MINUTES[1] OF MEETING NO. 69 OF
THE CENTRAL BANK COMMISSION
OF 27 MAY 2016

In attendance: Governor, Alan Ahearne, Patricia Byron, Blanaid Clarke, Sharon Donnery, John FitzGerald, Des Geraghty, Derek Moran, Cyril Roux, Michael Soden, Neil Whoriskey (Secretary).

Also present[2]: Eadaoin Rock (General Counsel), Gerry Quinn (Chief Operations Officer – Items 1-5, 7-8, 10-20), Gabriel Fagan (Chief Economist – Item 8), Ed Sibley (Director, Credit Institutions Supervision – Item 8), Mark Cassidy (Head of Financial Stability Division – Item 8), Sylvia Cronin (Director, Insurance Supervision – Item 9), Bernard Sheridan (Director, Consumer Protection – Items 6 and 9), Kieran Murphy (Head of Insurance Supervision Division – Item 9), Derval McDonagh (Head of Human Resources Division – Items 10-11), Glenn Calverley (Head of Organisational Risk Division – Items 10-11, 13-14), Billy Clarke (Deputy Head of Securities and Markets Supervision Division – Items 10-11), Paul Woods (Deputy Head of Organisational Risk Division – Items 13-14), Con Christofides (Organisational Risk Division– Item 13), Bernie Mooney (Deputy Head of Consumer Protection Division – Item 16).

1. Procedural Items

The Governor opened the meeting and noted it was quorate. When asking if members had any interests to declare, the Governor, in the context of the Insurance Supervision item, declared that a member of his extended family was employed in the insurance sector (company name supplied); it was agreed that this connection was not material.

The Governor suggested that a representative of the Communications Division attend Commission meetings in an observer capacity. While this would not include attendance for supervisory items, it would assist the Communications Division in its understanding of

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[2] Those members of management and staff presenting specific proposals for decision are only present when the item is being discussed by the Commission, and are not present when the decision is taken.

strategic and other issues. The Commission's views on this would be sought via written procedure.

The Commission adopted the agenda, with some re-ordering of items to facilitate those attending.

2. Minutes of Meeting of 28 April 2016

The minutes of the meeting of 28 April 2016 (Meeting No. 68) were agreed.

3. Matters Arising

The action items from the April 2016 meeting were noted.

4. Governor's Report

The Governor introduced this item. He noted he would be attending the ECB Governing Council meeting on 2 June 2016. He had recently addressed the International Capital Markets Association Conference where he had highlighted the important work the Bank was undertaking in relation to the investment funds sector and around shadow banking, in particular risks arising. He had also recently addressed the Insurance Europe Annual Conference. He noted the recent formation of the new Government and said he looked forward to the Bank engaging with Government and the Oireachtas on its legislative programme.

The Commission noted the Governor's Report.

5. Deputy Governor's Report (Central Banking)

Ms Donnery introduced this item (Paper No. 131 of 2016). She noted that she was giving the opening address to the forthcoming Centre for Economic Research and Policy (CEPR) Economic Symposium, which the Bank was co-organising and sponsoring. The CEPR was a

network of international researchers whose aim was to foster research activities to enhance policy making in Europe and beyond. This symposium would bring together leading economic historians to present research on topics such as exchange rate regimes, economic geography, human capital and economic growth, and to draw out lessons from the past which were of benefit to policy discussions of today.

She updated members on the issuance of the resolution levy notices to banks and investment firms in respect of the 2016 contribution period, in line with the EU Commission delegated Regulation. Institutions were required to pay their levy by no later than 15 June 2016 and the levies collected from Single Resolution Mechanism (SRM) institutions, primarily banks, would be transferred to the Single Resolution Board by no later than 30 June 2016.

Mr Whoriskey updated members on FOI, in particular the recent publication of the annual report of the Information Commissioner which referenced the Bank's stance on Schedule 1 related material.

The Commission noted the Deputy Governor's Report (Central Banking).

6. Deputy Governor's Report (Financial Regulation)

Part of this minute is omitted as it contains supervisory information.

