RegCORE Client Alert

Financial Services: Revisiting the Banking Union's Common Ethics Culture – revised SSM Guideline on harmonised ethics regimes

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QuickTake

The Banking Union generally but the Single Supervisory Mechanism (**SSM**) specifically, whether at the level of the European Central Bank (**ECB**) at its head or at the participating national competent authorities (**NCA**s) continue to focus on ensuring that the EU's Single Rulebook, as applied in the SSM context, is supplemented by a Single Supervisory Culture but also a harmonised ethics regime. In order to drive that forward the euro area central banks and NCAs formed the Ethics and Compliance Officer's Task Force (**ECTF**) to act as a single hub for information exchange and a forum to support coherent implementation of ethics across the Eurosystem and the Banking Union.[1] The ECTF was transformed into a permanent "Ethics and Compliance Conference" (**ECC**).

The ECB's Annual Report on Supervisory Tasks, which was adopted by the Governing Council on 31 March 2022[2] sets out what the ECB-SSM has achieved against its supervisory priorities set for 2021 but also provides a recap on how the SSM is strengthening its common ethics culture. Notably the Annual Report, confirmed that the ECC has "…made significant steps towards enhancing and harmonising the ethics regimes of NCAs through the substantive revision of the Guideline establishing the SSM Ethics Framework, which was adopted by the Governing Council." (the **SSM Ethics Guideline**).[3] With a view to addressing conflicts of interest more effectively, the SSM Ethics Guideline strengthens pre-employment and post-employment provisions as well as the rules on private financial transactions. The ECB-SSM and the NCAs will implement the new requirements by June 2023.

[1] The ECTF also has previously organised thematic sessions with external counterparts including the UN Ethics Office, the Office of the European Ombudsman and the European Court of Auditors, with the latter presenting its report on the ethical frameworks of selected audited EU institutions.
[2] Available here
[3] Available here.

This Client Alert provides an overview of the aims of the SSM Ethics Guideline and its impact on Banking Union supervised institutions (**BUSI**s) when dealing with their supervisors.

On 17 December 2021 the Official Journal of the European Union published the recast SSM Ethics Guideline which had been dated 2 November 2021 by the ECB and which the ECB(-SSM) and NCAs will operationalise by June 2023. This is the first major revision to the Eurosystem & SSM Guidelines which were originally adopted by the Governing Council in 2015.

At its heart the revised SSM Ethics Guideline does two things. First it aims to improve best practice standards generally but secondly and perhaps more fundamentally it aims to harmonise these across all NCAs i.e., a task where the tone must rightly be set at the top from the ECB irrespective of individual efforts advanced at the national level by various NCAs.

The revisions are timely and some are targeted and as a remediation response following a limited number of publicly identified conflict of interest failings at supervisory authorities more generally (not just in the EU-27) and/or due to non-authorised or improper private dealings in financial instruments by supervisory staff in respect of firms they supervise or exposures linked thereto. The same is also true in respect of the revisions strengthening procedures around cooling-in and/or cooling-off periods for relevant staff.[4]

Consequently, while the efforts of the ECB are very welcome, the implementation of this new code of conduct may also have spillover effects in the supervisory engagement with BUSIs. What the new SSM Ethics Guideline certainly does do is provide another additional enhancement to harmonising existing ethics and compliance standards (including the ECB's "Single Code"[5]), which in turn serves to reinforce the SSM's single supervisory culture and thus how BUSIs are measured in complying with the EU's Single Rulebook as applied in the Banking Union.[6]

Key requirements of the SSM Ethics Guideline

As an ECB rulemaking instrument, this new Guideline recasts i.e., replaces existing guidelines, notably those from 2015. Recital 4 of the SSM Ethics Guideline sets the overarching aims of this new framework so as to (our emphasis in bold):

> "…to maintain the highest standards of professional ethics and integrity, the **existing common minimum standards and rules aimed at preventing insider trading and the misuse of non-public SSM information, as well as at preventing and managing conflicts of interests, should be further developed**. To this end, the Governing Council considers it important that the ECB and the NCAs **adopt measures aimed at avoiding even any appearance of insider trading, misuse of non-public information or of possible conflicts of interest**. While the ECB and the NCAs should have certain latitude in defining the most appropriate framework for such measures, it is at the same time important – in order to adequately protect the reputation of the SSM – that, a set of aligned measures, in particular as regards rules on critical private financial transactions, should apply, as a minimum, to members of staff of the ECB and the NCAs when conducting SSM tasks. Those aligned measures should also apply to members of an internal body that has administrative and/or consultative functions relating directly or indirectly to the implementation of SSM tasks carried out by the NCAs.

Recital 4 is crucial in that setting a common goal and harmonised set of expectations of how to evidence compliance, it still leaves room for flexibility by individual authorities to apply additional standards where these do not deviate from the common grounds set in the SSM Ethics Guideline. NCAs are required to inform the ECB-SSM, without undue delay where prevented from complying with the objectives set out in the rules and take reasonable measures at tis disposable to overcome obstacles posed by national law so as to achieve a harmonised implementation of the SSM Ethics Guideline across the SSM.

