11th February 2025

Conduct Supervision
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By e-mail

Dear Chief Executive Officer
Dear Compliance Officer

Re: Digitalisation Thematic Review

You are receiving this letter as a Chief Executive Officer and Compliance Officer of a Credit Institution supervised by the Malta Financial Services Authority (referred to herein as the "MFSA" or the "Authority").

Background

The Authority considers that one of the main goals for its Licence Holders is to achieve high compliance standards while acting professionally, honestly and in accordance with the best interest of their clients when manufacturing and distributing their products and services.

The Authority uses various tools such as, onsite inspections, supervisory meetings, thematic reviews, and other off-site work to ensure that its Licence Holders achieve this goal.

Data and digitalisation are rapidly transforming economies and communities, promoting inclusive growth, addressing inequities, and improving public service delivery, thus enabling the achievement of the Sustainable Development Goals (SDGs) which are part of the UN 2030 Agenda for Sustainable Development.[1]

Furthermore, the EU aims to promote a human-centric vision for the digital economy and society worldwide through the implementation of the EU Digital Strategy[2] , the forging of new digital partnerships and by aiming to guarantee that digital economies are equitable and inclusive. This has been reflected in the priorities of both the EBA and ECB during the past years, whereby the concept of Digitalisation in banks has become one of the main areas of focus.

Credit Institutions are responding to new technology developments in their various areas of operations including meeting client demands in the provision of their services in a manner which provides value to clients and ensures positive outcomes. In this context, digitalisation is having an influence on Credit Institutions' front and back-office operations, as they provide new digital services while automating internal procedures.

[1] Transforming our world: the 2030 Agenda for Sustainable Development | Department of Economic and Social Affairs
[2] EU Digital Strategy - EU4Digital

Recognising the dynamic nature of digitalisation and its critical impact on the financial sector, the Authority has through its Conduct Supervision Function conducted a Thematic Review exercise (“the Exercise”) to evaluate how Credit Institutions in Malta are adapting to these changes and to identify the effectiveness of their digital services.

This review aimed to provide insight into the current state of digitalisation, highlight best practices, and offer recommendations to help Credit Institutions ensure that they continue to offer a positive customer journey to their clients, resulting in positive outcomes for the latter.

Methodology

A Thematic Review is an effective supervisory tool utilised by the Authority to focus supervisory efforts on specific areas of concern across a group of regulated entities, analysing common issues, risks, or practices, as opposed to focusing on a single authorised person. The publication of the findings of a Thematic Review renders this supervisory tool even more effective as it promotes transparency through the sharing of findings and insights with the industry and the public, which in turn fosters trust and confidence in regulatory processes.

Thematic Reviews also promote continuous improvement for regulated persons, and equally for regulators, through the assessment of industry practices and regulatory compliance, enabling stakeholders to identify areas for enhancement and implement necessary changes to improve overall outcomes.

The methodology used to assess the level of digitalisation available to customers within the local retail market together with its effectiveness, involved a multi-step approach. For the purpose of this Exercise, the Authority considered a number of locally authorised Credit Institutions which are currently providing services through digital channels, which amounted to a total of five.

The first step was an analysis of the public information available through the Credit Institutions’ websites to gain an understanding of the level of information a customer can obtain about such services. Subsequently, the selected banks were then provided with a comprehensive numerical data request to capture the respective trends across 2022 and 2023. The information requested related to mobile banking and internet banking usage, chatbots, usage of ATMs, branches, usage of cards and availability of other online products. This was complemented by a physical supervisory meeting with each of the Credit Institution on an individual basis. A number of pre-set questions were provided to the Credit Institutions in preparation for the said supervisory meeting.

The following sections in this letter constitute the Authority’s observations and expectations detailed information provided by the banks via the data requested and during the supervisory meetings held, apart from the additional communication exchanged with the institutions when deemed necessary.

General Market Observations

Client Onboarding

The majority of the Credit Institutions which were considered during this exercise do not offer online client onboarding as yet, but they reported that this is in the pipeline and the majority of these Credit Institutions plan to have it in place by 2025.

