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Individual Accountability Framework – Public Consultation
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Matter: Response To Central Bank of Ireland Consultation Paper 153 on Individual Accountability Framework

A Chara,

1. Introduction

1.1 Thank you for the opportunity provided by the Central Bank of Ireland ("**CBI**") Consultation Paper 153 on the Individual Accountability Framework Act 2023 (the "**IAF CP**") to provide our views regarding the CBI's implementation proposals for the Individual Accountability Framework and Senior Executive Accountability Regime (**"IAF/SEAR**").

1.2 We welcome the clarity brought by the IAF CP regarding aspects of the new regime. We also welcome the fact that the CBI is not proposing to adopt certain problematic aspects of the UK's Senior Managers Certification Regime (the "**UK SMCR**"), such as mandatory regulatory references (see CP, Question 1). We further agree with the CBI's proposal in the IAF CP not to require submission of statements of responsibility/management maps by in-scope firms, which removes an inefficiency that we are aware has caused considerable inconvenience for such regulated financial services providers ("**RFSPs**") under the UK SMCR (see CP, Question 8).

1.3 We comment here, from an industry perspective, on the key issues that we believe the CBI should further consider before finalising the implementing regulations. This response is submitted in our personal capacities and is based on our experience as partners in the Financial Services and Employment & Benefits Departments of Mason Hayes & Curran LLP advising clients active in the Irish domestic and international financial services markets. Where our comments respond specifically to the Questions that appear at p. 43 of the IAF CP, we give the appropriate cross-reference.

2. Extension of F&P Regime to financial holding companies (Questions 1, 16)

2.1 We find these proposals problematic. Traditionally, Ireland has adopted a "faithful transposition" approach to EU financial services directives, avoiding so-called "gold plating" (the term used where an EU Member State goes beyond directive requirements to impose

higher standards and more onerous requirements). This "faithful transposition" approach aligns with Ireland's traditional wish to maintain its standing as an attractive home state domicile for holding companies of all types, including financial holding companies. There is no EU law requirement to apply the CBI's F&P regime to directors or staff of Irish financial holding companies, so this would represent Irish "gold-plating" of EU law. Our understanding of the UK SMCR is that it does not automatically apply to directors or personnel of financial holding companies as such.

2.2 We fear that applying the CBI's F&P regime in full to all overseas directors of Irish holding companies could be a significant disincentive to locating new financial holding companies in Ireland. It may even incentivise existing holding companies to relocate to other EU domiciles.

2.3 Our preference would be that financial holding companies remain outside the scope of the CBI's F&P regime entirely. If some financial holding companies must be brought into scope, this should be limited to bank holding companies that require separate regulatory authorisation under CRD V. The CBI has discretion under the IAF Act, in our view, to define the scope of application in this way.

2.4 Within in-scope holding companies, we think that CF designation should only apply to those persons that have specific responsibility for compliance by the holding company with its financial services regulatory obligations imposed by virtue of its falling within the definition of "holding company" under the IAF Act. CF designation should not apply to other aspects of the holding company's compliance or to the conduct of the holding company's business generally.

2.5 We also struggle to see a policy justification for all directors and the Chair of in-scope holding companies automatically being PCF functions requiring pre-approval. We think that PCF designation should be limited to those directors of an in-scope financial holding company that, by virtue of such position, exercise specific and significant responsibilities in relation to the relevant subsidiary RFSP. Therefore, and by way of example, a holding company director that participates in a committee of the RFSP would be captured, but "regular" holding company directors would not.

3. Effective Dates (Question 1)

3.1 In the UK, the first consultation process conducted by the Prudential Regulation Authority (the "**PRA**") and the Financial Conduct Authority ("**FCA**") commenced in July 2014, but the UK SMCR did not become effective for the first UK in-scope firms until March 2016. The timelines proposed in Ireland for compliance seem to be significantly shorter – only 9 months from the start of consultation to the first proposed implementation deadline. It is difficult even to see how the CBI can itself meaningfully review and consider consultation responses that it will receive in June 2023 and produce revised regulations and guidance ahead of the proposed first deadline of December 2023.

3.2 Our industry engagement causes us to believe that firms need more time beyond 31 December 2023 to put in place robust arrangements to comply with the conduct standards and enhanced F&P obligations. This is particularly so since many firms must at the same time prepare responsibility statements and mapping under IAF/SEAR proposed to be effective from 1 July 2024.

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4. Scope of IAF/SEAR as including all INEDs/NEDs (Question 5)

4.1 Bringing all Independent Non-Executive Directors ("**INEDs**") and Non-Executive Directors ("**NEDs**") at Irish RFSPs within scope of IAF/SEAR goes beyond the scope of application of the UK SMCR to NEDs/INEDs in the UK, as we understand it. We are concerned that, particularly in the case of INEDs, requiring those individuals to assume responsibilities prescribed by the CBI and creating corresponding direct personal exposure to the CBI is inappropriate and potentially inconsistent with their general duties under corporate law.

