

**IMA response to ESMA CP
Guidelines on certain aspects of the MiFID compliance function requirements.**

The Investment Management Association (IMA) thanks you for the opportunity to comment on the above paper.

The IMA represents the asset management industry operating in the UK. Our Members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of £3.9 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles.

General Comments

We welcome this consultation from ESMA and agree there should be a degree of consistency as regards the function and role of compliance across member states, but are wary of attempts to introduce further organisational requirements in an area already following a raft of regulation.

In the UK, the compliance function is viewed as an important and integral part of investment firms and therefore it is difficult to understand what additional requirements this consultation is proposing, aside from further scrutiny and regulation.

Finally we would like to remind ESMA of the paper published by IOSCO in March 2006, called Compliance Function at Market Intermediaries – Final Report. This paper clearly and succinctly outlined the reasons why compliance should be independent; carry the necessary qualifications; and how the effectiveness of a compliance function can be assessed.

<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD214.pdf>

Response to Questions

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? Please also state the reasons for your answers.

We agree that where the compliance function adopts a risk-based approach this can help to determine the focus and scope of compliance monitoring, reporting and advisory activities.

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It can also help to ensure the compliance function's resources are used efficiently. We also agree that it is good practice for risk assessments to be undertaken on a regular basis, in order to identify any emerging new risks which may arise due to changing business models, IT systems and organisational arrangements, changes to the regulatory regime or other external factors.

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

We broadly agree with ESMA's views relating to the monitoring obligations of the compliance function.

We do, however, have concerns with the text in the guideline which states '*....Investment firms should ensure that the compliance function establishes a monitoring program that covers all relevant areas of the investment firm's investment services, activities and ancillary services....*'. Whilst we believe that the compliance function should evaluate all of the investment firm's services, activities and ancillary services, the risk based assessment will drive what is relevant in terms of the actual monitoring plan.

The guidelines should not be interpreted or implemented to mean that as part of the compliance function's annual monitoring plan, the compliance function should monitor all its regulated activities as a matter of course – investment firms should continue to carry out a risk-based monitoring plan.

Also, para 18 outlines the responsibilities for the compliance department with regards to a firm's complaints. This guidance seems to suggest that a compliance department is overseeing the complaints process. In some firms this may not be a suitable role for the compliance department, which should be providing independent monitoring for operational processes using a risk-based approach. However we also recognise that some smaller firms may want to include this function within the compliance department. Therefore we would ask for some consideration of proportionality within this para.

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

We question ESMA's guidelines relating to the reporting obligations of the compliance function, with the exception of the guideline which states '*....Some competent authorities require investment firms to provide them with compliance function reports. This practice provides competent authorities with first-hand insight into an investment firm's compliance activities, as well as any breaches of regulatory provisions. One competent authority also requires senior management to provide it with an annotated version of the report containing explanations of the compliance function's findings....*'.

In our view, this is merely a statement of fact outlining different practices across Member States and therefore does not constitute a guideline. We request that this guideline be removed. The request for reporting by the firm to the competent authority is already part of the supervisory process and does not form part of a risk-based strategy for competent authorities.

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

We broadly agree with ESMA's guidelines on the advisory obligations of the compliance function. We believe it is essential that senior management promote and enhance a strong 'compliance culture' within an investment firm. We also agree that the compliance function should educate and train staff on matters which are relevant to its regulated business and/or provide support to other units that provide staff training.

However, point 26(a), of the guidelines states that '....training and/or other support should focus particularly, but not exclusively, on:....(a) *the internal policies and procedures of the investment firm and its organisational structure;....*'. We are of the view that it is not a responsibility of the compliance function to provide training on such matters as organisational structure; rather, it is a first-line business responsibility.

We agree that the compliance function should be involved in all relevant correspondence with competent authorities. It is important that the compliance function has full visibility of any relevant compliance-related matters raised with the competent authority.

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

We agree with ESMA's guidelines on the effectiveness of the compliance function. For the compliance function to discharge its duties efficiently and effectively, it is imperative that it has the requisite human resources, IT resources and budget. It is also necessary for the compliance function to have the necessary skills, knowledge and authority required for its duties and for the function to receive the support of its senior management. In our view, the level of MiFID knowledge required by staff should be proportionate and relevant to their role.

However we would be reluctant to see the guidelines become too prescriptive as to the size and remit of an investment firm's compliance department, as this will depend on the organisation and complexity of the firm.

Also, there is a suggestion in para 41 that a newly appointed compliance officer needs some further specialist knowledge in order to fully understand the business model and inherent risks of their new investment firm – there does not seem to be any specific guidance in this section and therefore it may be better to be removed.

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?**

Please also state the reasons for your answers.

We agree with ESMA's guidelines, above. It is important that the compliance function performs its tasks and responsibilities on an ongoing permanent basis and is able to respond rapidly and re-focus resources to unforeseen events. However we would not like to see too much guidance on the regularity with which monitoring activities take place, as such monitoring will be determined on a risk-basis.

For the purposes of continuity, we also agree that there should be adequate stand-in arrangements for the responsibilities of the compliance officer during periods of absence.

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? Please also state the reasons for your answer.

We agree with the above statement. For the compliance function to discharge its duties effectively, it must have the necessary authority/status and be able to operate independently when performing its day-to-day tasks.

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?

We agree that investment firms should ensure they are organised such that the compliance officer and the compliance function are able to take decisions independently from the influence of other business units. If it were unable to, this would undermine the authority and independence of the compliance function.

We also agree that any decision to appoint or replace the compliance officer should be taken by senior management only.

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

We agree with ESMA's guidelines on exemptions and have no further comments to make in this area. However we would like to see an amendment to para 50, which does not take into account the size and complexity of a firm, which may decide to combine the compliance and legal areas.

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

We broadly agree with ESMA's guidelines regarding combining the compliance function with other functions. Whilst it would not be appropriate to combine the compliance function with the internal audit function, we do not consider that combining the compliance function with other internal functions such as legal, risk management or money laundering prevention to be an unsound approach, provided it does not create any conflicts of interest or impair the compliance function's independence.

We are supportive of the view that compliance staff should not be involved in the activities they monitor. For clarity, we would suggest that the title of ESMA's guidelines in this area be changed to 'Combining the compliance function with other internal control functions'.

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

We agree that if an investment firm outsources any or all of the compliance function, the firm should undertake a due diligence assessment on the service provider to ensure that the criteria in Articles 6 and 14 of the MiFID Implementing Directive are met.

We also believe it is essential that the investment firm performs ongoing monitoring of the service provider to ensure it continues to perform all of its duties effectively.

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? Please also state the reasons for your answer.

We agree that as part of the supervisory process Competent Authorities can review a firm's arrangements for the compliance function to ensure that the compliance function fulfils its responsibilities appropriately. However para 63 seems to suggest that a competent authority should assess an investment firm's compliance function is adequately resourced and organised – we assume that there is inference in this para that such assessment is during the authorisation process.

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?

Where a firm's business model changes, we are of the view that it is the responsibility of the firm itself to determine any amendments required to the organisation and resources of the compliance function. In such cases, we would expect competent authorities to review whether the compliance function is adequately resourced and organised as part of their usual ongoing supervisory process. This guidance seems to suggest such reviews would take place outside of the supervisory process.