



Governance, Accounting and Auditing Policy Division
Policy and Risk Directorate
Central Bank of Ireland
PO Box 559
College Green
Dublin 2

20th May 2011

Dear Sir/Madam

DIMA thanks the Central Bank of Ireland (CBI) for the opportunity to respond to its proposals for a revised fitness and probity regime for the financial services sector. It is essential for the proper governance and control of regulated entities that the individuals responsible for running or otherwise fulfilling a key function within such entities be of good repute and integrity, appropriately qualified, experienced and knowledgeable. As with many other aspects of the regulatory regime, it is also imperative that such requirements be applied in a proportional manner, reflecting the demands of the role and institution, rather than as a swingeing “one size fits all” approach. We are assured to see that the CBI retains proportionality as a tenet of its establishment and that the concept of proportionality is embodied within the consultation paper. The distinction between major and non-major institutions as defined in the corporate governance code for credit institutions and insurance entities published in 2010 provides a guide for assessing proportionality, alongside the differentiation between retail and wholesale entities.

DIMA comprises almost 70 insurers, reinsurers and captive managers engaged in international business from an Irish base. All our members currently are in the process of restructuring their operations in the run-up to the implementation of the Solvency II Directive on 1st January 2013, including fitness and probity requirements as outlined in Article 42 of the Level 1 text. Although CEIOPS provided advice around Level 2 measures on system of governance to the European Commission in October 2009, the final advice from the Commission is still awaited; this will form the basis for governance requirements across the whole European re/insurance industry. It is imperative that any requirements imposed in advance of the implementation of Solvency II by the CBI are not “out of line” with the Level 2 measures; neither should they be in excess of future European requirements, particularly since there is a stated aim that the future re/insurance regulatory landscape should be one of maximum harmonisation. It is worth noting at this juncture that the Level 2 advice provided by CEIOPS on system of governance and specifically directed at fit and proper requirements is still high level in nature. It is expected that there will be a Level 3 consultation paper dealing with systems of governance which will include fitness and probity within its remit; it is still, however, unclear when EIOPA will issue that consultation, and there is a distinct possibility that this may not happen until 2012.

In addition, we note that the International Association of Insurance Supervisors (IAIS) has undertaken a programme of updating its Insurance Core Principles (ICP), including “ICP 5 Suitability of Persons”. ICP 5 was adopted at the IAIS 2010 general meeting and is effective from October 2011. We note that ICP 5 includes the concept of “Significant Owners”. The IAIS

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defines a “significant owner” as “a person (legal or natural) that directly or indirectly, alone or with an associate, exercises control over the insurer.” This definition appears to be in excess of the provisions within the proposals for Controlled Functions as published in the CBI’s consultation paper (CP51), and the concept of “significant owner” is not referred to in CP51. We also note that in general, the requirements as described in ICP 5 are significantly less detailed and prescriptive than the proposals issued by the CBI in CP51.

General comments on CP51

The proposals within CP51 will ultimately result in a Statutory Instrument making regulations, rather than regulatory guidance which has generally been the outcome of consultation by the CBI and its predecessor. The consultation paper proposed a swift implementation date of 1st September 2011; we encourage the CBI to prioritise content and substance over an excessively demanding timeline, and to consider lengthening the implementation timeframe to ensure that industry can properly and effectively implement the new regime.

Industry is willing to enhance the proposed regulations by developing, in conjunction with the CBI, a non-binding best practice regime to cover areas where further guidance might otherwise be sought from the CBI. This will remove the burden of developing non-statutory guidance from the CBI, while enabling it to engage with industry to produce standards which achieve the regulatory aims in a practical and timely manner.

Currently, entities regulated by the CBI are covered by the Fit and Proper Requirements published in December 2008. Industry anticipates that the proposals outlined by the current consultation paper will supersede the entirety of the existing requirements. However, it is recommended that if this is the case, it is stated explicitly in the CBI’s communications around the new requirements.

