MALTA FINANCIAL SERVICES AUTHORITY

Annual Report and Financial Statements
31 December 2016

Board of Governors' report

The Governors present their report and the audited financial statements for the year ended 31 December 2016.

Principal activities

The Malta Financial Services Authority (MFSA) ('the Authority') is the single regulator for financial services in Malta, which incorporates credit institutions, financial and electronic money institutions, securities and investment services companies, regulated markets, insurance companies, pension schemes and trustees. The MFSA also manages the Registry of Companies, acts as the Resolution Authority and has been appointed as the Listing Authority.

The Authority is a fully autonomous public institution and reports to Parliament on an annual basis.

Review of the business

The Governors hereby report a surplus of €8,098,676 for the financial year 2016 (2015: €9,721,878). Income generated from applications fees, supervision fees and the Registry of Companies increased by 1% (2015: 6%) this year. The increasing level of regulatory activity and participation in European meetings across all areas of supervision, saw an increasing cost base for the operations of the Authority. Throughout 2016, the MFSA continued to play a core role in disseminating information to consumers, media and the industry, supporting industry education and training programmes, conducting seminars and meetings on legal, technical and regulatory developments, contributing to the framing of national and EU-wide technical policy development and exchanging views and experiences with other national regulatory and supervisory bodies.

Events after the reporting period

On 13 April 2017, by virtue of Act No. XVI of 2017, Article 45, it has been established that the Authority's Reserve Fund shall not at any time exceed the equivalent of the operational expenses registered in the preceding financial year as disclosed in the audited financial statements. The board of governors are in the process of quantifying the amount of past reserves to be distributed in 2017.

Results and surplus funds

The statement of comprehensive income is set out on page 7. The surplus funds for the financial year payable to Government, in terms of the Mata Financial Services Authority Act,1988 amount to €8,000,000 (2015: €7,000,000).

Governors

The Governors of the Authority who held office during the year were:

Prof Joe V Bannister B.Sc, M.Sc, D.Phil (Oxon) - Chairman
Dr Joseph Brincat B.A. (Lond), B.Sc (Econ) Lond, LL.D
Mr Frans Camilleri DSS (Oxon), Graduate Diploma (UEA), MA (UEA)
Dr John Consiglio Ph.D., M.Phil(Eur Studs)., MBA(Wales)., DipFS., Dip Law & Adm., Dip Bus. Law & Actcy., FCIB.
Dr Lauren Ellul B.Accty (Hons), Executive M.B.A. (Edinburgh & ENPC), Ph.D (Birm), F.I.A., C.P.A.
Mr Herbert Zammit Laferla AIFS
Dr Mario Vella B.A., M.Sc. (LSE), Dr. Sc. Oec (Berlin Humboldt) - appointed on 1 July 2016
Prof Josef Bonnici B.A.(Hons.) Econ, M.A., Ph.D. - resigned on 1 July 2016

Board of Governors' report - continued

Statement of Governors' responsibilities

In preparing the financial statements the Governors are responsible for;

- ensuring that the financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU and the Malta Financial Services Authority Act, 1988;
- selecting and applying appropriate accounting policies;
- making accounting estimates that are reasonable in the circumstances;
- ensuring that the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Authority will continue in operation as a going concern.

The Governors are also responsible for designing, implementing and maintaining internal control as the Governors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and that comply with the Malta Financial Services Act, 1988. They are also responsible for safeguarding the assets of the Authority and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The financial statements of the Authority for the year ended 31 December 2016 are included in the Annual Report 2016, which is published in hard-copy printed form and may be made available on the Authority's website. The Governors are responsible for the maintenance and integrity of the Annual Report on the website in view of their responsibility for the controls over, and the security of, the website. Access to information published on the Authority's website is available in other countries and jurisdictions, where legislation governing the preparation and dissemination of financial statements may differ from requirements or practice in Malta.

Auditors

PricewaterhouseCoopers have indicated their willingness to continue in office and a resolution for their re-appointment will be proposed.

On behalf of the board

Prof. Joe V. Bannister, B.Sc, M.Sc, D.Phil (Oxon)
Chairman

Joseph Demanuele F.C.C.A., F.I.A., C.P.A
Chief Operations Officer

Registered office
Malta Financial Services Authority
Notabile Road
Attard BKR 3000
Malta

24 April 2017

Independent auditor's report

To the Stakeholders of the Malta Financial Services Authority

Report on the audit of the financial statements

Our opinion

In our opinion:

- The Malta Financial Services Authority's financial statements give a true and fair view of the authority's financial position as at 31 December 2016, and of the authority's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU; and
- The financial statements have been prepared in accordance with the requirements of the Malta Financial Services Authority Act, 1988.

