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*Dear Sir or Madam*

**Consultation on Guidelines on certain aspects of the MiFID compliance function requirements**

Barclays is grateful for the opportunity to comment on ESMA's consultation paper. Barclays welcomes this guidance and is itself committed to striving for high standards of compliance. Subject to the comments below, we welcome and endorse the guidelines, and we welcome the fact that ESMA is seeking to promote both high standards in compliance functions and greater supervisory attention to the role of the compliance function.

This letter sets out a small number of high level points. More detailed points are covered in Annex 1.

As a matter of general application, we note that the draft guidelines generally impose duties on the compliance function. Where they do mention broader responsibilities, such as the adequacy of compliance resources, these responsibilities are given to the firm. While it may be implicit, it may be helpful if the guidelines were to address more explicitly the role of senior management in ensuring (i) that the business is run in a compliant manner, and that the compliance function acts as "a second line of defence", and (ii) that the compliance function is provided with adequate resources etc. It may also be worth making it clear that it is the responsibility of senior management to ensure that the firm is in compliance with MiFID requirements and to allocate responsibilities to the compliance function to other control functions and to Internal Audit as relevant to their business.

**Question 2: Monitoring**

We are sensitive to the fact that MiFID firms are enormously varied, from very simple operations through to the most complex, global organisations doing the most complex, global business. Therefore we think it right that ESMA should frame its guidelines in the form of principles that can be widely applied taking into account the specific nature of the business.

The paper sometimes strays from this model. In particular we would point to paragraph 14 of the supporting guidelines on monitoring. This presupposes that compliance functions are organised on a legal entity basis that then takes account of the other parts of the group. We fully acknowledge the importance of the legal entity. In many banks and investment firms,

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however, compliance is organised on a group or business unit basis, where the business unit may cover a number of separate regulated legal entities. An individual may be appointed as the compliance officer of the firm in question (and may be the compliance officer for a number of firms), but will be supported by compliance staff that are part of a group or business unit function. While banks that adopt this structure must ensure that adequate attention is paid to compliance by individual regulated entities, the group or business unit approach to the organisation is a legitimate organisational approach. It is also emphatically not outsourcing compliance as paragraph 70 of the draft guidelines seems to imply.

We believe that the guidelines should be drafted in a manner that is more neutral in relation to the structure of the firm.

### **Question 3: Reporting Obligations**

We would counsel caution in recommending the routine provision of compliance reports to the competent authorities, as suggested in paragraph 26 of the draft guidelines. The sharing of reports on a case by case basis is entirely appropriate, but routine sharing of all compliance reports may affect how reports are drafted and affect the content of reporting. Regular contact between competent authorities and firms may offer a better way to keep authorities informed and for them to come to an informed view of the effectiveness of a compliance function.


### **Question 4: Advisory Function**

We agree with and endorse the spirit of the recommendations here. We agree that compliance should be involved in and able to contribute regulatory advice to strategic decision-making and to the other significant decisions of the firm as paragraphs 34 and 35 suggest.

There is, however, a line to be drawn here and a tension with the independence obligation that the guidelines do not discuss - either in relation to the advisory role or in relation to the guideline on independence – and which should be more fully elaborated. We agree that compliance should be involved in the key processes of the firm as a trusted advisor, but it must be careful not to compromise its independence by taking business decisions. Standard setters and supervisors for their part also need to be wary of encouraging compliance beyond its advisory mandate to a point where it becomes actively involved in and a party to the business decision itself.

We hope that these observations and those in the Annex are useful and are, of course, ready to discuss them at your convenience.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Richard Quinn', written over a horizontal line.

Richard Quinn

**Q1: Do you agree that investment firms should ensure that, where the compliance function takes a risk-based approach, any comprehensive risk assessment is performed to determine the focus and the scope of the monitoring, reporting and advisory activities of the compliance function?**

- Risk assessment is one input to determining focus and scope

Adopting a risk-based approach for determining the focus and scope of compliance work requires risk identification, measurement and prioritisation. A risk assessment can play a role in risk identification, measurement and prioritisation effort, but should not be the sole determinant of compliance function activities. Senior management in the compliance function will use their governance arrangements to determine the function's scope and focus with the risk assessment output contributing the wider set of information used in such decision making.

