



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem



Annual Performance Statement

Financial Regulation 2016 - 2017

Central Bank of Ireland

21 April 2017

Dear Minister,

In accordance with Section 32L of the Central Bank Act 1942 (as amended), the Central Bank of Ireland (the Bank) is required to prepare an Annual Performance Statement on its financial regulatory activities undertaken during 2016 and planned for 2017. This document must be presented to you within four months after the end of each financial year.

I have the honour to enclose herewith the Annual Performance Statement for 2016-2017.

Yours faithfully,

A handwritten signature in black ink, appearing to be 'P. Lane', written in a cursive style.

Philip R. Lane
Governor

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Philip R. Lane
Governor

Foreword by the Governor

The focus of the Central Bank of Ireland (the Bank) in 2016, as regards its financial regulation mandates, was on continuing to protect the interests of mortgage borrowers and other Irish customers of financial service providers, and to improve the financial resilience of these firms and that of the financial system as a whole.

Looking forward to 2017, some of the key elements of our regulatory focus include:

- Working to ensure the best interests of consumers are protected by delivering on the key priorities as set out in our Consumer Protection Outlook Report, in particular the tracker examination review. Our goal is to ensure that the best interests of consumers are protected while recognising that expectations of what can be achieved through regulatory mechanisms need to be reasonable.
- Continuing to authorise new investment firms, insurers, and other financial institutions when they meet our standards, ensuring that they have in Ireland commercial and risk-management staff, skills, processes and effective decision-making powers.
- Successfully implementing the framework for the 2nd Directive for markets in financial instruments (the MiFID II/MiFIR framework).
- Continuing to fulfil our Single Supervisory Mechanism (SSM) responsibilities, working effectively within the SSM to deliver appropriate supervisory outcomes for Irish banks, notably the reduction of non-performing loan portfolios.
- Developing and implementing supervisory strategies to ensure a continued reduction in the overall risk profile of our regulated firms.
- Continued effective use of enforcement powers to achieve credible deterrence.
- Actively contributing to the development of relevant laws, regulations and technical standards in Europe to support soundness and stability, well-functioning financial services and markets and effective consumer protection.
- Effectively participating in European Supervisory Authorities (ESAs), fully contributing to EU and selected international regulatory debates.
- Ensuring that the Bank is well-positioned to predict, understand, assess, and respond effectively to developments coming from the Brexit decision and negotiations.

In April 2017, Cyril Roux will leave the Bank. He drove critical reforms in the way we conduct financial regulation in Ireland, including our successful integration into the SSM of banking supervision in the Eurozone, and the transformation of our insurance supervisory approach in line with the introduction of Solvency II. His is a leading voice in the European Supervisory Authorities and he has served Ireland well. Together with his essential contributions to our Macroprudential and Financial Stability mandates, and the running of the Bank as a whole, Cyril Roux has led Financial Regulation in Ireland with great strength and distinction and leaves a secure legacy. We wish him the very best for the future.



Interview with Cyril Roux, Deputy Governor – Financial Regulation

What are the financial regulation highlights of 2016?

The publication of the IMF's report on Ireland's financial sector in mid-2016 acknowledged the progress achieved by the Bank in discharging its financial regulation mandate and the work underpinning this achievement over the past number of years. The conduct of the review was itself a major project for the Bank. But let me stress the major progress made in 2016 in two epoch-defining, multi-year projects of financial regulation: the tracker mortgage examination, which will be brought to fruition for many affected customers this year, and the inquiry in persons concerned in the management of INBS – the Bank cleared in court a number of legal challenges brought against its powers and the case continues, underlying our commitment to holding individuals to account.

What were the biggest challenges to the Bank in delivering its mandate in 2016?

The retention and attraction of appropriately experienced and skilled staff remain a key challenge for the Bank, particularly in light of Brexit and the increased demands on the Bank as a result. We have made significant moves to address this in 2016 with the introduction of a comprehensive internal training programme for staff, ensuring continued improvement in the expertise level in the organisation. We have a skilled and motivated workforce in the Bank and they are committed to meeting the challenges presented to them.

Taking Brexit as an example, our planning for this year reflects the additional resources needed to deal with the applications for authorisation that will come our way. This will take the form of both an increase in staff recruited to the Bank, and contingency numbers for those areas where we think they might be needed. Experience is a key factor in hiring staff and we know that it will be a continuing challenge for us to recruit and retain the highly skilled people that are needed to effectively supervise sophisticated financial services firms. This challenge will increase if and when more firms enter the jurisdiction and begin staffing up.

You mentioned Brexit, which was at the forefront of everyone's minds during 2016, how did the Bank prepare for the Brexit vote?

Prior to the UK referendum on 23 June 2016, the Bank analysed and examined the regulatory, policy, economic and broader financial sector effects of a potential Brexit. That work prepared us for a number of potential Brexit scenarios.

From a regulatory and supervisory perspective, the focus has been to ensure that regulated firms were addressing and planning appropriately for the impacts, such as currency movements, liquidity provision and changes in economic outlook in the UK and in the Republic, in particular Irish firms having substantial business with UK clients, or with clients exposed to the UK economy, and/or having UK parents. We prod regulated firms to continue to consider and adapt to the potential implications for their business models and revenue streams. As such we have engaged extensively with regulated firms from all sectors.

Since June 2016, we have seen a material number of enquiries that are Brexit related and we have been approached by firms from across all sectors seeking preliminary engagement with the Bank regarding our authorisation process and supervisory expectations. Firms seeking authorisation in Ireland will find the Bank to be engaged, efficient, open and rigorous. We have considerable experience in dealing with authorisations and are ready to consider applications of firms seeking to operate commercially in and from Ireland.

Solvency II came into effect at the beginning of 2016, what has been the impact of this from a regulatory perspective?

Indeed, from 1 January 2016, all insurers in the European Union became subject to a new EU regulatory regime, Solvency II¹ following a lengthy period of preparation by both regulators and the insurance industry. The implementation of Solvency II presented many challenges, such as a transformation of the calculation of capital requirements.

Throughout 2016, a key focus was to ensure that the new regime was embedded effectively within the insurers we supervise. The Insurance Supervision Directorate has been reorganised with this in mind. The Directorate's new structure has been centred on the introduction of a revised engagement model, the creation of a dedicated analytics team, and on-site inspection capability. A key supervisory benefit of Solvency II is the increase in data granularity and consistency that we will be receiving from insurance firms, particularly with respect to annual and quarterly reporting.

We continued to communicate with industry regularly during the year and published guidance and letters to industry providing clarification to firms on specific issues as required.

Why has the Bank introduced changes to the mortgage measures in 2016?

The Bank had always committed to reviewing the measures on a regular basis and, on the introduction of the measures in February 2015, noted that it may, in future, consider it necessary to adjust any or all of the parameters of the proportionate Loan-to-Value (LTV) and Loan-to-Income (LTI) ratios in response to economic, market, or other developments. The first review, published on 23 November 2016, examined the early performance of the measures against the stated objectives and the potential side effects of the measures with a view to ensuring that the measures were correctly calibrated to prevent the build-up of risk in the financial system related to the property market.

The review was informed by data gathering and analysis by the Bank and by the submissions from external parties following the public call for evidence. The Bank undertook an extensive review of all the evidence

¹ Solvency II Directive (2009/138/EC).

submitted. We published research throughout the review process in addition to an extensive report on the outcome of the review process itself along with a feedback statement on the submissions received.

The review affirms that the overall framework is appropriate and the measures are contributing to financial and economic stability, reducing the risk of unsustainable lending and borrowing. A number of refinements were identified to improve the sustainability and effectiveness of the current framework, the most significant being the adjustment of the ceiling on the LTV ratio for all first time buyers at 90% from its previous level of 90% for loans up to €220,000 and 80% for the balance of loans above €220,000. These amendments came into force on 1 January 2017.

How does the Bank measure up to international standards?

As mentioned earlier, the Bank welcomed the publication of the IMF's Financial Sector Stability Assessment (FSSA) for Ireland on 28 July 2016, following completion of the Bank's participation in the IMF's review under their Financial Sector Assessment Program (FSAP). The FSAP is an in-depth exercise to assess the resilience of IMF member countries' financial sector, the quality of their regulatory and supervisory framework and their capacity to manage and resolve financial crises.

The assessment found that the Irish financial system has strengthened significantly since the financial crisis and has undergone major structural change stating that *"The authorities have been effective and vigorous in strengthening prudential regulation and supervision, implementing the lessons of the crisis, and keeping up with developments in European and international good practice."* The report acknowledged the strength of the Irish response to the crisis outlining that *"An effective policy response, supported by the IMF and European partners, and a flexible economy led to stabilization and a, by now well-entrenched, rapid recovery. . . The flexibility and extreme openness of the Irish economy, where multinationals— including offshore financial institutions—are major employers and investors, were key for the recovery."* The report also highlighted that *"A raft of regulations strengthening controls over the financial system have been introduced."*

Switching the focus to anti-money laundering, the Financial Action Task Force (FATF) is an inter-governmental body established to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The Bank played a leading role in the preparations and on-site visit of FATF as part of the Mutual Evaluation Review (MER) of Ireland during October and November 2016. This involved extensive engagement with other key agencies, firms and industry representative bodies and hosting of briefing sessions to raise awareness of the FATF MER process. The outcome of Ireland's MER will be determined at the FATF plenary in June 2017 and will lay the ground for further strengthening the Irish anti-money laundering and countering the financing of terrorism regime.

You will be leaving the Bank this year, what would you wish to stress at this juncture?

Ireland made a very thorough analysis of the failures of Financial Regulation in the previous decade and has overhauled its approach in all sectors. The deployment of assertive, risk-based supervision, underpinned by the effective use of its increased enforcement powers, complemented over the past few years by on-site inspections, proportionate supervision of lower impact firms, and more comprehensive and better integrated consumer codes and investment protection regulations, has brought the Bank in line with international standards. The range and size of financial firms is set to grow in Ireland, and if the Bank finds the ways and means to attract new colleagues and retain its skilled staff it will be well set to continue to protect effectively the customers' interests and the stability of the financial system.

Chapter 1: Overview of Financial Regulation in the Central Bank

1.1 Legal Framework and Statutory Objectives

The Bank was established by the Central Bank Act, 1942 (the Act). The functions of the Bank are set out in the Act with the primary objective of the Bank being that of price stability. The other statutory objectives of the Bank, which relate to the regulation of the financial services sector include:

- Stability of the financial system;
- Proper and effective regulation of financial institutions and markets, while ensuring that the best interests of consumers of financial services are protected; and
- Resolution of financial difficulties in credit institutions.

1.2 The Central Bank Commission

The Act provides that the activities and affairs of the Bank (other than the functions of the European System of Central Banks (ESCB)) are managed and controlled by the Commission. The Commission has the following statutory functions:

- Management and control of the affairs and activities of the Bank;
- Ensuring that the Bank's financial regulation and central banking functions are coordinated and integrated; and
- Ensuring that the statutory powers and functions conferred on the Bank are properly exercised and discharged.

The Commission has adopted its own terms of reference which sets out how it can best deliver on those responsibilities.

1.3 Delegation of Powers and Functions

The Act provides that any of the statutory functions may be delegated by the Commission to the Governor, a Deputy Governor or an employee of the Bank.