What we have audited

The Malta Financial Services Authority's financial statements, set out on pages 6 to 29, comprise:

- the statement of financial position as at 31 December 2016;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the authority in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act (Cap. 281) that are relevant to our audit of the financial statements in Malta. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

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Independent auditor's report - *continued*

To the Stakeholders of the Malta Financial Services Authority

Other information

The board members are responsible for the other information. The other information comprises the board of governors' report, which we obtained prior to the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the board members for the financial statements

The board members are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Malta Financial Services Authority Act, and for such internal control as the board members determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the board members are responsible for assessing the authority's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the board members either intend to liquidate the authority or to cease operations, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

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Independent auditor's report - *continued*

To the Stakeholders of the Malta Financial Services Authority

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the authority's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board members.
- Conclude on the appropriateness of the board members' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the authority's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the authority to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We have nothing to report to you in respect of these responsibilities.

PricewaterhouseCoopers
78, Mill Street
Qormi
Malta

Romina Soler
Partner

24 April 2017

Statement of financial position

	Notes	2016 €	2015 €
		As at 31 December	
ASSETS			
Non-current assets			
Property, plant and equipment	4	**13,022,960**	13,041,608
Held-to-maturity financial assets	5	**2,173,265**	2,175,195
Investment in subsidiary	6	**106,570**	133,476
Total non-current assets		**15,302,795**	15,350,279
Current assets			
Held-to-maturity financial assets	5	**-**	349,913
Trade and other receivables	7	**1,300,521**	1,034,061
Loans and receivables	8	**10,650,000**	10,675,000
Cash and cash equivalents	9	**1,661,287**	949,777
Total current assets		**13,611,808**	13,008,751
Total assets		**28,914,603**	28,359,030
EQUITY AND LIABILITIES			
Capital and reserves			
Capital fund	11	**1,164,687**	1,164,687
Asset funding reserve	12	**11,403,568**	11,403,568
Revaluation reserve	13	**2,868,924**	2,868,924
Employee pension fund reserve	14	**850,002**	775,002
Development reserve	15	**8,579,795**	8,556,119
Reserve fund		**1,164,687**	1,164,687
Total equity		**26,031,663**	25,932,987
Current liabilities			
Trade and other payables	10	**2,882,940**	2,426,043
Total liabilities		**2,882,940**	2,426,043
Total equity and liabilities		**28,914,603**	28,359,030

The notes on pages 11 to 29 are an integral part of these financial statements.

The financial statements on pages 6 to 29 were authorised for issue by the Board of Governors on 24 April 2017 and were signed on its behalf by:

JV Bannister

Prof. Joe V. Bannister B.Sc., M.Sc., D.Phil (Oxon)
Chairman

Joseph Demanuele F.C.C.A., F.I.A., C.P.A
Chief Operations Officer

Statement of comprehensive income

	Notes	Year ended 31 December 2016 €	2015 €
Income	19	**23,037,682**	22,846,824
Operating expenses	16	**(15,183,490)**	(13,405,182)
Operating surplus for the year		**7,854,192**	9,441,642
Impairment of investment in subsidiary	6	**(26,906)**	(14,903)
Finance income	18	**252,938**	265,663
Other income	20	**18,452**	29,476
Surplus for the year – total comprehensive income		**8,098,676**	9,721,878

The notes on pages 11 to 29 are an integral part of these financial statements.

Statement of changes in equity

	Notes	Capital fund €	Asset funding reserve €	Revaluation reserve €	Employee pension fund reserve €	Development reserve €	Reserve fund €	Total €
Balance at 1 January 2015		1,164,687	11,403,568	2,868,924	700,002	5,909,241	1,164,687	23,211,109
Comprehensive income								
Appropriation from income statement		-	-	-	-	-	9,721,878	9,721,878
Transfer to pension fund reserve	14	-	-	-	75,000	-	(75,000)	-
Transfer to development reserve	15	-	-	-	-	2,646,878	(2,646,878)	-
Total comprehensive income for the year		-	-	-	75,000	2,646,878	7,000,000	9,721,878
Transactions with stakeholders								
Surplus payable to Government in terms of Article 26 of Malta Financial Services Authority Act, 1988		-	-	-	-	-	(7,000,000)	(7,000,000)
Total transactions with stakeholders		-	-	-	-	-	(7,000,000)	(7,000,000)
As at 31 December 2015		**1,164,687**	**11,403,568**	**2,868,924**	**775,002**	**8,556,119**	**1,164,687**	**25,932,987**