The CBI’s consultation does not address issues likely to be faced by the majority of regulated entities with regard to legal issues such as existing contracts of employment for those in either Pre-approval Controlled Functions (PCFs) or Controlled Functions (CFs). Numerous factors include the ramifications to an individual’s Constitutional right to a living (Article 45, 2 (i) of the Constitution of Ireland – Bunreacht na hÉireann). Such factors need to be carefully considered in advance of implementation to ensure that the proposals within the consultation paper are not antithetical to existing rights and legislation. We would also encourage the CBI to ensure that requirements under the proposals for individuals to answer questions or produce documents which would be liable to expose those individuals to criminal charge are not subject to privilege.

Under the proposed structure of the new regime, covered institutions will not be allowed to make an employment offer to an individual until that individual has been approved by the CBI. There is no scope for organisations to make conditional offers, although this is widely used in practice in other employment contexts; if this structure is maintained, it will naturally result in a diminishing number of individuals being employed as CFs and PCFs. We understand that it is not within the CBI’s authority to remove this requirement; however, we suggest the CBI liaise with the Department of Finance to seek an amendment to the Central Bank Reform Act 2010 to remove this requirement.



There are general concerns over the length of time the authorisation process may take within the CBI. As these requirements are particularly pertinent during the recruitment process, which generally is a time-critical exercise, it is proposed that the CBI develop a service level response time environment for fitness and probity applications, with specific timelines for each stage of the process. Industry is willing to assist in the development of such an environment.

Where the CBI has identified jurisdictions which have a similar regime, it is proposed that an “equivalence” approach be taken so that an individual who has received an authorisation from another regulatory body can automatically receive an authorisation from the CBI, and *vice versa*. This type of approach is already adopted in several sectors (*vide* Society of Actuaries in Ireland, Chartered Accountants Ireland, Institute of Engineers of Ireland, Irish Taxation Institute, Law Society of Ireland) and would naturally commence with agreements with other European Member States and jurisdictions which were viewed as possessing equivalent regimes, perhaps under Solvency II criteria.

A number of companies operate outsourced models where CFs and PCFs are outsourced and not performed by employees of the regulated entity in Ireland. These functions may be outsourced to group companies or third party service providers and may be located in Ireland or outside of Ireland. In addition, the entity employing the outsourced CF/PCF may or may not be regulated itself. It is unclear how a company should deal with this situation. Where a group function is already covered by outsourcing guidelines and the approvals process in their home jurisdiction, a passporting type arrangement as outlined in the previous paragraph could provide a solution. Where such an arrangement cannot be established, it is recommended that regulated entities are entrusted to make a practical interpretation.

The Central Bank Reform Act 2010 provides for an appeals process for the benefit of individuals who are not approved by the CBI. However, it is not clear within the proposed regime how such an appeals process would be constructed or operated. It is only right and proper that an individual whose application is not upheld by the CBI has both the opportunity to learn the grounds on which such a decision has been taken, and has the option to challenge such a decision. This is particularly pertinent since an individual who has been declined previously by the CBI will need to disclose this in the future, where the CBI’s reasoning may have been, for example, one of lack of experience rather than a concern over issues such as personal integrity.

This consultation paper refers to a new online Individual Questionnaire (IQ) which is an intrinsic part of the Fit and Proper application process. It appears from the consultation that this form will be an enhanced version of the current IQ, and we would request the CBI consider that the form itself be the subject of consultation as well as collaboration to ensure the online system operates effectively.

Issues arise from the consultation paper around the attitude and treatment of an individual’s physical and mental abilities, which may be difficult and sensitive to deal with. It is more appropriate for an organisation to assess the ability of an individual to fulfil their duties, under established HR practices. If there were a requirement to dismiss a person from a CF on the basis of physical and/or mental abilities, this could lead to an action under the Employment Equality Acts 1998 and 2007. In addition, there may be difficulties in monitoring an individual’s management of their own financial affairs, which may be further complicated through data



protection issues. Circumstances beyond an individual's control may have resulted in what could be perceived as mismanagement; in addition, such requirements would imply that regulated entities would be required to undertake monitoring activity, for example undertaking Irish Credit Bureau (ICB) checks.

We note that the CBI refers to the "State" in several places in this consultation paper. We read this word as referring solely to the Republic of Ireland and no other State. In addition, where the paper refers to "State support", we read this as a reference to the State support for Irish domestic banks solely and not to other forms of State support such as grant aid.