The reasons behind such timelines were either due to priorities related to other projects or due to other underlying systems/tools which still need to be successfully developed such as online KYC and online ID Verification upon which full online onboarding will then be dependent. Currently, such Credit Institutions offer only online application forms which could be downloaded by the clients from their respective websites to be filled in by the clients themselves, in their own time, after which a physical appointment will be set at the Institution's premises to conclude the process.

The only two Institutions which offer a fully automated online onboarding pointed out that this is more popular amongst the younger generation and is still picking up with the older people. For verification purposes, these Credit Institutions also make use of biometric features, through the submission of 'selfies' by the applicants to compare them to the actual photo on the Identification Document provided by the applicant.

Some banks recognised that there could be issues when it comes to the onboarding of foreigners mainly due to language barriers and the provision of accurate documentation.

Regarding the monitoring of online onboarding abandonment, whenever such monitoring is in place, it is mainly focused on applicants who managed to complete most of the application but abandoned the process in the last stages of the onboarding process. Any applications which were unintentionally initiated (where the "apply now" button seems to have been pressed by mistake but no further details are inputted by the applicant) appear to be disregarded by the Credit Institution's systems when gathering data on onboarding abandonment.

Products Offered Through Digital Means

All deposit products of each Credit Institution in scope of the exercise could be offered digitally as long as the customer had previously been successfully onboarded. Mainly these are offered through internet banking and the mobile applications except for one bank which reported some products also being available online through a virtual branch.

Making particular reference to home loans, the Institutions in scope stated that such lending products can only be concluded physically due to the nature of the local Civil Law which obliges all parties (buyers and sellers) to be physically present for the final contract together with the appointed Notary, to sign the final deed.

One particular credit institution is offering credit cards where the relative credit agreement is signed through an electronic signature. This entity is also considering the conclusion of credit agreements for personal loans through a digital signature, for the future. The Authority noted that Credit Institutions which have a bigger market share in the local market, offer a larger variety of products/services which can be offered digitally. For example, one particular bank mentioned that it is now offering soft EPOS (Mobile EPOS) contracts to merchants and also batch SEPA/Non-SEPA payment contracts, both through the use of digital signatures.

On the other hand, Credit Institutions which are gaining momentum have a substantial appetite to be innovative and attract the younger generation through the digital products offered in order to start developing a long-term banking relationship with such a market segment.

It was also observed that locally, products which are offered only through online channels are very limited and only mentioned by two Credit Institutions (one product each). The rest of the products are accessible to the public either by applying for them in person, by visiting the credit institution's premises or else through the online channels offered by the respective credit institutions, although final purchase of these products would still require face-to-face interaction.

Accessibility of Digital Channels

Access to the various digital channels was one of the focus areas of this Thematic Review as the Authority sought to gain a better understanding of the digital channels that Credit Institutions are offering to their clients once they are onboarded and to assess the level of effectiveness of the available digital channels.

The data reported indicates that overall, branch footfall has decreased between 2022 and 2023 for both cash services and for outward payments, whilst the usage of digital services has increased. All Credit Institutions forming part of the Thematic Review highlighted that such a phenomenon was particularly driven by the COVID-19 pandemic. In fact, from the statistics collected, it was noted that on average, for the Credit Institutions in scope of this exercise, the percentage of clients enrolled in mobile banking/internet banking all exceeded 60%. Nearly all Credit Institutions reported an increase in enrolment by clients for digital channels between 2022 and 2023.

The following are the main digital channels that are provided by the Credit Institutions which were in scope for this Thematic Review:

i) Internet banking

Each Credit Institution in scope of this exercise, offers internet banking to its clients. Through internet banking, an individual is offered a vast range of services without the need to visit a branch. Such services typically include transferring of funds, making payments to third parties, bill payments, viewing account balances and transactions, ordering cheque books, requesting new PINs, ordering statements, and communicating with the bank through a secure messaging system to request information or file a complaint, amongst various other services. Over both years observed, there has been an increase of over 10% in inter-account transfers, outward payments and client instructions submitted through internet banking across the Institutions in scope.

ii) Mobile banking

Mobile banking has become more accessible for clients and is also offered by all the reviewed Credit Institutions. It was noted that some Institutions offer a replication of the internet banking services through the mobile banking application and are considered as being the same system/tool. On the other hand, some Credit Institutions offer the mobile banking service by means of a different system i.e. having different features where clients can access different services through the mobile banking application from those available via internet banking. This means that not all services which can be executed through internet banking can be executed through mobile banking.

