



The Corporate Governance
Association of Ireland

Arthur Cox Building
Earlsfort Terrace
Dublin 2
Ireland

secretary@cgai.ie

Prudential Policy Unit
International Credit Institutions
Financial Regulator
PO Box 9138
Dame Street
Dublin 2

June 23, 2010

Re: Consultation Paper 41 ‘Corporate Governance Requirements for Credit Institutions and Insurance Undertakings’ (‘CP41’)

Dear Sir or Madam,

Please accept this letter and attachments as the response of the Corporate Governance Association of Ireland (‘CGAI’) to CP41. As you may know, the CGAI (website: www.cgai.ie) is a professional association of members certified in corporate governance post-graduate studies. The CGAI’s aim is to promote best practice in governance across the commercial, public and voluntary sectors.

Further to recent events, the CGAI recognizes the need for the Financial Regulator to codify certain governance practices in the banking and insurance sectors in Ireland. It should be noted that codification is but a small element in the area of good governance. Good governance emanates from the demonstrated objective mindset of all individuals charged with decision making. Good governance is ultimately about the behavior of individuals. This includes both board members and senior management. In that regard, the CGAI would expect greater reliance be placed on the ‘Fitness and Probity’ tests’ than on codified governance rules.

In general, the CGAI welcomes CP41 but points to the area of PROPORTIONALITY where it considers CP41 to be deficient. CGAI believes that proportionality should be absolutely centre stage in CP41 and overriding to many provisions contained in CP41. It appears to the CGAI that CP41 assumes that all Institutions are of a size, complexity and risk profile equivalent to an institution that is of systemic importance to Ireland. Quite clearly the vast majority of Institutions do not fit this profile. CGAI

suggests that the Financial Regulator apply the provisions of CP41 to named institutions of ‘systemic’ importance. For all other Institutions, governance plans should be prepared by Institutions and approved by the Financial Regulator on a case by case basis. Such plans being specific to that Institution but based on the general underlying principles contained in CP41.

The CGAI believes that all Institutions should be required to document how they have sought to achieve governance excellence in a manner proportionate to their scale. The annual report should refer to the extent to which Institutions have taken account of emerging best practice, whether by reference to other codes or legislative provisions, or best practice in other institutions.

The CGAI believes that an active ongoing engagement between the FR and Institutions will best provide for sound governance in those Institutions. Otherwise, CP41 may unwittingly become the catalyst for ‘box ticking’ practices rather than its true intent of being of real and lasting value.

We attach specific observations and recommendation in a schedule hereto. We would welcome the opportunity to discuss any issues raised in this letter further with the Financial Regulator.

Yours sincerely,

Jerry J Kelly,
Chairman.

Schedule I: CGAI's observations and specific recommendations on CP41

PROPOSAL 1.2 (Summary):

We note the intent to draw up a governance code for the funds industry. In that regard, we draw the Regulator's attention again to the Governance Code published by the CGAI entitled "Code of Corporate Governance for Independent Directors of Investment Funds" (a copy of which is attached as Appendix 1)

REPORTING TO FINANCIAL REGULATOR 4.2 (Summary):

At what level within the Institution once knowledge of such an event becomes known does the 5 day clock begin? CGAI propose that this time requirement only becomes effective once such deviations have been confirmed by the Chief Compliance Officer (or such other designated person).

CONSULTATION PAPER

1.2.

We wish to stress our agreement with the two sentences of 1.2. Effective boards will be made up of competent people operating within appropriate structures and procedures and, above all, exhibiting appropriate behavior.

1.5

Corporate Governance: This definition should include "policies" in addition to "procedures, processes and attitudes...." This is recommended because all boards direct and provide oversight primarily through policies adopted by the board. This definition should be expanded to include the concepts of Responsibility, Authority and Accountability – three concepts which need to be defined appropriately to facilitate effective governance.

1.5

Director Independence: reference to cross-directorships should be added.

1.5

Control Functions: Add "legal" to the list of functions.

3.2

The second and third sentences might be re-worded to read: "Senior management play an important part at all times in ensuring effective governance because senior

managers are responsible for implementing the board's policies". It is not the role of senior management to provide oversight.

4.1.a:

We do not believe there is a need to require wholly owned subsidiaries of regulated Institutions to appoint an Independent Chairman, as such Institutions operate to their shareholders' (parent company's) mandates. These Institution may operate more effectively by being chaired by a non-executive (who might be an executive elsewhere in the group) rather than an independent director. In such cases, the CGAI recommends the appointment of a Senior Independent Director within the board of the Institution.

4.2.

We agree with the principle of non-executive involvement in all board decisions but, as drafted, this may lead to an undesirable practice of excessive sub-committee delegation.

4.4., 4.5. and 4.6.:

We strongly support the provision in 4.4. However, 4.5 and 4.6 attempt to hardcode the number of board memberships in seeking to achieve this aim. We believe that this is totally inappropriate. We believe that ALL directors should be adequately able to demonstrate both to the Institution and the Regulator that he/she has adequate time to achieve the principle outlined in 4.4.

5.6.

There are many cases (e.g., wholly owned subsidiaries of both foreign and domestic institutions) where the appointment of an independent chairman clearly could be counterproductive and ineffective. In such cases, we recommend the appointment of a Senior Independent Director.

5.7.

Given that Board always has the option of removing the Chairman, we believe that such appointments should be for a period of 3 years in order to provide continuity.

8.3

The word 'abdicate' is probably what was intended rather than 'abrogate'?

9.5.

We strongly support the concept of regular board evaluation. However, greater clarity is required from the Regular as to the accepted mechanics of such evaluation and to issues such as FOI requests and potential defamation proceedings.

10.2

We believe that this provision may be impractical as many stakeholders (every single employee, as an example) may not readily understand risk implications of complex financial products and transactions. We believe that the risk appetite definition should be agreed and understood by the board, management and, critically, the Financial Regulator.

11.3.

We are concerned that the imposition of this provision will lead to ‘Group Think’ i.e., good decisions may go unmade so as to avoid dissent. The requirement to have all discussions (as distinct from decisions) documented in detailed minutes is particularly excessive.

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Institutions should be required to document the Main Risks facing the Institution and to have the board review the list annually and report that it has done so. This provision is intended to secure board engagement in oversight of implementation of 18.4.

21.1.

We believe that it is critical for the Financial Regulator to be aware of the potential cost and effectiveness implications of going down the Sarbanes Oxley route, which this provision has the potential to do. The content of the guidelines will be critical. Facilitation of box-ticking should be avoided as much as possible. A requirement for narrative content may elicit better information on behavior.

The CGAI believes Institutions should be required by the Financial Regulator to produce a Crisis Plan from time to time to demonstrate how a serious financial or reputational risk would be handled. This should be linked to risk management procedures and the Main Risks facing the Institution.