- Risk assessment can be targeted at certain compliance functions or risk-based decisions

Typically a risk assessment will identify a relative risk ranking across specified (compliance) risks. The comprehensiveness and use of the risk assessment will be informed by the availability, relevance and reliability of its qualitative and/or quantitative inputs and the intended contribution of the risk assessment to informed decision-making. A risk assessment can be deployed in a targeted fashion to inform activities for some compliance activities, or to address particular compliance risk questions.

**Q2: Please provide your comments (with reasons) on any or all aspects of this guideline on the monitoring obligations of the compliance function.**

Barclays agrees that monitoring is an integral part of the role of the Compliance function, and agrees that Compliance functions in investment firms should establish a monitoring program.

We agree with the paper that the monitoring program should be risk-based (as noted in paragraph 15), as this is the only practical way for resources to be used efficiently and for the Compliance function to evaluate the business. To assist understanding of the risk-based nature of the guideline, however, we would suggest that the text in paragraph 12 is adjusted to note that "a risk based program should assess all relevant areas", rather than requiring a program which "covers all relevant areas".

Finally, it is worth noting that the 'Compliance risk' which the guideline says should be comprehensively monitored is a difficult term to define accurately, and in many cases requires a qualitative assessment. We would like the guidelines to acknowledge (perhaps in paragraph 16) that different approaches to monitoring will be appropriate in different sectors, institutions, and for different products, and that, therefore, different firms' monitoring programs may legitimately differ in approach.

**Q3: Please provide your comments (with reasons) on any or all aspects of this guideline on reporting obligations of the compliance function.**

Barclays agrees strongly that it is important that senior management of investment firms are made aware of compliance and regulatory developments. Further, we agree that where the compliance function makes significant findings, the compliance officer should report these promptly to senior management.

However, we are concerned that the guidelines as written could be read as emphasising form over substance. Escalation of issues from the compliance function to senior management in large firms can take many forms and, therefore, we do not agree with the apparent rigidity implicit in the references to "The written report" (paragraph 21), and the requirement that "reports should be prepared at least annually" (paragraph 20). The language used here seems to suggest that the compliance function should provide one or a few formulaic reports per annum. Rather than moving towards a formulaic annual report, we believe the guidelines should instead emphasise the importance of appropriate escalation on a timely basis to senior management. We would expect firms to be able to demonstrate a range of reports on compliance and regulatory issues, rather than pointing to one 'annual report'.

We believe that the format and timing of compliance reporting needs to be specific to the structure and arrangement of each particular firm. Finally, we think an 'annual report' approach will risk issues being left until too late, and/or a view from management that the annual process is routine in nature.

Our comments are based upon the assumption that senior management is defined as the executive level management of a firm rather than the Board.

Finally, we note your reporting of the fact that some competent authorities require investment firms to provide them with compliance function reports. We do not think that there should be a uniform approach from competent authorities on this matter, as (for reasons described above) we think that investment firms should be free to produce reports in a manner fit for their particular arrangements.

**Q4: Please provide your comments (with reasons) on any or all aspects of this guideline on the advisory obligations of the compliance function.**

It is helpful that the draft guideline reinforces the principles underlying the advisory role of the compliance function in relation to regulatory requirements. It is not clear that a firm or the compliance function itself can

'ensure' that a particular task is performed.

Paragraph 25 rightly highlights the importance of a 'compliance culture'. A strong 'compliance culture' will emphasise that each individual employee is responsible and accountable for complying with regulatory requirements relating to his or her tasks, functions and actions. The compliance function should be empowered and resourced adequately to provide advice to the firm and employees in order to enable each of them to meet the applicable regulatory requirements. Therefore, the draft guideline might be better phrased as: 'Investment firms should ensure that the compliance function is empowered to fulfil its advisory responsibilities including training for staff, day-to-day assistance for staff and participation in the establishment of new policies and procedures within the investment firm.'