Statement of changes in equity - continued

	Notes	Capital fund €	Asset funding reserve €	Revaluation reserve €	Employee pension fund reserve €	Development reserve €	Reserve fund €	Total €
Balance at 1 January 2016		**1,164,687**	**11,403,568**	**2,868,924**	**775,002**	**8,556,119**	**1,164,687**	**25,932,987**
Comprehensive income								
Appropriation from income statement		-	-	-	-	-	8,098,676	8,098,676
Transfer to pension fund reserve	14	-	-	-	75,000	-	(75,000)	-
Transfer to development reserve	15	-	-	-	-	23,676	(23,676)	-
Total comprehensive income for the year		-	-	-	75,000	23,676	8,000,000	8,098,676
Transactions with stakeholders								
Surplus payable to Government in terms of Article 26 of Malta Financial Services Authority Act, 1988		-	-	-	-	-	(8,000,000)	(8,000,000)
Total transactions with stakeholders		-	-	-	-	-	(8,000,000)	(8,000,000)
As at 31 December 2016		**1,164,687**	**11,403,568**	**2,868,924**	**850,002**	**8,579,795**	**1,164,687**	**26,031,663**

The notes on pages 11 to 29 are an integral part of these financial statements.

Statement of cash flows

	Notes	Year ended 31 December 2016 €	2015 €
Cash flows from operating activities			
Cash generated from operations	22	**8,477,507**	10,041,606
Interest received	18	**252,938**	265,663
Other income	20	**18,452**	29,476
Net cash generated from operating activities		**8,748,897**	10,336,745
Cash flows from investing activities			
Purchase of property, plant and equipment	4	**(412,070)**	(425,208)
Proceeds from disposal of property, plant and equipment		**276**	-
Redemption of long-term investments	5	**349,407**	-
Net movement in loans and receivables		**25,000**	(3,725,000)
Net cash used in investing activities		**(37,387)**	(4,150,208)
Cash flows from financing activities			
Payments to Government in terms of Article 26 of Malta Financial Services Authority Act, 1988		**(8,000,000)**	(7,000,000)
Net cash used in financing activities		**(8,000,000)**	(7,000,000)
Net movement in cash and cash equivalents		**711,510**	(813,463)
Cash and cash equivalents at beginning of year		**949,777**	1,763,240
Cash and cash equivalents at end of year	9	**1,661,287**	949,777

The notes on pages 11 to 29 are an integral part of these financial statements.

Notes to the financial statements

1. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

1.1 Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and the requirements of the Malta Financial Service Authority Act, 1988. They have been prepared under the historical cost convention as modified by the fair valuation of the land and buildings class of property. The preparation of financial statements in conformity with IFRSs as adopted by the EU requires the use of certain accounting estimates. It also requires the Governors to exercise judgement in the process of applying the Authority's accounting policies (see Note 3 – Critical accounting estimates and judgements).

New standards and interpretations not yet adopted

A number of new standards, amendments and interpretations are effective for annual periods beginning after 1 January 2016 and have not been applied in preparing these financial statements. None of these is expected to have a significant effect on the financial statements of the Authority, except the following set out below:

IFRS 9, 'Financial Instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. IFRS 9 was issued in November 2009 and October 2010. It replaces the parts of IAS 39 that relate to the classification and measurement of financial instruments. IFRS 9 requires financial assets to be classified into two measurement categories: those measured as at fair value and those measured at amortised cost. The determination is made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument. For financial liabilities, the standard retains most of the IAS 39 requirements. The main change is that, in cases where the fair value option is taken for financial liabilities, the part of a fair value change due to an entity's own credit risk is recorded in other comprehensive income rather than the income statement, unless this creates an accounting mismatch. The Authority is yet to assess IFRS 9's full impact. The Authority will also consider the impact of the remaining phases of IFRS 9 when completed by the Board. IFRS 9 is effective from 1 January 2018 subject to endorsement by the EU.

1. Summary of significant accounting policies - continued

1.2 Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in Euro, which is the Authority's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

All foreign exchange gains or losses are presented in the income statement.