Mr Roux introduced this item (Paper No. 132 of 2016). In relation to mortgage interest rates, he noted that a group of Irish MEPs had recently written to the ECB requesting it to investigate why Irish mortgage lenders do not pass on lower ECB refinancing rates. He also noted the Central Bank (Variable Rate Mortgages) Bill 2016 had passed the first stage at the Dáil, and this draft Bill needs to be referred to the ECB for consultation. One member noted that there had been various related commitments made in the recently published Programme for Government, including around the Code of Conduct on Mortgage Arrears, and that it would be useful to get clarity on that in the near term.

In relation to the recently completed Consumer Protection research on complaints handling in regulated firms, one member expressed concern at how this reflected on the culture of industry. Mr Roux noted that the Consumer Protection Code had recently been strengthened

in this respect and had resulted in some falling off in complaints to the Financial Services Ombudsman; however this remained an area of continued focus.

Some firm-related items, contained within the paper, were also discussed.

The Commission noted the Deputy Governor's Report (Financial Regulation).

7. Chief Operations Officer's Report

Mr Quinn introduced this item (Paper No. 133 of 2016). He noted that at end-April 2016 the headcount stood at 1,547 full time equivalent (FTE). While a total of 167 roles had been filled since the start of the year, the net increase was 30, reflecting the challenges that remained in recruitment.

In relation to the Fusion programme, there was evidence of a significant uplift in construction activity as the development moved in to its internal fit-out stage. There had also been an increase in the levels of staff engagement, including site visits and demonstrations for focus groups.

In the Currency area, banknote printing production targets remained on schedule. There would be an uplift in production of lower denomination banknotes following the recent decision by the Governing Council of the ECB to cease production of the €500 note.

Mr Quinn also updated members on the Bank's data centre operations.

The Commission noted the Chief Operations Officer's Report.

8. Financial Stability

(i) Financial Stability Overview

(ii) Potential Implications of Brexit

These items were taken together.

Mr Cassidy introduced these items. The main risks to financial stability related to the international environment, which had deteriorated further since the last presentation to the Commission in November 2015. There was a weaker macroeconomic environment with downward revisions to global growth forecasts. In addition, financial markets had been particularly volatile during the first half of 2016, reflecting uncertainty about global economic prospects and the future path of monetary policy in some large economies; rising political uncertainty, including in relation to Brexit; and concerns also about the health of the European banking system. Ireland remained particularly exposed to these heightened external risks, both from an economic and financial stability perspective, given the openness of the economy, reliance of the commercial property sector on international financial flows, and also the vulnerabilities that remained from the crisis including high household indebtedness. Domestically, the macroeconomic environment continued to improve and at a faster pace than previously expected; however, risks overall remained tilted to the downside.

The Bank would shortly be publishing its bi-annual Macro Financial Review which would cover these matters in some detail.

In relation to Brexit, Mr Cassidy provided an update on recent work undertaken in the Bank regarding the risks associated. The overall analysis contained in the two reports prepared for the Commission covered a broad range of potential scenarios and related economic and financial market effects; the potential impact on profitability and business models of financial-sector firms across all sectors, including banks, insurance and funds; implications of potential re-location of financial services firms and/or activities to Ireland; effects on the Central Bank’s balance sheet; and also implications for the work of the Bank including in relation to supervision, European regulatory policy, resolution, payments and the deposit guarantee scheme.

There already had been exchange rate effects with less evidence of any impact on sovereign yields or corporate markets. New estimates were provided of potential macroeconomic effects for Ireland under more adverse scenarios than initially considered. These included the potential for wider or second round implications for foreign demand, given the impact Brexit would have on the global economy, and also the possibility of a more adverse impact on the Irish labour market than under the original scenarios.

An update was presented on the preparedness of firms across all parts of the financial sector for risks relating to Brexit, including the supervisory engagement that had taken place over the past six months with banks and insurance companies with highest exposures to the UK. In terms of the Bank's own preparedness for any contingencies, a high level Task Force had been established and had examined an assessment of banks' sterling funding, foreign exchange hedging, and other relevant transactions that could be negatively affected by market volatility surrounding the outcome of the referendum and the required contingency planning response.

In the discussion that followed, members raised a number of points and questions. It was suggested the Bank should consider other risks when conducting its financial stability analysis; while not an immediate issue, the need to signal the risk of recovery turning into potential over-heating, and the implications for policy, was something that could feature in future reports. It was also argued that the greater risk lay in the lack of adequate housing supply; while another perspective was around the need to consider the risks that lie with intervention in the housing market. The possibility of more analysis on non-financial related sectors, such as pharmaceuticals, agriculture and tourism, was raised, in order to provide a full picture of the resilience of various building blocks of the economy. Concerns around the persistence of non-performing loans in the banks were also cited. Other members questioned what was being undertaken as regards contingency planning of banks for Brexit.

