



Banc Ceannais na hÉireann  
Central Bank of Ireland

Eurosystem

**CP 120**

**Second Consultation Paper on the  
Corporate Governance Requirements for  
Investment Firms and Market Operators**

# CONSULTATION PAPER 120

## Contents

Introduction .....	3
Submission of Responses.....	4
1. Definitions .....	5
2. Scope and Effective Date .....	7
3. Legal Basis .....	8
4. Composition of the Board .....	9
5. Chairman.....	10
6. Committees of the Board .....	11

## Introduction

The Central Bank of Ireland (the Central Bank) is committed to strengthening corporate governance standards and practices across the financial services industry. Through its supervisory engagement with Firms, the Central Bank has identified corporate governance deficiencies whereby poor corporate governance structures have resulted in Firms being exposed to increased risks. These deficiencies have contributed towards undermining board effectiveness, prudent management, good culture, strong risk management and oversight, and the safety and soundness of these Firms.

As a result of these governance deficiencies and taking into consideration developments relating to corporate governance in other sectors, a Consultation Paper (CP 94) was issued by the Central Bank in 2015 which proposed a range of corporate governance requirements for Firms (the Requirements). At the time, it was noted that the imposition of the Requirements would be subject to the transposition and coming into effect of Directive 2014/65/EU (MiFID II) and Regulation (EU) No 600/2014 (MiFIR). Subsequent to the publication of CP 94, the European Commission elected to delay the implementation of MiFID II and MiFIR by 12 months until 3 January 2018. The delay in implementing MiFID II and MiFIR resulted in delay in national transposition and in finalising the Requirements.

Given the recent implementation of MiFID II the Central Bank now wishes to finalise the Requirements in order to provide clarity to the industry and promote the highest standards of corporate governance within Firms.

The Requirements have been updated (the revised Requirements) to take into consideration the final provisions of European Union (Markets in Financial Instruments) Regulations 2017 (S.I. No. 375 of 2017) (the MiFID II Regulations), the delegated acts issued under MiFID II (the Delegated Acts) and the joint EBA and ESMA Guidelines on the assessment of the suitability of members of the management body and key function holders dated 26 September 2017 (including the additional ESMA Guidelines on the management body of market operators and data reporting service providers dated 28 September 2017) (the EBA and ESMA Guidelines). The revised Requirements outlined in this document therefore should be read in conjunction with the MiFID II Regulations, the Delegated Acts and the EBA and ESMA Guidelines.

In addition, the responses received in relation to CP 94 have been taken into consideration. The proportionality approach has remained as per CP 94, therefore the revised Requirements will apply to Firms authorised by the Central Bank that are designated as High, Medium High or Medium Low Impact

under the Central Bank's Probability Risk Impact System (PRISM)<sup>1</sup> and will not apply to Firms designated as Low Impact. However, Low Impact Firms are encouraged to adopt these revised Requirements consistent with best practice.

## Submission of Responses

The Central Bank welcomes responses on Consultation Paper 120 from all stakeholders, in particular relating to the appropriateness of the proposed requirements set out overleaf and also regarding the scope of the revised Requirements and the application of the principle of proportionality. Where a respondent agrees or disagrees with a proposal, he/she should set out reasoned arguments as to why the proposal is appropriate or inappropriate.

Responses can be submitted by email to: [CP120@centralbank.ie](mailto:CP120@centralbank.ie) or in writing, to:

Consultation Paper 120 on Corporate Governance Requirements for Investment Firms and Market Operators

Financial Risks and Governance Policy Division

Central Bank of Ireland

PO Box 559

Dublin 1

Responses should be submitted no later than **31 July 2018**. It is the policy of the Central Bank to publish all responses to consultations on the Central Bank's website. Confidential information should not be included in consultation responses.

**Financial Risks and Governance Policy Division**

**Central Bank of Ireland**

**10 May 2018**

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<sup>1</sup> For further information on PRISM, please refer to the Central Bank publication entitled 'PRISM Explained' which can be found on the Central Bank's website.

## 1. Definitions

The following is a list of definitions of terms used in the Requirements:

**Control functions:** collectively, the internal audit function, the risk management function and the compliance function.

**Corporate governance:** the procedures, processes and attitudes according to which an organisation is directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among the different participants in the organisation – such as the board, managers, shareholders and other stakeholders – and lays down the rules and procedures for decision-making.

**Director independence:** the ability to exercise sound judgement and decision making independent of the views of management, political interests or inappropriate outside interests.

The following criteria shall be considered and given reasonable weight when assessing director independence:

- Any financial or other obligation the individual may have to the Firm or its directors;
- Whether the individual is or has been employed by the Firm or a group entity in the past and the post(s) so held;
- Whether the individual is or has been a provider of professional services to the Firm in the recent past;
- Whether the individual represents a significant shareholder;
- Circumstances where the individual has acted as an independent non-executive director of the Firm for extended periods;
- Any additional remuneration received in addition to the director's fee, related directorships or shareholdings in the Firm; and
- Any close business or personal relationship with any of the Firm's directors or senior employees.

