

## Consultation on Corporate Governance Requirements for Investment Firms

### Consultation Paper 94

#### Response from Susquehanna International Securities Limited

Susquehanna International Securities Limited (“SIS” or “we”) is an investment firm and is regulated by the Central Bank of Ireland (“CBI”) under SI No 60 of 2007 – European Communities (Markets in Financial Instruments) Regulations 2007.

SIS has, since 2012, had a written corporate governance policy in order to ensure that all material aspects of its corporate governance are clearly and demonstrably in line with the EBA’s “Guidelines on Internal Governance” and best industry practise.

Adoption of the Central Bank of Ireland’s “Consultation on Corporate Governance Requirements for Investment Firms- Consultation Paper 94” (“CP 94 requirements”) as presented would require material alterations by SIS to its existing corporate governance policy and procedures and SIS therefore believes that it is apposite for it to comment on the suitability and scope of the proposed CP 94 requirements and the application of the principle of proportionality in relation thereto.

In the comments below we have utilised the same numbering and headings as used in CP 94 and have quoted (in *italics*) the relevant section of CP94 to which we are referring for ease of reference.

### Comments

#### **Introduction**

*“It is proposed that the requirements will apply to all Markets in Financial Instruments Directive (‘MiFID’) firms and non-retail investment intermediaries licensed or authorised by the Central Bank of Ireland (‘firms’) that are designated as High, Medium High or Medium Low Impact under the Central Bank’s Probability Risk Impact System (‘PRISM’). While MiFID II and CRD IV introduce new corporate governance requirements for investment firms, the requirements herein are intended to supplement these.”*

We believe that the blanket application of the all of the proposed CP 94 requirements across all MiFID firms designated as high, medium-high or medium low impact under PRISM is disproportionate, given (i) the breadth and diversity in the nature, scale, complexity and potential impact of the activities carried out by these disparate firms and (ii) the already extensive obligations that these firms have with respect to Corporate Governance under MiFID II, CRD IV and the CBI’s existing corporate governance requirements .

The proposed CP 94 requirements are detailed, prescriptive in their language and will be burdensome on all firms to implement. Furthermore, failure by a firm to comply with any provision of the proposed CP 94 requirements, whether it be an inadvertent or de minimis failure, will be a breach of a statutory instrument and as such leave the firm liable to sanction and reputational damage. The possibility of such

sanction and its knock-on consequences will themselves operate to increase the risk of doing business for firms in Ireland. We do not believe that the stated aims of the CBI justify the imposition of such a mandatory and detailed corporate governance regime without substantial application of the principle of proportionality. We believe that the necessary levels of corporate governance for firms can be achieved by way of the existing obligations and powers of the Central Bank.

## **1. Scope**

*“Additional requirements (as set out in Appendix 1) upon all firms designated as High or Medium High Impact by the Central Bank.”*

We believe that the blanket imposition of the additional requirements set out in Appendix 1 on all firms designated as High or Medium-High Impact by the Central Bank is disproportionate as it takes no account of the broad nature, scale and complexity of the activities of such firms and instead considers only a single aspect of the firm’s nature – its PRISM impact rating. Considering only one aspect of an Investment Firm’s nature is clearly at odds with the proportionality requirements set out in MiFID II and CRD IV. In addition the mandatory nature of the application of the requirements would seem in general to be at odds with any attempt at a proportionate implementation of the CP 94 requirements.

## **2. Definitions**

### **Director independence**

***Director independence:** the ability of a director to exercise sound judgement and decision making independent of the views of other directors or managers, political interests or inappropriate outside interests.*

We believe that the criteria set out for consideration of the independence of a director should not include the criteria regarding whether the “individual represents a significant shareholder”. We do not believe that this criteria is appropriate or helpful given the generally accepted purpose of the appointment of independent non-executive directors, that is, to bring an objective and external perspective to the Board which is independent of the management of the firm. Directors with links to significant shareholders are, we believe, demonstrably capable of bringing an objective and external perspective to the Board which is independent of the firm’s management. Excluding such Directors from the criteria of independence will, given the CP 94 requirements set out in sections 6.1 and 6.2 of Appendix 1 make it substantially more difficult for a shareholder to appoint such a director (without increasing the size of the Board to an impractical extent) and thereby exercise an extremely effective mechanism for shareholder oversight.

