EFAMA response to the EBA Consultation on Draft Guidelines on Outsourcing arrangements

I. GENERAL REMARKS

The European Fund and Asset Management Association[1], EFAMA welcomes the opportunity to provide comments to the EBA draft Guidelines on outsourcing arrangements.

Asset management companies in Europe provide services to collective investment undertakings and are covered by their sector-specific regulation, i.e. UCITS Directive[2] and AIFMD[3]. At the same time, a number of asset management companies are part of a banking group, in which cases the credit institution, i.e. the parent company, is called to ensure the consistent implementation of the requirements deriving from its own sectoral legislation (CRD/CRR) at the group-wide level. In particular, article 109 para 2 of CRD[4] foresees that competent authorities shall require the parent undertakings to implement arrangements, processes and mechanisms set out in Section II of Chapter II (Title VII) in their subsidiaries not subject to this Directive on a consolidated or sub-consolidated basis. It is important to stress that for subsidiaries such as asset management companies, that are covered by their sector-specific regulation, the additional application of the set of rules deriving from CRD is foreseen only at the group-level and on a consolidated basis and not at solo level. Group-level application means ensuring that consistent and not contradictory processes are in place intra-group and that is to be ensured by the consolidating entity. On the other hand, CRD doesn't foresee that the parent company's regulatory requirements are to replace the sector-specific ones, which are the ones targeted at the specific business model of the asset management companies and therefore the ones that apply at solo level.

[1] EFAMA is the representative association for the European investment management industry. EFAMA represents through its 28 member associations and 62 corporate members close to EUR 23 trillion in assets under management of which EUR 15.6 trillion managed by more than 60,000 investment funds at end 2017. Just over 32,000 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 28,100 funds composed of AIFs (Alternative Investment Funds). For more information about EFAMA, please visit www.efama.org

[2] Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

[3] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

[4] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC Text with EEA relevance

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In this respect, EFAMA considers it important to clarify that the EBA Guidelines on outsourcing arrangements are based on the mandate given by Article 74 (3) of the CRD and as such are first and foremost targeting the internal governance processes of a credit institution. In terms of the consolidated approach the parent credit institution shall ensure consistency at the group-level, but the provisions applying at solo level for asset managers belonging to a banking group remain the ones foreseen in the UCITS Directive and AIFMD. Any different approach will be an extension of the scope of EBA's mandate and would lead to regulatory inconsistencies such as requesting asset management companies-subsidiaries of banks to apply two different sets of rules as regards their outsourcing arrangements or to disregard their existing sector-specific regulatory framework, which they are not entitled to do.

In addition to the argument of legal consistency, the implementation of the sector-specific regulation for asset managers is also consistent with the need for proportionality as to the size, internal organization, nature, scope and complexity of the activities provided by an entity. AIFMD and UCITS Directive are explicitly focusing on the asset management business models and in that way they set the appropriate requirements also in the case of outsourcing arrangements. Ensuring this proportionate approach targeted at the needs of the sector is of paramount importance to the asset management industry, as outsourcing and delegation is a reliable, well-functioning and tested model, central to ensuring investor choice with the ability of European investors to access world leading investment expertise. Outsourcing of back office functions is also an important part of the asset management business model which allows for choice, competition, economies of scale, and enables firms to focus on core competencies. All of this provides investors with better value and choice. Therefore, a truly proportionate approach requires the application of sector-specific rules at the level of the entity rather than a common set of Guidelines applying for all companies in the same group, even more when the starting point for such Guidelines is solely the business model of the parent company.

In the case of AIFMD and UCITS the specific rules on outsourcing and delegation are consistent with the requirements under CRD and therefore the requirement for a consolidation at group level is already met. It is important to note as well that this understanding as to the priority of sector-specific rules and their application at solo-level is already foreseen in the Council's latest compromise text on the CRD V Proposal[5].

For that reason, EFAMA urges EBA to clarify in its Guidelines that sectoral legislation for banks' subsidiaries, where applicable to outsourcing arrangements, will prevail against the CRD rules – including the EBA Guidelines. We consider that this should be clearly presented early on in the draft Guidelines as to avoid legal inconsistencies and misinterpretations.