**Firm:**

- A MiFID Firm; or
- A non-retail investment intermediary, as defined in part (b) of the definition of "investment business firm" in regulation 2(1) of the Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) (Investment Firms) Regulations 2017, S.I. No. 604 of 2017).

**Group director:** A group director may be an executive, an executive director, a non-executive director or an independent non-executive director of an entity within the group.

**High Impact / Medium High Impact / Medium Low Impact:** in relation to a Firm, the Firm's designation as either High Impact, Medium High Impact or Medium Low Impact, respectively, under the Central Bank's Probability Risk Impact System (PRISM)<sup>2</sup>.

**Independent non-executive director:** a non-executive director who satisfies the criteria for director independence.

**MiFID II:** Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014.

**MiFID Firm:** an investment firm or a market operator authorised under Directive 2004/39/EC (MiFID) or under MiFID II.

**Non-executive director:** means a director without executive management responsibilities for the Firm or, in the case of a Firm which is part of a group, who may have executive management responsibilities assigned to him or her within the group.

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<sup>2</sup> For further information on PRISM, please refer to the Central Bank publication entitled 'PRISM Explained' which can be found on the Central Bank's website.

## 2. Scope and Effective Date

- 2.1. The Corporate Governance Requirements for Investment Firms and Market Operators (the Requirements) apply to all Firms authorised by the Central Bank of Ireland (the Central Bank) that are designated as High, Medium High or Medium Low Impact (the Relevant Firms).
- 2.2. The Requirements will not apply to Firms designated as Low Impact by the Central Bank. However, such Firms are encouraged to adopt these Requirements.
- 2.3. The Requirements will not apply to foreign incorporated subsidiaries of an Irish Firm. Such Firms are encouraged, however, to adopt equivalent good corporate governance practices.
- 2.4. The Requirements apply to the Relevant Firms with effect from 1 July 2019.

### 3. Legal Basis

- 3.1. Having regard to the MiFID II regime, these Requirements are conditions to which Relevant Firms are subject pursuant to Regulation 8 of the MiFID II Regulations or section 10(13) of the Investment Intermediaries Act 1995 as applicable.
- 3.2. The Requirements may be amended or supplemented by the Central Bank from time to time.
- 3.3. These Requirements are imposed in addition to, and shall not affect, any other corporate governance obligations and standards to which a Firm is subject otherwise than under these Requirements and other conditions and/or requirements set out in the licence or authorisation of a Firm. If a conflict arises between the Requirements and another corporate governance obligation or standard, the stricter of the obligations or standards should be met so as to ensure compliance with both sets of obligations.
- 3.4. A contravention of the Requirements may result in the Central Bank using any of its supervisory or enforcement powers, including, but not limited to, any or all of the following:
  - The imposition of an administrative sanction under Part IIIC of the Central Bank Act 1942 for failure to comply with a condition of authorisation;
  - The exercise of powers in respect of pre-approval controlled function or controlled function holders under Central Bank Reform Act 2010.



## 4. Composition of the Board

- 4.1. A Firm shall ensure that the board is of sufficient size and expertise to oversee adequately the operations of the Firm.
- 4.2. A Firm shall ensure that the board is composed of a majority of independent non-executive directors.
- 4.3. By way of exception to the general requirement, specified in Section 4.2, in the case of Firms that are subsidiaries of groups, the majority of the board of such subsidiary may also be composed of a following combination subject to the PRISM Impact of the Firm:
  - In the case of High Impact Firms, the majority of the board may be composed of group directors and independent non-executive directors provided that in all cases the Firm shall have at least three independent non-executive directors;
  - In the case of Medium High Impact Firms, the majority of the board may be composed of group directors and independent non-executive directors provided that in all cases the Firm shall have at least two independent non-executive directors;
  - In the case of Medium Low Impact Firms, the majority of the board may be composed of group directors and independent non-executive directors provided that in all cases the Firm shall have at least one independent non-executive director.

In any case the Central Bank retains the discretion to require that the Firm shall have a greater number of independent non-executive directors than specified in this Section.

- 4.4. Group directors shall act critically and independently so as to exercise objective and independent judgement.

## 5. Chairman

- 5.1. A Firm shall ensure that there is a Chairman appointed to the board of the Firm.
- 5.2. A Firm shall ensure that the Chairman has relevant financial services expertise, qualifications and experience, or be required to undertake comprehensive, relevant and timely training. In this context, relevant financial services expertise, qualifications and experience or training shall mean that the Chairman has the necessary knowledge, skills and experience and/or training required to comprehend each of the following:
- The nature of the Firm's business, activities and related risks;
  - His or her individual direct and indirect responsibilities and the board's responsibilities;  
and
  - The Firm's financial information.
- 5.3. A Firm shall ensure that the Chairman shall be an independent non-executive director. By way of exception to this general requirement, in the case of a Firm that is a subsidiary, the Chairman may be a group director. If a deputy Chairman is required, the role shall be taken by an independent non-executive director or in the case of a subsidiary, may be taken by a group director.