1.4 Members of the Commission

The Governor is the Chairman of the Commission. The other ex-officio members comprise the Deputy Governor (Central Banking), the Deputy Governor (Financial Regulation) and the Secretary General of the Department of Finance (the Department). The Minister for Finance appoints at least six, but no more than eight, other members of the Commission who typically hold office for a term of five years. Ex-officio members of the Commission remain members for as long they hold the office in question.

1.4.1 Governor

Philip R. Lane is the 11th Governor of the Bank, taking office on 26 November 2015. The Governor is appointed by the President, on the advice of the Government, for a term of seven years which may be extended by a further seven years. The Governor is an ex-officio member of the Governing Council of the European Central Bank (ECB). The Governor, or a substitute, must attend all meetings of the Governing Council. His roles and responsibilities are set out by the European Union (EU) Treaties, the ESCB Statute and the Act.

The Governor discharges his ESCB functions independently of the Commission and has sole responsibility for the performance of the functions imposed on him and the exercise of powers conferred on the Bank, by or

under the EU Treaties or the ESCB Statute. The independence of his role is enshrined in the EU Treaties and takes precedence over Irish law.

1.4.2 Deputy Governor (Financial Regulation)

Cyril Roux was appointed as the Deputy Governor (Financial Regulation) of the Bank on 1 October 2013. He is an ex officio member of the Commission. As the Deputy Governor (Financial Regulation) he is responsible for the all regulatory activities in the Central Bank including proper and effective regulation of financial institutions, markets and the protection of consumers of financial services.

Mr Roux is a member of the Supervisory Board of the Single Supervisory Mechanism (SSM)² and of the General Board of the European Systemic Risk Board (ESRB). He is a member of both the Management Board and the Board of Supervisors (BoS) of the European Securities and Markets Authority (ESMA), as well as being a member of the BoS of the European Banking Authority (EBA)³. Mr Roux was elected chair of ESMA's Investment Management Standing Committee in September 2016.

1.5 Internal Governance Structures

While the Commission has overall responsibility for the management and control of the Bank, there are a number of internal committees with responsibility to coordinate the development and implementation of policies and to advise and inform on major issues.

The Bank's internal governance includes the following committees, which are chaired by the Governor:

- The **Governor's Committee** oversees the preparation for Commission meetings and follow-up actions, approves senior appointments and considers other significant strategic issues.
- The **Senior Leadership Committee** ensures alignment of all activities and the successful execution of the Bank's strategy through the development and review of the organisational Balanced Scorecard. The Committee ensures the structures and activities across the Bank are aligned and coordinated, and focuses on delivering strategic outcomes agreed by the Commission.
- The **Financial Stability Committee (FSC)** is responsible for monitoring and assessing domestic and international economic and financial developments and for highlighting potential areas of concern in the Irish financial system. The committee's focus is, in particular, on risk mitigation strategies and the consideration, implementation and review of micro and/or macroprudential policy instruments. The role of this committee is both to advise the Governor, and to discuss with and inform key internal management on financial stability issues.
- The **Macroprudential Measures Committee's (MMC)** role is to advise on the regular reviews of bank-related national macroprudential measures and to make recommendations about maintaining or revising these rules as appropriate. The Bank is the designated national macroprudential authority in Ireland. In recent times, several macroprudential measures have been activated via the banking system. These include: borrower-based measures such as mortgage rules; the counter-cyclical capital buffer; the other systemically important institution buffer; and reciprocation of macroprudential policy measures taken by other member states. The scope of the MMC may evolve in line with shifts in the nature of macroprudential interventions in the Irish financial system.

² The SSM is a system of prudential supervision of credit institutions, comprising the ECB and the national competent authorities (NCAs) of participating EU countries, including the Central Bank of Ireland.

³ ESMA in Paris, the EBA in London and the European Insurance and Occupational Pensions Authority (EIOPA) in Frankfurt, are the three European Supervisory Authorities (ESAs) that replaced existing European architectures as part of the EU response to the 2007-2008 financial crisis. Further detail on the ESAs are contained throughout the document and Chart 3.9 includes a graphical representation of the ESAs.

The two high-level committees for Financial Regulation, chaired by the Deputy Governor (Financial Regulation), are:

- The **Supervisory Committee**, which advises him and relevant supervisory directorates and divisions on issues central to the management of supervisory risks and also on the development and enhancement of risk-based supervision and supervisory engagement, including Probability Risk and Impact System (PRISM)⁴ matters.
- The **Policy Committee**, which advises him on regulatory policy issues and initiatives including consultation papers, feedback statements, codes, guidelines, and regulations before their adoption by the Deputy Governor or by the Commission, in accordance with relevant delegations.

1.6 Organisation Chart – Financial Regulation

Responsibility for authorisation, supervision and regulation of financial service providers is allocated over seven directorates within the Bank which report directly to the Deputy Governor (Financial Regulation).

Up to the end of 2016, the Markets Supervision Directorate, headed by Mr Gareth Murphy, grouped the supervision of asset management firms, funds and securities. Following his departure from the Bank, this directorate was divided into two from 1 January 2017, leading to the creation of the Asset Management Supervision Directorate, overseeing investment firms and fund service providers, and the Securities and Markets Supervision Directorate, overseeing investment funds, securities and markets.

The first directorate thus created is a prudential supervision directorate, sitting alongside the Credit Institutions Supervision Directorate and the Insurance Directorate. The second directorate's core remit is investor protection and it sits alongside the Consumer Protection Directorate.

In the course of 2016, the Enforcement Division of the Enforcement Directorate was split into two, giving rise to the investigations and to the advisory divisions.

A description of the remit of each directorate is set out in **Chapter 3**. The chart overleaf shows the organisation of financial regulation as of January 2017 and the divisional structure of each directorate.

⁴ PRISM is the Bank's framework for the supervision of regulated firms. PRISM has been developed to enhance the Bank's ability to deliver judgement based, outcome focused supervision.

Central Bank Commission



Governor
Philip R. Lane



Deputy Governor
Cyril Roux



* Mary O’Dea will take up her position in early September 2017. Until that time, Grainne McEvoy, Head of Securities and Markets Supervision Division, will be Acting Director.

Chapter 2: The Bank's Key Financial Regulation Outcomes for 2016

The Bank continued to build on the work commenced in previous years to restore stability and confidence to the financial system, to build and develop the regulatory framework, and to ensure that the needs and interests of consumers are protected.

This chapter sets out five key financial regulation outcomes of the Bank in 2016. These outcomes were pursued in the delivery of the strategic responsibilities of the Bank as set out in the Strategic Plan 2016-2018. They were achieved through the completion of many actions by Bank staff across the regulatory directorates and supported by staff within the central banking and operations pillars, which include the legal and regulatory transactions divisions of the Bank.

Chapter 3 contains further details of these and other outcomes.

2.1 The protection of the customers' interests



KEY OUTCOME

1

The Bank protected the interests of the customers of financial service providers.

The Bank, through its actions, protected the clients of firms regulated by the Bank, including mortgage borrowers, credit union members, clients of investment firms, and policyholders of Irish insurers. The Bank alerted foreign regulators responsible when, in its view, Irish policyholders were put under risk of financial loss.

Key actions undertaken to achieve this outcome

- The multi-year Tracker Mortgage Examination, launched in the Autumn of 2015, is the most significant supervisory review that the Bank has undertaken under its consumer protection mandate, covering all mortgages of all lenders, which have been impacted. 2016 was a crucial year in progressing the Examination. At the end of December 2016, approximately 8,200 impacted accounts had been identified, and the Bank expects the lenders to engage with most impacted customers in the course of 2017⁵. The Bank monitors progress through structured direct engagement with each lender and its appointed external independent party and through on-site reviews and reviews of regular progress reporting. Where necessary the Bank will take appropriate supervisory action, including enforcement action, to ensure that fair outcomes are achieved for consumers, as demonstrated in the outcome of the November 2016 settlement agreement with Springboard Mortgages Limited, where the Bank issued a reprimand and imposed a fine of €4.5m in respect of breaches of the Consumer Protection Codes. The Bank also required the firm to provide redress and compensation to customers impacted by the breaches to the amount of €5.8m.
- Protecting the savings of credit union members is a key priority of the Registry of Credit Unions. On 1 January 2016, Regulations⁶ allowing a credit union to apply to the Bank for approval to retain individual members' savings in excess of €100,000 or increase individual members' savings in excess of €100,000 commenced. The aim of these Regulations is to increase the protection of members' savings not covered by the Deposit Guarantee Scheme. In November 2016, the Bank took action to liquidate Rush Credit Union. This action, was necessary given the scale of issues identified in the credit union: namely ongoing failures of governance, controls and lending practices which had completely compromised the financial position of Rush Credit Union. The savings of members of the credit union were protected.
- Since January 2016, any retail intermediary that fails to submit the Annual Return by the required date is immediately contacted by phone, email or on-site inspection team and enforcement action can be taken if deemed necessary. During 2016, the Bank pursued 126 retail intermediaries for breaches of Professional Indemnity Insurance (PII) cover (being an important protection for consumers if they have to make a claim against the firm), of which 117 cases were resolved. The remaining nine intermediaries are subject to ongoing supervisory action.
- Throughout the year the Bank carried out a great many supervisory engagements with regulated firms' executive management and boards, on-site inspections and thematic reviews, across a broad range of risk areas and sectors during 2016. Detailed risk mitigation plans (RMPs) were issued on foot of the findings of these supervisory engagements, to ensure that risks are mitigated, consumers are protected and that culture and governance are appropriate. Details of these supervisory engagements by sector are set out in more detail in **Chapter 3**.
- The Bank regularly engages with other regulators about the risks taken abroad by Irish firms, their business conduct and other issues. Conversely, the Bank engaged with several foreign regulators as regards Irish risks and complex set-ups more prone to failure and to the ultimate detriment of Irish customers. In most cases, satisfactory supervisory outcomes agreed with the Bank were reached by end 2016.

⁵ At end February 2017, approximately 9,900 accounts had been identified.

⁶ S.I. 1/2016 – Credit Union Act 1997 (Regulatory Requirements) Regulations 2016.

2.2 The strengthening of the finances of regulated firms



KEY OUTCOME 2

The Bank oversaw the strengthening of the capital structures of the firms it regulates and the restructuring of credit unions.

A breach of capital/solvency rules can pose a significant consumer risk, as it can affect a firm's ability to continue operating as a going concern and can lead to poor outcomes for consumers. Better capitalised firms are more resilient to adverse events and less susceptible to failure, reducing the likelihood of financial detriment to their consumers.

Key actions undertaken to achieve this outcome

As a result of the supervisory actions taken by the Bank, Irish banks and insurance companies took action to strengthen their capital bases and solvency positions respectively.

- While the aggregate transitional Common Equity Tier 1 (CET1) ratio for the retail banks remained broadly stable to September 2016, the fully loaded ratio improved from 11.8% to 15.1%. These changes were as a result of capital restructuring by the banks to enhance their fully loaded capital positions. The aggregate fully loaded CET1 capital positions of international banks operating in Ireland are well above the European average.
- The Bank continued to actively drive reductions of Non-Performing Loans (NPLs) for the retail banks, which declined by 26% over the course of 2016 (equivalent to a €15.2bn reduction). Lower NPLs increase a bank's profitability, reduce funding costs and release bank capital.
- Non-life companies strengthened their solvency position and underwriting discipline during 2016; resulting in improved balance sheets and loss ratios, with all domestic life and non-life companies successfully meeting solvency capital requirements under the Solvency II regulatory framework by Q4 2016. The Bank has also ensured that firms have increased support from their parent companies and have put in place more extensive reinsurance cover in a number of cases.