4.2 We do not agree with the argument raised by the CBI that the standards to be imposed on directors under IAF/SEAR will be consistent with and will go no further than those that apply under general corporate law. At a very basic level, a director's responsibility under corporate law is to her/his company and not to third parties, while under IAF/SEAR, directors will be exposed to financial liability to the CBI for alleged failure to adhere to inherent, prescribed and any other responsibilities.

4.3 Creating such an explicit dual focus of legal responsibility for directors of regulated firms is troubling. It could put directors in a position of conflict of duties, or even lead to a situation where on a day-to-day basis, a NED/INED of a RFSP could perceive her/his responsibilities and exposures to the CBI as being more important than those owed to the company.

4.4 We believe that the current regime, under which NEDs and INEDs are subject to PCF pre-approval, coupled with the application to them of the F&P Regime and of the general conduct standards, is sufficient to ensure appropriate discharge of their duties by both NEDs and especially by INEDs.

5. Scope of responsibilities of NEDs/INEDs under IAF/SEAR (Question 3)

5.1 The IAF CP identifies certain specific prescribed responsibilities to be allocated to a NED or INED under IAF/SEAR (draft Regulation 5(3)). We fear that these responsibilities could, in some cases, be inappropriate for NEDs and INEDs (e.g., there is no obvious justification for placing a NED or INED in charge of whistleblowing effectiveness, since this is a matter that goes as much to the maintenance and development of good internal workplace culture as to board oversight).

5.2 In other cases, (e.g., maintaining the independence of the compliance, risk, and internal audit functions) formally allocating these responsibilities to NEDs/INEDs could result in confusion regarding the respective limits of Board and management responsibilities for the relevant functions, the appropriate reporting lines for the relevant function holders and the ability of those function holders to participate fully in the senior management team. The CBI has not to date published detailed "Three Lines of Defence" guidance and there is already, we believe, confusion in the industry regarding the meaning of "independence" as a concept applied to control functions.

5.3 The UK regime does not, as we understand it, require the allocation of specific responsibilities to NEDs or INEDs in preference to other senior managers. We suggest therefore that, if NEDs/INEDs must be in scope of SEAR at all (see our comments in this respect under Question 5), RFSPs should have full flexibility regarding allocation of responsibilities to them.

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6. Splitting of prescribed responsibilities (Question 4)

6.1 The IAF CP states that prescribed responsibilities cannot be split between PCFs (although job sharing will be permitted), but that the effect of IAF/SEAR should not be to alter RFSPs management and governance structures. This position seems to us inconsistent (since for example it prevents a firm from maintaining co-heads of business units).

6.2 The UK FCA, as we understand it, is less prescriptive in this regard and permits firms to split prescribed responsibilities where the split can be justified as being appropriate in the circumstances. We think that the CBI should permit the splitting of responsibilities by applying a similar test.

7. Oversight of outsourced PCFs (Question 9)

It is quite common for certain control function roles, such as the Head of Internal Audit, or Head of Actuarial Function in an insurance firm, to be outsourced. We do not understand which other internal PCF could be formally responsible under IAF/SEAR for the oversight of those persons and how such formal oversight could be consistent with the "Three Lines of Defence" model. This proposal should be revised and clarified.

8. Reasonable steps (Questions 10/11)

The CBI has sought to provide guidance regarding "reasonable steps" for the purposes of the duty of responsibility under IAF/SEAR. This guidance is, we think, sufficiently flexible to accommodate RFSPs' varying business models. However, we believe it leaves open the possibility that PCFs could in practice be exposed to enforcement risk under SEAR where (a) they have made simple mistakes or (b) they have taken steps to discharge their duties which in a commercial context would generally be considered sufficient, but which in either case have had severe consequences. We think that the CBI's "reasonable steps" guidance should formally state that it does not expect to hold individuals responsible for simple mistakes or errors of judgement, even if those mistakes or errors of judgment have had severe consequences.

9. Breadth of, and lack of specific definition of, concept of "other responsibility" (Question 3)

9.1 The IAF CP states that in-scope RFSPs must identify "*any functions, business areas or projects that are not captured by Inherent and Prescribed Responsibilities but that are included in management responsibilities maps and must allocate these to a PCF as an "Other Responsibility"*".

9.2 The draft Regulations are very prescriptive in this respect. Draft Regulation 6(1) requires the firm to identify "each of the activities, business areas and management functions constituting the overall business of the firm" and to allocate responsibility for each of these to a PCF. There is no concept of materiality employed here. Even if a concept of materiality were to be included in the Regulations, this identification/allocation requirement would impose a significant burden on firms, requiring them to map the bulk of their internal administration and operations and to allocate specific regulatory responsibility for every aspect thereof to a designated PCF.