In response Mr Cassidy noted that supply/demand imbalances were inherent in the property sector. The macroprudential measures were designed to limit boom/bust cycles but could not totally eliminate them. The supply side still required some policy measures. He also noted that the investment environment for commercial real estate was driven by international funds and non-bank financing. There was a considerable amount of analytical work ongoing in the financial stability function in the Bank in order to assess these and other issues. Mr Sibley said that non-performing loans remained a high priority, both local and at the SSM level. In relation to Brexit preparedness, the Governor said the immediate issues were to ensure adequate liquidity lines were available in the event of market disruption. There was good preparedness both in the Bank and in the wider banking community for this.

The Commission noted the Financial Stability Update.

9. Insurance Supervision

Part of this minute is omitted as it contains supervisory information.

Ms Cronin introduced this item. She noted the Commission had been provided with a detailed document in advance of the meeting (Paper No. 136 of 2016), which covered: the insurance market in Ireland; a detailed look at each sub sector, including their risks and the work being done to mitigate those risks; and the other work that was being undertaken in the Insurance Directorate. Ms Cronin focused her comments on three key challenges and how they were being addressed.

Firstly, Solvency II had been introduced at the start of the year. This represented a significant new regulatory environment, both for firms and how they were supervised. Capital requirements were now based on a much more detailed and comprehensive quantification of the risks present in the business. For some of the largest firms supervised by the Bank, this was quantified using an Internal Model; firms now had to set out clearly the capital they needed, and the Bank had to be satisfied with the appropriateness of that calculation. A robust approval process had been put in place. A key focus of the actuarial and analytics team will be to use the increased amount of data available under Solvency II to: assess the ongoing appropriateness of firms Internal Models; build early warning indicators; and provide an analysis of firms' Own Risk and Solvency Assessments (ORSA) to ensure they had identified risks and uncertainties and had adequate risk management frameworks, capital and reserves in place.

A second key challenge was around the provision of business on a cross border freedom of services (FOS) or freedom of establishment (FOE) basis. It was expected that this model would grow. The Directorate had consolidated its cross-border team into one larger sectoral team. There were also separate dedicated supervisory teams managing the larger cross border writers that have significant branch presence across Europe. The Bank headed several Supervisory Colleges and Irish insurance supervisors also participated in a large number of Supervisory Colleges in other European jurisdictions, and beyond. In relation to inward services, the Directorate was working closely with Consumer Protection to highlight to foreign regulators potential concerns at an early stage; while not yet on a statutory footing, there was greater engagement in terms of seeking quarterly returns from significant branches, and quarterly information from any company with a material amount of business that was operating in Ireland on a FOS basis. The Bank was also working with the European Insurance

and Occupational Pensions Authority (EIOPA) on amending the General Protocol on collaboration between supervisory authorities to increase the level of co-operation and information sharing.

The final key challenge identified was around domestic non-life firms, where underwriting losses had been incurred and investment income was insufficient to offset these losses. In the second half of 2015 all of the firms took action to address the situation. This included: price increases, particularly on motor business; increased focus on reserve adequacy and claims settlement rates; renewed business strategies focused on underwriting discipline; expense reduction, including redundancy programmes and changes to pension scheme structures; and capital management actions to meet the requirements of Solvency II, including capital increases and increased parental support. For its part, the Bank's supervisory plan had been designed to ensure it was satisfied that the actions taken by firms were robust enough to contest the challenging environment. The supervisory strategy was supported by the on-site team, focused on claims, underwriting and operational risk, and the actuarial team, focused on reserving and pricing. The Consumer Directorate was also working in the non-life space. Its work plans this year included a thematic review of claims handling in the domestic motor lines of business, with a focus on damages rather than personal injury.