Detailed comments

Section 2: Central Bank Reform Act, 2010

3 (b)

Without a definitive timeframe in which the CBI will commit to provide a decision about designating an individual as approved or not as fit and proper, it will be difficult for entities to undertake an efficient recruitment process. It is recommended that the CBI provide a specific timeframe of ten working days for this.

3 (d)

The Act gives the CBI the power to designate positions as Controlled Functions (CFs). Schedule 1 outlines the functions to be considered CFs by using the wording of Section 20(2) of the Act. It is important the scope of CFs be kept focussed to minimise unnecessary administration which could be a significant burden.

3 (e)

The CBI should clarify the minimum level of due diligence of firms, bearing in mind issues around the timing of new appointments of PCFs and potential limitations on independent verification of appointee information.

3 (f)

As stated elsewhere in this submission, it is vital that the CBI provides a written reason in the event that it decides to refuse to appoint an individual to a PCF or suspend, remove or prohibit an individual from carrying out a CF, to both the individual and the institution.

Section 3: Purpose of this consultation

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Industry welcomes the CBI's commitment to adopting a proportionate and risk-based approach in the use of its powers. To this end, a clarification from the CBI as to how and when it will assess within a firm the roles which are to be prescribed as PCFs would be welcomed, based on the firm's size and complexity, and the reporting lines of the CFs.



Section 4: Terminology and legal basis

Controlled Functions

For clarity we would request the CBI indicate the functions that fall within each of the three categories of function that the CBI is permitted to prescribe as CF roles – significant influence roles, compliance roles and minimum competency roles (Section 20 (2) of the Act) – and give the basis upon which each function has been categorised.

It is unclear how the CBI will deal with individuals carrying out CFs outside the State, by Group entities and outsourced functions. It is proposed that the CBI considers where the responsibility for fitness and probity of outsourced activities should lie. We submit that this is the responsibility of the outsourced regulated entity outside the State with due diligence being conducted on the regulated entity rather than the individual performing the outsourced activity.

Pre-approved Controlled Functions

The CBI's proposal (9a) that it "must approve in writing the appointment of a person to a PCF before a firm can offer to appoint that person to the function" would have the consequence of an individual being required to complete the PCF approval process in advance of being offered a role within an organisation. Many of the individuals which would be appropriate for PCFs are senior, highly qualified and highly experienced, and their expertise may be directed to non-regulated firms or firms in other jurisdictions should a lengthy process be undertaken in advance of an offer of employment be made. Thus we propose the CBI seek to have the position amended to enable a conditional employment offer to be made, subject to the individual receiving approval by the CBI.

For clarity, we would request the CBI indicates the basis on which it has concluded that the Schedule 2 roles, other than Director, CEO and Secretary, have been designated as significant influence roles and therefore prescribed as PCFs on an industry-wide basis.

It is proposed that the CBI clarify when and how it will assess at a particular firm level the roles within the firm that are to be prescribed as PCFs (as provided for under Section 22(3) and (4) (a) (iv) of the Act) based on the firm's size/complexity and the reporting lines of the firm's CFs.

It is proposed that the CBI specify the types of functions (on an industry wide basis or by reference to a particular class or classes of firm) that fall within each of the three categories set out in the Act (Section 20 (2) (a)-(c)) giving the basis on which each function has been so categorised. The CBI should clarify when and how it will assess at a particular firm level the roles within the firm that are to be prescribed as PCFs (as provided for under Section 22 (3) and (4) (a) (iv) of the Act) based on the firm's size/complexity and the reporting lines of the firm's CFs.

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The consultation paper refers to the fitness and probity and level of vetting for roles or functions outside the CFs and PCFs being a matter for firms, "subject of course to complying with the



required standards of fitness and probity”. It is not clear what these required standards would be since the roles are not captured within the fitness and probity regime.

It is proposed that industry wide CFs should comprise: Director, CEO, Secretary, Partner, Sole Trader, Head of Underwriting, designated Investment Officer, designated Actuary, designated Risk Management Officer, designated Compliance Manager, Internal Audit or Financial Control, Minimum Competency Roles.

