



BNP PARIBAS

**BNP PARIBAS Response to ESMA Consultation Paper 2011/446:
Guidelines on certain aspects of the MIFID Compliance Function
requirements.**

To: ESMA (submitted online to www.esma.europa.eu)

February 20th, 2012

BNP Paribas ("BNPP") is a European leader in global banking and financial services, with a broad international coverage and a strong presence in all key financial centres. Ranking as the first bank in eurozone in terms of deposits, Standard and Poor's rates the Group as one of the six strongest banks globally.

The Group employs over 200,000 people in more than 80 countries, including 159,600 in Europe, with a very significant focus across its four domestic markets: 64,600 in France, 18,800 in Italy, 18,000 in Belgium and 3,800 in Luxembourg. BNP Paribas enjoys key positions in Corporate and Investment Banking, Private Banking & Asset Management, Insurance, Securities Services and Retail Banking.

BNP Paribas is pleased to provide its views on the issues raised in the ESMA's public consultation on the Guidelines on certain aspects of the MIFID Compliance function requirements (the "Consultation").



Approach of BNP Paribas to the Compliance Function

BNP Paribas, as a leading international financial institution, with highly diversified activities that encompass not only investment services but also banking and insurance activities:

- Has an extensive approach to compliance, i.e. seeking to observe all the applicable legal and regulatory provisions, professional and ethical standards, and of guidelines laid down by the Board of Directors, instructions issued by general management and Group procedures, in particular those regarding protection of the Group's reputation,
- Regards as key issues compliance with banking and financial regulations, which in many cases are applicable on a consolidated basis, instructions and procedures, and protection of the Group's reputation,
- Has organized a Compliance function :
 - That through its opinions, oversight and independent second level reviews, provides a reasonable assurance of the efficiency and consistency of the system for verifying the compliance of the Group's operations and for protecting its reputation, and of its permanent internal control,
 - That acts under the following principles of action:
 - Compliance is the responsibility of each and all and the existence of the Compliance function does not remove individual responsibility of any employee,
 - Compliance function's missions and responsibilities extend to the entire Group and are performed in conditions guaranteeing its freedom of judgment and action
 - In the area of procedures and standards, Group compliance rules prevail over local rules whenever these latter rules are less strict or demanding.
 - That, within its internal control framework, is part of the level two of permanent control, the level one being covered by the businesses and the level three of internal control (periodic control), on a full independence basis, being covered by internal audit.



Detailed Consultation Response

As a matter of consistency, we decided to follow the ESMA list of questions.

Compliance Risk Assessment

Question 1: 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.

The practice described in the paper is in line with BNP Paribas' standards.

Monitoring Obligations of the compliance function

Question 2: Please provide your comments (with reasons) on any or all aspects of this guideline on the monitoring obligations of the compliance function.

The guideline is in line with BNP Paribas' practice, however we would like to emphasise the following points:

- On a general basis, the Consultation paper puts strong focus on monitoring obligations (ref question 2) and reporting obligations (ref question 3) of the Compliance function, which can be regarded as "after the fact" (or ex-post) actions. The Consultation paper does not put upfront the "advisory" role of Compliance Function, and does not put any emphasis on the ex-ante controls (such as the controls exercised within validation or approval process and more generally preventive compliance controls) the performance of which should be the first mission of the Compliance function. In our opinion, i) the order of questions 2 to 4 should be amended to 4), 2) and 3) and ii) "advisory obligations" should be extended to "ex ante controls". It should also be stressed that advisory function and ex ante compliance controls are intimately connected, as the advice given could lead, in critical cases, to a veto (ref answer to question 4 here under) for a transaction.
- In our view the Compliance function should be strongly integrated, across activities (investment services, banking services and other financial services ...), and across entities within groups. The focus on a responsibility of compliance function centred only on investment services (ref answer to question 10 here under) and of individual investments firms within groups should be strongly challenged. Within groups, especially leading international



financial institutions that are often organized under a cross border matricial model, that have a wide range of financial activities that are linked by numerous operational systems, and that are submitted to numerous national legislations, responsibility of compliance should be shared between the Compliance function at group level and at affiliates level and exercised within a common framework of standards.

- The draft guidelines mentions (ref § 14) Compliance acting through on site inspections. It also mentions (ref §17) 17 that reviews by the internal audit function should be co-ordinated with the monitoring activities performed by the Compliance function.

Wording between periodic and permanent control is not clear enough. First, first and second levels of control (permanent control) and third level of control (periodic control) should be clearly segregated and their independence stated. Compliance may, when needed, ask periodic control to carry reviews and its monitoring activities should take into account reviews by the internal audit function, but in any case must not lead to breaches in the independence of the latter (e.g. if the monitoring led Compliance to assess the audit plan and recommend amendments).

Reporting Obligation of the Compliance Function

Question 3: Please provide your comments (with reasons) on any or all aspects of this guideline on reporting obligations of the compliance function.

As mentioned in the answer to question 2, question 3 should come after question related to advisory and ex ante controls obligations and question related to monitoring obligations.

Ref §29: If it is intended that Compliance function should periodically assess the level of awareness then guidance should be given as to how this should be achieved and evidenced and testing or surveys and appraisals by managers based on evidence.

Regarding ex-post controls, the practice described in the paper is in line with BNP Paribas' standards. However, the consultation paper does not focus enough on reporting on prevention and ex-ante controls. The reports described are ex-post controls oriented and do not show the Advisory and prevention need.

Whilst recognising the importance of the strength and rigour of the firms compliance programme it is problematic to report definitively on its



effectiveness. Incidents and breaches are discovered or become apparent after the event has occurred. In some cases many months or years after. Therefore, to be definitively reporting on the effectiveness of the program may be misleading and inaccurate unless it is caveated "to the best of our current knowledge and belief".