## 6. Committees of the Board

- 6.1. Firms shall ensure, subject to Section 6.4 below, that the board establishes, at a minimum, both an audit and a risk committee.
- 6.2. High Impact Firms shall ensure, subject to Section 6.24 below, that the board establishes a remuneration committee.
- 6.3. In the case of Medium Low and Medium High Impact Firms, where the board comprises 5 or less members, the full board, including the Chairman and the Chief Executive Officer, may act as the audit committee and/or the risk committee. The Firm shall ensure that the board does not carry out such functions in the absence of having obtained the Central Bank's prior approval in writing to do so. In such cases Sections 6.13 and 6.19 continue to apply. Minutes of these meetings shall reflect that the board was sitting as the audit committee or as the risk committee.
- 6.4. Where a Medium Low and Medium High Impact Firm is part of a wider group which has a group audit committee and/or a group risk committee, the Firm may rely on those committees, provided that the board is satisfied that they are appropriate to the specific circumstances of the Firm, and that the board has documented its assessment in this regard.
- 6.5. The board is responsible for the oversight of each of its committees. A Firm shall ensure that, in deciding whether or not to establish a board committee, the board would, in the absence of establishing that committee, continue to have appropriate time available to it, to adequately discharge its responsibilities.
- 6.6. A Firm shall ensure that the non-executive directors and in particular the independent non-executive directors play a leading role in these committees or where the functions are carried out at group level, they play a leading role in satisfying the board that the firm's audit and risk functions are adequately carried out.
- 6.7. A Firm shall ensure that the audit committee and risk committee shall have at least one shared member.
- 6.8. A Firm shall ensure that when appointing committee members, the board assesses and satisfies itself as to the relevant expertise and skills of members and as to their ability to commit appropriate time to the committee.

- 6.9. A Firm shall ensure that committee membership is reviewed by the Firm and subject to renewal by the Firm with an appropriate frequency. The renewal frequency shall consider the balance of experience and independence required.
- 6.10. A Firm shall ensure that cross-committee membership by an individual is managed by the Firm to ensure that no one individual exercises excessive influence or control over the activities of one or more committees.

### Terms of Reference

- 6.11. A Firm shall ensure that it establishes clear written terms of reference for the board and each committee which outline the authority, functions, membership, and reporting lines of the board and each committee as well as meeting frequency, voting rights and quorums.
- 6.12. A Firm shall ensure that the board and each committee regularly reviews its terms of reference to ensure their continuing appropriateness, and that each committee provides recommendations on revisions to its terms of reference to the board, where the committee deems necessary. A Firm shall ensure that such reviews are documented and that they take place at least annually.

### Audit Committee

- 6.13. A Firm shall ensure that the Chairman of the audit committee is an independent non-executive director.
- 6.14. A Firm shall ensure that the audit committee is composed of non-executive directors, including at least one independent non-executive director.
- 6.15. A Firm shall ensure that the audit committee as a whole has relevant financial experience and at least one member has an appropriate qualification.
- 6.16. A Firm shall ensure that neither the Chairman nor the Chief Executive Officer shall be a member of the audit committee.
- 6.17. A Firm shall ensure that the attendance by the Chief Executive Officer or Chairman at audit committee meetings shall be by invitation only and shall be managed to ensure the independence of the committee and the maintenance of appropriate relationships with other parties, especially external auditors.

- 6.18. A Firm shall ensure that the audit committee operates in a manner consistent with ensuring its independence and reports its activities and decisions to the board of directors.

### Risk Committee

- 6.19. A Firm shall ensure that the Chairman of the risk committee is a non-executive director or an independent non-executive director.
- 6.20. A Firm shall ensure that the risk committee is composed of a majority of non-executive directors or independent non-executive directors or a combination of both.
- 6.21. A High Impact Firm shall ensure that no single individual will hold the position of Chairman of the audit committee and Chairman of the risk committee simultaneously.

### Remuneration Committee

- 6.22. A Firm shall ensure that the Chairman of the board is not also the Chairman of the remuneration committee.
- 6.23. A Firm shall ensure that, where possible, all members of the remuneration committee are independent non-executive directors but, in any event, that the majority of members of the committee are independent non-executive directors.
- 6.24. Where a High Impact Firm is part of a wider group which has a group remuneration committee, the Firm may rely on that committee, provided that the board is satisfied that it is appropriate to the specific circumstances of the Firm, and that the board has documented its assessment in this regard. In this circumstance, the Firm shall promptly inform the Central Bank of this decision. The Central Bank retains the discretion to require the Firm to establish its own remuneration committee.



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