

Our ref: CMcD/ec

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Risk, Governance and Accounting Policy Division,
Central Bank of Ireland,
P.O. Box 559,
Dame Street,
Dublin 2

RE: RESPONSE TO CONSULTATION PAPER CP 69- REVIEW OF THE CORPORATE GOVERNANCE CODE FOR CREDIT INSTITUTIONS AND INSURANCE UNDERTAKINGS

Dear Sir/ Madam,

Firstly, we would like to welcome the opportunity to make submissions in relation to Consultation Paper 69 ('CP69') on the review of the Corporate Governance Code for Credit Institutions and Insurance Undertakings ('the Code'). As part of our review of CP 69, we looked closely at the existing associated Corporate Governance regime, introduced in Ireland in 2010. We also considered the Corporate Governance regulatory environment in similar jurisdictions and considered elements of the UK Corporate Governance Code, formerly the Combined Code.

In Part A and Part B, we will address the queries posed within the 'Summary of More Significant Changes' and the 'Specific Areas for Comment' respectively and the underlying rationale and general principles that need to be addressed. Part B comprises our comments and questions on individual aspects of the proposed amendments.

PART A: SUMMARY OF MORE SIGNIFICANT CHANGES

Risk Committee

The Central Bank is seeking to understand whether this amendment would be seen to be proportionate in the context of institutions' operations and current practice.

We welcome this proposal and consider that a risk committee would benefit in terms of effectiveness and independence by being composed of a majority of Non-executive Directors. Consideration may be given by the CBI to increasing this in respect of high impact firms, to align with other regulations such as the Capital Requirements Directive IV, by advising that the committee be entirely composed of Non-Executive Directors.

The appointment of the CRO

We agree that the requirement to appoint of a CRO is a positive inclusion in the Code, particularly in respect of high risk firms. We would note however, that this amendment may cause some potential issues for smaller low risk firms, who may face significant challenges when attempting to appoint an existing member of staff to the role and effectively demonstrate their competence to undertake this PCF role. A transition period may be appropriate here or CRO's who lack the appropriate competence may be permitted to perform the role subject to agreeing an appropriate and time bound education and/or mentoring programme.

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D. Murray
R.J. Nolan
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B. O'Callaghan
M. Reilly
K. Sheehan
C. Treacy
N.A. Walsh

P. Brennan
D.J. Butler
P. Cronin
P. Cullen
M. Glynn
N. Griffin
C. Hynes
J. O'Connor

D. O'Donovan
J. O'Flynn
D. Power
P. Reck
M. Sheehan
J. Whelan
P. Whelan

D. Carson
D. Dalton
A. Flanagan
M. Flynn
H. Goddard
D.F. Hearn
C.P. Hughes
D. Lehane
S. Mohan
C. O'Connell
D. O'Flanagan

B. Jennings



Section 12.8 of the revised code provides that the CRO would report to the Board Risk Committee while also having direct access to the Chairman of the Board. We would suggest that to increase the oversight in this context it would be appropriate for the CRO to also maintain a secondary reporting line to the CEO, in addition to the primary reporting line to the Committee.

Board Meetings

Having reviewed feedback received from supervisors and institutions regarding the practical, operational and strategic issues surrounding the implementation of this requirement, the Central Bank invites comments on this requirement.

We note that to maintain effective oversight and achieve successful governance high impact firms will be required to meet frequently. It is our view that effective governance would dictate that meetings would take place as and when they are required within the context of each particular company. The imposition of such a quantitative obligation reverts to a 'tick box' generic approach to governance rather than encouraging a risk based tailored approach. Instead boards should be required to demonstrate, if required by the CBI, why it believed the number of meetings it held were effective and appropriate.

Should the quantitative obligations be retained by the CBI, and as , it is noted that a higher number of meetings may be required to take place at certain periods of the year, we would suggest that the requirement for high impact firms be aligned with that of that of lower impact firms as set out in the revised Section 16.1.

Chairman

In general we welcome this amendment in respect of a Chairman operating in a group company structure. It is also noted that this is in line with the more recent relaxation in such requirements from an international perspective as the revised versions of the UK code have omitted the recommendation that the Board Chairman chair only one FTSE 100 company.

PART B: SPECIFIC AREAS FOR COMMENT

Composition of the Board

The Central Bank is seeking specific feedback from respondents as to whether a provision in relation to diversity requirements should be introduced into the Code and, if so, the nature of any such requirement.

As set out in the consultation paper the issue of diversity, and in particular gender diversity, has been an area of much discussion in the past number of years with a variety of measures undertaken across the globe ranging from obligatory quotas to optional considerations. Legislative, regulatory and voluntary solutions have all been adopted to various degrees within different jurisdictions and across corporate structures in an effort to reduce the "phenomenon of groupthink" through increased diversity in board appointments.