Moreover there is no evidence to suggest and the CBI has offered no such evidence that a Director who represents a shareholder(s) can be considered to be any less independent of management or to carry out their roles in a manner which is likely to be deleterious to the stated aims of the CP 94 requirements.

#### **4. Reporting to the Central Bank**

*4.2 Any firm that becomes aware of a material deviation from these requirements shall without undue delay and in any event within 5 business days report the deviation to the Central Bank, advising of the background and the proposed remedial action.*

*4.3 Each firm shall submit an annual compliance statement as set out at Section 24, in accordance with any guidelines issued by the Central Bank, specifying whether the firm has complied with the requirements.*

We would ask that the CBI give further details regarding the appropriate materiality threshold that should be applied by firms with respect to both reporting of deviations and the preparation of the proposed annual compliance statement. Without such guidance it remains up to each individual firm to interpret the materiality threshold in a vacuum. This will inevitably lead to the uneven application of the CP 94 requirements across the industry and leave firms taking a conservative approach at a disadvantage to those with a more generous interpretation of the materiality threshold. Leaving such threshold entirely undefined will effectively lead to more conscientious firms facing an increased regulatory burden.

Furthermore with respect to the Annual Compliance Statement as set out in Section 24, is unclear what purpose such statement serves. As an firm is already required under Section 4.2 to report any material deviation from the CP 94 requirements, what will be the compliance statement achieve other than to reiterate the firms material compliance with the CP 94 requirements or to restate any material deviation as previously reported?

#### **5. General Requirements**

*5.7 A firm shall ensure that any director who has any material concern about the corporate governance of the firm shall be required to report the concern without delay to the board in the first instance and if the concern is not satisfactorily addressed by the board within 5 business days, the director shall be required to promptly report the concern directly to the Central Bank advising of the background to the concern and any proposed remedial action. This is without prejudice to the director's ability to report the concern directly to the Central Bank at any stage.*

It is unclear how the firm can ensure the reporting by a director of such concerns. We believe that this requirement should be restated such that the firm would require any director to report such material concern to the Board.

*5.9 A firm shall ensure that it discloses in its annual report that it is subject to these requirements.*

It is unclear to us what this requirement is attempting to achieve. The fact that a firm will be subject to the CP 94 requirements will be a matter of law and should not require restatement in the annual financial statements. We believe the CBI should avoid the layering of excessively detailed yet largely unnecessary requirements within the CP 94 requirements. Such requirements add nothing to the effective corporate governance of the firm but increase the administrative burden of compliance and the risk of inadvertent breach of the CP 94 requirements.

## **6. Composition of the Board**

*6.6 A firm shall ensure that each member of the board devotes sufficient time to the role of director and associated responsibilities, and that each director's letter of appointment to the board shall clearly stipulate his or her annual time commitment to the firm. The firm shall also ensure that a sufficient time buffer is included in each director's annual time commitment to provide for any irregular occurrences that may emerge throughout the year, and that each director is required to disclose in writing to the board any other time commitments they may have and any subsequent changes to these commitments.*

Given that the obligation to devote sufficient time to the role of Director and associated responsibilities is an obligation of the Director, it is unclear how the firm can ensure compliance with this.

*6.11 A firm shall ensure that a formal review of board membership is carried out by the board at least once every three years. A firm shall ensure that its policy in relation to the frequency with which board membership is renewed shall be documented and that the renewal frequency shall consider the balance of experience and independence required.*

We are uncertain what this requirement is attempting to achieve. What would such a formal review of board membership actually consist of and what would it aim to achieve? In reality each Director's membership of the Board of a firm is under continual review and where the performance of a Director is believed to be unsatisfactory that is not going to be something which arises by reason of a three yearly review. We believe the CBI should avoid the layering of excessively detailed mandatory requirements within the CP 94 requirements. Such requirements add nothing to the effective corporate governance of the firm but increase the administrative burden of compliance and the risk of inadvertent breach of the CP 94 requirements.

