



European Securities and
Markets Authority

MiFID II Supervisory briefing

Supervision of cross-border activities of investment firms





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1 Introduction

1.1 Overview

ESMA is required to play an active role in building a common supervisory culture by promoting common supervisory approaches and practices.

Given the importance of the provision of investment services across the EU under Directive 2014/65/EU¹ (MiFID II), and concerns that emerged in the past on instances of cross-border activities provided to the detriment of investors' interests, the Board of Supervisors (BoS) of ESMA decided to launch in 2021 a peer review on National Competent Authorities' (NCAs) supervision of cross-border activities of investment firms.

On 9 March 2022, ESMA published a peer review report on the supervision of cross-border activities of investment firms.² In its report, ESMA identified the need for home NCAs to significantly improve their approach in the authorisation, ongoing supervision and enforcement work, relating to investment firm's cross-border activities to retail clients. This includes calibrating their supervisory work to the nature, scale and complexity of those firms' cross-border activities and the risks they pose.

Effective supervision of cross-border activities by home NCAs is crucial to ensure that retail clients benefit from the same level of protection regardless of where the firm providing those activities is based. In light of the pursuit of developing an effective European capital market, and retail investors increasingly accessing investment opportunities across the EU, ensuring investor protection and the proper functioning of the single market is a key mission for ESMA and NCAs.

This supervisory briefing has been designed for supervisors as an accessible introduction to the supervision of cross-border activities to retail clients by investment firms in accordance with MiFID II. It summarises the key elements of the rules and also includes indicative questions that supervisors are expected to ask themselves, or a firm, when assessing the approach to the supervision of cross-border activities to retail clients of investment firms.

The content of this briefing is not exhaustive and does not constitute new policy. It has been designed to be used in the way that best fits with supervisors' methodologies (whether distributing the briefings internally, or passing them to external bodies, such as auditors, for example). When supervising cross-border activities to retail clients, NCAs may consider the nature, scale and complexity of their firms' cross-border activities and the risks they pose in prioritising any engagement in application of this supervisory briefing. However, ESMA is of the view that, to apply a risk-based approach in relation to the supervision of

¹ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

² [ESMA42-111-5534](#).

cross-border activities to retail clients, there are certain minimum steps/actions that need to be taken by the supervising NCA. This includes, at authorisation stage, assessing whether a firm has cross-border plans and whether it is fit to carry them out. It also means collecting minimum data on firms' cross-border activities to retail clients on a regular basis (extent, complaints linked to cross-border activities, for example)³. As part of their ongoing supervision, it also entails i) ensuring that specific cross-border risks are sufficiently captured in the general risk-based approach that the NCA applies and, ii) when performing investigations / inspections on overall firms' activities, ensuring adequate representation of firms providing cross-border activities in the sample of firms selected and/or through samples relating to firms' cross-border activities (e.g. selection of files of foreign clients) based on their nature, scale and complexity. For instance, based on the information collected, the supervising NCA would need to then increase the focus on cross-border activities in its monitoring and/or investigations/inspections if it found out that firms are substantially active on a cross-border basis. The supervising NCA may also choose to prioritise its monitoring of certain types of cross-border activities depending on their scale and/or if they tend to target mostly retail clients or if they relate to complex and/or risky products.

1.2 Scope

This supervisory briefing is aimed at competent authorities (as defined in MiFID II).

It applies in relation to the supervision of cross-border activities, especially to retail clients, provided under Article 34 of MiFID II.

1.3 Status of this document

The supervisory briefing is issued under Article 29(2) of the ESMA Regulation which enables ESMA to develop new practical instruments and convergence tools such as supervisory briefings. The purpose of these tools is to promote common supervisory approaches and practices. The content of this supervisory briefing is not subject to any 'comply or explain' mechanism for NCAs and is non-binding.⁴

1.4 Purpose

MiFID II and its implementing measures were adopted to offer a higher level of protection to investors and ensure the uniform application of the requirements in the EU. In this context, MiFID II recognises the importance to allow the provision of investment services across the EU. This is a key element of the single market of financial services as it fosters

³ The scope and level of granularity of the information to be collected may depend on the application of the risk-based approach. Hence, NCAs with firms having extensive and/or complex/risky cross-border activities should have a more granular/sophisticated data collection system when it comes to the cross-border activities of the firms they supervise.

⁴ Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.

competition and expands the offer available to consumers who can choose among a broader number of financial institutions and investment opportunities.