1.3 Property, plant and equipment

All property, plant and equipment is initially recorded at historical cost. Land and buildings, comprising mainly the Authority's offices, are shown at fair value based on periodic valuation, less subsequent depreciation of buildings. Valuations are carried out on a regular basis such that the carrying amount of property does not differ materially from that which would be determined using fair values at the end of the reporting period. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset, and the net amount is restated to the revalued amount of the asset. All other property, plant and equipment is stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Authority and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of land and buildings are credited to other comprehensive income and shown as a revaluation reserve in equity. Decreases that offset previous increases of the same asset are charged in other comprehensive income and debited against the revaluation reserve directly in equity; all other decreases are charged to profit or loss.

Items of property plant and equipment comprise land and buildings, furniture, fixtures and fittings and equipment and are initially recognised at acquisition cost. Subsequently they are carried at acquisition cost less subsequent depreciation and impairment losses.

1. **Summary of significant accounting policies** - continued

1.3 Property, plant and equipment - continued

Land is not depreciated as it is deemed to have an indefinite life. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amount to their residual values over their estimated useful lives, as follows:

	%
Furniture, fixtures and fittings	20
Equipment	20

Buildings are depreciated over an estimated useful life of 100 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with carrying amount and are recognised in the income statement. When re-valued assets are sold, the amounts included in the revaluation reserve relating to the assets are transferred to retained earnings.

1.4 Investment in subsidiary

The investment in subsidiary is accounted for by the cost method of accounting, i.e. at cost less impairment. Cost also includes directly attributable costs of the investment. Provisions are recorded where, in the opinion of the Governors, there is an impairment in value. Where there has been an impairment in the value of an investment, it is recognised as an expense in the period in which the diminution is identified.

The results of subsidiaries are reflected in the Authority's separate financial statements only to the extent of dividends receivable. On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is recognised in the income statement as income or an expense.

1.5 Financial assets

1.5.1 Classification

The Authority classifies its financial assets, other than investment in subsidiary, in the following categories: loans and receivables and held-to-maturity. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

(a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Authority provides money, goods or services directly to a debtor with no intention of trading the asset. They are included in current assets, except for maturities greater than twelve months after the end of the reporting period. These are classified as non-current assets. The Authority's loans and receivables comprise trade and other receivables, term deposits and cash and cash equivalents in the statement of financial position.

1. **Summary of significant accounting policies** - continued

1.5 Financial assets - continued

1.5.1 Classification - continued

(b) Held-to-maturity financial assets

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Authority's management has the positive intention and ability to hold to maturity. If the Authority were to sell other than an insignificant amount of held-to-maturity financial assets, the whole category would be tainted and reclassified as available-for-sale. Held-to-maturity financial assets are included in non-current assets, except for those with maturities less than twelve months from the end of the reporting period, which are classified as current assets.

1.5.2 Recognition and measurement

The Authority recognises a financial asset in its statement of financial position when it becomes a party to the contractual provisions of the instrument. Financial assets are initially recognised at fair value plus transaction costs. Loans and receivables and held-to-maturity financial assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is the initial measurement amount adjusted for the amortisation of any difference between the initial and maturity amounts using the effective interest method.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Authority has transferred substantially all risks and rewards of ownership or has not retained control of the asset.

1.5.3 Impairment

The Authority assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. The Authority first assesses whether objective evidence of impairment exists. The criteria that the Authority uses to determine that there is objective evidence of an impairment loss include:

- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- it becomes probable that the borrower will enter bankruptcy or other financial reorganisation.

1. Summary of significant accounting policies – continued

1.6 Trade and other receivables

Trade receivables comprise amounts due from customers for services performed in the ordinary course of operations. If collection is expected in one year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in the income statement. When a receivable is uncollectible, it is written off against the allowance account for trade and other receivables. Subsequent recoveries of amounts previously written off are credited against profit or loss.

1.7 Cash and cash equivalents

Cash and cash equivalents are carried in the statement of financial position at face value. In the statement of cash flows, cash and cash equivalents include cash in hand, deposits held at call together with short-term, highly liquid investments that are readily convertible into known amounts of cash, and which are subject to an insignificant risk of changes in value.

1.8 Trade and other payables

Trade payables comprise obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

1.9 Provisions

Provisions for legal claims are recognised when the Authority has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

1. Summary of significant accounting policies - continued

1.10 Revenue recognition

The Authority recognises revenue when the amount of revenue can be reliably measured, when it is probable that future economic benefits will flow to the entity, and when specific criteria for each of the Authority's activities have been met, as described below:

(i) Income from registration fees is recognised on the date of registration.
(ii) Income from annual fees is recognised by reference to the stage of completion of the transaction, which equates to a systematic recognition of revenue as it accrues over time.
(iii) Income derived from the Registry of Companies is recognised when payment is received which, in view of the profile of companies including dormant and defunct companies, is determined by the Authority to be the point in time when there is a probability that the economic benefits associated with the revenue will flow to the entity.
(iv) Interest income from investments is reported on an accrual basis using the effective interest method.