Further engagement and supervisory initiatives to improve the financial soundness of regulated firms and sectors include:

- Through the Bank's engagement on the Supervisory Review and Evaluation Process (SREP) and Risk Mitigation Plans (RMPs) issued to Fund Service Providers to implement a capital planning framework, the Bank has ensured that a robust capital assessment of firms is being carried out and a more detailed understanding at board level of the risks facing firms and associated capital was achieved.
- Following public consultation in 2016 on the introduction of a risk-based Capital Requirement Framework for Market Operators (MOs) in Ireland to replace an existing bespoke framework, the new framework will be live by end-Q2 2017. The revised framework sets the basic capital requirement for MOs and will align the key risks of a MO more closely to the capital requirement.
- As part of a process to conduct a review of the Internal Capital Adequacy Assessment Process (ICAAP) to increase the supervisory focus and financial analysis of low impact MiFID investment firms within scope of CRD IV, a new SREP Questionnaire was issued to 13 of these firms.

Building on the increase in the pace of restructuring activity that had emerged during 2015, restructuring of the credit union sector in order to address the viability and operational challenges that face many credit unions has continued. Most mergers provide an important starting point to address financial and operational weakness in credit unions and to provide a broader scope of product and services offerings to members.

2.3 Holding regulated firms and individuals to account



KEY OUTCOME 3

The Bank has held regulated firms and individuals to account through the effective use of its Enforcement tools.

The assertive, risk-based approach to financial regulation in Ireland is underpinned by a robust use of the full range of the Bank's enforcement powers. When regulated firms, persons concerned in their management or individuals breach their obligations, the Bank will consider the most appropriate use of its powers against them.

Key actions undertaken to achieve this outcome

- The Bank concluded nine Administrative Sanctions Procedure (ASP) cases; resulting in fines of €12.05m being imposed by the Bank, the largest total amount of fines imposed in one year to date.
- Public statements in respect of fines imposed by the Bank in 2016 are published on the Bank's website. The publication of ASP outcomes informs financial services firms about issues identified by the Bank, how a firm or individual fell below the expected standard and why a particular regulatory response was adopted, which serves to improve compliance generally in all firms and sectors.
- The first ASP case arising from an ECB instruction under SSM Regulations concluded by way of settlement with KBC Bank Ireland plc in October 2016. The Bank imposed a fine of €1.4m on the firm in respect of breaches of the Code of Practice on Lending to Related Parties 2010 and the Code of Practice on Lending to Related Parties 2013.
- In November 2016, the Bank concluded an ASP case with Springboard in respect of breaches of obligations to tracker mortgage customers. The Bank issued a reprimand and imposed a fine of €4.5m on the firm in respect of serious breaches of the Consumer Protection Codes 2006 and 2012. In addition, the Bank required the firm to implement a major redress and compensation programme under which the firm provided to affected customers €5.8m as at November 2016.
- In July 2015, Notices of Inquiry were issued in respect of Irish Nationwide Building Society (INBS) and five individuals who were concerned in the management of INBS. In response, two of these individuals brought High Court proceedings seeking to prevent the Inquiry as against them from proceeding and, in one case, challenging the constitutionality of the Bank's ASP powers. The constitutional challenge ran over April and May 2016 and, on 29 July 2016, the High Court decided that the ASP was not an administration of justice and was, therefore, constitutional. The High Court judgments with respect to the Bank's ASP uphold the very real and significant public interest in the proper regulation of the financial sector, the need to investigate suspected wrongdoing and the deployment by the Bank of its statutory enforcement powers. The Inquiry in respect of the five individuals concerned in the management of INBS is currently proceeding.
- A case in relation to the failure to hold adequate professional indemnity insurance was also referred to Inquiry in 2016. This case was subsequently settled in July 2016, with the Bank imposing a fine of €2,750 on an insurance intermediary, Seamus Sutcliffe t/a The Mortgage Centre, for breaches of European Communities (Insurance Mediation) Regulations 2005.
- In May 2016, the Bank published a public statement confirming the issue of a prohibition notice under the Fitness and Probity regime in respect of Darren Gleeson, a former director of a retail intermediary. This prohibition notice prevents Mr Gleeson from acting in any controlled function indefinitely.
- The Bank issued a suspension notice, using its powers under the Fitness and Probity regime, to the former Manager of Rush Credit Union. In September 2016, the Bank successfully applied to the High Court for an order extending this suspension notice.
- The Bank successfully defended an appeal to the Irish Financial Services Tribunal (IFSAT) by Mr David Redmond of the Bank's 2015 decision to refuse his application for authorisation as a sole trader on fitness and probity grounds.

2.4 Enhanced regulations protecting customers and investors



KEY OUTCOME

4

European and domestic regulations were enhanced to protect consumers and investors and strengthen regulated firms.

A number of significant regulatory changes came into effect in 2016, driven by European law makers or by the Bank, enhancing the protection of investors and customers of financial service providers.

Key actions undertaken to achieve this outcome

- On 1 January 2016, Ireland implemented Solvency II – the new regulatory regime for insurance undertakings and it is now embedded within day-to-day supervisory activities. The regime compels insurers to focus and devote significant resources to the identification, measurement and proactive management of risks. More robust risk management and governance requirements means consumers are better protected. Robust assessments of pre-approved controlled function holders were undertaken, particularly for the critical functions roles introduced under Solvency II.
- New Investor Money Regulations (IMR) came into effect on 1 July 2016. The IMR are designed to ensure the safeguarding of investor money held in collection accounts by Financial Service Providers (FSPs). The Bank established the population of FSPs holding investor money and evaluated how the new requirements have been embedded. The Bank assessed the strength of operational and governance arrangements in relation to the protection of client assets and investor money.
- Ireland implemented the Market Abuse Regulations (MAR) and related directives aimed at ensuring greater transparency and market integrity in July 2016. The new legislation strengthens the legal framework underpinning the detection and sanctioning of market abuse and covers new offences, such as attempted market abuse and inciting, aiding and abetting these offences.
- In September 2016, the Bank published its first cross-industry policy communication on IT and cybersecurity risks which set out a clear statement of the standards, practices and quality that the Bank expects firms to demonstrate in managing these risks. The communication provides guidance on key areas including IT risk management and governance, cybersecurity, IT outsourcing and business interruption. The communication provided a yardstick for supervisors against which they can measure firms' progress in effectively managing and mitigating IT and cybersecurity risks.
- The Bank's Code of Conduct on the Switching of Payment Accounts with Payment Service Providers (PSPs), which came into effect on 21 September 2016, replaces the previous current account switching code. The purpose of the new statutory code is to facilitate switching by consumers between PSPs, including banks, and is part of the transposition of the new Payment Accounts Directive (PAD) in Ireland.
- In November 2016, the Bank consulted on changes to the Minimum Competency Code (MCC), which sets minimum professional standards for staff of FSPs when they are dealing with consumers in relation to retail financial products. The proposed changes relate to a number of areas including minimum experience required, product design and credit unions.
- The Bank published a package of targeted rules and detailed guidance directed at the governance practices, compliance management and effective supervision of fund management companies. This package sets high standards for how directors and management carry out their roles and how fund management companies should operate in order to demonstrate compliance with their regulatory obligations.
- The Bank introduced, by amending the Consumer Protection Code 2012, a number of increased protections for variable rate mortgage holders. The enhanced measures, which apply from 1 February 2017, require lenders to explain to borrowers how their variable interest rates have been set, including in the event of an increase. The measures also improve the level of information required to be provided to borrowers on variable rates about other products.

2.5 Completion of the Financial Sector Assessment Program (FSAP)



KEY OUTCOME 5

The Bank successfully completed the FSAP conducted by the International Monetary Fund (IMF) during 2016.

The IMF carried out an in-depth analysis to assess the stability of the Irish financial system, including the banking and funds sectors. The programme included assessment in the following areas:

- The resilience of the financial sector (risk and vulnerabilities assessment);
- The quality of the regulatory and supervisory framework; and
- The capacity to manage and resolve financial crises.

The FSAP was a priority in 2016 as it was the first FSAP since the financial crisis. The assessment found that the Irish financial system has strengthened significantly since the financial crisis and has undergone major structural changes. It also found that the prudential regulation and supervision in Ireland had improved greatly since the previous IMF assessment in 2013 and found the Bank to be effective and thorough in providing intrusive and assertive supervision.

The FSAP identified some remaining challenges and made a number of recommendations, including in relation to safeguarding regulatory independence, increasing length of service, and implementing new regulatory regimes.

Key actions undertaken to achieve this outcome

- Extensive collection, validation, assessment and analysis of data to ensure the smooth running of the FSAP.
- Considerable Bank-wide resources devoted to working constructively and collaboratively with the IMF.
- Stress testing undertaken by the Bank as part of the FSAP to examine the resilience of the Irish banking system to solvency, liquidity and contagion risks.
 - » The stress test found that funding and credit risks remain the two main vulnerabilities in the banking sector, with some banks exposed to liquidity risks under a severe scenario. The analysis also found that banks are less vulnerable to direct contagion risks.
- A further stress test of Irish money market funds, which fed directly into the asset management portion of the IMF's final report. Arising from this work was the first ever collection of daily redemption data from Irish investment funds which will form the basis of joint research with the IMF on investment fund liquidity analysis.
- A number of initiatives are ongoing in the Bank and SSM related to the FSAP recommendations.

Further detail on the IMF FSAP is outlined in **Chapter 8**.

Chapter 3: Directorate Overview and Outcomes



Bernard Sheridan
Director of Consumer
Protection

3.1 Consumer Protection Directorate

Objectives

A core statutory objective of the Bank is to seek to ensure that the best interests of consumers of financial services providers are protected. The Bank's consumer protection objectives are based on the expectation that firms are acting in the best interests of their customers, are treating them fairly and with dignity and respect. The annual Consumer Protection Outlook Report (CPOR)⁷, last published in February 2017, describes how objectives will be achieved and what the main priorities are. The Bank's work, which is risk and evidence based, is focused on delivering the right outcomes for consumers and seeks to influence a consumer-focused culture in all firms. This enables consumers to have confidence in the decisions they make.

The Consumer Protection Directorate contributes to the Bank's delivery of its mission to protect consumers within the three broad functions performed in the directorate i.e. supervision, gatekeeper and consumer policy. The directorate assesses applications for authorisation from individuals and firms across a number of retail sectors⁸ and also monitors and investigates compliance by firms with consumer protection and prudential requirements. Robust supervisory action is taken where elevated risks, actual or potential, are identified. Regular research is conducted and through policy work the directorate seeks to ensure the consumer protection framework is fit for purpose.

