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**PIRC RESPONSE TO THE CONSULTATION ON
THE CORPORATE GOVERNANCE
REQUIREMENTS FOR INVESTMENT FIRMS AND
MARKET OPERATORS IN IRELAND**

ABOUT PIRC

PIRC provides a variety of corporate governance research, advisory and data analysis services to institutional investors. These include research on governance standards and compliance among listed companies, analysis of general meeting resolutions and proxy voting advice in line with PIRC policies. PIRC also provides customised client templates and interpretation of client policies, outsourced vote execution, reporting on proxy voting activity and auditing of third party actions.

Since the inception of PIRC's Corporate Governance Service, PIRC has argued that corporate governance best practice has been an important element in reducing the risk of corporate failure and enhancing shareholder returns over the long-term.

PIRC considers that investors have a responsibility to develop consistent, informed and fair corporate governance policies which are relevant to the particularities of the market and promote good practice across it, as well as at individual companies.

PIRC RESPONSE TO THE CONSULTATION

The Irish Central Bank is seeking consultation on the revised requirements which promote the highest standards of corporate governance within firms following the recent transposition of the MiFID II regulations. The Central Bank has welcomed responses on Consultation Paper 120¹, relating to the appropriateness of the proposed requirements. PIRC has provided its views of each requirement whilst factoring the latest transpositions.

1. Definitions

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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.

PIRC's view: Mostly agreed. Regarding the terms under requirement 2.2, PIRC does not consider that the market capitalization of a public company should limit its approach to corporate governance, as smaller companies also have a need for sufficient independent representation.

¹ "Second Consultation Paper on the Corporate Governance Requirements for Investment Firms and Market Operators", Last accessed 05 July 2018, <https://www.centralbank.ie/docs/default-source/publications/Consultation-Papers/cp120/cp120--second-consultation-paper-on-the-corporate-governance-requirements-for-investment-firms-and-market-operators.pdf?sfvrsn=4>

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.

PIRC's view: Agreed, no comments.

4. Composition

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.

PIRC's views: It is believed there should be more specification regarding sufficient size of the board by the Central Bank. PIRC considers that the Board should be of sufficient size so that the requirements of the business can be met and that changes to the board's composition, and that of its committees, can be managed without undue disruption, and should not be so large as to be unwieldy. PIRC considers this principle in respect of boards that are significantly larger or smaller than the average of seven or eight directors. With regards to section 4.2, PIRC believes that the Board should include an appropriate combination of executive and independent non-executive directors to the point that no individual or small group of individuals can dominate the Board's decision taking.

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.

PIRC's view: PIRC supports any provision where the Chair should meet the definition of independence upon appointment. It is believed that a chairman that does not meet said provisions is likely to have difficulty in effectively fulfilling at least some of the Chairman's roles.

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.

PIRC's view: PIRC considers that for the purpose of best practice, the main Board committees (that is, the audit, remuneration and nomination committees) should be exclusively comprised of independent directors. Whilst the terms under section 6.16 state that neither the Chairman nor the Chief Executive Officer shall be members of the audit committee, there are concerns as these terms have not been stipulated for the remuneration committee. PIRC believes that executives should only attend meetings by the remuneration committee at the request of the committee and for relevant periods of the meetings. In addition, in section 6.14 there is no clear instruction that at least the majority of the members of the audit committee should be independent (which would be in line with the EU Audit Directive and considered the very minimum in terms of best practice). While section 6.13 recommends that the chair of the committee be independent, which is welcomed, audit committees under section 6.14 could still comprise a majority of directors not considered to be independent.

For more information relating to the content of this document, or to request a copy of PIRC's shareholder voting guidelines, please email info@pirc.co.uk.

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