1.11 Operating leases

Leases of assets in which a significant portion of the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

1.12 Government grants

Grants from the Government, including national Government and EU, are recognised at their fair value where there is a reasonable assurance that the grant will be received and the company will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the income statement over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to property, plant and equipment are included in non-current liabilities as deferred government grants and are credited to profit or loss on a straight-line basis over the expected lives of the related assets.

2. Financial risk management

2.1 Financial risk factors

The Authority's activities potentially expose it to a variety of financial risks namely market risk, credit risk and liquidity risk. The Authority's risk management is coordinated by the Board of Governors and focuses on actively securing the Authority's short to medium term cash flows by minimising the exposure to financial markets. Long-term financial investments are managed to generate lasting returns.

The Authority does not actively engage in trading of financial assets for speculative purposes nor does it write options. The most significant financial risks that the Authority is exposed to are described below.

2. Financial risk management - continued

2.1 Financial risk factors - continued

(a) Market risk

In view that the investments in Malta Government bonds (see Note 5) are accounted for at amortised cost, the Governors do not consider that the Authority is exposed to significant market risk.

(b) Credit risk

The Authority's exposure to credit risk is limited to the carrying amount of financial assets recognised at the reporting date, as summarised below. The Authority's exposures to credit risk as at the end of the reporting periods are analysed as follows:

	Notes	**2016**	2015
		€	€
Held-to-maturity investments	5	**2,173,265**	2,525,108
Trade and other receivables	7	**954,193**	740,611
Loans and receivables	8	**10,650,000**	10,675,000
Cash and cash equivalents	9	**1,661,287**	949,777
		15,438,745	14,890,496

The Authority assesses the credit quality of its customers taking into account financial position, past experience and other factors. It has policies in place to ensure that sales of services are affected to customers with an appropriate credit history. The Authority monitors the performance of its receivables on a regular basis to identify incurred collection losses, which are inherent in the Authority's receivables, taking into account historical experience.

The Authority's receivables, which are not impaired financial assets, are principally in respect of transactions with customers for whom there is no recent history of default. Management does not expect any losses from non-performance by these customers. None of the Authority's financial assets are secured by collateral.

As at 31 December 2016, trade receivables of €22,833 (2015: €22,833) were impaired, and the amount of the provisions in this respect are equivalent to these amounts. Reversal of provisions for impairment arises in those situations where customers recover from unfavourable circumstances and accordingly start meeting repayment obligations. The Authority does not hold any collateral as security in respect of the impaired assets.

Credit risk in relation to cash and cash equivalents and held-to-maturity investments is considered to be limited, since the counterparts and issuer are reputable banks, and the Government of Malta respectively.

(c) Liquidity risk

The Authority is exposed to liquidity risk in relation to meeting future obligations associated with its financial liabilities, which comprise trade and other payables (Note 10). Prudent liquidity risk management includes maintaining sufficient cash and committed credit lines to ensure the availability of an adequate amount of funding to meet the Authority's obligations.

2. Financial risk management - continued

2.1 Financial risk factors - continued

(c) Liquidity risk - continued

The Authority monitors liquidity risk by reviewing expected cash flows, and ensures that no additional financing facilities are expected to be required over the coming year. The Authority's liquidity risk is not deemed material in view of the matching of cash inflows and outflows arising from expected maturities of financial instruments.

2.2 Capital risk management

The Authority's equity, as disclosed in the statement of financial position, constitutes its capital. The Authority's objectives when managing capital are to safeguard the respective entity's ability to continue as a going concern in order to provide returns and benefits for stakeholders, and to maintain an optimal capital structure to reduce the cost of capital. The Authority's equity is maintained in line with the provisions set within the Malta Financial Services Authority Act, 1988.

In view of the nature of the Authority's activities and its financial position, the capital level as at the end of the reporting period is deemed adequate by the Governors.

2.3 Fair values of financial instruments

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as Level 1 in view of the Quoted prices (unadjusted) in active markets for identical assets or liabilities.