⁷ <https://www.centralbank.ie/docs/default-source/Regulation/consumer-protection/consumer-protection-outlook-report/consumer-protection-outlook-report-2017.pdf?sfvrsn=2>

⁸ Payment Institutions, Electronic Money Institutions, Credit Servicing Firms, Retail Credit Firms, Moneylenders, Mortgage Intermediaries and Mortgage Credit Intermediaries, Insurance Intermediaries, Investment Intermediaries, Debt Management Firms, Bureaux de Change, Money Transmission Firms and Home Reversion Firms.

2016 Key Outcomes

The Tracker Mortgage Examination

In October 2015, the Bank announced that it had launched a broader examination of tracker mortgage-related issues. The Examination is the most significant supervisory review that the Bank has undertaken, to date, under its consumer protection mandate. Due to the significance of the work, and the general public interest in the review, the Bank has published regular updates on progress with the Examination.

The initial phase of the Examination required lenders to put governance structures and systems in place to conduct a comprehensive examination. Lenders were required by the Bank to appoint external independent third party assurers to oversee the Examination and to ensure that it is being carried out in line with the Bank's Framework for the conduct of the Examination. The second phase of the Examination is ongoing and involves extensive internal reviews of lenders' mortgage books to identify customers who fall within its scope. The Bank continues to monitor lenders' progress through direct engagement with each lender and its appointed external independent party and through on-site reviews and regular reviews of progress.

When groups of impacted customers are identified, in the first instance, the lender must stop charging the incorrect rate of interest on the customer's account. The lender must then communicate this to the customer, to ensure that any further customer detriment is stopped as early as possible. Once a full review of the customer's account is complete, following external independent third party assurance, the lender will then issue a letter to the customer explaining the nature of the error, the correct rate to apply to the customer's account and information on the next steps in the Examination, including the redress and compensation process. Where necessary, the Bank will take appropriate supervisory action, including enforcement action, to ensure that fair outcomes are achieved for consumers, as demonstrated in the outcome of the November 2016 settlement agreement with Springboard.

Enhancing the Consumer Protection Framework for Borrowers

The Bank introduced, by amending the Consumer Protection Code 2012, a number of increased protections for variable rate mortgage holders. The enhanced measures, which apply from 1 February 2017, require lenders to:

- Explain to borrowers how their variable interest rates have been set, including in the event of an increase;
- Improve the level of information required to be provided to borrowers on variable rates about other products;
- Produce and publish a summary statement of their policy for setting each variable interest rate;
- For increases in a variable interest rates, lenders will be required to include the reason for the rate increase in the notification provided to the borrowers; and
- Notify variable rate borrowers of alternative mortgage options that could provide savings for the borrower, both on an annual basis and also when notifying borrowers of an increase in the variable interest rate, including details of where the borrower can get more information to assist customers wishing to switch mortgage providers.

Commission Payments to Intermediaries

In July 2016, the Bank published a discussion paper on the topic of the payment of commissions to intermediaries by insurance companies, banks and other financial firms for the sale of their products, in order to stimulate discussion and obtain feedback on the risks and benefits to consumers from this practice. The objective of this initiative was to identify any additional consumer protection measures which should be considered in order to encourage responsible business conduct, fair treatment of consumers and to avoid

conflicts of interests. The responses to the discussion paper and the Bank's ongoing stakeholder engagement, including with consumer groups, will inform the Bank's ongoing consideration of this matter and its technical advice to government on the implementation of the Markets in Financial Instruments Directive (MiFID II)⁹ and the Insurance Distribution Directive (IDD)¹⁰. In this context, it is planned that a consultation paper will be published in 2017, outlining proposed measures to strengthen protections for consumers in this area.

Minimum Competency Code (MCC) Review

The Bank first introduced the MCC in 2007 which established minimum professional standards for staff of financial service providers when they are dealing with consumers in relation to retail financial products. The Bank has commenced a review of the Code. In November 2016 a consultation paper was published setting out a number of proposed changes including minimum experience required, product design and credit unions. Taking into consideration the consultation feedback, the Bank will introduce the new requirements in 2017.

Protecting the Interests of Consumers of Failed Foreign Insurance Companies

During 2016, the Bank has also been dealing with the failure of two foreign insurance companies (Enterprise Insurance from Gibraltar and Gable Insurance from Liechtenstein) which were operating in Ireland on a Freedom of Services (FOS) basis. A priority has been to work with the home regulator to ensure that Irish policyholders' interests were being protected and that policyholders were kept informed of developments through updates on the Bank website, and also requiring the relevant insurance brokers to inform their policyholders of what steps they should be taking to ensure they continue to have insurance cover.

Facilitating Switching of Payment Accounts

The Bank's Code of Conduct on the Switching of Payment Accounts with Payment Service Providers (PSPs), which came into effect on 21 September 2016, replaces the previous current account switching code. The purpose of the new statutory code is to facilitate switching by consumers between PSPs more generally, including banks, and is part of the transposition of the new Payment Accounts Directive (PAD)¹¹ in Ireland. It sets out the process, including timeframes, which PSPs must comply with when helping consumers switch accounts. On 22 November 2016, the Bank published its latest Consumer Protection Bulletin on Current Accounts and Switching. This Bulletin showed that in the first half of 2016 there were 3,600 switches carried out under the switching code and that 99% of switches were completed within the time required by the Code.

Case Study 1: Thematic reviews focusing on key consumer risks

During 2016, the Bank conducted a number of product-specific thematic reviews where it was thought there was a potential risk to its consumer protection objectives.

Health Insurance

In March, the Bank published the findings from the thematic reviews of four health insurance providers. The thematic reviews focused on how providers were engaging with and/or advising their consumers during the annual renewal process. The main findings were:

- Renewal notices did not provide sufficient information to consumers on the importance of contacting their insurer to ensure that they are being offered the most suitable policy to meet their needs.
- Providers collected less information from consumers purchasing online prior to making recommendations, compared to the face-to-face or telephone-based sales processes.
- Three providers' websites, when recommending a policy, did not offer consumers options from their full range of available policies.

9 Directive 2014/65/EC

10 Directive 2016/97/EC

11 Directive 2014/92/EU

Case Study 1: Thematic reviews focusing on key consumer risks

The Bank required providers to enhance the content and presentation of the information contained in policy renewal notices. Based on the findings of this work, consumers now have much enhanced protections when purchasing and renewing their health insurance policies, including:

- Providers must include warning notice on renewals to clearly explain to consumers that their policy will auto-renew if they do not contact their health insurance provider prior to their renewal date;
- Providers must proactively encourage consumers to make contact to ensure that the provider assesses if there are more suitable policies available; and
- Provider's website quotation facilities are enhanced to provide greater policy choice - all policies are available to consumers who wish to purchase a policy online.

Structured Retail Products (SRPs)

The Bank highlighted in its 2016 CPOR the risks to consumers from firms selling higher risk products in the low interest rate environment, as well as poor product oversight and governance. One of the priority themes identified in that Report was a review of the SRPs market in Ireland, as these products are being offered to consumers as an alternative to deposits. The Bank undertook a thematic review which consisted of a desk-based review of 20 investment and stockbroking firms and credit institutions manufacturing and/or distributing SRPs, followed by on-site inspections in five of these firms. The main findings included:

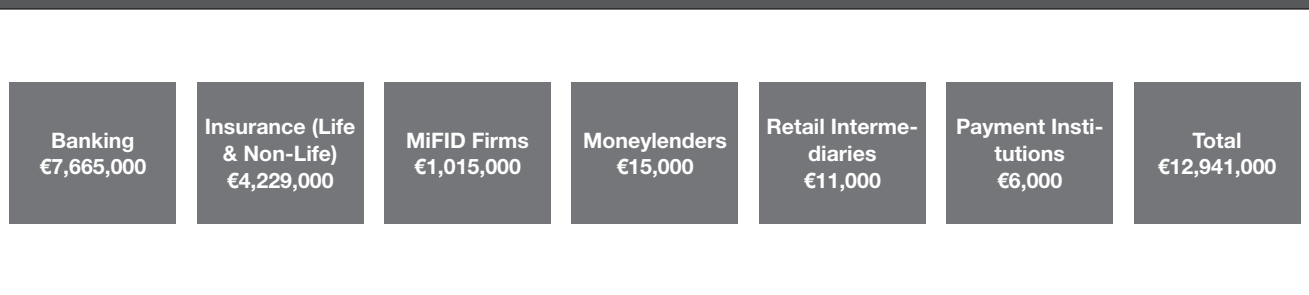
- There had been a significant move away from the sale of capital protected deposit-based products towards more complex, capital at risk products;
- Weak product governance arrangements were identified in a number of firms in areas including target market identification and product testing; and
- Credit Linked Notes¹² are being sold by a small number of firms to consumers and, in some cases, the higher risks associated with such products are not being adequately highlighted.

All of the issues identified were subject to individual supervisory action with the relevant firms.

Consumer Restitution

The following consumer restitution has been made by firms in each sector both on foot of errors reported by firms (required by the Code) and also as a result of issues identified through supervisory activity¹³.

Chart 3.1: Consumer Restitution 2016¹⁴



¹² Credit Linked Notes are particularly complex SRPs that can carry a much higher risk than other products. Due to the nature of the products, they may not be suitable for most consumers.

¹³ Figures for restitution on foot of issues identified through supervisory activity were €13K approximately and have been incorporated into restitution on foot of errors reported.

¹⁴ Please note the figures for consumer restitution are approximate.

Monitoring Compliance across the Retail Intermediary Sector

There were 2,457 retail intermediaries supervised by the Bank at 31 December 2016. These firms provide advice and sell insurance, investment and mortgage products on behalf of insurance companies, banks and other firms. The Bank monitors the sector through analysis of financial returns, trigger-based supervision and spot-check on-site inspections to identify and mitigate issues that may negatively impact on consumers. Thematic reviews also continue to be an important supervisory tool for this sector of the industry, given its size. The following thematic reviews/supervisory work were conducted in 2016:

- **Review of Compliance with Minimum Reporting Standards**

A significant thematic review continued throughout 2016 to target retail intermediaries that were not meeting the minimum standards in terms of complying with reporting and other obligations to the Bank. The Bank's objective was to target a culture of non-compliance, which can often signal other issues in those firms that can impact negatively on consumers.

At end-2016, of the 421 firms in-scope of this inspection, 411 of these firms had either submitted the annual returns or revoked their authorisation. The majority of revocations were submitted on a voluntary basis following supervisory engagement. Additionally, in 2016 the review was extended to include a further 61 firms, resulting in 28 unannounced on-site inspections. At end-2016, all 61 firms have either submitted the annual returns or voluntarily revoked their authorisations. To maintain these high levels of compliance with minimum standards into the future, a new monthly trigger process was established to enable early targeting and remediation of firms that failed to submit the annual returns on time. At end-year, the new process is working successfully with 36 firms subject to ongoing supervisory action.

- **Debt Management Firms**

Building on the thematic review of debt management firms' compliance with the Consumer Protection Code in 2015, the Bank further strengthened its supervision of this sector by requiring all Debt Management firms to submit an annual return. This return provides key information on firms in the sector, ensuring that they continue to comply with the requirement to be solvent and that they hold the correct level of PII.



