

TRANSCENDENT GROUP INSIGHT

ESMA GUIDELINES ON CERTAIN ASPECTS OF THE MIFID II COMPLIANCE FUNCTION REQUIREMENTS

On June 6th the Swedish FSA, similar to other national competent authorities, announced that it has notified ESMA that it will apply ESMA's guidelines on certain aspects of the MiFID II compliance function requirements ("the Guidelines").

The final Guidelines were published by ESMA in June 2020 and the translations to all official EU languages were published on April 6th 2021. The guidelines became applicable two months after of the date of publication of the translations, i.e. June 6th 2021.

The Guidelines are largely the same as the 2012 ESMA Guidelines on certain aspects of the MiFID compliance function requirements which it replaces. However, the Guidelines include updates that enhance clarity and foster greater convergence in the implementation, and supervision, of the MiFID II compliance function requirements.

Background

After the great financial crisis in 2008 it became apparent that the rules on the compliance function in MiFID I was not sufficient. The rules were subsequently strengthened by guidelines from ESMA on certain aspects on the compliance function. These obligations have been further strengthened, broadened and detailed under MiFID II and further clarified by the updated Guidelines.

Scope of the Guidelines

The Guidelines are addressed to investment firms and credit institutions providing investment services and activities, investment firms and credit institutions selling or advising clients in relation to structured deposits, UCITS management companies and external alternative investment fund managers when providing investment services and activities in accordance with the UCITS directive and the AIFMD.

What has changed?

As previously mentioned the Guidelines remains largely unchanged and to some extent the requirements that are now outlined in the Guidelines were already best practice. Below you can find a summary of the main amendments to the Guidelines.

Guideline 1 - on the compliance risk assessment

This guideline is not new, but further enhances the requirement of the compliance function to conduct a risk assessment to ensure that compliance risks are comprehensively monitored. The compliance function shall establish a risk based monitoring programme on the basis of the compliance risk assessment to determine its priorities and the focus of the monitoring, advisory and assistance activities.

Guideline 2 - on the monitoring obligations of the compliance function

The guideline provides a number of examples of suitable tools and methodologies for monitoring activities that could be used by the compliance function.

One of the examples is that the compliance function could interview, when necessary, a relevant sample of firm's clients.

Guideline 3 - on the reporting obligations of the compliance function

This guideline has been amended to clearly outline that the compliance reports are mandatory and a suitable tool to warrant the necessary management attention. The mandatory compliance reports should cover all business units involved in the provision of investment services, activities and ancillary services provided by a firm. Where the report does not cover all of these activities and services of the firm, it should clearly state the reasons for this.

Furthermore, the guideline clarify in more detail what the reports should include.

In addition, it is outlined that - subject to the proportionality principle - firms should favour an organisation where the compliance function and the complaints management function are properly separated.

If the firm is part of a group, the compliance function should also consider the need for additional reporting lines to any group compliance function.

Guideline 4 - on the advisory and assistance obligations of the compliance function

The guideline clarifies that the compliance function should provide support and training not only to staff, but to management as well.

It is stressed that firms should promote and enhance a 'compliance culture' throughout the firm, which should be supported by the senior management. The compliance culture should not only aim at engaging staff with the principle of improving investor protection, but also be contributing to the stability of the financial system.

Furthermore, it is highlighted that the compliance function should be participating in the establishment of new policies and procedures within the firm. The firm's remuneration policy and the firm's product governance policies and procedures are specifically mentioned.

Guideline 5 - on the organisational requirements of the compliance function

It is underlined in the guideline that it is important that the firm puts in place necessary arrangements to ensure an effective exchange of information between the compliance function and other control functions as well as with any external auditors.

In addition, it is also clarified that in ensuring that compliance staff have access to the relevant information for their tasks at all times, firms should provide access to all relevant databases and records such as recordings of telephone conversations and electronic communications referred to in Article 76 of MiFID II Delegated Regulation.

Guideline 6 - on the skills, knowledge, expertise and authority of the compliance function

This guideline is new, although this requirement was previously included in other parts of the guidelines.

In short, a firm's compliance staff shall have the necessary skills, knowledge and expertise to discharge their obligations under MiFID II. Furthermore, the compliance function shall need to have the necessary authority pursuant to MiFID II. These requirements should in particular be

taken into account by firms when appointing a compliance officer. A compliance officer should demonstrate high professional ethical standards and personal integrity.

Guideline 10 - on combining the compliance function with other internal control functions

The guideline follows the existing principle on the separation of functions. The guideline further highlights that a firm should favour an organisation where control functions are properly separated. The combination of the compliance function with other control functions may be acceptable if this does not compromise the effectiveness and independence of the compliance function. Where the compliance function is combined with other control functions or where it is also responsible for other tasks (for example anti-money laundering), the firm should ensure that it allocates enough resources for MiFID II compliance at all times.

Concluding reflections

As outlined above, the changes to the Guidelines are not substantial. Nevertheless, firms should ensure that their existing organisation, policies, processes, controls and monitoring frameworks are in line with the new Guidelines.

If you need help ensuring that your Compliance function is organised and carries out its tasks in compliance with the Guidelines, please reach out to us at Transcendent Group – we would be happy to assist.

Please reach out



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