Frankfurt am Main,
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BVI[1] Position on EBA's Consultation Paper on Draft Guidelines on internal governance under Directive (EU 2019/2034), EBA/CP/2020/27

We take the opportunity to present our views on the consultation paper of the EBA related to guidelines on internal governance under the IFD.

In general, we welcome the approach taken to involve the proportionality principle as a main principle of the guidelines and to consider the existence of different legal structures of investment firms. However, we see the need to amend or to clarify the guidelines at least on the following topics:

- **Scope of the previous governance rules under CRD:** As addressed in the EBA hearing we do not share EBA's assessment that the CRD IV governance requirements already apply to all investment firms covered by the IFD governance rules. The EBA explained during the hearing that this would be the reason why there is no need to change anything under the IFD in contrast to the current CRD approach in general. We expressly disagree with this assessment. According to a difference in the definitions of investment firms in the CRR/CRD and the IFD, certain investment firms in the meaning of the IFD are not covered by the current CRD governance framework. The definition of investment firms in the CRR/CRD does not involve entities providing certain MiFID services (such as portfolio management) without a licence to hold client money or to deal on own account (cf. Article 4(1)(2)(c) CRR – so called limited licence firms). They do not qualify as institutions in the meaning of CRD IV for which the CRD governance rules apply (cf. Article 4(1)(2) CRR which expressly does not include such limited licence firms in the meaning of Article 4(1)(2)(c) CRR). Irrespective of the coming into force of the IFD, such limited licence firms are (and have been) out of scope of the governance rules of CRD IV. This is not only a purely national German implementation, but already clearly delimited due to the definitions in the CRD/CRR framework.

  In Germany, we have a number of such limited licence firms which do not reach the thresholds in Article 12 IFR and for which the IFD framework lays down new rules for the first time regarding the governance requirements in addition to the MiFID requirements which require considerable implementation effort. This is the reason why the principle of proportionality is very important.

- **Scope of the new guidelines:** We would like to highlight that not all competent authorities comply with the internal governance guidelines established by the EBA under the CRD framework (cf. compliance table). In particular, BaFin does not comply with the provisions on formal independence (para 32 of the guidelines under the CRD). This exception results from the non-compliance confirmation regarding the Joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU. We expect that the competent authorities will publish the same non-compliance statement under the IFD guidelines which follow the guidelines under the CRD. Therefore, it could be appropriate to review the scope and content of the guidelines based on the

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non-compliance table and to reduce the requirements in an appropriate way. This applies even more as investment firms are already subject to the MiFID governance requirements. In avoiding double regulation and more complexity of the requirements, we also request to delete all requirements which are not covered by Article 26 IFD, but subject to the MiFID requirements (such as whistleblowing processes, conflict of interest management etc.) or other Directives (such as Directive 2015/849/EU, cf. ***paragraph 35*** of the draft guidelines). A dedicated reference to the MiFID requirements could be included in the guidelines to clarify that there is no gap in this regard.

- **Small and non-interconnected investment firms:** We share the EBA's assessment that investment firms which do not meet the conditions set out in Article 12(1) IFR are not subject to the governance requirements in accordance with Article 26 of the IFD and out of scope of these guidelines. We also agree with the assumption that these firms should also have robust governance arrangements as stated in ***paragraph 24 of the introduction remarks*** of the consultation paper (background and rationale). Moreover, Article 29(3) IFD which refers to the treatment of risks, in particular liquidity risks, also applies to small and non-interconnected investment firms. However, we request to clarify that small and non-interconnected investment firms are not required to set up governance rules regarding liquidity risks on an intra-day basis as a standard process. The introduction remarks in paragraph 24 of the consultation paper could be understood in such a way. We suggest clarifying that the principle of proportionality and the types of liquid assets should be considered. In most cases, small investment firms hold their own funds via unencumbered short-term deposits at a credit institution where it makes no sense to review the liquidity of the deposits on an intra-day basis. Moreover, according to Article 43(1) IFR or Article 6(3) IFR, competent authorities may exempt small and non-interconnected investment firms from the liquidity requirements. In these cases, it is also not appropriate to set up such strict processes.