Ed Sibley

Director of Credit Institutions Supervision

3.2 Credit Institutions Supervision Directorate

Objectives

The Credit Institutions Directorate comprises three Banking Supervision Divisions: Supervision, Inspections and Analysis; and the Registry of Credit Unions. The Bank's prudential supervision objectives are to protect consumers and financial stability by demanding of Irish credit institutions that they:

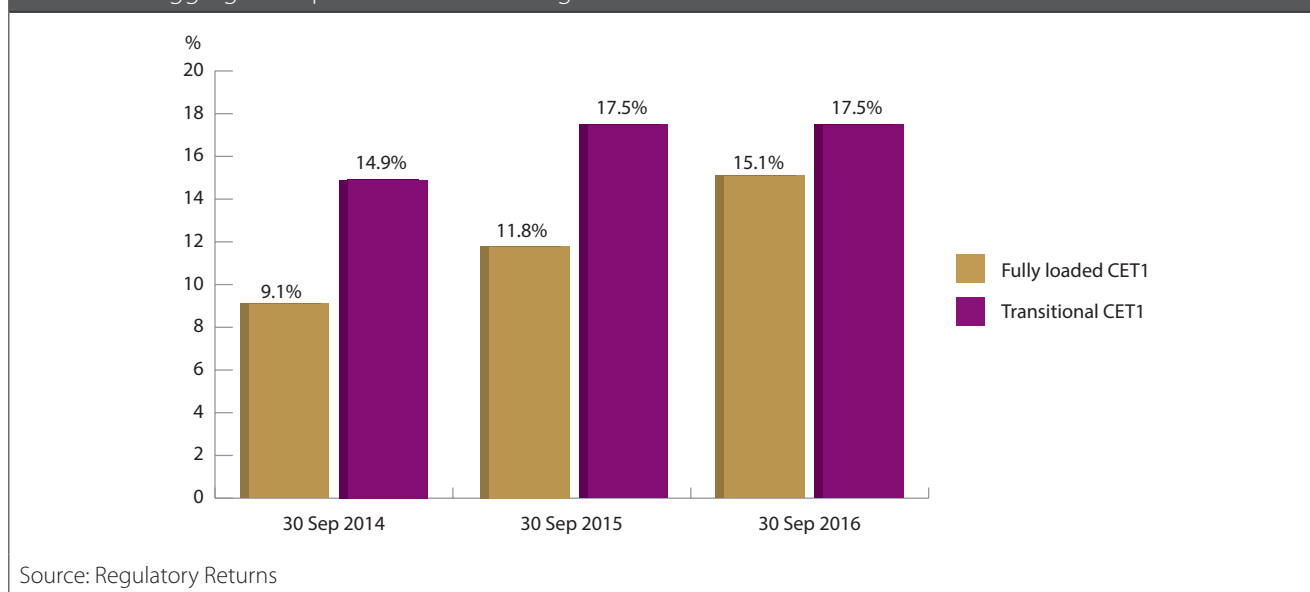
- Have sustainable, capital generating business models over the economic cycle;
- Are governed and controlled appropriately, with clear and embedded risk appetites, which drive an appropriate culture within them;
- Have sufficient financial resources (considering both capital and liquidity needs); and
- Are resolvable in the event of a failure without recourse to the Irish taxpayer.

2016 Key Outcomes

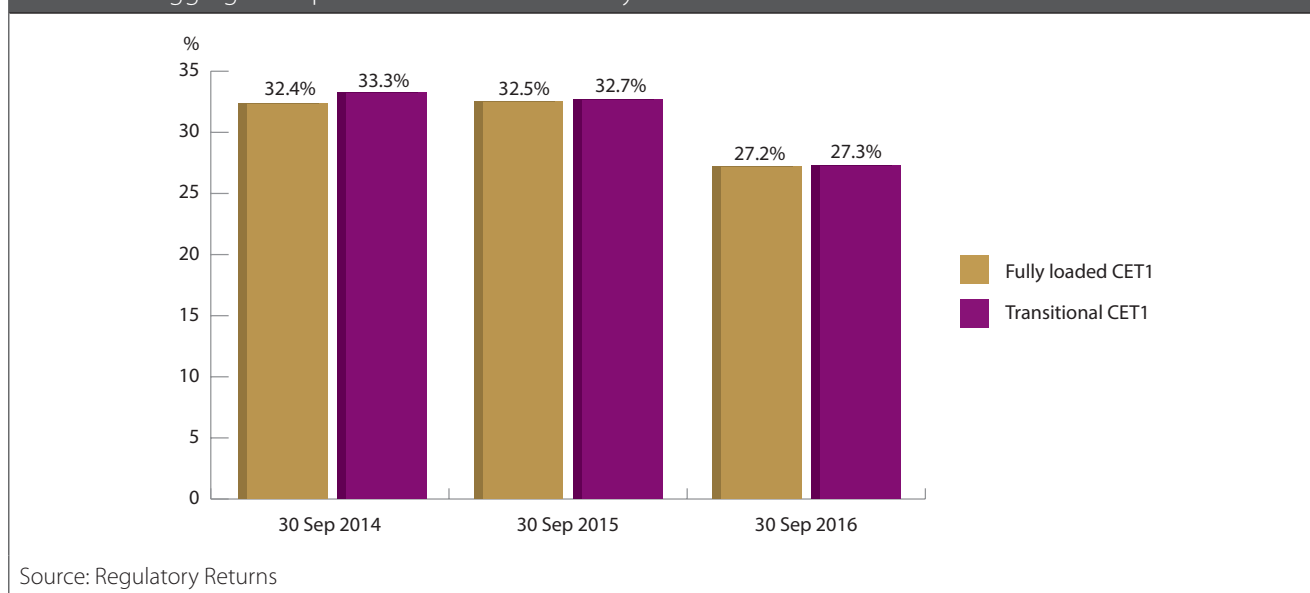
Improving Capital Ratios

While the aggregate transitional Common Equity Tier 1 (CET1) ratio for the domestically focused retail banks remained broadly stable to September 2016, the fully loaded ratio¹⁵ improved from 11.8% to 15.1%. These changes were as a result of capital restructuring by the banks to enhance fully loaded capital ratios, increased profitability offset somewhat by dividend payments and further deleveraging. Fully loaded levels are lower than transitional capital ratios due to deductions for deferred tax assets and grandfathering of capital instruments. The CET1 capital ratio trends are illustrated in the chart below. The improved capital ratios of these banks bring their CET1 ratios within the range of average European ratios. Notwithstanding this improvement, the stress test exercises conducted in 2016, including the IMF FSAP bank stress test exercise, highlights that vulnerabilities remain.

¹⁵ One of the main objectives of the CRD IV / CRR framework is to increase the resilience of the banking sector by strengthening the quality of regulatory capital. For this purpose, the framework sets stricter rules for the definition of capital, and includes a phasing-out of capital no longer eligible as regulatory capital, such as deferred tax assets. Banks are not expected to meet fully loaded CET1 ratios until 2024, although much of the transition will be complete by 2018.

Chart 3.2: Aggregate Capital Ratios – Retail Significant Institutions

While the aggregate fully loaded CET1 capital positions of international banks operating in Ireland have reduced this year from 32.5% to 27.2%, they are well above the European average.

Chart 3.3: Aggregate Capital Ratios – Internationally Focused Banks

Reduction of Non-Performing Loans (NPLs)¹⁶

The Bank's approach to NPL resolution is focused on ensuring banks are sufficiently capitalised, hold appropriately conservative provisions, and have fit for purpose resolution strategies and operations while ensuring the fair treatment of customers. At December 2016, NPLs for the retail banks reduced by €15.2 billion or 26% over the previous 12 months. Improvements were evident across all portfolios and were driven by a mixture of resolution activities including restructures, asset sales, and loan portfolio disposals. NPLs have reduced in every quarter since their peak in Q3 2013. However, as of Q3 2016, NPLs for the domestically focused retail SIs remain elevated and stood at 19.3% of gross loan exposures, equivalent to €43.9 billion.

¹⁶ NPL definition is per the EBA ITS on supervisory reporting on forbearance and non-performing exposures under Article 99(4) of Regulation (EU) No 575/2013 (CRR).

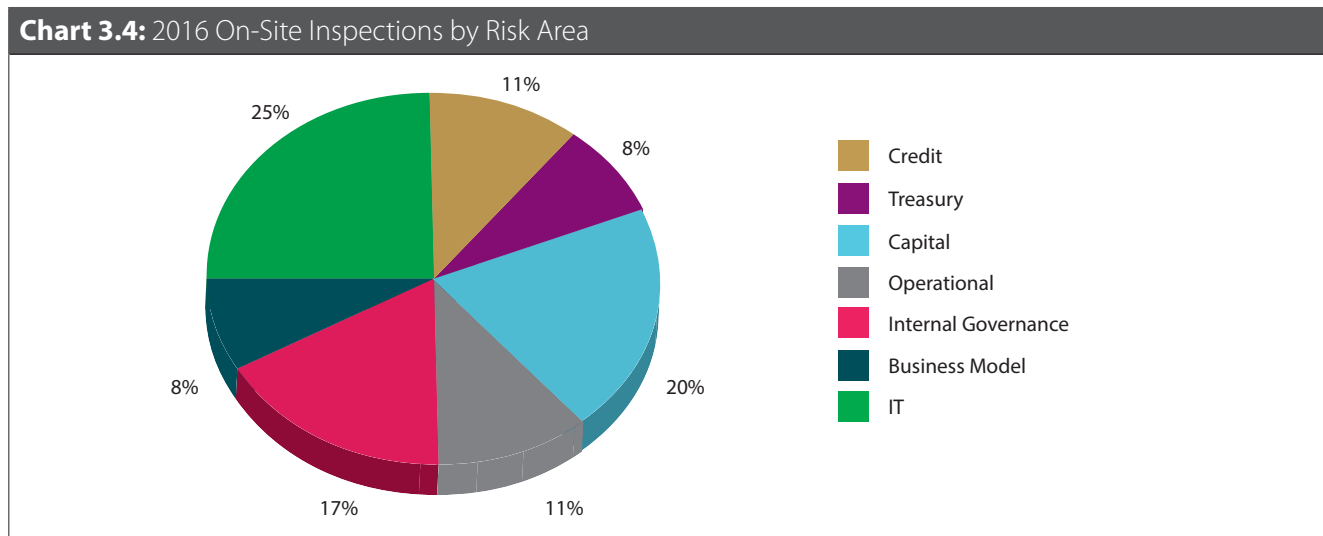
The SSM NPL Task Force published draft guidance on NPLs in September 2016, which is nearing finalisation after a public consultation process. Supervisory and inspection work, taking into account this guidance, as well as additional reporting, is based on a bank by bank approach, challenging the plausibility of banks' NPL resolution strategies, and how they will achieve targeted NPL reduction. In terms of overall progress, commercial NPLs for the retail banks reduced by 57% since the start of 2015 reducing from €38.4 bn to €16.5 bn. Retail NPLs reduced by 28% during the same period, equivalent to a reduction of €10.5 bn. Over 111,400 PDH residential mortgages have been restructured in Ireland by the retail banks and 88% of these loans are meeting the terms of the restructure.

On-Site Inspections

As 2016 was the second full year of operation of the SSM, the SSM methodology for on-site inspections continues to be enhanced and changes are fully embedded into the performance of inspections.