It was noted that some Banks offered limited services through mobile banking, such as not being able to change or order a new card PIN, or not having the possibility of ordering a cheque book from the mobile banking application. Another Credit Institution reported that outward payments cannot be executed through the mobile application without prior engagement via internet banking. This is so because initially, the client has to log into the internet banking, save the beneficiary's details, and only from then onwards any outward payments can be affected through the mobile application. This means that certain services which can be conducted through the mobile application are not fully independent from the internet banking, since some actions need to be processed through internet banking before being able to do such transactions through mobile banking.

From the data collected, the use of mobile banking by clients is on the rise. In fact, the percentage increase of transactions and requests submitted through mobile banking has increased by a larger percentage compared to the increase observed for internet banking usage. It is evident that clients are opting to use their mobile applications more often than their internet banking to access their accounts and process transfers between accounts.

Additionally, these observations are a good indication that customers are opting to use more digital services rather than visiting the branch for simple banking services.

It was noted however, that whenever clients execute a card transaction, these are not immediately reflected in the client's account statement. In fact, such transactions on both the internet banking and mobile banking platforms normally appear as blocked funds until the merchant claims the funds. For some Institutions, the way such transactions are being reflected on the statement is also dependent on the type of card used to affect the payment. The Authority expects that account statements and summary of recent transactions acquired by the client through internet banking, mobile banking or ATMs, are to reflect card transactions accurately and instantly. While it is understood that "blocked funds" represent pending transactions, Credit Institutions should provide clear explanations and consistent formatting in the account statement to avoid confusion. Clients should also be able to receive real-time mobile notifications or updates on transactions, clearly stating whether the transaction is pending, blocked, or completed, regardless of the type of card being used.

iii) ATMs

All Credit Institutions in scope of the exercise except for one, offer their clients access to ATMs. Some institutions offer a wide range of ATMs all over the Maltese Islands while others have a smaller range. One particular Credit Institution has opted to set up an agreement with a third-party provider and provides free ATM cash withdrawals to its customers through the third-party ATMs.

On the other hand, some Credit Institutions allow their clients to have access to a larger number of ATMs belonging to other Credit Institutions, whilst waiving certain fees up to a certain limit/usage per month. During this Thematic Review, the documentation related to the Tariff of Charges of the respective banks was analysed to ensure that it captures the relative fees in a clear and concise way. The Authority has noted that most institutions are increasing their ATM network and are upgrading their ATMs both in terms of hardware and software.

Some new ATM features are expected to be introduced in the near future and will include identity card scanning. This feature will allow clients to provide an updated Identification Card through the ATM, without the need to visit the branch to update their particulars. Another added feature will be an increase in the volume of notes which can be deposited at one go through the ATM and the possibility of contactless deposits/withdrawals, which will also help in reducing hardware issues related to the card reader.

One particular Credit Institution explained that some of its ATMs, particularly those in busy areas, will be accepting up to 500 notes at one go instead of 100 notes, to accommodate corporate clients. During Covid-19, there was a significant increase in the use of ATMs and this uptake has continued ever since. However, at this point, a plateau appears to have been reached.

The number of withdrawals effected through ATMs and the respective monetary value of these transactions have more or less remained at the same level. It was noted that overall, there was a slight dip of around 1.08% in the number of ATM cash withdrawals versus a 2.2% increase in the monetary value of the cash withdrawals executed through the ATMs. This indicates that cash is still very prominently used for day-to-day purchases.

Upon further analysis, there was a considerable overall decrease in the number of transactions (cash/cheque deposits, withdrawals and outward payments) executed over the counter at the Credit Institutions' branches, while a substantial increase was registered in transactions executed through internet banking and mobile banking.