We refer to the principle set out in the UK Corporate Governance Code 2012¹ that gender is one of a range of diversity factors which should be considered when determining board composition and appointments. It is widely accepted that board diversity is a positive concept and key to a board's ability to function effectively leveraging off different skill sets, experiences, qualifications, nationalities and gender to maximise understandings, identify different perspectives and balance the decision making process. We agree with this concept of diversity to the extent that it makes the board more effective, however, we consider that gender is but one factor in the context of the board selection process. It is our

¹ "The search for board candidates should be conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender."

view that the spirit of the existing code sought to move away from a 'tick box' approach to governance by requiring institutions to take a holistic view of their corporate governance arrangements.

On this basis, a more appropriate test would require the board to demonstrate that it operates effectively and one criteria in this regard would be composition of the board. Diversity will be a consideration in this regard but other factors such as experience, background and challenge of board members may lead to better decisions.

For example diversity can help overcome groupthink but equally, if not implemented correctly, can lead to malfunctioning disparate board. We would point out that there has been significant progress in increasing female representation on UK Boards in the wake of the 2011 Davies report, without the imposition of regulatory requirements. Since 2010, female board appointments have increased by nearly 50%.

We do appreciate that there is an increased global awareness of the fact that female board members are significantly in the minority and there would be merit in the introduction of appropriate measures to address this inequality. We feel that this may be achieved without increasing the significant challenges already faced in the area of board composition, and suggest below possible options for consideration.

1. Option A

Obligation on the Board to report annually in respect of how it has operated effectively as a group. This could include an appropriate boardroom diversity policy, including the measurable objectives it has met in the period. Such a report should form part of the annual compliance statement.

2. Option B

Obligation on the Board to introduce a policy on board composition effectiveness including gender diversity requiring the issue to be considered and documented in respect of each appointment.

Directorship Limits

The Central Bank invites your comments on how this requirement has operated and if the limits are appropriate.

We appreciate that time is a finite resource which poses a realistic constraint for Directors in accepting Board invitations and understand that Board membership must be considered in the context of their ability to effectively complete their responsibilities.

The introduction of board limitations has been met with a mixed reaction from the financial services industry. Director feedback has indicated that they have had more time to concentrate on their roles in the period since the introduction of the code and this must be seen as a positive associated outcome of these provisions. However, as a corollary to this, these time limitations have also had the associated effect of limiting the supply of appropriate Directors in the market. Ireland's anomalous quantitative approach does not sit easily with the limited pool of suitable candidates in Ireland, compared to larger markets. Institutions have commented that these restrictions have resulted in increased difficulties in making appropriate appointments to the Board and that this issue is compounded by the timelines surrounding pre-approval obligations under the 'Fitness and Probity' regime. The current 'one size fits all' quantitative approach omits to consider other time pressures a Director may face such as their employment status. Under the current regime, an unemployed person is treated the same as an employed person, however their availability would be entirely different. The application of the limitations has also caused a degree of confusion for institutions as a Director may be present on a variety of Boards with various risk profiles both inside and outside the financial services sector and it is unclear how therefore these limitations would apply. Furthermore, quantitative limitations are not conducive to the ideals of board diversity.

While we agree that quantitative *guidance* is beneficial to avoid the over-stretching of Director's time, we would note that Ireland is exceptional in the application of such restrictions in this context. To address the issues identified within the industry, while retaining the benefits of the provisions, we would suggest the replacement of the current quantitative limitations with quantitative guidance supported by an obligation to document each appointment in this context. Institutions would be obliged to complete a case by case analysis of the time resources and Directorships occupied by each Director at appointment and at any stage thereafter where that Director undertakes a new role. This analysis would accompany each application for approval as a PCF 1, 2, 3 and 8. This amendment would streamline the existing process whereby Directors hold a mixture of financial and non-financial roles within high and low risk organisations. Each appointment would be made in the context of the specifications of the individual role, the availability of the appointed person and the overall composition of the Board resulting in a more diverse and effective appointment.

General Comments

To enhance the code, the CBI could consider the introduction of a positive obligation to demonstrate that it has been established appropriately and has operated in an effective manner. This could include items such as robust challenge or the rejection of ideas based on regulatory considerations.

To increase the oversight, consideration may be given to the possible assignment by the Board of specific responsibilities to Directors. They would take the role of championing their assigned subjects to ensure an appropriate consideration is given by the Board to key issues. It is important to note that this championship scheme should not divert from the normal functioning of the Board or serve to personalise or diminish responsibility for issues which the Board retains as a whole.

PART C: DETAILED COMMENTS AND OBSERVATIONS

This part of our response takes individual provisions of CP69 and documents comments on those provisions.