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9.3 Many such internal units, although forming part of the firm's overall business, could at best be tangentially relevant to the firm's compliance with financial services regulation. It seems to us excessive to require that PCFs be personally responsible and exposed to potential sanctions for every potential administrative and operational failure at a regulated firm in this way. A viable alternative formulation could for example be that "Other Responsibilities" should comprise:

> "*responsibilities falling within an activity, business area and management function of a regulated firm where a material failure to discharge such responsibilities, viewed objectively by a well-informed third party, would be reasonably likely to result in the firm committing a prescribed contravention."*

9.4 We fear that, if the CBI does not give clearer guidance regarding its expectations or otherwise limit the scope thereof, there could be a wide variation in approach to the definition of "Other Responsibilities" among RFSPs. Some could adopt a very granular approach to mitigate perceived individual risk, while others might opt for a broader approach to mitigate administrative burdens. To promote consistency, we think the industry would benefit from clearer CBI guidance in this respect.

10. Mapping of intra-group relationships (Question 7)

10.1 The IAF CP states that the CBI expects significant intra-group service arrangements to be included within management responsibilities maps and we agree that they should be included. We are concerned however that the proposals as drafted could lead to confusion regarding the need to include normal and BAU group reporting arrangements and the level of detail that will be required in this regard.

10.2 Irish subsidiaries will often be represented at group regional or group holding company committees, will form part of a group external audit and will be subject to group internal audit, but it is difficult to understand why standard group reporting arrangements would need to be captured in management responsibilities maps. There should be no normal circumstances where a group reporting arrangement, taken alone, could lead to personnel at holding company level being regarded by the CBI as *de facto* exercising RFSP senior management responsibilities. As a result, the mapping of group reporting lines should be irrelevant to the discharge of these responsibilities and to the CBI's oversight of IAF/SEAR. We recommend therefore that these proposals be clarified and limited more appropriately in their scope.

11. Temporary Appointments (Question 14)

11.1 We recommend that the CBI should use the opportunity presented by the IAF CP to revise the current F&P Regime to introduce a more streamlined approach to temporary appointments to PCF roles. The ability for firms to appoint temporary officers under Regulation 11 of the Central Bank Reform Act 2010 (Sections 20 and 22) Regulations 2011 is quite constrained. The CBI's F&P Guidance currently contemplates that (outside the COVID 19 pandemic) the temporary appointment approach can only be used in the most severe circumstances, and death is given as the sole example.

11.2 We think that the concept of "exceptional circumstances" in which it would be appropriate to appoint a temporary officer with the CBI's permission but without the need for explicit PCF

clearance (which would often take too long to obtain) should be further expanded and a more pragmatic approach taken. For example, where a PCF holder resigns unexpectedly and a recruitment process is necessary, we are aware that firms in practice find the current regime impractical. There should be a route for firms to temporarily fill a PCF position for a short-interim period (e.g. 6 months) with CBI consent but without the need for a full F&P pre-clearance. Our understanding is that such a possibility exists in the UK regime.

12. Determining responsibility for aspects of the firm's affairs (Questions 6/7)

12.1 In paragraph 2.8.9 of the draft Guidance, it is stated that responsibility is a matter of substance and that it may be necessary to look beyond the Management Responsibilities Map and Statements of Responsibilities to determine the individuals that are responsible for aspects of a firm's affairs.

12.2 We find it difficult to see how this could operate in practice, at least for "Other Responsibilities", since these are currently defined in the draft Regulations as responsibilities that are derived from the exercise of responsibility mapping in the first place. It seems to us therefore that, as the draft Regulations currently stand, only Inherent and Prescribed Responsibilities could be deemed by the CBI to adhere to a particular PCF in the absence of specification to that PCF in a Management Responsibilities Map and Statements of Responsibilities.

12.3 Any ambiguity in this regard could be highly material to PCFs in the context of future enforcement of SEAR against individuals. This point should therefore be fully clarified in the final Guidance.

13. Conduct standards – management of conflicts of interest (Question 12)

13.1 Paragraph 5.2.5 of the draft Guidance states that all actual and potential conflicts of interest should be assessed, communicated, discussed, and documented at in-scope firms. This requirement goes well beyond existing regulatory obligations (for example under MiFID II) to maintain appropriate policies and procedures in this regard and is far too wide and intrusive in our view as an aspect of a general conduct standard.