Training (Para.26) on regulatory requirements and a firm's relevant policies and procedures generally is one task of the compliance function. Of course, it need not be the compliance function itself which is responsible for preparing, delivering or arranging relevant training; and training provided or arranged by the compliance function will be only part of the education provided to employees of a firm in relation to their regulatory responsibilities.

Paragraph 29 requires assessment of staff awareness and application of policies and procedures. Awareness and application are different elements of a firm's compliance framework. Therefore, the role of the compliance function in relation to each of them may be distinct. A specific requirement for periodic assessment of staff awareness would be unduly prescriptive about how a firm should best ensure that its employees are appropriately trained and competent for their respective roles. In some firms, particularly those with structured formal training programmes utilising on-line delivery methods, effective assessment of relevant knowledge and understanding may be an aspect of the training programme. However, in some other firms, such assessment could be ongoing and informal or unrecorded. Any assessment need not be the responsibility of the compliance function itself – it could be performed by line management or internal audit, for example. However, the compliance function should be consulted about the development and delivery of the relevant elements of the firm's training programme and the methods for assessing relevant knowledge and understanding. Where the compliance function does not perform those functions directly, it should be informed about any individuals who do not complete relevant training or are assessed negatively in any aspect of relevant knowledge or understanding.

Paragraph 30 mentions day-to-day assistance. It should be noted that issues may arise day-to-day which are not solely compliance matters or are unusually complex and difficult. In either case, it may be appropriate to involve line management, other control functions or outside advisers or consultants. While Compliance officers should advise, they should ensure that they do not get drawn into decision making that could compromise their independence.

In relation to Paragraph 33, the compliance function should be informed of all relevant correspondence with competent authorities where the function is not the author or recipient of such correspondence.

Additional possible tasks of the compliance function in performing advisory responsibilities may include: participating in industry fora for discussion of current issues and possible developments; review and approval of trades requiring specific pre-approval; and review and approval of requests for material exceptions from a firm's policies and procedures relating to regulatory responsibilities. Those tasks need not be the sole responsibility of the compliance function – such responsibilities may be shared with line management and/or other control functions.

**Q5: Please provide your comments (with reasons) on any or all aspects of this guideline on the effectiveness of the compliance function.**

We strongly support efforts to ensure a robust and effective compliance function and are in general agreement with the guidelines.

**Q6: Do you agree that, in order to ensure that the compliance function performs its tasks and responsibilities on an ongoing permanent basis, investment firms should provide:**

- (i) adequate stand-in arrangements for the responsibilities of the compliance officer which apply when the compliance officer is absent; and**
- (ii) Arrangements to ensure that the responsibilities of the compliance function are performed on an ongoing basis?**

We agree that the Compliance function should perform its tasks and responsibilities on an ongoing permanent basis. As such, documented Business Continuity arrangements should be in place to ensure continued coverage in the event that they are absent.

In paragraph 42 'compliance officer' and 'compliance staff' are referred to as though they are distinct. Is the intention here to distinguish between the Head of Compliance at an investment firm and his reports or between a person with sole responsibility for compliance at a smaller firm and those who would replace him in his absence?

It is important to be clear in terms of the definitions around roles and responsibilities within the Compliance function

**Q7: Do you agree that investment firms should ensure that the compliance function holds a position in the organisational structure that ensures that the compliance officer and other compliance function staff are independent when performing their tasks?**

The independence of both the Compliance function and Head of Compliance within a large organisation is necessary to effectively manage Compliance risk. Independence 1) minimises the potential for conflicts of interest between Compliance and business objectives 2) enables the Compliance function to carry out its responsibilities effectively 3) enables timely escalation of regulatory failings to senior management.