Provision	Comments
<p>Section 3.6</p> <p>"... If a conflict arises between the Code and another corporate governance obligation or standard, the stricter of the obligations or standards should be met so as to ensure compliance with all sets of obligations. "</p>	<p>It is not always possible to meet both obligations. For example, a situation may arise where by meeting one obligation it may be possible to breach another. Clarity in respect of such scenarios would be welcomed.</p>
<p>Section 4.2</p> <p>"Any institution which becomes aware of a material deviation from this Code shall within 5 business days report the deviation to the Central Bank, advising of the background and the proposed remedial action. "</p>	<p>Further clarity in respect of this provision would be useful.</p> <p>It is unclear as to what constitutes 'aware' i.e. is it knowledge of the facts or actual knowledge?</p> <p>It is unclear what is meant by the institution in this context. Does it refer to the Board, Senior Management, persons occupying PCF roles etc.</p> <p>What constitutes a 'material' deviation? Would it be appropriate to align this with the risk rating on the register?</p>

Provision	Comments
<p>Section 6.3 "...The system of governance shall promote an appropriate risk culture at all levels of the institution and shall be subject to regular internal review."</p>	<p>We would suggest the rewording of this paragraph to "The system of governance shall communicate and promote..." for the sake of clarity.</p> <p>As a 'risk culture' can be challenging to define, we would suggest that this be replaced with a 'Risk Appetite Statement, supported by the associated policies and procedures'.</p>
<p>Section 7.5 "Directors should attend each board meeting in person wherever possible. However, due to the location of some directors, physical attendance may not always be possible, in which case videoconferencing or teleconferencing is permissible."</p>	<p>We would suggest the inclusion of the following words. "...and such Directors will be considered to be in attendance for these purposes under the Code"</p>
<p>Section 7.6 "An institution shall ensure a majority of its directors are reasonably available to the Central Bank at short notice, if so required. "</p>	<p>We would suggest that the definition of 'available' should be expanded to include availability by telephone, conference or in person.</p>
<p>Section 7.8 and 7.9</p>	<p>As stated above, Directors will often hold a variety of Directorships across different types of organisations. Therefore, additional clarity would be welcomed in respect of the application of these limitations in such circumstances.</p>
<p>Section 8.11 "... However, in the case of institutions which are not designated as High Impact institutions and are subsidiaries of groups, the Chairman may also hold the position of Chairman of a credit institution or insurance undertaking or reinsurance undertaking (including those authorised outside of the State) simultaneously provided that these roles reside within the group and the Chairman has sufficient time available to fulfil his or her role and function as the Chairman of an institution. The prior approval of the Central Bank shall be obtained prior to the Chairman assuming any such additional roles."</p>	<p>Further clarity in respect of the wording here would be appreciated in this context, as it is unclear whether the chairman of the group entity may also be chairman of the subsidiaries or if the chairman may only occupy the role of chairman in the subsidiaries.</p>
<p>Section 12 – Chief Risk Officer</p>	<p>Is there a restriction on the CRO also occupying the role of the CRO in another entity or subsidiary?</p>
<p>Section 12.8 "The CRO shall report to the board risk committee with direct access to the Chairman of the board."</p>	<p>Guidance would be welcomed in respect of who would set the CRO rewards and staffing/resource provisions.</p>

Provision	Comments
<p>Section 15.8 “The board shall ensure that it identifies risks to be addressed by contingency plans based on the areas where it considers the institution to be especially vulnerable and that these are reviewed, updated and tested on a regular basis.”</p>	<p>Guidance would be welcomed in respect of what constitutes ‘especially vulnerable’.</p>
<p>Section 15.1 “The board shall meet as often as is appropriate to fulfil its responsibilities effectively and prudently, reflective of the nature, scale and complexity of the institution. In any event, the board shall meet at least 11 times during any calendar year and at least once per calendar month for 11 months of the year.”</p>	<p>To align with the proposed changes set out at 16.1 to increase flexibility, we would suggest that this requirement be amended to require the Board to meet five or six times in each half year period, with a minimum of 11 meeting in each calendar year.</p>
<p>Section 20 – General Requirements of Committees</p>	<p>Guidance would be welcomed in respect of whether it would be appropriate for a single person to be on all sub-committees of the Board.</p>
<p>Section 23.5 “The audit committee as a whole shall have relevant financial experience and at least one member shall have an appropriate qualification.”</p>	<p>The wording here may be mis-interpreted as one member not being required to have the relevant financial experience.</p> <p>Question: Should this be recent and relevant experience?</p>
<p>Section 23.5 “The risk committee as a whole shall have relevant financial experience. “</p>	<p>We would suggest the inclusion of risk in this statement: “The risk committee as a whole shall have relevant risk and financial experience.”</p> <p>Again, should this state recent and relevant experience?</p>

Thank you for considering our response to CP69 and we would welcome the opportunity to engage further with you in relation to this consultation.

Yours faithfully,



Colm McDonnell
 Partner