These observations clearly indicate a trend where over-the-counter transactions are being shifted to digital channels. In fact, it was noted that many clients are opting to pay by means of a debit card, inter-account transfers or SEPA payments while the usage of cheques is decreasing drastically.

One is to consider that Credit Institutions' client-base has increased from 2022 to 2023. Furthermore, the market penetration by foreign Credit Institutions and Financial Institutions offering debit cards to their clients has also aided to retain the popularity of ATM transactions.

Decisions related to ATM locations were also dependent on branch relocation as well as customer needs and demands based on analysis conducted by the banks in question. The Authority expects that Credit Institutions carry out regular snap checks on ATMs to ensure that they are fully operational and that if any particular maintenance is required, this is carried out as quickly as possible and with the least disruption of the service being offered.

iv) Websites

Websites can be used by customers to obtain information about products being offered and download user guides where available, without the need to visit branches. Some Credit Institutions have done enhancements to their websites with the aim of making such websites more attractive and user friendly to customers. The Authority expects all Credit Institutions to continuously review their websites and make the necessary enhancements to ensure that all information available is accurate, clear and not misleading.

Digital identification/verification

For access to internet banking, clients can use credentials and use a password generated through an internet key/dongle or a code generated through SMS. This is generally the case where a mobile application is not utilised, because in such cases the code is generated through the mobile application itself.

In order to access a bank's mobile application there are normally two options: either through the insertion of a PIN and the other is by means of biometrics such as face ID or fingerprint, depending on the type of operating system utilised by the client's mobile phone.

Additionally, all institutions in scope are required to adhere to the two-factor authentication process in terms of the Payment Services Directive II whenever a client decides to execute an outward payment either through a mobile application or through internet banking.

Card Services and Usage

Overall, a vast majority of cards offered by Maltese Credit Institutions are contactless and with this new accessibility, card usage has increased significantly, particularly during the COVID-19 pandemic. Increasing the limit triggering a PIN insertion requirement and decreased merchants' resistance for low value transactions, have led to an increase in card usage. This is in addition to the 3D Security features which make customers feel more secure when effecting online card payments.

Conversely, the Authority has noted that such increase in card usage was coupled with an increase in chargeback requests since customers appear to have been increasingly falling for scams which unfortunately are being very professionally created, making it hard to recognise their fraudulent nature. It was positively noted that few chargeback requests remain pending, and that card usage is normally supported by instant SMS notification. This allows customers to immediately recognise any unauthorised transactions from their end. As mentioned above, Credit Institutions are expected to promptly notify clients of any withdrawals or transactions through electronic means, such as SMS or other digital platforms, to enhance transparency and security on clients' accounts. Additionally, banks should continue educating their clients about potential scams, providing guidance on how to recognize and avoid such scams.

Some Credit Institutions stated that they are considering ways how clients can affect deposits without actually utilising a card. This is mainly for corporate clients that would not be comfortable sharing the company's debit cards with their staff responsible for effecting the company's deposits. One Bank also mentioned the possibility of offering a virtual card and with corresponding physical card being optional. The majority of the Credit Institutions in scope are still working on tokenisation of their cards (attaching them to a digital wallet). Credit Institutions are encouraged to increase their investment in tokenisation of cards due to the significant benefits it offers in terms of enhanced security and customer convenience.

Accessibility for clients/contact points

Customers can generally contact institutions through the following channels:

- Branches
- Call centres
- Chatbot (not applicable for all banks)
- Digital banking (internet banking and mobile banking), including secure messaging
- Self-service machines
- Website
- Facebook messenger
- Phone service

The number of branches has remained the same between 2022 and 2023. One particular Credit Institution explained that its customer outreach through branches is being restructured in terms of the number of offices available, the type of services being offered in each branch and the availability in terms of days and opening times. Such changes were considered following an analysis conducted by the Credit Institution itself which included data relating to branch footfall, clients' expectations and needs.

