Davy House, 49 Dawson Street, Dublin 2, Ireland
T +353 1 679 7788 F +353 1 679 6423 davy@davy.ie www.davy.ie

DAVY

Prudential Policy Unit
International Credit Institutions
Financial Regulator
PO Box 9138
College Green
Dublin 2

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Consultation Paper CP41

We understand the impetus behind the proposals set down by the Financial Regulator in its consultation paper CP 41 entitled "corporate governance requirements for credit institutions and insurance undertakings". While we note that this paper was specifically tailored with those entities in mind, we also welcome the opportunity to make a submission on behalf of investment firms on the content of same.

Our submission seeks to set out the fundamental differences between credit institutions and insurance undertakings (otherwise known as "institutions") on the one hand and investment firms on the other, details of which are set out below. We do not consider it appropriate that this proposal be extended to investment firms. We believe that any discussion as to the application of further corporate governance requirements for investment firms should be properly considered in the context of industry-specific risks which relate to the business of investment firms. Further, any review of the corporate governance arrangements in place for investment firms would be better informed following due consideration of the structures and the ownership arrangements which are currently in place.

It should be noted that even within that category of "investment firms", a number of sub-categories exist, namely certain firms form part of a larger institution and may form part of an entity which itself is quoted on one or more stock exchanges. Others are smaller owner-managed businesses which provide investment business services to its clients, and do not represent contagion risk for a parent entity.

It should be noted that none of the owner-manager firms in Ireland are quoted entities. The owners of such businesses are generally employees of the firm and some hold executive board positions. Given that the livelihood and the equity of those very individuals is at stake in the proper management and control of the firm, risk management of the activities of the firm is always a significant focal point.

In respect to Davy for example, the board includes three non-executive directors and the firm already has in place Audit and Compliance Committees. Membership of both committees is confined to non-executive directors and they are both chaired by independent non-executive directors.

Investment firms differ from institutions in a number of respects:

1. Banks are a fundamental intrinsic component of the financial system, with their essential role being to connect those who have capital (such as investors or depositors), with those who are seeking capital (such as individuals wanting a loan, or businesses wanting to grow). On the other hand, investment firms are involved in the provision of investment business services regarding various securities and assets to meet specified investment goals for the benefit of their clients.

2. It is widely acknowledged that credit institutions are of systemic importance to the functioning of the wider financial system as means of providing capital and credit. Investment firms on the other hand are not generally regarded as being of systemic importance.

3. The importance of banks is even more clearly pronounced for those which are members of the clearing and payment systems. A failure by any credit institution would have a negative and possibly even a catastrophic impact on the functioning of the wider financial system. By contrast, as already stated the function of investment firms is simply to provide investment business services to its clients.

4. All client assets (deposits or policyholder funds) are reflected on the balance sheet of credit institutions and the debtor/creditor relationship comes into force between the institution and the customer. In investment firms, all customer assets are entirely held off balance sheet in ring-fenced client asset accounts. These accounts are themselves subject to detailed prescriptive rules as set out in the Client Asset Requirements. The rules stipulate that an independent audit and report of same must be issued to the Financial Regulator every six months.

5. Furthermore, the Capital Requirements Directive, and in turn the Internal Capital Asset Requirements for regulated financial services firms as set down by the Financial Regulator themselves clearly recognise and acknowledge the fundamental differences in the risk dynamics of institutions and investment firms.

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Due to these fundamental differences, we do not consider that the views reflected in this consultation paper should apply to investment firms. We would consider it prudent that any proposed discussion as to the application of corporate governance requirements to investment firms should be considered in the context of the specific risks relating to the individual business of the investment firms. Furthermore, as already outlined above, it is difficult to treat all investment firms in the same manner due to the different structures and ownership arrangements in place.

For these reasons we would suggest that it would be appropriate in discussions and consultations for the Financial Regulator to engage with a representative group of independently owned investment firms on the proposals for corporate governance requirements. We would be happy to assist in putting such a group together.

We trust that this submission letter provides some valuable input to this consultative process and we are happy to discuss the content of same in more detail with you if required.

Yours sincerely

Ger Knowles

Ger Knowles
Head of Regulation & Compliance