During 2016, 36 on-site inspections across seven risk areas were completed in 15 banks. Seven dedicated inspection teams focused on the key risk areas of: credit risk; capital; liquidity risk; operational risk; IT risk; governance; and business model analysis, as summarised in chart 3.5 below

As a result of the inspection work, reports were issued on each, that contained findings which were ranked in accordance with the SSM Methodology, and the ranking was used by supervisors in developing the remediation plans which are issued to the relevant credit institutions. This work led to improvements and ongoing enhancements to governance, internal controls and risk management in credit institutions inspected, in addition to increased provisioning and improvements to IT infrastructure in certain cases.



Case Study 2: Thematic Inspections on LSIs

Whilst LSIs are subject to in-depth inspections in specific risk areas, the Bank sees Thematic Inspections as an effective, proportionate way to inspect aspects of the internal controls, risk management and governance of LSIs. Thematic work allows the Bank to compare practices in a range of LSIs and issue thematic reports to help banks compare their *modus operandi* to good practices.

IT Risk Thematic Inspection in LSIs

The Bank conducted a thematic inspection on IT Risk Management and IT Security across a number of LSIs in the latter part of 2016. This inspection was conducted on the back of an IT Risk Self-Assessment Survey conducted in late 2015 in these institutions. The inspection team spent approximately four weeks on-site in each of the institutions reviewing their IT risk management frameworks, governance, monitoring and reporting practices, with an additional focus on IT security.

The findings of the on-site work indicate that the banks were overly optimistic in the 2015 self-assessment about the maturity of their IT risk management functions and controls. The failings that emerged from the inspection included poor IT risk governance and oversight practices, insufficient IT risk identification and assessment, and over reliance on IT services provided by group functions without adequate governance and monitoring in place at a local level. A sectoral report and industry letter detailing the outcomes of this work will be published in 2017.

Regulatory Reporting Thematic Inspection

The Bank completed a Thematic Inspection of Regulatory Reporting during 2016 in a number of LSIs to assess the extent to which it can rely on the accuracy and integrity of regulatory returns submitted. The banks were selected based on a combination of risk assessment ratings, previously identified issues in this area and consideration of the importance of the regulatory returns to the Bank in the performance of its regulatory role. The inspection focused on the banks' processes for the generation of: (i) Risk Weighted Assets (RWAs) and own funds for Common Reporting (COREP); (ii) off-balance sheet items, Financial Reporting (FINREP); (iii) Large Exposure Returns (LEX); and (iv) Liquidity Coverage Ratio (LCR). Whilst some good processes were identified, key failings identified by the inspectors include:

- (i) A lack of comprehensive procedural documentation;
- (ii) Inadequate resources in the Regulatory Reporting Function;
- (iii) Inadequate reconciliation and data quality assurance processes;
- (iv) Weaknesses in the three lines of defence;
- (v) Errors in the calculation of Credit RWAs;
- (vi) Shortcomings in the calculation of the Operational Risk capital charge;
- (vii) Issues relating to the accuracy and completeness of the LCR; and
- (viii) Shortcomings in relation to calculation of the LEX.

A subsequent remediation programme has been issued to each of the banks inspected.

Auditor Assurance

The Central Bank (Supervision and Enforcement) Act 2013 provides the powers to require the external auditor of a specified regulated financial service provider to conduct an examination with regard to the obligations imposed by certain provisions of financial services legislation identified by the Bank.

In 2016, the Bank sought assurance on the following topics LCR, Pillar III disclosures; risk appetite limit setting and new product approval processes.

The Bank also extended the Auditor Assurance Process to a number of LSIs in 2016, with a specific focus on assurance around governance of RMPs.

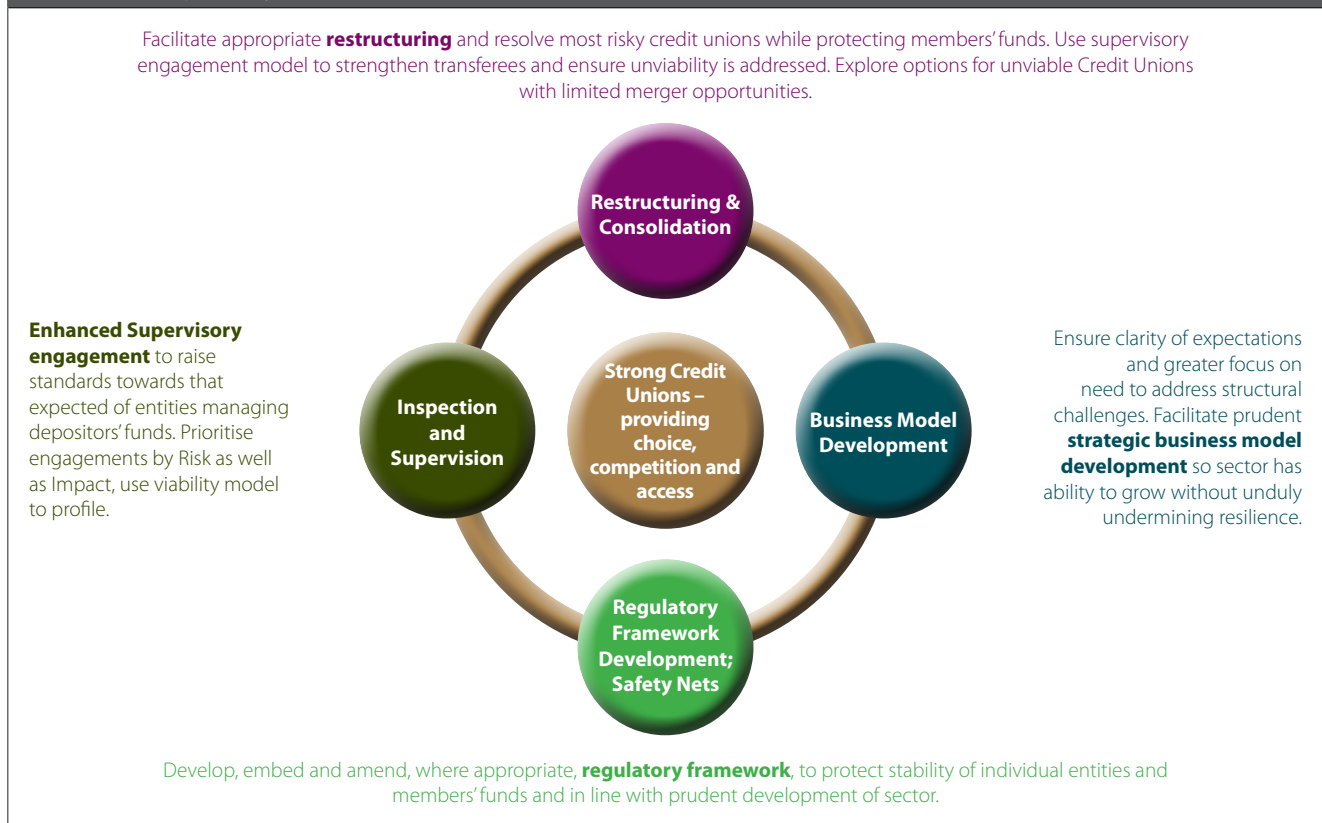
Review of Macroprudential Measures

The Bank participated in the review of the Regulations¹⁷, ensuring that its calibrations were consistent with both the objectives and appropriate bank-specific risk management strategies. As part of the review process, detailed information was gathered from each institution, covering governance, operational processes, lending exceptions, institutions' own policy changes, and data remediation. This analysis fed into the identification of a number of refinements to improve the sustainability and effectiveness of the original framework. The Bank will continue to monitor compliance with the regulations as well as the evolution of mortgage market lending standards.

Registry of Credit Unions

The statutory function of the Registry is to ensure the protection of members' funds by credit unions and the maintenance of the financial stability and well-being of credit unions generally. The mission and vision for the credit union sector is "Strong Credit Unions in Safe Hands" – financially and operationally sound, well governed credit unions, able to serve members now and in the future through effective regulation, supervision and credible threat of enforcement.

Chart 3.5: Regulatory Framework for Credit Unions



¹⁷ S.I. No. 47 of 2015 – Central Bank (Supervision and Enforcement) Act 2013 (Section 48) (Housing Loan Requirements) Regulations 2015

2016 Key Outcomes

Regulatory Framework Development; €100k limit

In 2016, the Registry received 73 applications from credit unions, to retain individual member savings (in excess of €100,000), of which 62 have been approved. The Registry have also received applications from six credit unions to increase individual member savings in excess of €100,000, primarily for the purpose of facilitating existing members.

Credit Union Advisory Committee

In December 2015, the Minister for Finance invited the Credit Union Advisory Committee (CUAC) to carry out a review of the implementation of the Recommendations set out in the March 2012 Report of the Commission on Credit Unions. The Registry provided a significant amount of data and analysis to support the review and made a formal Submission to the review group, setting out the Bank's position on key areas. The CUAC's report, which was published on 6 July 2016, identified that the majority of recommendations made by the Commission on Credit Unions had been implemented. It set out recommendations in relation to a number of areas including tiered regulation; longer term lending limits; consultation and engagement; governance; restructuring; business model development.

Following on from the report, the Department of Finance has established an implementation group, which it will Chair, and comprises representatives from the credit union representative bodies, the Bank, the Department and a CUAC representative.

Inspections and Supervision

The Registry undertook a significant supervisory engagement plan that resulted in more than 160 individual credit unions being subject to an on-site assessment by supervisors. This cohort included credit unions across an array of type (industrial and community), location (suburban and rural), asset size and impact rating. Significant weaknesses from both strategic and operational perspectives were highlighted arising from these engagements and, consequently, the Registry issued outcome focused risk mitigation programmes for each of these credit unions to ensure that unacceptable levels of risk are reduced to acceptable levels. In particular, supervisors highlighted concerns in relation to a lack of: strategic focus of boards; weak basic control frameworks in relation cash management and reconciliations; the need for underwriting standards and embedding of risk and compliance functions.

During 2016, two thematic reviews covering the areas of Outsourcing, and Fitness and Probity were carried out. The purpose of these reviews was to determine the standard of compliance by credit unions with the regulatory requirements of each of these areas.

- The main findings in relation to Outsourcing were that, while a number of material activities are outsourced by credit unions, understanding and compliance surrounding outsourcing requirements has not kept pace with regulatory requirements. In particular in relation to the required level of governance and challenge over selection, analysis of contracts, quality control and ongoing oversight of performance. The Registry issued a report on the findings of the inspections in Q1 2017.
- In relation to Fitness and Probity the main findings were that, while some credit unions demonstrated that they had fully engaged with the regime, other credit unions take a minimalist compliance approach. There was limited demonstration of quality and completeness of due diligence undertaken on prospective role holders, lack of meaningful succession planning and failure to document processes. The Registry issued a report on the findings of this theme on 6 February 2017.

The on-site engagements make a positive contribution to the Registry's ongoing drive to reduce the level of risk in the sector through the implementation of outcome focused risk mitigation plans. The information gathered as a result of these engagements also provided the Registry with a more in-depth understanding of the strengths and weaknesses of individual credit unions, which will feed into future decisions as consolidation of the sector continues.

Restructuring and Consolidation

A significant level of restructuring activity occurred during 2016, building on 2015. Restructuring of the credit union sector continued to be necessary to address the viability and operational challenges that face many credit unions. As of now there are 289 active credit unions down from 339 at the start of 2016 (and 377 at the start of 2015). Most mergers provide a new starting point to address financial and operational weakness in credit unions and to expand product and services offerings to members.

