



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Settlement Agreement between the Central Bank of Ireland and Aviva Life & Pensions Ireland Limited

The Central Bank of Ireland (the “**Central Bank**”) has entered into a Settlement Agreement with effect from 17 December 2012 with Aviva Life & Pensions Ireland Limited (the “**Firm**”), a regulated financial services provider, in relation to breaches of Regulation 10(3) of the European Communities (Life Assurance) Framework Regulations 1994, as amended (the “**Regulations**”). The Central Bank had regard to the Guidelines for Insurance Undertakings on Asset Management in assessing the Firm’s compliance with Regulation 10(3) of the Regulations.

Reprimand and fine

The Central Bank reprimanded the Firm and required it to pay a monetary penalty of €1,225,000.

Breaches

The breaches identified are that certain of the Firm’s administrative procedures and internal control mechanisms were not adequate in respect of its stock lending activity in contravention of Regulation 10(3) of the Regulations, as follows:

- the Firm failed to adopt an adequate investment policy or adequate investment objectives for stock lending;
- the Firm failed to impose sufficient parameters for stock lending on its investment managers;
- the Firm failed to ensure that there were in place adequate reporting and internal control systems designed to monitor that stock lending was being managed in accordance with an adequate investment policy and investment mandate(s);



- the Firm failed to monitor the performance of the investment managers in relation to stock lending adequately against Board approved policies and procedures;
- the Firm failed to have adequate systems of internal control present to ensure that its stock lending investment activities were properly supervised;
- the Firm failed to review its investment policies on an annual basis; and
- the Firm did not set risk limits in respect of stock lending, and did not receive regular information from its risk management function on asset exposures and the associated risks.

Background

The Central Bank's Insurance Directorate conducted a survey into the use of liquidity swaps among high and medium high impact insurance undertakings. As a result of information gathered during the survey and a further information gathering exercise, the Central Bank carried out an inspection of the Firm's use of liquidity swaps. As a result of information gathered during this inspection, the Central Bank became aware of the details of the Firm's stock lending activity and discovered these breaches. The Firm's stock lending activity was performed by an investment manager within the Aviva group pursuant to an investment management agreement.

The Firm's stock lending

Failure in adopting an adequate investment policy or adequate investment objectives and failure to impose sufficient parameters on its investment managers

1. In November 2000, the Firm entered into an Investment Management Agreement ('the IMA'), with Hibernian Investment Managers Limited (currently known as Aviva Investors Ireland Limited ('AIIL')), a member of the Aviva Group.



2. Following an amendment to the IMA in 2002, AILL entered into a further outsourcing contract with another of the Aviva Group companies, Morley Fund Management Limited (currently known as Aviva Investors Global Services Limited ('AIGSL')) for the performance of stock lending activities.
3. The Firm failed to adopt an adequate investment policy or adequate investment objectives in relation to stock lending. The Firm also failed to impose sufficient parameters for the performance of the stock lending activities on its Investment Manager, AILL.
4. The Firm updated its investment policy in 2009. Again, the Firm failed to impose sufficient parameters on AILL in relation to stock lending. This investment policy remained in place from 2009 until 2012.
5. In June 2010, a novation occurred and the rights of AILL under the IMA transferred to AIGSL, and AIGSL continued to perform stock lending on behalf of the Firm.

Failures in monitoring and control

6. From September 2003 until August 2009, the Firm's Investment Committee received stock lending revenue information on a monthly basis from AILL.
7. Then, from September 2009 until October 2011, the Firm's Investment Committee received stock lending revenue information and received misstated stock lending exposure information from AILL and subsequently AIGSL. Information on revenues and exposures was inadequate to allow the Firm to properly monitor and control stock lending activity carried out under the IMA on its behalf.



Failures to identify incorrect information

8. During the period September 2009 to October 2011, the Firm's Investment Committee received misstated stock lending exposure information from AILL and subsequently AIGSL. On average, this information was understated by a factor of 30. The inclusion of the misstated figures arose because the reports identified the information on the basis of average rather than total exposures. The Firm failed to ensure that it had adequate systems of internal control present to detect the misstatement in its stock lending exposures.

Failure to review the adequacy of the investment policy

9. The Firm did not review the adequacy of its overall investment policy in 2010 and 2011.

Failure in the risk management function

10. Finally, from 1 August 2004 until January 2012 the Firm did not set risk limits in respect of stock lending, and did not receive regular information from its risk management function on asset exposures and the associated risks in respect of stock lending.

Penalty Decision Factors

The taking of this case and the penalty imposed reflect the seriousness with which the Central Bank views any breaches of the regulatory requirements which are designed to ensure the protection of life assurance policyholders.

This case evidences serious inadequacies in the Firm's systems and controls in relation to stock lending.

In deciding the appropriate penalty to impose, the Central Bank has taken the following into account:



- the Board of the Firm decided to cease stock lending upon becoming aware of the issues identified above and have committed to implementing a variety of new internal controls and risk limits in order to improve governance should it recommence stock lending; and
- the new Board and management of the Firm co-operated during the process and settled at an early stage in the administrative sanctions procedure.

The Central Bank confirms that the matter is now closed.

- End -

The Central Bank of Ireland has entered into a Settlement Agreement on 17 December 2012 with Aviva Life & Pensions Ireland Limited, a regulated financial services provider, in relation to breaches of the European Communities (Life Assurance) Framework Regulations 1994.

The Central Bank of Ireland's Fiona Muldoon, Director of Credit Institutions and Insurance Supervision and Peter Oakes, Director of Enforcement, issued a joint comment stating:

“Where a firm outsources investment activity, it must ensure that it has adequate investment policies, procedures and quantitative parameters to manage that investment activity in a way that is appropriate to the firm’s balance sheet, and that it has sufficient information to allow it to properly monitor and control that activity. It is inadequate and unacceptable for firms to rely on group controls or group limits. The Central Bank reminds firms that they remain responsible for all regulatory obligations notwithstanding any reliance upon group controls or group limits.

The pursuit of enforcement actions in respect of systems and controls failings is a Central Bank Enforcement Priority for 2012. The Central Bank has previously stated that where



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serious breaches of these regulatory requirements occur, regulated entities and their management can expect vigorous investigation and follow-up by the Central Bank.

Where the actions of a firm undermine the Central Bank's achievement of its statutory objectives, the firm should expect that enforcement action will follow, especially where the breach falls within our stated Enforcement Priorities."