In the discussion that followed one member noted that in the non-life sector, and particularly in motor insurance, the issue of pricing was critical. By chasing market share the industry had under-priced. It was positive that the Bank was now getting more granular data through the Solvency II process which would hopefully lead it to recognise such trends in the future. Ms Cronin noted that, while the Bank did not have a price regulation role, its prudential focus was on trying to ensure firms were stable with sufficient funds to pay out claims. Solvency II did give the Bank a greater line of sight into various business lines. One of the challenges, however, was in relation to firms operating in Ireland on a FOS basis, where the prudential responsibility lies with the foreign supervisor; the same access to data was not available to the Bank in these instances; but it was pressing the need at EU level to get access to that information. Mr Sheridan said that the market was very price transparent; there was a lot of information available to consumers and an ease of switching. The risk was that the firms were focusing primarily on price and had over-played that hand.

Another member asked how best to tackle issues most efficiently in the industry, including where problems might be identified in one firm with a read over to others. A number of

supervisory tools are potentially available, including remediation programs, auditor assurance, enforcement powers, fitness and probity; it would be useful to see what was most effective. Mr Murphy said that the Bank chose the most appropriate power when dealing with issues. While Enforcement was necessary in some instances, it was a significant step that could potentially take some years to conclude. Actions were based on the best use of resources in parallel with the outcome that was being sought, most often the time bound requirement for remedial action.

The Commission noted the Insurance Supervision Update.

10. Revised Staff Trading Rules

Mr Clarke introduced this item. As advised to the Commission at its meeting on 24 March 2016 (Paper No. 90 of 2016) the Employee Trading Rules had to be amended to comply with ECB Guidelines on an Ethics Framework which, based on Commission approval, would apply to the Bank from 1 June 2016. Amendments to the Rules had been limited to the changes required for compliance with the ECB Guidelines and points of clarification that arose in the course of the review of the Rules by the Bank and the ECB. The amended Rules were set out in the paper with changes from the current version highlighted.

The Guidelines required the Bank to ensure that the list of restricted transactions may be adjusted at short notice to reflect the decisions of the Governing Council. In order to give effect to this requirement in an efficient manner it was proposed to delegate to the Governor the power to adjust the list of transactions set out in Section 2 of the Rules to reflect decisions of the Governing Council.

The proposed changes had been reviewed by the Operations Committee and recommended for approval by the Commission. Staff representative groups were informed of the changes and had raised no comments.

The Commission approved the amended Staff Trading Rules; approved, in accordance with section 18F of the Central Bank Act 1942, the delegation to the Governor of the power to adjust the list of transactions set out in Section 2 of the Rules at short notice to

reflect the decisions of the Governing Council of the ECB; and, confirmed that the foregoing delegation shall be a 'Delegation' for the purposes of minute no. 9 of meeting no. 19 of the Commission of 28 March 2012 and that the decision in that minute no. 9 shall apply to the foregoing delegation.

11. Revised Staff Code of Ethics

This item had also been considered by the Risk Committee at its meeting on 26 May 2016.

Mr Calverley introduced this item. From 1 June 2016, the Bank must comply with new ECB Guidelines which laid down the principles for a harmonised Ethics Framework for the Eurosystem and Single Supervisory Mechanism. The Commission, at its meeting on 24 March 2016 had previously considered a draft revised Code of Ethics (previously the Code of Ethics and Behaviour) for staff (Paper No. 90 of 2016) to comply with the Guidelines.

The draft Code of Ethics had been further developed in order to comply with Guidelines and to clearly define the standards of ethical conduct the Bank and its staff should uphold. The Code would be issued to all staff via the intranet, Plaza, and published on the Bank's website.

The Commission approved the revised Staff Code of Ethics.

12. Revised Commission Code of Ethics

Since the establishment of the Commission, it had operated under the terms of an agreed Code of Conduct. The Code was reviewed in 2012 and agreed by the Commission in October 2012 (Paper No. 130 of 2012). The existing Code became effective from 1 January 2013.

From 1 June 2016, the Bank was legally bound to comply with the ECB Guidelines, which laid down the principles for a harmonised Ethics Framework for the Eurosystem and Single Supervisory Mechanism. Internal rules adopted by the Bank in fulfilment of the provisions of the Guidelines were required to apply to members of Bank bodies, defined to include members of decision-making and other internal bodies other than staff members. As the

Commission was a decision-making body of the Bank it was within the scope of the Guidelines, therefore, it had been determined that the Code be revised. In that context, a review of the Code was undertaken to ensure compliance with the Guidelines and to take account of resulting changes to the Staff Code of Ethics and Staff Trading Rules for consistency. A number of amendments to the previous Code had been proposed, which also reflected the requirements in the revised Staff Code.