*6.12 A firm shall in circumstances where an independent non-executive director of a firm:*  
*(1) has been a member of the board of that firm for nine years or more at the time of the imposition of these requirements, or*

*(2) reaches nine years of membership of the board of that firm at any time following the imposition of these requirements (which period of membership shall be calculated so as to include time spent as a member of the board prior to the imposition of these requirements),*

*ensure that a formal review of that individual's membership of the board is carried out at the next scheduled board meeting of the firm and shall document its rationale for any continuance of the membership of that board member and so advise the Central Bank in writing.*

As with section 6.11 above, we believe that the addition of such detailed mandatory regulations into the CP 94 requirements adds nothing to the effective corporate governance of a firm but greatly increases administrative burden and legal risk of compliance. A requirement to review such membership "at the next scheduled board meeting" after the passing of (an arbitrary) 9 year period is extremely difficult to schedule for and guarantee that such a potentially distant anniversary is recognised. Obviously a breach of such a requirement could have serious consequences for a firm and we believe that the CBI should, in considering the CP 94 requirements, endeavour to formulate them giving consideration to the practicalities of the implementation.

## **7. Chairman**

*7.2 A firm shall ensure that the Chairman leads the board, encourages critical discussions, challenges mindsets and ensures effective communication between executive and non-executive directors.*

Given that the manner in which a Chairman leads a Board is not something that a firm can control we do not believe that firm should have such obligation. It is unclear how the firm can ensure compliance with this.

*7.5 A firm shall ensure that the Chairman shall attend and chair board meetings.*

Given that the Chairman of the Board is not likely to be available for every board meeting, the CP 94 requirements should provide for the appointment and utilisation of a vice-chairman who is a group director. This section should also clarify that attendance of the chairman by electronic means (conference call or video link) is permissible.

*7.9 A firm shall ensure that the prior approval of the Central Bank shall be obtained prior to the Chairman taking on any other directorships (other than within the group), as the responsibilities and required time commitment for a Chairman may be significant.*

We believe that this requirement should be removed from the CP 94 requirements for the following reasons:

- a. The requirement is disproportionate to the amount of time that an additional directorship is likely to consume. For example no such prior approval is required for the Chairman taking up new employment or additional roles within existing employment or any number of other activities which could consume substantially more of the Chairman's time;

- b. The requirement disproportionately affects the Chairman of the Board. Whereas the Chairman is likely to have a somewhat higher time commitment than the other Directors of the Board is not clear that in a well-functioning board this requirement is much greater than that of an ordinary board member. This would be particularly the case where the Chairman is a group Director;
- c. The requirement for such a prior approval is a requirement which could greatly fetter the Chairman's ability to earn a livelihood and will make the Chairman's role substantially less attractive. An INED or group director is less likely to accept the role of Chairman if the possibility exists that such role will prevent him/her from accepting new INED positions or joining a board in an executive capacity;
- d. The addition of this requirement for prior approval adds a further administrative burden which must be monitored and leaves the company open to sanction in the event that the Chairman doesn't notify the Company promptly of such an appointment. The addition of such burden should be weighed against the expected gain that the requirements will bring in terms of improved corporate governance;
- e. As the firm will be in a better position than the CBI to assess the time impact of any additional directorships on the Chairman's performance, this matter should be reserved to the Board of the firm;
- f. The CBI has offered no details of the criteria by which they will make the decision whether or not to grant such an approval. By preserving for itself such unfettered powers the CBI is acting disproportionately and increasing the burden and risk of compliance on firms.

*7.10 A firm shall ensure that no individual who has been the CEO, an executive director or a member of senior management of the firm during the previous 5 years shall advance to the role of Chairman of that firm.*

We believe that the five-year period is disproportionately long and risks the loss of retired executive's expertise to the board.