The level of service being provided through chatbots varies between Credit Institutions. Whilst some opt not to offer it or offer it only to certain types of customers, it was noted that in certain instances a chatbot is supported by live agents if required, in order to enhance the clients' experience. Also, some Credit Institutions do plan to enhance the chatbot service, for example, through enabling the setting up of appointments through the chat or by connecting it to the core system itself. A Credit Institution is also considering offering the chatbot in Maltese.

For those Credit Institutions offering the use of chatbots, it was noted that issues resolved via this medium have increased between 2022 and 2023, indicating that the chatbots have become more user-friendly and effective.

Virtual meetings proved successful during the COVID-19 pandemic, despite various drawbacks; however, credit institutions consider that customers still tend to prefer face-to-face interaction. In fact, most pointed out that although they still offer virtual meetings to their clients, many still prefer the physical meeting especially when discussing Home Loans.

Technology advancements – AI

While certain Credit Institutions have made significant technological advancements over others, just two of the Credit Institutions subject to this Thematic Review currently use Artificial Intelligence (AI) in the following areas: chatbot, payment screening and fraud detection. All Credit Institutions have confirmed that AI is not yet being used for credit scoring, signalling an opportunity for future exploration and development.

The Authority encourages Credit Institutions to further embrace AI, particularly to improve the client experience throughout their banking journey by customising services and products for individual needs and identify new business opportunities. AI technology has the potential to streamline various processes, providing quicker and more efficient service. In addition, AI tools can play a crucial role in detecting fraudulent payments and identifying potential security breaches, safeguarding clients against fraud and cyber threats. This has been emphasised by the European Banking Federation in their position paper on AI in the Banking Industry issued on 1st July 2019.

Several institutions are currently exploring the possibility of incorporating AI into their workflows, indicating an awareness of the technology's potential and a proactive approach to modernization. The Authority believes that wider AI adoption will not only improve operational efficiency but also drive innovation within the banking sector.

Long Term Initiatives

Credit Institutions' future plans in the context of digitalisation of their services depend on their digital strategy and progress. All those Credit Institutions which are not currently offering digital onboarding are planning to offer such a service in the coming years. Apart from this, tokenisation is also part of the banks' plans for the future. Credit Institutions are also looking at ways to enhance the payment services they offer such as through additional mandates with card service providers or to allow SEPA payments to be initiated through the mobile application where this is still not available.

Loan origination and servicing may be eventually linked to the Credit Institutions' digital systems and the digital KYC procedures which will in the future impact the online onboarding and potentially making it a much faster process. The current motivation to upgrade systems is enabling Institutions to improve their digitalised services and also to be able to offer enhanced/additional verification features. Digitalisation of receipts and statements is also picking up, in view of ESG initiatives.

As a good practice, the Authority encourages Credit Institutions to explore the concept of allowing clients to contact the Credit Institutions' call centres directly through their mobile apps. This feature would streamline the verification process, as logging into the app already confirms the caller's identity, eliminating the need for call centre agents to ask multiple verification questions.

Challenges faced by Credit Institutions

Credit Institutions in Malta face numerous challenges in transitioning to a more digital environment, including mainly their client base's demographics and mindset, cyber risks and security requirements, together with the relative regulatory landscape. One should also not neglect the social aspect in Malta with special consideration towards the cultural expectations of many individuals still have the physical presence of a Credit Institution's branch close to where they live and/or work.

Implementing a digital strategy incrementally is crucial due to limited resources. Digitalisation must be sustainable, balancing better customer service, compliance with changing regulations, system evergreening, and cyber risk mitigation. The Authority expects that ongoing enhancements are done to the existing infrastructure to ensure that the system remains efficient, secure and capable of meeting evolving client needs.

A better customer journey is recognised to be achievable through continuous feedback from the customers, focus groups, scoring at branches and monitoring reviews related to digital applications. Credit Institutions stated that overall, they conduct surveys, monitor complaints and eventually share the results within their organisation in order to take the necessary action to improve the clients' journey.

Credit Institutions should keep in mind that clients compare their last experience to the best experience they had. Therefore, they are expected to consistently deliver the highest quality service, whether through digital channels or other means.