Finally, we understand the need for consolidation and consistency of processes and arrangements in the case of a banking group, we consider however that this cannot be achieved by EBA alone, given its mandate on banking regulation and its expertise linked to the banking business model, hence the lack of mandate and expertise related to other business models. Therefore, we consider it necessary to

[5] Article 109 (2): *"Subsidiary undertakings, not themselves subject to this Directive, shall comply with their sector-specific requirements on solo level."*

enhance the cooperation among the ESAs for regulatory standards and Guidelines applying to different market sectors, in a way that ensures proportionality to different business models and allows for a different leading role among the ESAs based on the type of the business targeted. In the case of asset managers ESMA has the competence to regulate on sector-specific rules and a better knowledge of the activities of the management companies and the risks involved. It should therefore remain the leading Authority as regards the application of outsourcing arrangements by them.

II. EFAMA COMMENTS TO THE QUESTIONS OF THE CONSULTATION

Q1: Are the guidelines regarding the subject matter, scope, including the application of the guidelines to electronic money institutions and payment institutions, definitions and implementation appropriate and sufficiently clear?

As mentioned in our general remarks, we would urge EBA to clarify already in the scope of its Guidelines that the sector-specific rules apply at solo level for subsidiaries of banks and have priority over the CRD rules.

We suggest the following changes in paragraphs 9[6]:

"9. Without prejudice to Directive 2014/65/EU (MiFID II), ***Directive 2009/65/EC (UCITS) and Directive 2011/61/EU (AIFMD)*** *the Commissions delegated Regulation (EU) 2017/565 containing requirements regarding the outsourcing for institutions providing investment services and performing investment activities and respective guidance issued by the European Securities and Markets Authority regarding investment services and activities, institutions referred to in Directive 2013/36/EU should also comply with these guidelines* ~~***on a solo basis***~~*, sub-consolidated basis and consolidated basis as set out in Articles 21, and Articles 108 to 110 of Directive 2013/36/EU."*

Q2: Are the guidelines regarding Title I appropriate and sufficiently clear?

Paragraph 18 suggests an extended scope of the EBA Guidelines in a way that these are to apply also at solo level for the subsidiaries of a credit institution. For reasons explained in our general remarks we consider this is inconsistent with article 109(2) of CRD and with the existing sector-specific rules. We would therefore suggest the following addition to paragraph 18[7]:

"In accordance with Article 109(2) of Directive2013/36/EU, these Guidelines should apply on the sub-consolidated and consolidated basis. For this purpose, the EU parent undertakings and the parent undertaking in a Member State should ensure that internal governance arrangements, processes and mechanisms in their subsidiaries, including payment institutions are consistent, well-integrated, and adequate for the effective application of these Guidelines at all relevant levels. ***Subsidiary undertakings, not themselves subject to this Directive, shall comply with their sector-specific requirements on solo level****."*

[6] Changes are suggested in bold, italics
[7] Changes are suggested in bold, italics

Q8: Are the guidelines in Section 9.2 regarding the due diligence process appropriate and sufficiently clear?

While we recognize the importance of ESG factors we note that absent an agreed taxonomy, further disclosures on how relevant ESG factors are integrated in the outsourcing arrangements would be more appropriate than mandating specific standards that may not be fit for the service to be provided each time.

Q10: Are the guidelines in Section 10 regarding the contractual phase appropriate and sufficiently clear; do the proposals relating to the exercise of access and audit rights give rise to any potential significant legal or practical challenges for institutions and payment institutions?

EFAMA would like to stress that although Guidelines as to the contractual phase may be helpful, outsourcing arrangements are a much bespoke business process and the risks to be addressed are not necessarily to be described in a general way a priori. For that reason, flexibility as to the way these arrangements are to be concluded each time is also necessary.

Q13: Are the guidelines in Section 13 appropriate and sufficiently clear, in particular, are there any ways of limiting the information in the register which institutions and payment institutions are required to provide to competent authorities to make it more proportionate and relevant? With a view to bring sufficient proportionality, the EBA will consider the supervisory relevance and value of a register covering all outsourcing arrangements within each SREP cycle or at least every 3 years in regard of the operational and administrative burden.

The register is one of the core changes within these Guidelines and it can be of added value in terms of internal use and organization. However, what is crucial is an overarching risk management process (as regards the value of the contracts, the impact on the firm and clients, the complexity, the ability to switch services etc.) to which the register can play a complementary role. Therefore, the priority should remain at the level of assessing and prioritizing risks, whereas the register can be used as a reference tool to help put in place such a process and keep at hand relevant information of contractual nature that is useful for the monitoring of contracts. As a matter of proportionality, the register should include the outsourcing arrangement of critical or important functions and disregard or be much alighted on other arrangements.

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