Our comments below address the consultation questions most relevant to this issue.

General Position: Recognition of Professional GRC Firms as Key Function Providers

We strongly support the Guidelines' emphasis on robust governance, independence of mind, and the suitability of key function holders. However, the draft text implicitly assumes that KFHs operate as employees of the regulated entity, whereas in practice a significant proportion of KFH roles, particularly Compliance, Risk Management, MLRO, Internal Audit and CFO roles, are performed by professionals within specialised GRC firms.

This model is not only well-established but also enhances the very objectives the Guidelines seek to achieve.

We therefore propose that the Guidelines explicitly recognise that Key function holders may operate within professional GRC firms, supported by structured teams, documented methodologies, and internal governance frameworks that enhance their capacity, independence, and effectiveness.

This recognition is essential for proportionality, supervisory convergence, and the practical implementation of the Guidelines across the EU.

The following are several reasons why we believe that GRC firms should be explicitly recognised:

1. Enhanced Capacity and Expertise Through Team-Based Support

GRC firms operate with multi-disciplinary teams, lawyers, risk specialists, AML/CFT experts, accountants, data specialists, who collectively support the designated KFH. This model provides:

- greater depth and breadth of expertise than a single in-house individual could offer
- peer review and quality assurance



- scalability to meet increased regulatory expectations
- access to specialised knowledge, including ESG, ICT/AI risk, and cross-border regulatory developments

This is fully aligned with the Guidelines' requirements for adequate knowledge, skills, and experience (Title III, Section 6).

2. Continuity of Service and Reduced Key-Person Risk

GRC firms ensure uninterrupted performance of key functions through:

- internal succession planning
- cross-trained staff
- documented procedures and methodologies
- the ability to immediately allocate additional resources during crises

This directly supports the Guidelines' objectives on ongoing suitability, time commitment, and robust governance arrangements.

3. Independence of Mind and Reduced Conflicts of Interest

A KFH engaged through a GRC firm is not financially dependent on the regulated entity, reducing risks of undue influence.

This strengthens:

- independence of mind (Title III, Section 9.2)
- the ability to challenge management
- the objectivity of reporting to the supervisory function

4. Better Regulatory Engagement and Higher Standards of Compliance

GRC firms typically work with multiple regulated entities and maintain:

- up-to-date knowledge of supervisory expectations
- strong working relationships with competent authorities
- early awareness of regulatory developments

This leads to more consistent, higher-quality compliance outcomes across the market.

5. Proportionality for Start-Ups and Smaller Entities

For smaller or newly authorised entities, hiring full-time senior KFHS is often impractical. GRC firms provide:

- cost-effective access to senior expertise
- flexibility in scaling resources
- a pathway to build internal capacity over time

This is fully consistent with the proportionality principle (Title I).



Responses to Specific Sections of the Guidelines

Preliminary Note on Question Numbering in Section 5.2

The numbering of questions in Section 5.2 of the consultation paper does not fully align with the titles and substantive sections in the main text. To ensure clarity and precision, this submission responds by reference to the relevant title or section heading rather than relying solely on the numbering in Section 5.2.

Subject matter, scope, definitions

With regards to subject matter, scope and definitions, we recommend clarifying that:

- Key function holders may be outsourced or provided through professional GRC firms, provided that the individual designated as KFH meets the suitability criteria and the firm maintains adequate governance, resources, and oversight mechanisms.
- The definition of “key function holder” should explicitly include individuals operating within external professional service firms.

This clarification would align the Guidelines with market practice and the outsourcing frameworks under CRD, MiFID II, and EBA Guidelines on Outsourcing Arrangements.

Title II – Scope of Suitability Assessments

We support the enhanced clarity on suitability assessments. However, we propose adding that when a KFH operates within a GRC firm, the assessment should consider both the individual’s suitability and the firm’s organisational capacity, including its internal governance, quality assurance, and resource allocation.

This ensures proportionality and recognises the team-based delivery model. Suitability assessments should consider both the individual’s competence and the organisational capacity of the GRC firm supporting the role.

This reflects established market practice and aligns with the proportionality principle.

Title III – Notions of Suitability

This title deals with time commitment, number of directorships, adequate knowledge, skills and experience, collective suitability, reputation, honesty and integrity and independence of mind and independent members. Specifically, question 3 poses the following question:

Question 3: Independent non-executive directors:

The Joint GL set out provisions on independent non-executive members of the MB. The Joint GL apply in a proportionate manner and distinguish between different types of



entities (GSII, OSII and other institutions) and specify that for institutions other than significant ones only one independent director as a minimum is required. Furthermore, the Joint GL provide criteria for the assessment of “being independent”. In light of the above, the EBA and ESMA would appreciate further input on the impact of the independence criteria.

Do you have any views on the provisions regarding these independence criteria? Please share any experiences related to the effectiveness, clarity, or implementation of these independence criteria across different business models/types of institutions.

We welcome the emphasis on independence of mind and the safeguards intended to ensure objective oversight. However, we believe the Guidelines should more fully reflect the diverse ways in which independence is achieved in practice, both through:

1. Professional GRC firms, and
2. Individuals acting in their personal capacity as independent non-executive directors (INEDs).