## **8. Chief Executive Officer**

*8.4 A firm shall ensure that the CEO's contract is reviewed by the board on renewal and at least once every 5 years.*

Where a firm is part of a larger group the CEOs contract is likely to be fixed/negotiated at a group level and as such would not be suitable for review by the Board. We believe therefore that an exemption should be made with respect to CEOs of subsidiary firms.

## **9. Independent Non-Executive Directors**

*9.2 A firm shall ensure that independent non-executive directors are identified clearly in the firm's annual report.*

As with section 6.11 & 6.12 above, we believe that the addition of such detailed mandatory regulations into the CP 94 requirements adds nothing to the effective corporate governance of a firm but increases administrative burden and legal risk of compliance. A breach of such a requirement could have serious consequences for a firm and we believe that the CBI should, in considering the CP 94 requirements, endeavour to formulate them giving consideration to the administrative burden and legal risk created by adding such requirements against the expected gain that the requirements will bring in terms of improved corporate governance.

*9.5 A firm shall ensure that dedicated support is made available to independent non-executive directors on any matter requiring additional and/or separate assistance to that available in the normal board process.*

We would query why such support would be “dedicated” to the independent non-executive directors and would not be made available to the group directors and executive directors? We believe that this requirement would be better formulated by the removal of the reference to dedicated.

## **10. Non-Executive Directors and Executive Directors**

*10.5 A firm shall ensure that dedicated support is made available to non-executive and executive directors on any matter requiring additional and/or separate assistance to that available in the normal board process.*

We would query whether this “dedicated” support is the same or separate from that being made available under section 9.5. We believe that this requirement would be better formulated by the removal of the reference to dedicated.

## **12. Appointments**

*12.1 A firm shall ensure that the board is responsible for appointing a CEO and senior management with appropriate integrity and adequate knowledge, experience, skill and competence for their roles.*

Within a group context it is not realistic to expect that the Board of a subsidiary firm would be responsible for appointing the CEO and senior management of the subsidiary. Within a group context such appointments are likely to span multiple subsidiaries and the decisions with respect to such appointment will be made at a group level. At best it may be possible that the board of the firm would be able to ratify such appointments.

*12.7 A firm shall ensure that the board puts an appropriate succession plan in place in relation to the board.*

The CBI should provide further elaboration as to what is required in such an “appropriate succession plan”.

*12.9 A firm shall ensure that the board, or nomination committee where one exists, establishes a written policy on diversity with regard to the selection of persons for nomination to become directors.*

It is unclear to us how the introduction of the mandatory requirement for such a diversity policy is within the remit of the CBI in the context of the stated aims of the CP 94 requirements. We would also reiterate the points made above in respect of 6.11, 6.12 and 9.2.

### **13. Risk Appetite**

*13.8 A firm shall ensure that the board identifies risks to be addressed by contingency plans based on, inter-alia:*

- The areas where the board considers the firm to be especially vulnerable;*
- The risk appetite of the firm; and*
- The risk management system of the firm.*

*The firm shall also ensure that such contingency plans are reviewed, updated and tested on a regular basis and at least annually.*

We believe that the CBI should provide further detail in the CP 94 requirements regarding the requirement to produce contingency plans. The current wording doesn't provide sufficient detail to allow a firm be certain of its compliance with the requirements to produce such plans.

### **14. Board Meetings**

*14.2 A firm shall ensure that a detailed agenda of items for consideration at each board meeting, together with minutes of the previous board meeting, are circulated in advance of each board meeting to allow all directors adequate time to consider the material, and that sufficient and clear supporting information and papers are also circulated.*

While we agree that it is desirable that a detailed agenda together with minutes of the previous board meeting are circulated prior to each board meeting there may be circumstances where the production of both of these documents is not practical prior to an urgent board meeting. If the CP 94 requirements make the production of such documents mandatory before every board meeting then this will adversely affect administrative flexibility of the Board. Firms should not be made to



choose between the compliance with this requirement and their ability to hold an urgent board meeting. For example, if a requirement to hold an urgent board meeting arises hours after the previous meeting concluded, then under the CP 94 requirements it would not be possible for such a meeting to be held until a detailed agenda and the draft minutes of the previous meeting were prepared and circulated to the directors.