Once the Code was approved it was intended to send it to the Minister for Finance asking the Minister to consider requiring appointed members of the Commission to comply with the Code as a condition of service pursuant to 24A of the Central Bank Act 1942. It was also proposed to publish the Code on the Bank's website.

The Commission approved the Code of Ethics for Members of the Central Bank Commission.

13. Central Bank Superannuation Fund: Rebalancing Policy Review

Part of this minute is omitted as it contains commercially sensitive information.

This item had also been considered by the Risk Committee at its meeting on 26 May 2016.

Mr Woods introduced this item. A rebalancing policy was generally accepted to be valuable in helping to maintain a pension fund's risk and return profile, which could otherwise drift significantly due to market movements over time. The accompanying paper (Paper No. 140 of 2016) outlined the possible advantages and disadvantages of the current rebalancing policy, and highlighted that risk based approaches to rebalancing were becoming best practice, and that adopting such an approach may be more efficient for the Superannuation Fund in light of the more diversified, multi-manager allocation now in place and to support possible further diversification in the future.

The Commission approved: that the Pension Fund allocation not be rebalanced at this time; that the Pension Investment Advisory Committee (PIAC) make an assessment of the need to rebalance the Pension Fund allocation annually in Q4; that where the assessment identifies a need to rebalance the Pension Fund it is carried out as early as operationally possible in Q1 of the next year; and that details of the assessment and any

subsequent rebalancing be included in the Annual Superannuation Fund Investment Performance Report.

14. Strategic Review of Business Continuity Management

Part of this minute is omitted as it contains commercially sensitive information

This item had also been considered by the Risk Committee at its meeting on 26 May 2016.

Mr Woods introduced this item. A rebalancing policy was generally accepted to be valuable in helping to maintain a pension fund's risk and return profile, which could otherwise drift significantly due to market movements over time. The accompanying paper (Paper No. 140 of 2016) outlined the possible advantages and disadvantages of the current rebalancing policy, and highlighted that risk based approaches to rebalancing were becoming best practice, and that adopting such an approach may be more efficient for the Superannuation Fund in light of the more diversified, multi-manager allocation now in place and to support possible further diversification in the future.

The Commission approved the revised 2016 Business Continuity Management Policy.

15. Delegation of Powers and a Summary of Powers Retained by the Commission

The Commission noted the framework of the delegation of functions and powers in place in the Bank and the summary of powers retained to the Commission.

16. Charity Committee Annual Report 2015

Ms Mooney introduced this item. Following a decision of the Commission in 2011, a Charity Committee comprising staff representatives was established to oversee the management of the Bank's Benevolent Fund. Final approval for the Fund's expenditure came from the Director of Human Resources.

The Committee's main tasks were to recommend the distribution of the Benevolent Fund, to promote volunteering among staff members, support charitable endeavours undertaken by

staff and occasionally organise charity events within the Bank. The Committee also provided periodic updates to the Governor. This report was provided to update the Commission on the work of the Charity Committee in 2015. It was proposed that, subject to any input from the Commission, a summary of the report will be published on the Bank's intranet. One member noted the national role of the Bank and the importance of geographical considerations when disbursing the funds. The Governor referenced the recent fundraising event organised by staff, which attracted a large audience and was very successful. He expressed his thanks to all involved.

The Commission noted the report of the Charity Committee for 2015; and agreed to the publication of the report on the Bank's intranet.

17. Statement of Accounts to 31 March 2016

This item had also been considered by the Audit Committee at its meeting on 26 May 2016.

The Commission noted the Statement of Accounts to 31 March 2016.

18. Financial Risk Information Pack

It was noted that the Risk Committee had agreed that the Financial Risk Information Pack would now be circulated on a quarterly basis.

The Commission noted the Financial Risk Information Pack.

19. Minutes of Meetings of Sub Committees

The Commission noted the minutes of the meetings of the Audit Committee of 24 February 2016, and of the Risk Committee of 23 March 2016.

20. Any Other Business

The Governor informed the Commission that Ms Donnery had been reappointed to Chair the ECB Working Group on Non-Performing Loans (NPLs), which was now entering its second phase.

The meeting concluded.