The scope of this supervisory briefing is the MiFID framework for cross-border activities under Article 34 of MiFID II, in which the free provision of services in the EU (without establishment in the host Member State) rests on the supervision of the home NCA and on the cooperation between home and host NCAs. The direct intervention by host NCAs on passported firms is a last-resort tool, through the possibility to adopt precautionary measures. This model partially differs from the supervisory model when branches are established.⁵ The model is consistent with investor protection since it ensures that the same MiFID rules are applicable across the EU. On the other hand, the digitalisation of financial services has clearly increased the weight of cross-border services (i.e. without a branch presence) and therefore requires home NCAs to adapt their supervisory approach to this new context. The increasing exposure of retail clients in a given jurisdiction to service providers authorised in other jurisdictions in the EU, also warrants the need for host NCAs to have more visibility on cross-border activities provided in their territory; therefore, the reference in this supervisory briefing to information to be collected by home NCAs on firms' cross-border activities is also important to facilitate cooperation and exchange of information among home and host NCAs.

This supervisory briefing is designed to help supervisors structure their supervisory approach to cross-border activities provided by their firms, and is structured around the following elements:

- authorisation of firms with cross-border plans pursuant to Articles 5, 6 and 7 of MiFID II⁶;
- processing of passport notifications pursuant to Article 34 of MiFID II⁷ and their impact on the supervisory approach applied to firms;
- arrangements in place to carry out ongoing supervisory activities;
- carrying out of ongoing supervision; and
- carrying out of investigations and inspections.

Each element refers to the relevant legislation as well as provides examples of the sort of questions that supervisors could ask to test whether the supervision of cross-border activities of investment firms in their jurisdiction is adequate.

⁵ In this case, the closeness of host NCAs to the branch and to retail investors in the host jurisdiction justifies, in the legislative approach, giving supervisory competences to host NCAs, mostly limited to compliance with conduct of business rules (i.e. the rules regulating the relationship branch/customers, both established in the host country). Organisational requirements remain under the supervision of home NCAs, due to their expected firm-level setting. Cooperation remains key also in this scenario and, when issues arise, precautionary measures by host NCAs are also possible in areas under the home NCA's supervision. While additional local conduct rules are allowed, under strict conditions, for domestic firms and branches (both locally established), the MiFID model is consistent with the single market since it avoids, to the extent possible, that additional local rules risk undermining the single market.

⁶ Only in respect of investment firms.

⁷ Only in respect of investment firms.

2 Supervisory briefing

2.1 Authorisation of firms with cross-border plans

In accordance with Article 7(1) of MiFID II, an NCA shall not grant authorisation unless and until such time as it is fully satisfied that the applicant firm complies with all MiFID II requirements.

For applicant firms with cross-border plans, the authorisation stage is the first and a key opportunity for the authorising NCA to understand the applicant firm's cross-border plans and to assess whether it is fit to operate according to such plans.

Article 6 of Commission Delegated Regulation (EU) 2017/1943 already requires that the applicant firm provides to its authorising NCA information shedding some light on its cross-border plans (where relevant).

For instance, the programme of operations that the applicant shall provide must include: i) the geographical distribution of the intended activities, ii) the domicile of prospective customers and targeted investors, iii) the marketing and promotional activity and arrangements, including languages of the offering and promotional documents, iv) the Member States where the advertisements are most frequent and visible, (v) the type of promotional documents (in order to assess where effective marketing will be mostly developed) and vi) the identity of the applicant's direct marketers, financial investment advisers and distributors as well as the geographical localisation of their activity.

Whilst such information is already useful, it is important for NCAs to i) ensure they have all the information they need in relation to the applicant firm's cross-border plans and ii) assess the information collected to make sure that the applicant firm is fit to provide service on a cross-border basis.

As such, NCAs should be expected to i) have a defined supervisory approach in relation to the authorisation process and controls on applicant firms that indicate at authorisation phase their plans to carry out cross-border activities and ii) actually assess whether the applicant firms' organisational structure and arrangements are adequate considering the nature and extent of their cross-border plans.

Relevant legislation: Articles 5, 6 and 7 of MiFID II, Commission Delegated Regulation (EU) 2017/1943 and Commission Implementing Regulation (EU) 2017/1945

Questions

General

- Does the NCA have a defined supervisory approach in relation to the authorisation process and controls on applicant firms with cross-border plans?

- Does it include targeted criteria and controls at authorisation stage to assess information in relation to the applicant firm's cross-border plan?
- Does it cover the overall structure and capability of the applicant firms' proposed governance and risk management structures and processes to operate in other Member States?
- Is the NCA's supervisory approach reflected in the internal guidance / authorisation manual made available to the NCA's authorisation officer?