During 2016, the Registry continued to engage proactively with the Credit Union Restructuring Board (ReBo) and individual credit unions on restructuring proposals in order to ensure that each proposal took account of the Bank's legal and regulatory requirements and policy on restructuring. This pace of restructuring activity is expected to decrease over 2017, following completion of ReBo's mandate and given that the more obvious transfers have occurred. However, the Registry remains supportive of the strategic need for restructuring, with a continued focus on an assessment that projects are appropriately risk managed and that business improvements are being delivered.

The Registry will continue to closely monitor the performance of credit unions that have undertaken recent transfer projects, to review the progress made and to assess if the viability and operational challenges faced by credit unions are being addressed on an ongoing basis.

Case Study 3: Rush Credit Union (In Liquidation)

Introduction

Protecting the savings of credit union members is a key priority of the Registry. Strongest action is taken where severe failures are evident in a credit union, particularly a failure to put in place, operate and test the systems and controls that are necessary to protect the members and the credit union. Without proper systems and sufficient challenge, there is a serious risk of fraud or other loss to members which can lead ultimately to the loss of the credit union itself. In November 2016, action was taken to liquidate Rush Credit Union. This action was necessary given the extremely severe issues in the credit union, displaying failures of governance, controls and lending practices, which the credit union consistently failed to address, leading to the financial position of the credit union being unredeemable.

Following an application by the Bank to the High Court, Jim Luby and Tom Rogers of McStay Luby were initially appointed as joint provisional liquidators on 2 November 2016 and subsequently as joint full liquidators to Rush Credit Union on 21 November 2016.

Business Model Development

Within the Registry, the strategic importance of business model viability and sustainability is recognised. Therefore, a new unit was established with a mandate to engage on business model changes with credit unions (collectively, bilaterally or through representative bodies or other agencies) in order to take well developed proposals, grounded in a deep understanding of the risks involved and which are supported by risk focused business plans and key financial analysis that includes implications for return on assets and balance sheet impact.

The Bank, during 2016, approved a suite of additional services known as a Member Personal Current Account Service (MPCAS). MPCAS provides for a current account for everyday payments, supporting mobile apps payment instruments debit card and online technologies. This represents a significant and positive development for many credit unions who wish to provide current account services and payment instruments such as debit cards to their members.



Sylvia Cronin
 Director of Insurance
 Supervision

3.3 Insurance Supervision Directorate

Objectives

The Bank is responsible for the prudential supervision of insurance undertakings authorised in Ireland. The Bank's prudential supervision objectives are to protect policyholders by demanding of Irish (re)insurance undertakings that they:

- Have sustainable, capital generating business models over the economic and underwriting cycles;
- Are governed and controlled appropriately, with clear and embedded risk appetites, which drive an appropriate culture within them; and
- Have sufficient financial resources to pay out claims in full when they fall due.

In carrying out this role, the Bank monitors the risks posed by undertakings along with issuing standards, policies and guidance, which undertakings are expected to meet.

In 2016, the Bank focused on the delivery of a new engagement model, including increasing supervisory activities via a dedicated on-site inspection team and enhancing the use of analytics.

2016 Key Outcomes

Delivery of New Engagement Model

As part of the transition to Solvency II, the Bank reviewed the appropriateness of the overall PRISM engagement model for the supervision of insurance undertakings. This complemented the Insurance Supervision Directorate's re-organisation, introducing a dedicated on-site inspection and significantly expanding analytical capabilities. As a result of the PRISM review, the supervisory engagement model for (re)insurance undertakings has been enhanced to ensure appropriate risk based supervision under Solvency II. During 2016, a number of key changes to the PRISM system have been implemented, including:

- Development of the PRISM model to ensure engagement is proportional to both the impact and probability risk profile of the firm. This occurs on a risk-by-risk level, ensuring that supervisory effort is focused on those risks at elevated levels until the risks are mitigated;

- Development of Targeted Risk Assessments (TRAs) – i.e. each risk category has a dedicated TRA that is completed for each firm and the incorporation of on-site inspection activity;
- A realignment of the PRISM risk categories in order to more closely match Solvency II; and
- Enhanced engagement for low impact firms and with groups, in particular in supervisory colleges.

Supervisors have been operating in accordance with the revised PRISM model from Q1 2016. This has resulted in a wide range of supervisory reviews in the delivery of an appropriate level of supervisory engagement. In total over 1,400 PRISM engagements occurred during 2016, capturing meetings with executive management, TRAs, thematic reviews, and on-site inspections.

Alongside the Bank's supervisory engagement with regulated undertakings there was regular interaction with industry stakeholders via monthly meetings, regular publications, website updates and industry briefing events. Supervisors also actively engaged with other regulators, together with increased engagement at EIOPA level through participation in the expert network groups.

Non-Life Insurance Supervisory Engagement

2016 supervisory engagement for the non-life sector focused on number of key themes:

- Using the Own Risk and Solvency Assessment (ORSA) process to assess the adequacy of target capital and to review capital planning activities;
- Claims and underwriting inspections;
- Governance and oversight of private motor pricing thematic review; and
- Reserve adequacy assessments for high impact companies.

RMPs have been implemented as a result of these reviews, which has resulted in enhanced pricing governance and oversight and certain reserve strengthening following reserve adequacy reviews. The Case Study below provides further background to one of these reviews, the governance and oversight of private motor pricing.

Case Study 4: Thematic Review - Governance and Oversight of Private Motor Pricing

Historically one of the leading causes of failure in general insurance companies has been setting insurance premiums at a level that is not sufficient to fully cover policyholder claims. In the context of the Bank's responsibility for prudentially supervising insurance companies, the Bank reviewed the oversight and governance of private motor insurance pricing in 2016. This was in response to developments in premium rates and the claims environment which can ultimately impact on the solvency of firms. The Bank's objectives included driving a greater awareness of the impact of key pricing assumptions on future profitability at a company and market level and understanding if there were any capital requirement implications arising from the assessment of companies' pricing governance and risks.

Key Findings

The main findings of the review at an industry level were:

- There has been a time lag between the increase in injury costs and price increases.
- Recent price increases have been largely driven by the increasing cost of injury claims.
- Companies have allowed for emerging claims trends to varying extent, reflecting continuing uncertainty in the claims environment.
- There is a wide variation in the degree of pricing sophistication and level of resources across companies; and
- There has been a growth in the market share of foreign insurance companies operating here on a Freedom of Establishment and FOS basis.

Case Study 4: Thematic Review - Governance and Oversight of Private Motor Pricing

Actions Taken

The Bank has followed up with firms in relation to the findings from the review with a view to:

- Driving a greater awareness of the impact of key pricing assumptions on future profitability at a company and market level;
- Challenging companies to ensure they have appropriately considered the changing claims and pricing environment when developing their business plans and when assessing their own solvency needs; and
- Promoting robust pricing processes across the industry for 2016 and beyond.

Company-specific findings were communicated directly to the relevant firm and have informed ongoing engagement on matters such as reserve strength, pricing adequacy and underwriting processes. In particular, the Bank will continue to monitor how the cost of settling injury claims compares to estimates made for pricing and reserving.

In addition, the Bank has engaged with other regulatory authorities, where relevant, to share findings and raise their awareness about claims costs trends and elevated underwriting risks for insurers operating in Ireland.

Building and Improving Analytics Capability

The Bank's change programme to ensure full implementation of Solvency II included the establishment of a new dedicated analytics function within the directorate. This was in recognition that Pillar III of Solvency II is dedicated to improving disclosure and transparency. The end result is a sea-change in the volume and breadth of information that regulated entities are required to report to the Bank. Whereas it was feasible under Solvency I for supervisors to review manually regulatory returns, the scale of reporting is such now that the data can only be interpreted using modern analytical techniques. The vision for this analytics function is for supervisory decision making to be informed to the maximum extent possible by analysis of data.

The key areas of focus in 2016 have been:

- *Building the Analytics Platform*: This has required the recruitment of a multi-disciplinary team of accountants, risk analysts, actuaries and data analysts. In addition, there has been a substantial investment in IT infrastructure to process returns. There has also been significant engagement with industry to support their own preparations;
- *Quality Assessment (QA)*: Firms commenced reporting on a quarterly basis in May 2016. This was the start of an important investment by the Bank in assessing the quality of these initial returns, and the tracking of remediation as it has occurred across firms. While the QA process will be ongoing for 2017, there have been notable improvements observed already; and
- *Insightful Analytics*: In order to produce insightful analytics that positively contribute to supervisory decision making, a range of key risk indicators and descriptive statistics have been made available to supervisors.

Increasing Supervisory Activities - On-site Inspections Teams

Also, as part of the directorate's reorganisation, a dedicated on-site inspections team was established in December 2015. The purpose of the team is to increase the intrusiveness of supervisory activities. The on-site inspections team provides support across all insurance sectors and performed inspections in the non-life, life, health and managed companies' sectors in 2016. Firm specific findings letters were circulated to individual firms following each inspection, and industry letters with common themes identifying required areas of improvement will be circulated in the coming months in the areas of claims management, underwriting discipline and operational risk management.

The key areas of focus for the on-site inspections team during 2016 were:

- *Claims management and underwriting discipline across the domestic non-life and health sector:* This involved the inspection of policies, procedures and the internal control frameworks within the claims and underwriting functions of companies. Supervisory actions were recommended to strengthen the internal controls in both areas. The actions in relation to claims were mostly about the management of large and complex claims and quality assurance activities. Those relating to underwriting covered the monitoring and reporting of the use of discounts, strengthening of controls of underwriting authorities and the required improvement of the quality of underwriting rationales.
- *Risk management within the domestic non-life and life sectors:* Evidence based assessments of risk management frameworks and risk culture within companies, with a particular focus on operational risk management were completed. These inspections identified both weaknesses in the design and operating effectiveness of these frameworks, including deficiencies in risk identification, measurement, management, monitoring and reporting.
- *Less complex companies¹⁸:* The on-site inspection team was core to the implementation of the bespoke supervisory model introduced for less complex companies in 2016 with the completion of a thematic review of 13 of these companies. This inspection focused on the areas of governance and risk management under Solvency II (See *Case Study below*).

Case Study 5: Low Impact Sector Companies

Background and Context

The Directorate's supervisory approach continues to develop and evolve. Over half of the authorised reinsurance undertakings supervised by the Bank are rated as low impact under the PRISM framework and generally are captives owned by groups. The lines of business typically underwritten include fire and natural forces, other damage to property and general liability. Most functions are outsourced to captive management firms or third party professional services providers. Captive management firms provide day-to-day-services such as finance, claims handling, compliance, actuarial services and risk consulting. Accountancy firms and actuarial firms primarily provide the other third party services.

In line with recommendations from the IMF in its Report on Observance of Standards and Codes (ROSC) issued in May 2015, the Bank moved from a reactive engagement model for low impact undertakings to a proportionate, bespoke engagement model.

The on-site inspections team conducted a thematic review, focusing on governance, risk management frameworks and internal controls of a sample of low impact firms (13, c. 10% of the population). The inspections team assessed companies against Solvency II and the Corporate Governance Requirements for Captive Insurance and Captive Reinsurance Undertakings 2015 (the Corporate Governance Requirements).