The following table presents the authority's assets and liabilities that are measured at fair value at the respective dates:

	Level 1
	€
31 December 2016	
Held-to-maturity financial assets	2,880,789
31 December 2015	
Held-to-maturity financial assets	3,180,916

At 31 December 2016 and 2015 the carrying amounts of cash at bank, receivables, payables and accrued expenses reflected in the financial statements are reasonable estimates of fair value in view of the nature of these instruments or the relatively short period of time between the origination of the instruments and their expected realisation.

3. Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

In the opinion of the Governors, the accounting estimates and judgements made in the course of preparing these financial statements are not difficult, subjective or complex to a degree which would warrant their description as critical in terms of the requirements of IAS 1.

4. Property, plant and equipment

	Land and buildings €	Furniture, fixtures and fittings €	Equipment €	Total €
At 31 December 2014				
Cost or valuation	12,370,286	2,059,827	3,908,471	18.338.584
Accumulated depreciation	(159,124)	(1,793,852)	(3,381,281)	(5,334,257)
Net book amount	12,211,162	265,975	527,190	13,004,327
Year ended 31 December 2015				
Opening net book amount	12,211,162	265,975	527,190	13,004,327
Additions	33,600	44,695	346,913	425,208
Disposals	-	(8,245)	(1,554)	(9,799)
Depreciation charge	(80,000)	(50,175)	(257,752)	(387,927)
Depreciation released on disposal	-	8,245	1,554	9,799
Closing net book amount	12,164,762	260,495	616,351	13,041,608
At 31 December 2015				
Cost or valuation	12,403,886	2,096,277	4,253,830	18,753,993
Accumulated depreciation	(239,124)	(1,835,782)	(3,637,479)	(5,712,385)
Net book amount	**12,164,762**	**260,495**	**616,351**	**13,041,608**
Year ended 31 December 2016				
Opening net book amount	12,164,762	260,495	616,351	13,041,608
Additions	12,372	46,900	352,798	412,070
Disposals	-	-	(26,683)	(26,683)
Depreciation charge	(80,161)	(55,106)	(295,175)	(430,442)
Depreciation released on disposal	-	-	26,407	26,407
Closing net book amount	12,096,973	252,289	673,698	13,022,960
At 31 December 2016				
Cost or valuation	12,416,258	2,143,177	4,579,945	19,139,380
Accumulated depreciation	(319,285)	(1,890,888)	(3,906,247)	(6,116,420)
Net book amount	**12,096,973**	**252,289**	**673,698**	**13,022,960**

4. **Property, plant and equipment** - continued

Fair value of land and buildings

The Authority's office building was revalued on 31 December 2012 by independent professionally qualified valuers. The valuation was conducted by DeMicoli & Associates (a firm of architects). The book value of the property was adjusted to the revaluation and the resultant surplus, was credited to the revaluation reserve (refer to Note 13). The Board of Governors has reviewed the carrying amount of the property as at 31 December 2016 and no adjustments to the carrying amount were deemed necessary as at that date taking cognisance of developments that occurred during the current financial year.

The Authority is required to analyse non-financial assets carried at fair value by level of the fair value hierarchy within which the recurring fair value measurements are categorised in their entirety (Level 1, 2 or 3). The different levels of the fair value hierarchy have been defined as fair value measurements using:

- Quoted prices (unadjusted) in active markets for identical assets (Level 1);
- Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2);
- Inputs for the asset that are not based on observable market data (that is, unobservable inputs) (Level 3).

The recurring property fair value measurement at 31 December 2016 uses significant unobservable inputs and is accordingly categorised within Level 3 of the fair valuation hierarchy.

The Authority's policy is to recognise transfers into and out of fair value hierarchy levels as of the beginning of the reporting period. There were no transfers between different levels of the fair value hierarchy during the year ended 31 December 2016.

A reconciliation from the opening balance to the closing balance of non-financial assets for recurring fair value measurements categorised within Level 3 of the value hierarchy, is reflected in the table above.

Valuation processes

The valuation of the property is performed regularly on the basis of valuation reports prepared by independent and qualified valuers. At the end of every reporting period, the COO (Chief Operations Officer) assesses whether any significant changes in the major inputs have been experienced since the last external valuation. The COO reports to the Board of Governors on the outcome of this assessment.

When an external valuation report is prepared, the information provided by the valuers – and the assumptions and the valuation models used by the valuers – are reviewed by the COO. This includes a review of fair value movements over the period. When the COO considers that the valuation report is appropriate, the valuation report is recommended to the Board of Governors. The Board of Governors considers the valuation report as part of its overall responsibilities.