Independent Individuals Acting in Their Own Capacity

While GRC firms provide structural independence, individual INEDs remain a cornerstone of effective governance. Many such individuals bring decades of sectoral experience, cross-industry knowledge, professional judgement developed through varied roles, independence rooted in personal reputation and ethical standards.

It is therefore important that the Guidelines do not inadvertently discourage or economically disincentivise individuals from taking up INED roles.

Economic and Professional Development Considerations

Excessively restrictive expectations, such as rigid limits on the number of roles, prescriptive minimum hours, overly granular expectations of involvement may have unintended consequences.

Individuals may be discouraged from investing in their own development, including in emerging areas such as ICT, AI, cyber risk, ESG, or digital operational resilience.

The pool of qualified INEDs may shrink, particularly in smaller Member States or specialised sectors.

The cost of governance may rise disproportionately, affecting smaller or start-up entities most acutely.

A balanced approach is therefore essential.



The Fine Line Between Effective Supervision and Micro-Management

The Guidelines should explicitly recognise that Independence of mind does not equate to continuous operational involvement.

If expectations on time commitment or documentation become too onerous, there is a real risk that INEDs drift into micro-management, undermining the distinction between supervisory and executive functions. Boards become operationally entangled, contrary to good governance principles.

This risk is particularly acute in areas such as ICT and AI, where the Guidelines rightly expect board-level understanding, but where supervisory oversight must remain strategic rather than operational.

Risk of Boards Becoming Compliance-Driven at the Expense of Strategy

If regulatory expectations, explicit or perceived, require excessively detailed minutes, exhaustive documentation of every challenge raised, continuous demonstration of “visible” independence, boards may become compliance-oriented rather than strategy-oriented, overly focused on documenting challenge rather than exercising judgement, and potentially less effective in guiding long-term business development.

This is not aligned with the purpose of the management body under CRD/MiFID II, which includes setting strategy, ensuring sustainability, and overseeing risk, not merely satisfying procedural expectations.

Risk of Performative Behaviour by INEDs

If the regulatory environment implicitly rewards “visible challenge”, INEDs may feel compelled to be unnecessarily vocal, raise points for the sake of documentation, or adopt adversarial positions to demonstrate independence.

This can distort board dynamics and undermine constructive, trust-based governance.

Recommendation

We recommend that the Guidelines explicitly acknowledge that:

- Independence of mind is demonstrated through judgement, objectivity, and freedom from undue influence, not through volume of interventions or hours spent.
- Both GRC-firm-based KFMs and individual INEDs contribute meaningfully to independence, albeit through different mechanisms.



- Proportionality must apply not only to entities but also to individuals, to avoid discouraging participation in governance roles.

As an industry organisation, IFSP has had the opportunity to discuss its member's experiences related to the effectiveness, clarity, or implementation of these independence criteria across different business models/types of institutions in Malta. The points outlined above highlight these experiences from a high level, but ensuring proportionality remains a key consideration. It is important that the right balance is achieved between strategic direction and supervision both at an entity level and at the level of the competent authorities, so as to ensure that creativity and business growth is not stifled due to disproportionate or ineffective control mechanisms.

Title IV – Human and Financial Resources for Training

GRC firms typically maintain structured training programmes for their staff, including KFHs. Such firm-level training programmes should be recognised as satisfying the requirement for ongoing training and induction.

Title V – Diversity

GRC firms contribute positively to diversity by developing broad talent pipelines and mentoring junior professionals who may later transition into in-house roles. This strengthens the overall governance ecosystem and should be recognised as a positive contribution.

Title VI – Suitability Policy and Governance Arrangements

Where key functions are outsourced, the entity's suitability policy should explicitly reference the governance and quality-assurance frameworks of the GRC firm and the firm's internal controls, escalation processes, and resource allocation mechanisms

Competent authorities should accept documentation provided by GRC firms as part of suitability assessments.

Title VII – Assessment of Suitability by Entities

Entities should be permitted to rely on internal suitability assessments conducted by GRC firms, and firm-level documentation supporting the competence and capacity of the KFH.

This approach supports proportionality and reduces duplication.

Title VIII – Assessment by Competent Authorities

Competent authorities should consider:

- the track record and organisational capacity of the GRC firm



- the firm’s governance, quality assurance, and resource model
- the structural independence provided by the GRC-firm model

This ensures a consistent and proportionate supervisory approach.

Conclusion

We support the objectives of the revised Joint Guidelines. To ensure proportionality, supervisory convergence, and practical implementation across the EU, the Guidelines should explicitly recognise the role of professional GRC firms and the continued importance of independent individuals acting in their personal capacity.

This model enhances independence, strengthens governance, improves continuity, increases access to expertise, supports smaller and newly authorised entities, and aligns with supervisory expectations and market practice.

We believe that incorporating these considerations will materially improve the effectiveness and clarity of the Guidelines

A handwritten signature in blue ink, appearing to read 'Wayne Pisani', with a horizontal line underneath.

Wayne Pisani

Chair of the IFSP Regulated Business Sub-Committee