Subject to our general comments, we would like to comment on the detailed questions as follows:

Question 1: *Are subject matter, scope of application, definitions and date of application appropriate and sufficiently clear?*

In general, we request to review and amend the terms used with regard to the definitions of 'financial institutions' and 'investment firms'. It must be clarified that only investment firms covered by Article 26 IFR are subject of these guidelines. This applies at least to the following requirements:

- **Status of these guidelines** (***paragraph 1*** of the draft guidelines)**:** We request replacing the term '*financial institutions, including investment firms*' with the term '***investment firms covered by Article 26 of the Directive (EU) 2019/2034'***.

- **Subject matter:** We request clarifying the subject matter in ***paragraph 5*** of the draft guidelines based on the scope of Article 26 IFD as follows:

  '5. These guidelines specify the internal governance arrangements, processes and mechanisms that investment firms that are subject to Directive 2019/2034/EU must implement in accordance with ~~*Section 2 of Chapter 2*~~ ***Article 26*** of Directive 2019/2034/EU in order to ensure effective and prudent management of the investment firms.'

- **Legal scope**: The reference in ***paragraph 7*** of the draft guidelines to the definition of financial institutions of the EBA Delegated Regulation and the MiFID II definition of investment firms is very far reaching and not in line with the scope of the IFD framework. This would involve several entities which are not in scope of the IFD framework but provide MiFID services (such as credit institutions

providing MiFID services). The scope of the EBA guidelines should be clearly limited to investment firms in the meaning of Article 2 IFD (authorised and supervised under MiFID II) which do not meet the conditions of Article 12 IFR. Therefore, we request amending the addressees of the draft guidelines (paragraph 8) as follows:

> '7. These guidelines are addressed to competent authorities as referred to in point (v) of Article 4 (2) of Regulation (EU) No 1093/2010 and defined in point 5 of Article 3(1) of Directive 2019/2034/EU, and to ~~*financial institutions as referred to in Article 4 (1) of Regulation (EU) No 1093/2010that are*~~ investment firms ~~*as defined in Article 4(1)(1) of*~~ ***as referred to in Article 2(1) of Directive 2019/2034/EU authorised and supervised under*** Directive 2014/65/EU and do not meet all of the conditions to qualify as small and non-interconnected investment firms under Article 12(1) of Regulation (EU) 2019/2033 ("investment firms").'

Question 2: *Is title II sufficiently clear? Do you see other criteria to add or to delete as inappropriate?*

Regarding the criteria for application of the **proportionality principle** addressed in ***paragraph 20*** of the draft guidelines, we would like to highlight that the amount of assets under management are not suitable and eligible to be a stand-alone criterion in order to ensure an appropriate implementation of the governance requirements. We are aware that the amount of assets under management is a threshold for the own capital requirements, but this is appropriate for that purpose since operational risks could affect all portfolios managed. However, in setting up governance requirements, the nature, scope and complexity of the activities provided by portfolio managers should be relevant (such as the underlying risk profiles of the business activities that are carried out). In addition to the authorised activity, the type of investment policies and strategies of the portfolios managed, the national or cross-border nature of the business activities and the additional licences to provide MiFID services should be relevant. Therefore, we request to clarify that in assessing what is proportionate, the focus should be on the combination of all the mentioned criteria (size, internal organization and the nature, scope and complexity of the activities).

Moreover, we request adding a general provision (***new paragraph***) that a higher level of sophistication should be expected where investment firms are authorised to hold clients' money or assets or provide services and activities listed in point (6) and (7) of Section A of Annex 1 to Directive 2014/65/EC. This would be in line with the current approach applicable for limited licence firms defined in Article 4(1)(2)(c) CRR to which the CRD governance rules do not apply. Moreover, the draft EBA guidelines on remuneration policies and practices also address that approach as part of the proportionality principle (cf. paragraph 80 of the draft remuneration guidelines).