**Q8: Do you agree that investment firms should ensure that the organisation of the compliance function guarantees that the compliance officer's daily decisions are taken independently from any influence of the business units and that the compliance officer is appointed and replaced by senior management only?**

The Compliance function needs to be structured so as to assist the Compliance Officer in making independent decisions (see reasons in answer to question 7). In making decisions, Compliance is to be mindful of the interests of the firm, its shareholders and its clients and its regulatory responsibilities and not of any particular business area or employee. Senior management should be responsible for ensuring an effective Compliance function operates independently within an organisation. Amongst other things this will include senior management being responsible for the appointment or removal of the Compliance Officer (Head of Compliance).

**Q9: Please provide your comments (with reasons) on any or all aspects of this guideline on Article 6(3) exemptions.**

We agree with the criteria which should be taken into account when deciding which firms may benefit from the exemptions under Article 6(3). A quantitative assessment would be preferable, however this would be difficult to put into effect and in the absence of such, then the list of criteria provided should allow investment firms to decide whether they may benefit from the exemptions.

We agree that where the compliance function is combined with other functions due to the nature, scale, and complexity of the firm's business, then this may be a good indication that the firm would fall under the exemption. However, where the firm makes use of the exemption based on the scenario where, due to nature of business, a separate compliance officer is not warranted, then the firm needs to ensure that any potential conflicts of interest are managed effectively.

We agree that the compliance function should generally not be combined with other functions where this could undermine the compliance function's independence.

**Q10: Please provide your comments (with reasons) on any or all aspects of this guideline on combining the compliance function with other functions.**

We support the guidance associated with combining the compliance function with other functions.

In particular, we agree that compliance activities should not be combined with activities of other functions which generate conflicts of interest or compromise the effectiveness of the Compliance function including its oversight of the business.

**Q11: Please provide your comments (with reasons) on any or all aspects of this guideline on outsourcing of the compliance function.**

We support the clarification sought by the EBF such that the guidelines make no distinction between group-internal and external outsourcing and request ESMA to clarify whether such a difference would have any impact in the conditions for outsourcing

**Q12: Do you agree that competent authorities should also review, as part of the ongoing supervisory process, whether measures implemented by investment firms for the compliance function are adequate, and whether the compliance function fulfils its responsibilities appropriately?**

We agree that there should be an adequacy assessment of the Compliance function on a periodic basis, but this should primarily be part of the internal control and assessment framework of investment firms whereby the assessment is supported by Internal Audit or other function to ensure independence.

We further suggest that the content and output of the review should be agreed in conjunction with the competent authority and the firm to ensure that the approach is appropriate for the type, nature, size and complexity of firm in question, and meets the standards expected to comply with the regulatory requirements.

We acknowledge that the competent authorities will want to form a view of the adequacy of the Compliance function as part of their risk assessment.

**Q13: Do you agree that competent authorities should also assess whether amendments to the organisation of the compliance function are required due to changes in the scope of the business model of the investment firm, and where such amendments are necessary, monitor whether these amendments have been implemented?**

We believe that amendments to the organisation of the compliance function as a result of changes to the business model of the investment firm is the responsibility of the investment firm to ensure that business model changes are appropriately addressed by the compliance function.

Such changes should be communicated by the investment firm to the competent authority who should rely upon the investment firm to provide the appropriate evidence and justification to demonstrate that the firm has successfully implemented changes to the compliance function accordingly.

Clearly if the competent authorities form the view that changes have not been appropriately carried through, they have a duty to intervene. However, absent failure or inadequacy of the function, it is the firm that should be responsible for its compliance arrangements and changes to them, rather than the competent authorities.

- **Internal audit** (paragraph 53 of the CP) – the CP refers to internal audit as having ‘oversight’ of the compliance function. Since this could be interpreted as implying some degree of ongoing supervision or authority which is not the normal role of internal audit. We suggest that this text be revised such that the compliance function could be said to be within the scope of internal audit's independent assurance process. [Lloyd Bailey]