13.2 Also, paragraph 5.2.5 states that all individuals are required not to participate in decision making/discussion where it could reasonably be perceived that a potential conflict of interest exists. This behavioral standard was previously only applied to directors of banks and insurers under the relevant Corporate Governance Codes. It requires a standard of assessment that is, in practice, difficult to apply (since it requires application of the presumed perspective of a third party). In our opinion, requiring all staff to apply third-party perceptions to determine the possible existence of perceived conflicts is far too onerous a standard for them to apply in normal commercial life and this should be removed from the guidance.

14. Conduct standards – honesty and integrity (Question 12)

14.1 Paragraph 5.2.6 of the draft Guidance refers to individuals not adhering to firm policies and procedures and/or providing incorrect information to the firm, its customers, employees or the regulator as examples of potentially dishonest behaviour. It should be made very clear in the final Guidance that the CBI recognizes that non-adherence to firm policies and

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procedures and the provision of incorrect information can be entirely innocent and can occur without any intention to act dishonestly or misleadingly.

14.2 We think that these matters should not be given in the final Guidance as examples of potential breaches of the conduct standard of honesty and integrity. In truth, they are more appropriate to the conduct standard of acting with due skill, care, and diligence. They do not necessarily go to an individual's honesty and integrity in the absence of further facts (e.g., wilful and deliberate breaches of firm policies).

15. Conduct standards – reporting to regulators (Question 12)

15.1 Paragraph 5.3.10 of the draft Guidance states that an individual that considers that a decision may not be in the best interests of customers "should" report to relevant regulatory bodies "where required". It is important for the CBI to be clear that the law currently only imposes pro-active reporting obligations on individuals holding PCF functions in certain specific circumstances.

15.2 There should not be an implication in the IAF/SEAR Guidance that a CF or PCF that fails to report where reporting is not mandatory has failed to take "reasonable steps" to meet the conduct standards. Alternatively, if the CBI does believe that CFs and PCFs should pro-actively report to it, even where they are not legally obliged to do so, it should make this requirement very clear. Many legal complexities could arise in such circumstances, not least whether a person reporting voluntarily to the CBI could be exposed to liability to the RFSP for breach of confidence or even defamation, and whether such a person would be entitled to disclose personal data in any report as a matter of GDPR.

15.3 The Guidance text should not therefore be taken to suggest that the conduct standard should be interpreted as creating an implied and wide-ranging "duty to whistleblow" for all CFs and PCFs in RFSPs. Alternatively, if it is the CBI's intention that the conduct standard should be interpreted in this way, it should make this very clear and also specifically address the legal risks that individuals could be exposed to as a result thereof.

16. Conduct standards – "loopholes" (Question 12)

16.1 Paragraph 5.4.3 of the draft Guidance states that "loopholes or technicalities" should not be relied on by individuals to justify taking certain action or behaviour in dealing with the CBI. However, this language has no sensible basis under the Irish legal and regulatory system (outside perhaps of specific legislative contexts such as tax law) where laws and regulations must normally be interpreted based on the clear language thereof. It is not the regulated firm's responsibility to guess at and apply the regulator's presumed intentions.

16.2 All laws and regulations should therefore be sufficiently well and clearly drafted to avoid ambiguity, but where ambiguity exists, and firms/individuals take reasonable action, they should not subsequently be criticized by the regulator for having "exploited loopholes" and failed to adhere to a conduct standard requiring good regulatory engagement. This passage of the draft Guidance should, in our view, be removed.

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17. Additional Conduct Standards – incoming EEA branches (Question 12)

17.1 We understand that one of the Additional Conduct Standards (ACS) regarding reporting to the CBI will apply to PCFs and CF1s of incoming EEA branches (see Appendix 5 Table 11). However, since incoming EEA branches do not have PCFs and designated CF1s, it is not immediately clear to which staff within the branch the additional conduct standards will apply. It is also not clear that imposing reporting duties on staff of incoming EEA branches is consistent with EU law as regards the division of responsibilities between "home" and "host" supervisors. We believe that it would be more appropriate and consistent with EU law for only the basic conduct standards to apply to staff of incoming EEA branches.

17.2 Alternatively, if the CBI goes ahead with imposing a reporting obligation on staff of incoming EEA branches, it should clarify the respective roles of the "home" and "host" supervisor in these circumstances. It must be recalled in this context that some EEA member states impose explicit banking secrecy laws, such that staff of an EEA branch could be exposed to liability under those laws if they cannot demonstrate that disclosure to a foreign regulator was made under a valid obligation.

The IAF/SEAR regime will be an important enhancement to Ireland's regulatory system, but its implementation needs to be carefully calibrated to the circumstances of Ireland's financial industry, both domestic and international. We commend the CBI for its efforts to date in this regard. We trust that this response is of further assistance in this respect and are happy to provide further input as required.

Yours faithfully

Sent by email, no signatures.

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