It is proposed that industry wide PCFs should comprise: Director, CEO, CFO, Secretary, Partner, Sole Trader, Head of Underwriting, Investment and Chief Actuary.

The CBI should clarify when and how it will assess at a particular firm level the roles within the firm that are to be prescribed as PCFs (as provided for under Section 22 (3) and (4) (a) (iv) of the Act) based on the firm’s size/complexity and the reporting lines of the firm’s CFs.

It is proposed that in addition to tailoring the level of due diligence to the function being filled or maintained the required due diligence should also be tailored to the size/complexity of the firm where the role resides. In the circumstance where an entity has been designated a major institution under the corporate governance code, or otherwise give rise to systemic risk, this could govern the extent to which additional PCFs are required.

The CBI refers in (i.c.) to Section 20(2)(c) of the Act. This refers to a function being prescribed as a CF in relation to the provision of a financial service and, among other things, the giving of advice or assistance to a customer, and responsibility for dealing in or having control over a customer’s property. These responsibilities are clearly with regard to consumer interaction and thus it should be stated that these provisions do not apply to wholesale business.

The CBI asks whether it should provide non-statutory guidance on what it considers to be appropriate levels or types of due diligence. Industry would be willing to develop a non-binding best practice regime in conjunction with the CBI to achieve this aim.

Section 5: Standards of Fitness and Probity

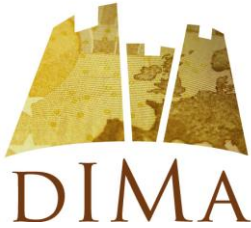
Fitness – competence and capability

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The capabilities referred to in this paragraph may be better achieved through on the job training and performance rather than at the point of recruitment. In addition, the proposals in this paragraph could prevent career progression.

20 paragraph 1 bullet 3

This should be amended to read that person has “sound knowledge of financial services” rather than “the business”. If the proposal remains in its current format, it would prevent individuals moving from one sector of financial services to another, reducing diversification and precluding companies from gaining the benefit of experience in other sectors of the industry.



20 paragraph 1 bullet 6

It is proposed that the CBI provide guidance on how this assessment is to be carried out.

Financial Soundness

It cannot be ascertained from the proposals set out by the CBI as to where the baseline of “financial soundness” is calibrated. There may be issues such as negative equity scenarios or others relating to wider economic conditions which are outside an individual’s control which may be interpreted as questioning an individual’s “financial soundness”, although this would not be a fair application of this criterion. In addition, there may be data protection issues involved in an employer seeking evidence of financial soundness, and we recommend the Central Bank seek guidance from the Data Protection Commissioner about the appropriateness of, for example, a potential employer conducting ICB credit checks, as well as the general requirement.

Section 6: Transitional Arrangements

We also note the proposal for a 1st September 2011 implementation date for the new regime. Individuals who already hold Controlled Functions (CFs) and Pre-approval Controlled Functions (PCFs) will continue in those functions under transitional arrangements, subject to the firms maintaining records and signing off that they are satisfied that the individuals are fit and proper.

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It is proposed that the CBI define what is expected on the basis of “reasonable grounds”.

Section 7: Processing Fitness and Probity applications

The provision of an online IQ form is welcomed, but we request the CBI considers providing a back-up facility should the online facility fail in any way. Experience of such systems would indicate that even the slightest variation from the form’s convention would have the potential to cause issues over the submission of such a form.

Since the IQ would be a fundamental element of any recruitment process, we request that the CBI commit to a specific timeframe to respond to the IQ application, including the conduct of an interview where deemed necessary, in order to facilitate the efficient recruitment of senior individuals within firms. We propose ten working days would be an appropriate timeframe.

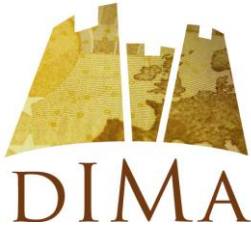
In circumstances where an individual has already completed a satisfactory IQ from a previous successful application but is required to update this, it is proposed that the CBI develop a short form version with a five working day response time.

39 paragraph 1 bullet 3

It is proposed that the CBI provide a copy of the proposed online IQ form for industry to provide feedback before concluding the consultation process.