Recital 5 complements Recital 4 in stating that:

> "To further safeguard the trust of supervised entities and Union citizens that members of staff of the ECB and the NCAs, as well as members of their bodies, serve with complete professional impartiality, perceptions of conflicts of interests should be avoided. To this end, those members of staff and members of bodies who have access to market sensitive information should be required to comply

[4] See further official public commentary from December 2021 available here

[5] Which applies as a code of conduct for all members of high-level ECB bodies and their alternates.

[6] A selection of additional materials are available here.

with specific rules and standards when conducting private financial transactions, in particular where those transactions involve regulated entities."

Recital 11 clarifies that while the SSM Ethics Guidelines are only applicable to the performance of SSM tasks, "…it is nonetheless desirable that the ECB and the NCAs apply equivalent standards to members of their bodies, their staff and others performing non-SSM related tasks."

Article 2 sets out some key definitions. Some of these are quite established concepts (such as non-public information and/or market sensitive information as well as conflict of interest) whereas others are new. This includes the definition of "short-term trading" which "…means the purchase and subsequent sale of a financial instrument or the sale and subsequent purchase of the same financial instrument within 90 calendar days."

Article 6 sets out rules on conflicts of interest in terms of identification, reporting and mitigation thereof. These apply to both conflicts that arise in the context of previous and current: occupational activities, financial holdings, private activities or personal relationships. The article also requires a mechanism in place to facilitate cooling-in and cooling-off periods as well as during unpaid leave.

Article 7 sets out a prohibition on receiving "advantages" for themselves or any other person in a way that is connected to their performance of their official duties and responsibilities. While the provisions of this Article reflect existing concepts on prevention of receiving gifts and hospitality (over a certain monetary threshold) the article is somewhat stricter in the standards of independence than in previous standards.

Part 3 of the SSM Ethics Guideline and thus Arts. 8 to and including 11 set out rules on professional secrecy, prohibition on disclosure or misuse of non-public information and both general principles as well as specific restrictions on private transactions (whether for their own account or on the account of any third party). Investments generally should have a medium to long-term investment horizon and go through a personal account dealing policy checklist (although this is not set out in the rules, it is implied that this is maintained by each relevant authority). Article 11 sets out further restrictions for persons with access to market sensitive information or those that are or may be perceived as closely related to the performance of SSM tasks in engaging in critical private financial transactions. What this does is effectively prohibit transactions, or require authorisation (with or without embargoes) and reporting by such persons in trading of equity, debt or derivatives transactions in respect thereof related to instruments issued by BUSIs. A reporting obligation applies for disclosure of non-discretionary trading arrangements i.e., through an independent third party asset manager.

Chapter III of the SSM Ethics Guideline conclude the rules by requiring the ECB-SSM and NCAs to implement independent ethics and/or compliance functions (where these do not exist or strengthen those that do). Internal compliance monitoring and reporting of non-compliance along with remedial actions as a follow-up are also conceptually catered for and the ECB-SSM and NCAs will have to operationalise these.

Outlook for BUSIs

While the objectives and the requirements of the SSM Ethics Guidelines are predominantly aimed at the Banking Union authorities in the context of SSM but also non-SSM tasks and equally, while these have to be operationalised, through various differing internal authority-specific measures, the new framework may have some additional impact for BUSIs and financial services firms more generally. This includes that as part of the operationalisation and running of this new framework relevant supervisory staff may require:

1. BUSIs and other relevant financial services firms (particularly asset managers and/or insurers) to include (on an ad hoc or potentially recurring basis) additional confirmations to such staff that it has either taken note of the relevant restrictions and/or operated in a manner that does not contravene independence restrictions imposed by the new regime;
2. Certify (on an ad hoc or potentially recurring basis) that it has not provided any "advantages" to any SSM staff. Already the ECB in certain instances, ranging from conferences to other public engagements, requires non-financial corporates to take note of various independence restrictions and confirm their understanding thereof;
3. BUSIs and financial services firms (notably brokerages) may have to carefully review list of private clients to ensure that they are not, whether as SSM staff, or those linked to (by relationship) or household to relevant SSM staff so as to avoid any perception that they are aiding and abetting financial crime, insider dealing, market abuse and/or any circumvention efforts. While this may not mean that such SSM staff or related persons should be offboarded as clients, additional information may need to be gathered both at inception and over the duration of a client relationship to ensure that the regulated financial services firm is complying with its own obligations on investment restrictions and/or transaction monitoring. An issue here will be as to where to draw the line of which financial instruments are fully restricted as a JST staff member (or indeed someone in his household) supervising say a set number

of BUSIs in the JST's remit, may not be (unless the operationalisation of the SSM Ethics Guidelines calls for that) prohibited from trading financial instruments that are subject to supervision by other JST members. Equally, some firms may need to consider as to whether, having identified relevant persons to whom restrictions of the SSM Ethics Guidelines apply, they need to extend a lookback to positions that were acquired prior to that person becoming SSM staff and a divestment at a later point in time i.e., an issue that was publicly reported as having been investigated (even if ultimately dropped) in the case of one NCA.

As this new framework falls into place for public sector staff, financial services firms may need to adjust their systems and controls as well as onboarding documentation to ensure they can manage compliance accordingly.

About us

PwC Legal is assisting a number of financial services firms and market participants in forward planning for changes stemming from these proposals.

If you would like to discuss any of the developments mentioned above, or how they may affect your business more generally, please contact any of our key contacts or PwC Legal's RegCORE Team via de_regcore@pwc.com or our website.

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