## **17. Committees of the Board**

*17.1 A firm shall ensure, subject to paragraph 17.2 below, that the board establishes, at a minimum, both an audit committee and a risk committee. Where the board comprises only 3 members, the full board, including the Chairman and CEO, may act as the audit committee and/or the risk committee. In such cases Section 20.3 and 21.3 continues to apply. Minutes of these meetings shall reflect that the board was sitting as the audit committee, or risk committee. The firm shall ensure that the board retains responsibility for the oversight of each of its committees.*

*17.5 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.*

It is unclear from these 2 sections whether the CP 94 requirements will mandate the establishment of an audit committee and a risk committee. Can the full board decide to retain the audit monitoring and risk monitoring functions for itself or will delegation to a board committee be mandatory. Furthermore it is unclear from the CP 94 requirements whether board committees must be comprised of only directors of the firm or whether they can also be made up of other employees of the firm or group? We believe that in order to allow for the correct balance of skills on any committee it would be important to allow committee membership by non-board members.

## **18. General Requirements of Committees of the Board**

*18.8 A firm shall ensure that committees report regularly to the board and that the minutes of all committee meetings are circulated to the board in advance of board meetings.*

We believe that practically speaking compliance with this CP 94 requirement is going to be administratively very difficult given the number of committees, and the frequency and timing of both committee and board meetings. This requirement also raises the same issues as section 14.2 regarding the flexibility to hold urgent meetings.

## **20. Audit Committee**

*20.2 A firm shall ensure that the audit committee is composed of non-executive directors, including at least one independent non-executive member.*

As set out above in respect of sections 17.1 and 17.5, is unclear in the current CP 94 requirements whether the Board can retain the function of audit review for the full board whether it is mandated to delegate this to an audit committee. We note that section 21.1 of the CP 94 requirements permits a firm to “propose to the Central Bank that the board itself carry on the function which would otherwise be delegated to a risk committee”. No such specific delegation is provided for in respect of the audit committee. We believe that such an explicit derogation from the audit committee requirements should be provided for.

In addition it is unclear from section 20.2 whether any executive directors can be included in the membership of the audit committee.

## **21. Risk Committee**

*21.1 A firm shall ensure that the board establishes a risk committee which is separate from the audit committee and which has responsibility for oversight and advice to the board on the current risk exposures of the firm and its future risk strategy. A firm may propose to the Central Bank that the board itself carry out the functions which would otherwise be delegated to a risk committee but 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.*

We would agree with the CBI’s proposal that firms should be permitted to retain the risk management oversight at the board level. We believe however that the CP 94 requirements should provide additional detail regarding the criterion the CBI would utilise in deciding whether to grant approval for the retention of the risk management oversight at the board level. Without such detail it is not possible for a firm to determine whether or how it should approach such an issue.

## **24. Compliance Statement**

*24.1 A firm shall submit to the Central Bank a compliance statement specifying, in accordance with any relevant guideline issued by the Bank, whether the firm has complied with the requirements during the period to which the statement relates. This compliance statement shall be submitted to the Central Bank on an annual basis or with such other frequency as the Central Bank may notify to the firm from time to time. In the event of the firm deviating materially from the requirements, the compliance report shall include a report on any material deviations, advising of the background to the breach and the actual or proposed remedial action.*

As set out above, in respect of section 4.3 of the CP 94 requirements, it is unclear to us what purpose such a compliance statement serves, given the existing obligations under the CP 94 requirements that any material deviation is reported to the CBI. Can the CBI clarify what additional information it is hoping to gain from the production of such a compliance statement? As stated

above in respect of sections 6.11, 6.12 and 9.2 we believe that the imposition of material burdens on firms where there is no obvious gain in respect of corporate governance should be something that the CBI avoids.