On the information to be collected

- Does the applicant firm have cross-border plans? Has the applicant firm provided to the NCA all the information related to such plans and required under Commission Delegated Regulation (EU) 2017/1943?
 - What is the geographical distribution of the intended activities?
 - Where will the domicile of prospective customers and targeted investors be located?
 - What are the marketing and promotional activity and arrangements intended by the firm, including their geographical location and languages of the offering and promotional documents? What are the Member States where the advertisements will be most frequent and visible? What is the identity of the applicant's direct marketers, financial investment advisers and distributors as well as the geographical localisation of their activity?
- Has all of the above information been provided for the following three years?
- What other information does the NCA need to conduct its assessment of the applicant firm's cross-border plans and arrangements and organisation associated therewith?
 - What are the applicant firm's reporting lines for the cross-border activities?
 - Is the applicant firm outsourcing activities in host Member States?
 - What is the applicant firm's complaints procedure in relation to the cross-border activities? What are the languages in which cross-border clients can submit their complaints? Does the applicant firm have the language capacity to deal with complaints in languages of the host Member States?
 - What arrangements has the applicant firm put in place regarding its internal control functions to take into account its cross-border activities? Do internal control functions have language capacity matching the geographical distribution of the intended cross-border activities? Will the internal control function get support regarding local legislation, where relevant?

- Is the information provided by the applicant firm sufficiently detailed to allow the NCA to conduct its assessment?

On the assessment

- Are the applicant firm's organisational structure and arrangements adequate considering the nature and extent of its cross-border plans?
- If the applicant firm intends to rely on third parties for the marketing of its cross-border activities and/or the provision of certain cross-border services, does the firm have the necessary skilled personnel to control the activities of such third parties (such as tied agents)? For instance, is the applicant firm's personnel in capacity of controlling marketing materials, including in different languages?
- Has the applicant firm duly identified the persons in charge of the cross-border activities and reporting lines? Are the responsibilities and reporting lines clear?
- Does the applicant firm's complaints procedure adequately consider the cross-border activities of the applicant firm? Does it also take into account possible complaints that may be directed at the firm's third party marketers/providers?
- What are the controls in place in relation to the cross-border activities of the applicant firm (including on the firm's tied agents/introducing brokers/direct marketers/distributors)? Their frequency?
- What support is available for internal control functions to perform their tasks in relation to the cross-border activities of the applicant firm (language, local legislation...)? Is it adequate?

2.2 Processing of passport notifications pursuant to Article 34 of MiFID II and their impact on the supervisory approach applied to firms

In accordance with Article 34 of MiFID II, home NCAs shall process passporting notifications completely and timely share them with host NCAs.

In addition, and as previously mentioned, it is essential that firms active cross-border be adequately structured and organised to do so. The passporting stage is often regarded as a formal process with little flexibility given to the home NCA. However, it gives indications as to a firm's new or changed cross-border plans.

Under their general supervisory responsibilities and powers, home NCAs should take into account whether further inquiries should be made in relation to the relevant passporting notifications.

It is therefore essential that home NCAs, when receiving passporting notifications:

- adequately reflect them in their monitoring systems and supervisory planning;
- consider/enquire whether they may entail substantial changes to the firm's cross-border activities and, if so, consider whether the firm is fit to operate accordingly.

There may be cases where the passporting notifications received indicate a drastic change to the firm's cross-border dimension.⁸ In such case the home NCA should ensure that the firm is fit to operate in accordance with its new cross-border plans. Indeed, the firm may need a substantial reorganisation qualifying as a material change to the initial set-up of the firm at the point of initial authorisation (under Article 21 of MiFID II). As firms should undergo extensive scrutiny at authorisation stage, when they declare the intention to provide cross-border activities, in order to ensure that they are well organised to undertake such activities it may be relevant to replicate the same level of scrutiny in those cases where the start of cross-border activities is accompanied by substantial organisational changes that would make the initial authorisation assessment as no longer relevant.

Relevant legislation: Articles 21 and 34 of MiFID II, Commission Delegated Regulation (EU) 2017/1018 and Commission Implementing Regulation (EU) 2017/2382.

Questions

- How are passporting notifications recorded in the NCAs' systems? Are they easily available to supervision officers?
- Are passporting notifications also recorded in the NCA's monitoring systems and taken into account in the NCA's supervisory planning?
- What is the process in place to understand the impact of the passporting notifications received on the firm's cross-border activities?
- Is there an alert system (automatic or manual) when a firm with no passport submits passporting notification(s) or where an important number of passporting notifications are submitted indicating a rather substantial change in the firm's cross-border plans?

2.3 Ongoing supervision

Firms' cross-border activities carry specific risks and create additional challenges for effective supervision. Therefore, it is important that an NCA has policies, procedures and a demonstrable supervisory framework which clearly set out how supervision is carried out in relation to cross-border activities and that NCAs dedicate adequate operational resources to the ongoing supervision of firms' cross-border activities.

Monitoring of firms' cross-border activities provides an overview of the risks involved and serves as a basis for the prioritisation of further and more specific supervisory actions.