4. Property, plant and equipment - continued

Valuation techniques

The Level 3 fair valuation of the Authority's land and buildings was determined by using a comparative approach whereby the current selling prices and rental values of similar developments were compared in order to obtain an equitable rental value of the property. The significant unobservable inputs in the valuation include:

Equivalent rental values	based on the actual location, type and quality of property supported by current market rents for similar properties.
Capitalisation rates	based on actual location, size and quality of the property and taking into account market data at the valuation date.

Information about fair value measurements using significant unobservable inputs (level 3)

			Significant unobservable inputs	
Description	**Fair value at 31 December 2016 and 2015** €	**Valuation technique**	**Equivalent rental value** €	**Capitalisation Rate** %
Office building	12.3m	Capitalisation of equivalent rental yield	0.77m	6.25

The higher the rental yield and the lower the capitalisation rate, the higher the fair value. Conversely, the lower the rental value and the higher the capitalisation rate, the lower the fair value.

Historical cost of land and buildings

If the land and buildings were stated on the historical cost basis, the amounts would be as follows:

	2016 €	2015 €
Cost	**10,291,818**	10,279,446
Accumulated depreciation	**(319,285)**	(239,124)
Net book amount	**9,972,533**	10,040,322

5. Financial assets

Financial assets include the following investments:

	2016 €	2015 €
Non-current		
Held-to-maturity investments	**2,173,265**	2,175,195
Current		
Held-to-maturity investments	**-**	349,913
As at 31 December	**2,173,265**	2,525,108

The movements during the year in held-to-maturity investments, which comprise Malta Government Bonds, were as follows;

	2016 €	2015 €
Opening net book amount	**2,525,108**	2,527,593
Amortisation	**(2,436)**	(2,485)
Redemptions	**(349,407)**	-
Closing net book amount	**2,173,265**	2,525,108

6. Investment in subsidiary

	2016	2015
	€	€
Cost and carrying amount	**133,476**	148,379
Impairment charge	**(26,906)**	(14,903)
Carrying amount	**106,570**	133,476

The subsidiary at 31 December 2016 and 2015 is shown below:

Subsidiary undertaking	**Registered office**	**Class of shares held**	**Percentage of shares held %**
Malta International Training Centre Limited	Malta Financial Services Authority Notabile Road Attard BKR 3000 Malta	Ordinary shares	99.9

The following information available to the Authority relates to Malta International Training Centre Limited ("the subsidiary"):

	Assets	Liabilities	Turnover	Loss before tax
	€	€	€	€
2016	**145,678**	**39,111**	**192,978**	**(19,777)**
2015	181,014	47,541	233,873	(26,705)

The Governors consider that the effect of consolidating the assets, liabilities and results of the subsidiary in the Authority's financial statements is not material.

The Governors have also entered into discussions to sell its investment on a going concern basis.

7. Trade and other receivables

	2016	2015
	€	€
Current		
Trade receivables – gross	**846,626**	617,128
Less: Provision for impairment of trade receivables	**(22,833)**	(22,833)
Trade receivables – net	**823,793**	594,295
Prepayments	**346,328**	293,450
Accrued income	**130,400**	146,316
	1,300,521	1,034,061

8. Loans and receivables

	2016	2015
	€	€
Deposits with banks or credit institutions	**10,650,000**	10,675,000

The above deposits earn interest at a fixed rate.

9. Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following:

	2016	2015
	€	€
Cash and cash equivalents	**1,661,287**	949,777

10. Trade and other payables

	2016	2015
	€	€
Current		
Trade payables	**867,029**	443,616
Indirect taxation	**233,962**	199,593
Accruals	**734,737**	756,107
Deferred income	**1,047,212**	1,026,727
	2,882,940	2,426,043

11. Capital fund

The capital fund of €1,164,687 represents the initial contribution by the Government to the Authority in 1994 upon its establishment.

12. Asset funding reserve

	€
Balance as at 31 December 2016 and 2015	11,403,568

The asset funding reserve had been created to provide for the purchase of property, plant and equipment.

13. Revaluation reserve

	2016	2015
	€	€
Balance as at 1 January and 31 December	**2,868,924**	2,868,924

The revaluation reserve is not distributable.

14. Employee pension fund

	2016	2015
	€	€
Balance as at 1 January	**775,002**	700,002
Transfer for the year	**75,000**	75,000
As at 31 December	**850,002**	775,002

The employee pension fund reserve has been created to set aside reserves to prepare for the potential employee pension fund that may be set up for the benefit of the employees at the opportune time.