MFSA's Expectations

The Authority positively notes the Credit Institutions' digital achievements and commitments during the past years. Credit Institutions have embarked on offering better digital services whilst retaining services at branches, and therefore meeting the demands of all customer cohorts as much as possible. Out of the five institutions observed, only one institution operates almost fully online.

By reviewing factors such as the adoption of digital banking services, investment in technology, customer engagement, speed of implementation and regulatory compliance, it becomes clear that certain Credit Institutions lead the way in embracing digital transformation. These distinguish themselves through innovative approaches, substantial investments, and a strong commitment to enhancing customer experiences and operational efficiencies.

In this context, the Authority expects that the Banks' main focus is to be on the holistic customer journey to digitalised services rather than just on how profitable the products themselves are. Focusing on the customer journey entails providing sufficient information and guidance including a clear and user-friendly channel with information about the Credit Institution's products and services.

While digitalisation is encouraged and supported by the Authority, Credit Institutions are expected to remain mindful of their obligation to provide full, efficient, and accessible services to clients who are not tech-savvy. These clients should not be disadvantaged and must continue to receive the same level of care and support as other customers. In this regard, Credit Institutions are also expected to engage with their customer base to provide appropriate guidance how to use digital services securely. In particular, clients should be constantly assisted with their queries and encouraged to use the digital means, to make the client's journey more convenient. Whilst, education on digital services is essential and plays a crucial role in this development, Credit Institutions are expected to ensure that non tech savvy clients are still guaranteed access to their services in an efficient manner.

Credit Institutions are expected to educate, raise awareness and alert their customers about scams and fraud, providing a plan of action in case someone falls victim to such activities. In this context, in order to encourage the customers to use digital channels, it is strongly recommended that detailed demos including step-by-step explanations are to be uploaded on the Bank's website or through other channels such as YouTube channels and even through screen displays within the branches. This approach has already started being adopted by some of the Institutions observed and is definitely a good practice.

Credit Institutions are expected to seriously consider introducing an automated notification process for clients to be alerted of all debit transaction (irrespective of the amount debited) within their accounts without the need for clients to opt for such a service, where this is not yet available. This will facilitate clients to monitor the account activity instantly and hence reporting immediately to the bank should there be any suspicious activity. Further to the recommendations made by the Arbiter for Financial Services related to the case ASF 050/2024 on 22nd November 2024, the Authority strongly recommends that Credit Institutions offer adequate safeguards relating to the transfers to third parties from payment accounts (such from as savings and current accounts) to limit the detriment to clients resulting from fraudulent transactions effect from clients' payment accounts. Such safeguards could include, for example, offering clients the possibility to establish limits for payments to be effected from their accounts – clients would be able to amend such limits from time to time without incurring additional fees. Furthermore, in this context credit institutions are encouraged to continue educating their clients on the importance of not sharing usernames, passwords and PINs with third parties.

While the Authority notes and supports the efforts of Credit Institutions to explore the integration of AI into their workflows, they are expected to ensure that any AI systems implemented are secure, reliable, and designed to mitigate cybersecurity risks while maintaining the continuity and quality of services provided to clients.

Credit Institutions are encouraged to consider other client verification options such as calls through the mobile application which offer bank staff automatic verification of customers. This results in the process of handling queries becoming more efficient.

Credit Institutions are to ensure that implementation of their digital transformation strategy does not lead in any way to exclude any sections of society from the financial services industry. In addition to this, Banks should be mindful when setting their fee structure, making sure as much as possible that through their fee structure they would not be effectively be forcing the less tech-savvy customers to use digital means in order to avoid higher fees.

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Finally, it was noted that some data requested by the Authority was not successfully completed or marked as 'not available' by certain Licence Holders. In this regard, the Authority expects Credit Institutions to maintain sufficient Record to monitor the development of their digitalised services and the usage thereof by clients.

Way Forward

The Authority will engage with institutions in the future through other supervisory interactions to monitor the progress of Banks' digitalisation and the respective impact on customers. Should you require any clarification on the above, please do not hesitate to contact the Authority's Conduct Supervision Function on conductbanking@mfsa.mt.

Kindly be guided accordingly.

Yours Sincerely
Malta Financial Services Authority

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