## **Appendix 1 to the Corporate Governance Requirements for Firms**

### **Additional requirements on High and Medium High Impact firms**

#### **6. Composition of the Board**

*6.1 A firm shall ensure that its board is of sufficient size and expertise to oversee adequately the operations of the firm, and in any event shall ensure that its board is comprised of a minimum of five directors. In particular, the board shall comprise sufficient representation by executive directors to ensure that it is not dominated by one individual executive;*

*6.2 A firm shall ensure that the board is comprised of a majority of independent non-executive directors. By way of exception from this general requirement, in the case of firms that are subsidiaries of groups, the majority of the board may be composed of a combination of group directors and independent non-executive directors, provided that in all cases the subsidiary shall have at least two independent non-executive directors or such greater number as is required by the Central Bank. Group directors shall act critically and independently so as to exercise objective and independent judgement.*

With respect to sections 6.1 and 6.2 the CBI appears to be endeavouring to achieve two incongruent aims, firstly that the Board has a substantial representation of executive directors and secondly that the Board is a majority composed of independent (and/or group directors). It should be noted however that attempts to achieve the former of these aims would require the addition of sufficient executive directors to dilute any possible dominance of one individual director whereas a simultaneous attempt to achieve the latter aim would require the addition of large numbers of independent or group directors to counterbalance the additional executive directors. Achieving both such aims will inevitably lead to the Board growing to an unwieldy size, reduce administrative flexibility, increase cost, dilute the level of expertise contained in the Board. We believe that the requirement to have a majority of independent non-executive is and/or group directors is misplaced and will lead to a reduction in the efficacy of the board.

#### **12. Appointments**

*12.6 A firm shall ensure that the board formally reviews its overall performance and the performance of individual directors, relative to the board's objectives, at least annually, and documents all such reviews. The firm shall ensure that an evaluation by an external evaluator is undertaken every three years and that the evaluation is provided to the Central Bank. Where the external evaluation is critical of the performance of the board, the Central Bank reserves the right to increase the frequency of subsequent evaluations until acceptable performance is noted.*

We believe that the CP 94 requirement for the mandatory evaluation of the Board by an external evaluator is unnecessary. The requirement to engage such an external evaluator will be a substantial drain on management, board and administrative resources, a distraction from the business of running the firm and be a substantial recurring cost. We cannot foresee that such an external evaluator will add value to the corporate governance of the firm particularly in light of the rigorous and detailed requirements that have been mandated by the CBI in the CP 94 requirements (together with the existing requirements of the CBI, CRD and MiFID). The CP 94 requirements as set out already require the Board to report immediately on any material deficiencies in the corporate governance regime. We believe that the CBI should at a minimum carry out a cost benefit analysis on how such a regular external evaluation could be considered worthwhile. Additionally with respect of a firm which is a group subsidiary the use of an external evaluation is even less likely to improve the corporate governance of the firm.

## **17. Committees of the Board**

*17.1 A firm shall ensure that subject to paragraph 17.2 below and the following exception in relation to firms which are part of a group, a firm that is High Impact or Medium High Impact shall ensure that the board establishes audit, risk, remuneration and nomination committees. Where a firm is part of a wider group, where remuneration and nomination committees exist, it may decide to utilise the group's committees and not to establish separate remuneration and nomination committees. In those circumstances, the firm shall promptly inform the Central Bank of this decision. Notwithstanding any decision by the firm to utilise the group's remuneration and nomination committees, the Central Bank retains the discretion to require the firm to establish its own remuneration and nomination committees. The firm shall ensure that no single individual holds the positions of chairman of the audit committee and chairman of the risk committee simultaneously. The firm shall ensure that the board retains responsibility for the oversight of each of its committees.*

We believe that the CBI should provide additional clarification as to the make-up and function of the remuneration and nomination committees. In the context of a group it is inconceivable that a subsidiary entity could have its own meaningfully independent remuneration and nomination committees and therefore we believe that the exception is essential for a group subsidiary.

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