15. Development reserve

	2016	2015
	€	€
Balance as at 1 January	**8,556,119**	5,909,241
Transfer for the year	**23,676**	2,646,878
As at 31 December	**8,579,795**	8,556,119

The development reserve had been created to set aside reserves intended to finance long term projects to improve, upgrade and expand the Authority's facilities and services. During 2016, a transfer of €23,676 (2015: €2,646,878) was registered into the reserve.

16. Expenses by nature

	2016 €	2015 €
Depreciation of property, plant and equipment (Note 4)	**430,442**	387,927
Employee benefit expense (Note 17)	**9,444,581**	8,386,914
Professional fees	**1,612,257**	785,243
Implementation of ECB – Single Supervisory Mechanism	**1,534**	430,159
Promotional expenses	**664,410**	735,741
Governors' emoluments*	**167,121**	167,030
Other administrative expenses	**2,863,145**	2,512,168
Total operating expenses	**15,183,490**	13,405,182

Auditor's fees

Fees charged by the auditor for the statutory audit amount to €5,975 (2015: €5,975).

In addition to the above, during 2016 one of the Governors acted as Consultant to the Board and received additional remuneration amounting to €12,000.

17. Employee benefit expense

	2016 €	2015 €
Wages and salaries	**8,491,352**	7,498,061
Social security costs	**542,777**	472,967
Other staff costs	**410,452**	415,886
	9,444,581	8,386,914

Average number of persons employed by the Authority during the year:

	2016	2015
Managerial	**206**	181
Administration	**60**	57
	266	238

18. Finance income

	2016 €	2015 €
Interest income from demand deposits	**130,752**	142,021
Interest income from Government bonds	**122,186**	123,642
	252,938	265,663

19. Income

Income represents fees from services rendered during the year as follows:

	2016 €	2015 €
Authorisations	**509,925**	761,400
Securities and markets supervision	**2,341,399**	2,204,956
Insurance and pensions supervision	**2,018,625**	1,902,688
Conduct	**510,582**	413,804
Banking supervision	**4,190,229**	4,173,085
Listing authority income	**496,250**	386,350
Registry of companies	**12,970,672**	13,004,541
Total income	**23,037,682**	22,846,824

20. Other income

	2016 €	2015 €
EU grants designated for specific purposes	**18,452**	29,476

EU funds designated for specific purposes amounting to €44,333 at 31 December 2016 (2015: €62,785) are amortised to profit or loss over the term of the service concession.

21. Tax expense

Section 30 of the Malta Financial Services Authority Act, Cap 330 exempts the Authority from any liability to pay income taxes.

22. Cash generated from operations

Reconciliation of operating surplus generated from operations:

	2016 €	2015 €
Operating surplus for the year	**7,854,192**	9,441,642
Adjustments for:		
Depreciation of property, plant and equipment (Note 4)	**430,442**	387,927
Amortisation of investment (Note 5)	**2,436**	2,485
Changes in working capital:		
Trade and other receivables	**(266,460)**	(72,184)
Trade and other payables	**456,897**	281,736
Cash generated from operations	**8,477,507**	10,041,606

23. Commitments

	2016 €	2015 €
Capital expenditure		
Capital expenditure that has been authorised by the Board of Governors but has not yet been contracted for	**1,497,218**	2,300,000
Operating leases		
Less than one year	**95,545**	25,924
Between 2 and 5 years	**327,907**	-
Other		
Sponsorship approved by the Board of Governors	**-**	500,000
	1,920,670	2,825,924

The MFSA total sponsorship for the renovation of the State Rooms at San Anton Palace is capped at €1million. Such a commitment has been accounted for in the 2016 and 2015 financial statements.

24. Related party transactions

Except for transactions disclosed or referred to previously, the following significant transactions, which were carried out principally with related entities, have a material effect on the operating results and financial position of the Authority:

	2016	2015
	€	€
Surplus payable to Government	**8,000,000**	7,000,000

Key management personnel compensation, consisting of Governors' remuneration is disclosed in Note 16.

25. Events after the reporting period

On 13 April 2017, by virtue of Act No. XVI of 2017, Article 45, it has been established that the Authority's Reserve Fund shall not at any time exceed the equivalent of the operational expenses registered in the preceding financial year as disclosed in the audited financial statements. The board of governors are in the process of quantifying the amount of past reserves to be distributed in 2017.

26. Statutory information

The Malta Financial Services Authority (MFSA) ('the Authority') is the single regulator for financial services in Malta enacted by virtue of the Malta Financial Services Act, 1988 and reports to the Maltese Parliament.