Furthermore, we request to clarify in ***paragraph 26*** that a '*sustainable business model*' does not mean an ESG business model with the requirement to ensure strategies based on sustainable finance models.

As already mentioned in our introduction remarks, the provisions on formal independence of members of the management body in ***paragraph 37*** of the draft guidelines do not apply in Germany. We therefore welcome the reference to '*without prejudice to national law*'. However, we suggest reviewing the need for such a provision in these guidelines because this is already addressed in the Joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU. Any kind of double regulation should be avoided and could help to set up practicable and unambiguous rules.

Question 3: *Is title III sufficiently clear and appropriate?*

We request reviewing all references to 'parent investment firms and their subsidiaries' and all other terms and definitions used in the **group context**. It seems that the terms used do not comply with the definitions and scope of the prudential consolidation of IFD/IFR framework in all cases. For example, not every parent company of an investment firm group is an investment firm. This applies in particular to the general group approach in ***paragraph 77*** of the draft guidelines. We therefore disagree with the scope definition to the effect that the '*parent investment firms and their subsidiaries*' should ensure that governance arrangements are consistent and well-integrated on a consolidated basis.

In that context, we refer to our position paper on the Draft RTS on prudential consolidation of investment firm groups (Article 7(5) of the IFR) where we addressed our concerns in the group context.

Question 4: *Is Title IV appropriate and sufficiently clear? In particular the one on conflict of interest and RPT at investment firms. Should we keep it like this?*

As already mentioned in our introduction remarks, we request avoiding any double regulation or more complexity of the requirements. We suggest to delete all requirements which are not covered by Article 26 IFD, but subject to the MiFID requirements (such as whistleblowing processes, conflict of interest policy) and already addressed in other guidelines such as the joint ESMA and EBA guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU. These requirements are not covered by the mandate given to the EBA to issue guidelines according to Article 26 IFD. The scope of the internal governance guidelines should be limited to:

- a clear organisational structure with well-defined, transparent and consistent lines of responsibility
- effective processes to identify, manage, monitor and report the risks that investment firms are or might be exposed to, or the risks that they pose or might pose to others,
- adequate internal control mechanisms, including sound administration and accounting procedures,
- remuneration policies and practices that are consistent with and promote sound and effective risk management.

Question 5: *Is Title V appropriate and sufficiently clear?*

We have the impression that the guidelines (in particular the requirements on the tasks and responsibilities of the risk management function) are only focussed on the investment firms risk profile. In general, this is an appropriate approach. However, investment firms providing portfolio management without a licence on dealing on own account or holding client assets or money have their risk management focus on the portfolios managed. We therefore would like to clarify that the governance rules cover these activities in an appropriate and proportionate way.

Question 6: *Is Title VI appropriate and sufficiently clear?*

We assume that the EBA is aware of further developments and the new proposals on digitalisation of operational resilience (DORA) to cover ICT risks and activities provided by ICT parties. The proposal of a new Regulation will cover all internal risk management requirements of supervised entities in that context and due to a lack of legal requirements will replace the current supervisory approaches. We therefore request reviewing the provisions in the draft guidelines in order to avoid double regulation and additional administrative burden through implementation of different provisions on different times.

Question 7: *Is Title VII appropriate and sufficiently clear?*

The proposed external transparency requirements are not part of the mandate given to the EBA in Article 26 IFD. We therefore request limiting the provisions to internal transparency and deleting the provision on external transparency. This applies even more as the Member states shall ensure that the competent authorities have the power to publish certain information (cf. Article 44 IFD). The content of such public information should be the decision of the competent authorities which perfectly know and understand the business models and legal structures of the investment firm markets in each country.

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