The reporting as described may also lead to a risk of duplication between the Compliance programs and reviews and the internal audit programs.

The consultation paper limits reporting to Senior management. Conditions of reporting to each corporate bodies (Senior management and Board of directors or its committees) should be specified, the wording is not precise enough.

The description of contents of the compliance report seems rather prescriptive (ie Correspondence with competent authorities).

Advisory obligations of the compliance function

Question 4: Please provide your comments (with reasons) on any or all aspects of this guideline on the advisory obligations of the compliance function.

The practice described in the paper is far under BNP Paribas' standards.

As already said under answer to question 2, the Advisory obligations of the compliance function are at least as important as the monitoring obligations (described in III.II) and the reporting obligations (described in III.III).

- The Compliance function should participate with at least a strong voice to validation or approval processes of activities, transactions, products.
- "Advice" of the Compliance function should be compulsory in significant cases and eventually lead to a veto that can only be superseded by the senior management, through an escalation process. This escalation process should be described by each firm in its internal Policies, and therefore be proportionate to its organisation. However, firms should be able to exercise a degree of discretion.
- As a consequence, the wordings of the consultation "provide assistance", "provide compliance expertise and advice", "should be involved", "encourage business units to consult",....should be strongly strengthened and detailed.



In practice the periodic assessment that the staff holds the necessary level of awareness is very challenging in large organizations, to reach satisfaction on.

Effectiveness of the compliance function

Question 5: Please provide your comments (with reasons) on any or all aspects of this guideline on the effectiveness of the compliance function.

As for most banks, the separation between Mifid and non-Mifid compliance officer is not a group practice, our purpose is that the same individual can cover different regulation. The final objective remains the protection of the soundness of the financial services provider and of its reputation, of client's interest and market integrity.

Permanence of the Compliance Function

Question 6: 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.

Under prudential regulation (ref operational risk framework), financial institutions have the obligation to put in place business contingency plans. This obligation applies to business units and functions, among them the Compliance function.

Independence of the compliance function

Question 7: 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.

Question 8: 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 in-dependently from any influence of the business units and that the compliance officer is appointed and replaced by senior management only?

BNP Paribas agrees that it is critical that Compliance function must perform its tasks with independence. Anyway, such independence should be combined with proximity with transactions and operations that is also critical. Independence and proximity can be achieved by a combination of a proper position of the function (e.g. reporting line to high levels of management) appointment and replacement by senior management and strong escalation processes to senior management

Within BNP Paribas' procedural arrangements, the position, organisation, resources and independence of compliance function are described in an Internal Control charter and in a Compliance function Charter, which we believe is a good practice.

The draft guideline wording (ref §45) related to the appointment and replacement of the compliance officer by senior management or the supervisory function ("body" would be more appropriate) should be completed by the mention "in compliance with the applicable corporate law". (as under some local corporate laws, e.g. continental European laws, such appointment or replacement cannot be performed by the supervisory body, but only by senior management).

Exemptions

Question 9: Please provide your comments (with reasons) on any or all aspects of this guideline on Article 6(3) exemptions.

The draft guideline (ref §50) states that the Compliance function should generally not be combined with the legal unit. BNP Paribas, although it complies with this statement, believes that a more open position should be taken on the combination with the legal unit, as on one hand Legal should be responsible for legal watch, on the other a prime duty of Compliance function is to give an assurance of compliance with laws and regulation, fields in which strong cooperation with legal unit can bring much added value.



The same §50 states also that the Compliance should not be “subordinate to internal control functions”. As Compliance is an internal control function, this statement should be amended in “subordinate to another internal control function” (e.g Risks function) unless in large entities. Any kind of conflict of interest should be avoided.

Combining the compliance function with other functions

Question 10: Please provide your comments (with reasons) on any or all aspects of this guideline on combining the compliance function with other functions.

See our comments to Question 9.

The consultation paper should also address the widespread situation that investment services firms have very significant other activities, especially banking activities, to which are attached also obligations to maintain a Compliance function. As these other activities, especially banking activities, and investment services are very often much entangled, as there are very extensive overlaps between compliance obligations and as under banking regulations, risks, including compliance risks, must be monitored on a consolidated basis, these firms maintain in their organization an integrated Compliance function. This should be recognized as a standard practice for investment services firms that are also banks, or members of a group with diversified activities.

To support this comment please note that draft guidelines in Annex III apply to investment firms “including credit institutions”.

It should also be noted that if on one hand internal audit function should perform examination of the compliance function, on the other compliance function should reciprocally exercise an oversight on compliance of internal audit with applicable laws and regulations. Once again the protection of the soundness of the financial services provider and of its reputation, of client’s interest and market integrity is the objective to keep in mind.

Outsourcing of the compliance function

Question 11: Please provide your comments (with reasons) on any or all aspects of this guideline on outsourcing of the compliance function.



In relation to outsourcing, it should be clearly distinguished between:

- a. outsourcing within a group: Within a group, outsourcing of compliance should be recognized a standard practice subject to legal formalities such as board approval and,
- b. outsourcing outside the group (or if the firm is not member of a group): Draft guidelines stated in §56 to 60 and 62 should be regarded as an exception, require specific permission and be adapted to each case, especially if there is a single group function (e.g. §58 needs to be redrafted in the case of outsourcing within a group in order to mutualize functions; §60 also, considering the case that there could be a single group Compliance function).

Review of the compliance function by competent authorities

Question 12: 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.

Question 13: Do you agree that competent authorities should also assess whether amendments to the organization 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 existing national regimes regarding the appointment and notification of compliance officers should be maintained.

We would be happy to provide further detail on any of our comments if ESMA find this helpful.

Yours faithfully

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