⁸ This could be the case for instance of a firm authorised many years before the decision to commence cross-border activities, previously operating locally and then deciding to actively and substantially market services in other MS.

Firms' passporting notifications currently only provide information on the activities a firm is allowed to undertake and not on the extent of such activities. In order to build adequate supervisory arrangements tackling risks arising from firms' actual cross-border activities, NCAs should periodically collect and process information on these activities, at least relating to the jurisdictions in which the services are provided, the type(s) and number of clients involved, the type(s) of activities and services provided and instruments involved. In addition to such basic information on firms' cross-border activities, home NCAs may need to monitor the cross-border activities of authorised firms and the relevant risks in more details, as well as complaints received in relation to firms' cross-border activities.

A home NCA should process the above-mentioned information to identify which firms or activities may need prioritisation. Furthermore, based on the nature, scale, and complexity of authorised firms' cross-border activities and of the financial instruments used, including the types of clients of the firm, home NCAs should make use of ongoing supervision tools such as periodic engagements, reviews and sample checks to regularly check that firms' cross-border activities are carried out in compliance with applicable rules.

Relevant documentation in relation to a firms' cross-border activities (e.g. websites, client agreements, marketing communications, records of telephone conversations) is often written / performed in a language other than the native language of the NCA or English. To be able to assess such information and thus to ensure effective supervision of firms' cross-border activities, home NCAs should have in place, with respect to the information that firms provide to the NCA, reporting or translation requirements that would allow the NCA to monitor activities carried out in a different language. Where appropriate, the home NCA may also request cooperation to the host NCA.

Questions

General

- Are the risks related to firms' cross-border activities specifically and sufficiently considered in the NCA's risk-based approach?
- Where the NCA periodically calculates a risk score for firms, are risks related to firms' cross-border activities adequately taken into account in calculating such risk scores? Does the NCA also use indicators specific to cross-border risks, next to other indicators? (e.g. the number of jurisdictions the firm operates in, the number of clients served on a cross-border basis, etc.)?

Monitoring

- What kind of information is periodically collected on firms' cross-border activities?
- Does the information collected provide adequate insight into the extent and risks of firms' cross-border activities (at a minimum, per firm, an NCA would need to have information the jurisdictions in which the services are provided, the type(s) and

number of clients involved, the type(s) of activities and services provided and instruments involved)?⁹

- How are firms' cross-border activities monitored by the NCA? Does the NCA monitor other aspects than complaints relating to firms' cross-border activities?
- Does a firm with cross-border activities have marketing communications in other languages? Are these communications monitored by the NCA? If yes, how? What kind of tools does the NCA have to be able to assess marketing communications in languages different from the official language of the NCA's home jurisdiction? For example, does the NCA make use of an artificial-intelligence tool, translation tools or staff capable of assessing such languages?
- How are complaints relating to firms' cross-border activities identified and assessed?

Processing of information

- How is the information on firms' cross-border activities used in supervision? For example, is such information used in determining the firms and topics to be selected for investigations?
- Does the information on firms' cross-border activities feed into the NCA's risk-based approach, for example because it is part of the information used to determine a firm's periodic risk score?
- Is the information on firms' cross-border activities accessible and brought to the attention of the relevant supervisory staff?

Ongoing supervisory tools

- How are firm's cross-border activities considered in the NCA's supervisory plans, for example for the coming year? What kind of activities have been planned for such firms? If not, why?
- What kind of ongoing supervisory tools will be used to assess firms' cross-border activities? For instance, is the NCA specifically monitoring complaints and marketing communications to identify elements relating to cross-border activities?

2.4 Investigations and inspections

Questions

⁹ The scope and level of granularity of the information to be collected depends on the application of the risk-based approach. Hence, NCAs with firms having extensive and/or complex/risky cross-border activities should have a more granular/sophisticated data collection system when it comes to the cross-border activities of their firms.



- Is the NCA conducting investigations/inspections looking at specific cross-border aspects/topics? If not, why?
- Do the planned investigations sufficiently consider firms' cross-border activities? For example:
 - Does the selection of firms sufficiently cover firms with cross-border activities?
 - Do the topics considered sufficiently reflect topics that are relevant for firms' cross-border activities (e.g. topics that may be identified through the ongoing monitoring activities)?
 - Does a sample of client files assessed include clients served on a cross-border basis?

Use of tied agents and third parties in cross-border activities

- Is the NCA checking that firms using tied agents and third parties in their cross-border activities have effective internal controls and oversight (policies, procedures, control measures, etc.) on these third parties' organisation and activities, and performs due diligence of the same?
- Is the NCA also including sample files from clients intermediated by tied agents and third parties in its investigations/inspections?

Cooperation with other NCAs

- Does the home NCA have criteria to decide whether or not to open an investigation / inspection where it receives a request from another host NCA to open an investigation / inspection?