39 paragraph 1 bullet 3

It is unclear as to what circumstances would lead to a Garda clearance being required, and implies that all PCFs must be based in the State. This contradicts the corporate governance



code, which permits non-executive group directors (located outside the State). Clarification on the CBI's thinking on this issue would be appreciated.

Section 8: Questions relating to the proposed Standards of Fitness and Probity

41 paragraph 1 (i)

See comments responding to Appendix 2.

Section 9: Implementation/Further Considerations

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It is proposed that the CBI should allow sufficient time for firms to receive and review the revised regulations and the IQ form before the implementation date of 1 September 2011.

Appendix 2

3.2a

Agree.

3.2b

Agree.

3.2c

Disagree. This is already adequately covered under the previous point. It is proposed that the CBI delete 3.2c or provide guidance on what additional matters are to be captured by 3.2c and specify how firms are to assess the extent if any to which the appointee's or employee's performance for a State-aided firm contributed to the necessity for such State financial support.

3.2d

Agree.

3.2e

Agree.

3.2f

Disagree. As with all roles (CF and non-CF), this should fall to be governed and managed under the firm's HR policies, sick leave arrangements, etc. It is neither possible nor appropriate to specify a minimum standard of physical and mental health for a particular role, and the standard should be deleted.

3.2g

Agree. Provide guidance as per CF/PCF role as to what is understood by "concurrent responsibilities" that might impair ability to discharge duties.

3.2h



Agree.

4.1a

Agree.

4.1b

Agree.

4.1c

Agree.

4.1d

Agree subject to the wording being revised as follows: "The person has been dismissed on the grounds of dishonesty or fraud from any profession, vocation, office or employment or from a position of trust, fiduciary appointment or similar, whether or not remunerated." Guidance to be provided on how this question can be "vetted" if necessary, particularly for PCFs if a reference is not obtainable from the previous employer, Garda clearance is not available, etc.

4.1e & 4.1f

Agree subject to the following addition to (e): "The person has been a director of a company that was struck off the register of companies by the Registrar of Companies other than at the request of the company, having no liabilities to discharge."

4.1g

Disagree. This is sufficiently captured by 4.1b, h-l. A person is entitled to a presumption of innocence until successfully prosecuted and if successfully prosecuted this will be captured by ongoing monitoring of CFs.

It is proposed that this standard is deleted.

4.1h

Agree, subject to deleting "or is subject to any pending and current proceedings which may lead to such a conviction". A person is entitled to a presumption of innocence until successfully prosecuted and if successfully prosecuted this will be captured by ongoing monitoring of CFs.

4.1i

Agree subject to deleting "or he or she is a party to any pending proceedings in respect of which there are reasonable grounds for considering that any such judgement may be made." A person is entitled to a presumption of innocence until successfully prosecuted and if successfully prosecuted this will be captured by ongoing monitoring of CFs. (Non-statutory guidance) not required.

4.1j

Agree subject to deleting "the subject of any investigation or disciplinary proceedings or been". A person entitled to a presumption of innocence until successfully prosecuted and if successfully prosecuted this will be captured by ongoing monitoring of CFs.



4.1k

Agree subject to deleting “acknowledged or consented to”.

4.1l

Comment reserved pending clarification as to the meaning of a civil penalty enforcement action.

4.1m

It is unclear how a regulated entity would have insight and knowledge of this, and what would be deemed uncooperative rather than challenging.

4.1n

Agree.

4.1o

Agree subject to deleting “as a result of the removal of the relevant registration, authorisation, membership or licence”.

4.1p

Agree subject to deleting “investigated” and “criticised”.

4.1q

Disagree. This is sufficiently captured by the other points within this section.

5.2a

Disagree. This is sufficiently and more appropriately captured by the following points.

5.2b

Agree.

5.2c

Agree.

5.2d

Agree.

5.2e

Agree.

5.2f

Disagree. This is already captured by reference to “state or elsewhere” in previous points.

5.2g

Agree.



We would be willing to meet with you to discuss this submission in further detail and to work with the CBI to develop a best practice regime.

Yours sincerely

Sarah Goddard
CEO
DIMA

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