The Solvency II regime requires that companies adopt a more dynamic risk-based approach and put in place an effective risk management system. Senior management must consider all risks to which the insurer is exposed and ensure that risk and capital management are integrated. An effective risk-management system comprises strategies, policies, processes and reporting procedures necessary to identify, measure, monitor, manage and report, on a continuous basis the risks, to which the company could be exposed, and their interdependencies.

¹⁸ PRISM Low Impact companies - typically captives owned by groups who operate in sectors such as: accountancy, financial services, pharmaceutical and motor industries.

Case Study 5: Low Impact Sector Companies

Under the Corporate Governance Requirements a board is required to understand the risks to which the company is exposed and document a risk appetite for the company. The appetite should be expressed in qualitative terms and also include quantitative metrics to allow tracking of performance and compliance with the agreed strategy. This is also subject to annual review by the board.

The thematic on-site review highlighted that the areas of outsourcing and compliance with Solvency II legislation were below expectations.

Key Findings and Actions Taken

- In general, the relevant agreements around outsourcing were found to be not fully compliant with Solvency II legislation. In the majority of the undertakings inspected, there were no agreements in place between the undertaking and the group, where group provided a critical or important service to the undertaking. Where agreements were in place, with a third party or with group, they failed to set out or establish the use of key performance indicators and key risk indicators in their outsourcing arrangements.
- In many instances the risk appetite statements of the companies under inspection did not adequately reflect and document the company's appetite for risk.
- In most instances risk management policies and sub-policies were not adequately detailed to reflect the complexity of the undertakings.
- Identified risks were not subjected to a sufficiently wide range of stress tests or scenario analyses in order to provide an adequate basis for the assessment of the overall solvency needs.

The Bank recommended that the boards of the companies perform a review to ensure that all policies required under Solvency II are in place and the risk appetite statements are compliant with the Corporate Governance Requirements.

The results of these actions will be that low impact managed companies will have greater oversight and control of outsourced providers, will be Solvency II compliant and will have strengthened risk management frameworks in place. Common findings from the inspections have been shared with the industry through the Directorate's quarterly newsletter.

Auditor Assurance

Similar to the work being undertaken for credit institutions as referred to in **Chapter 3.2**, the Bank also commissioned the external auditors of select (re) insurance undertakings for the first time in 2014 to conduct an Auditor Assurance exercise on internal governance focusing on: underwriting, reserving, operational and risk management.

Given IT systems now play a central role in the operation of (re) insurance undertakings, there is a heightened risk of IT systems failure and/or cyber trigger events. In this context, during 2016 the Bank sought auditor assurances to the extent to which insurance undertakings have complied with their obligations in respect of cybersecurity (which relate to governance, risk management and outsourcing). As part of this exercise 10 high impact undertakings are required to prepare a report setting out the description of the internal governance arrangements performed by the board of directors and senior management over cybersecurity. The relevant auditor then undertakes an examination and prepares two reports, an assurance report and a review and recommend report, for submission to the Bank. The supervision teams will assess the strengths and weakness faced by these insurers from review of these submissions in Q2 2017.



Michael Hodson

Director of Asset Management Supervision

3.4 Asset Management Supervision

Objectives

The Asset Management Supervision Directorate is responsible for the authorisation and supervision of financial services firms combining MiFID investment firms, stockbrokers, market infrastructure firms and fund service providers (FSPs).

The Bank's objectives are to safeguard the interests of investors and clients of financial services firms by demanding of these firms that they:

- Have sustainable, risk assessed business models over the economic cycle;
- Are governed and controlled appropriately, with suitable structures in place and with clear and embedded risk appetites which drive an appropriate culture within them;
- Have sufficient financial resources; and
- Comply with applicable regulations on client assets and investor monies.

Chart 3.6: Asset Management Supervision



2016 Key Outcomes

Recovery and Resolution Planning

The Bank Recovery and Resolution Directive¹⁹ (BRRD) came into effect on 15 July 2015. The BRRD set out requirements for in-scope firms to draft recovery plans setting out actions which the firm would take to address a scenario where it is breaching or likely to breach its obligations under the CRD IV²⁰.

Supervisors worked closely with the Bank's Resolution Division to review the recovery plans relevant for firms it supervises. Procedures and checklists were implemented to ensure compliance with all aspects of the regulations and enable peer comparison of the recovery plans submitted to identify good and poor practices across all firms in scope.

Of the 11 recovery plans submitted by firms deemed in scope, four were deemed materially deficient, requiring redrafting and resubmission. The remaining seven firms submitted plans which were deemed sufficient, but these firms were given additional feedback on how the plans could be improved for the next annual submission date.

Case Study 6: Implementation of the Investor Money Regulations, 2015

Background and Context

The Bank recognised the need for greater clarity on the proper protection of investor money, i.e. money held by FSPs on behalf of investors. To address this uncertainty, the Bank developed the Investor Money Regulations (IMR) applicable for the first time to FSPs, which came into effect on 1 July 2016.

The Bank's Client Asset Specialist Team (CAST) is responsible for the supervision and inspection of client asset and investor money arrangements and the monitoring of risks to the safekeeping of client assets and investor money in relevant firms. The establishment of CAST was to ensure specialist supervisory resources are allocated to the supervision of client asset risk and that investment firms and FSPs maintain high standards of investor protection.

Key Actions and Initiatives – Timeline

On 30 March 2015, the IMR and IMR guidance were published. To supplement these, the IMR Q&A was published in October 2015 and industry presentations were delivered throughout 2015 and 2016.

In 2016, the Bank focused on the implementation of the IMR. Establishing the population of FSPs in-scope was the key priority for this process in order to ensure that FSPs holding investor money became subject to robust supervision. During the first half of 2016, the Bank engaged extensively with the FSP industry and representative bodies. The Bank communicated with individual FSPs, requiring them to review their business models and establish any investor money implications.

Ten FSPs were identified as being subject to the IMR and therefore permitted to hold investor money under their authorisation. Each of these FSPs was required to provide a detailed account of their IMR arrangements and appoint a Head of Investor Money Oversight in advance of the implementation deadline. All out-of-scope FSPs had a condition imposed on their authorisation preventing them from holding investor money without the prior approval of the Bank.

The focus in late 2016 was on post-implementation supervision of the ten in-scope FSPs. Engagements with the FSPs conducted during the period had the objective of establishing the extent to which investor money is being held and assessing how individual FSPs had implemented arrangements to comply with the IMR. The engagements allowed CAST to evaluate compliance with the new requirements and determine how the role of the newly appointed Head of Investor Money Oversight had been embedded in the FSPs.

¹⁹ S.I. No. 289 of 2015

²⁰ Directive 2013/36/EU

Drive to Improve Culture

Regulated firms promoting a client-focused culture, which is fair and mindful of the wider financial services and economic environment in which they operate, are aligned with the Bank's mandate of investor protection, market integrity and financial stability. Throughout 2016, the Bank led a concerted drive to improve the culture within supervised firms. Evidence suggests that firms which have a culture of managing risks effectively require substantially less supervisory interventions.

Where poor culture has been identified, RMPs have been imposed. These RMPs have focused on improvements to internal risk functions, reporting lines and the appointment of additional Independent Directors. The output of this focus on improving culture has been increased independent challenge at board level, strengthened second lines of defence (especially risk and compliance functions) and improved culture and mind-set within supervised firms.

Risk Mitigation - Focus on Low Impact Investment Firms

A key objective of the Bank's Strategic Plan 2016-2018 is to embed its assertive supervision stance by extending on-site inspection activities and to increase supervisory activities for entities deemed to be low impact under PRISM.

During 2016, the Bank committed additional resources to the supervision of low impact firms. A project was undertaken to conduct a review of the ICAAP for low impact investment firms within scope of CRDIV. Under ICAAP requirements, a bank needs to ensure that it possesses adequate capital resources in the long term to cover all of its material risks. To facilitate this review, a new SREP questionnaire was designed and issued to 13 low impact MiFID Investment Firms within scope of CRDIV.

Following an assessment of firms' responses, five firms were selected for on-site inspections. During the on-site inspection phase, supervisors noted a variety of issues pertaining to (i) corporate governance arrangements, (ii) operation of the compliance function, (iii) a deficiency in policies and procedures, (iv) risk framework and (v) oversight of third party arrangements. Detailed RMPs were issued to the relevant firms following the on-site assessment phase of this review.

This process enabled the Bank to significantly enhance supervisory engagement with low impact investment firms by (i) providing a broad overview of a firm's risk management framework, (ii) enabling supervisors to review a firm's strategy and structure, (iii) enabling supervisors to assess a firm's ICAAP in a relatively short period of time and (iv) facilitating the identification of red flags to determine areas requiring immediate focus. Further focused low impact firm supervisory initiatives will continue in 2017.

Thematic Reviews

A number of thematic reviews were conducted by the Bank in 2016. These inspections continued work from 2015 where follow-up was warranted or focused on areas of potential emerging risk. Such inspections cover a broad spectrum of firms and are conducted on a cross-sectorial basis. Supervisory staff examined areas including depositary oversight, sub-fund governance (director time commitments), risk function oversight, outsourcing arrangements by investment firms, conflicts of interest and client reporting.

Findings arising from these inspections included, identification of divergence in quality of risk frameworks, significant variation on allocation by directors of time commitment to sub-funds and lack of board ownership in relation to identification and management of conflicts of interest. In addition, good practices and adequate procedures were noted in relation to the production and issuance of client reporting. Findings were shared through the issue of industry letters outlining key findings and putting forward recommendations regarding enhanced governance/compliance practices as appropriate. The findings will direct the Bank's supervisory interventions and may inform future policy development.

Case Study 7: Review of Outsourcing of Fund Administration Activities**Background and Context**

The Bank regularly reviews the controls and procedures in place surrounding outsourcing arrangements to assess compliance with the Fund Administrator outsourcing requirements²¹ and to evaluate best practice in the industry. Due to the growth in scale of outsourcing arrangements within the fund administration industry in Ireland in recent years, the evolution of Fund Administrators' outsourcing arrangements to globally located Outsourcing Service Providers (OSPs) presents challenges to the Bank's supervisory approach. Outsourcing is a key area in relation to operational risk and is now integral to the business model of a significant number of Irish Fund Administrators.

The extent of outsourcing among certain larger Irish Fund Administrators is extensive. Of the five firms that formed part of this review, a slight majority of fund administration activities were carried out in OSPs at 31 December 2015. The following key observations were also noted:

- Not all firms under review demonstrated comprehensive outsourcing records maintained;
- For the most part, OSPs are not regulated or if regulated, are not regulated in the same way as Fund Administrators in Ireland; and
- The majority of firms under review have no tolerance level set in respect of the amount of outsourcing permitted for a specific fund administration activity.

Key Actions and Initiatives – Timeline

The findings from the review were shared through the issuance of an industry letter in March 2017. The observations and recommendations in the letter were issued to assist Fund Administrators who outsource their activities. The letter outlined examples of good practice and aims to support the development of a consistent interpretation of the outsourcing requirements.

It should be noted that any proposed outsourcing submissions by Fund Administrators will be considered by the Bank on the basis of the cumulative effect/impact (i.e. the level of activities carried out by OSPs) the proposed outsourcing arrangement will have on the relevant firm when reviewed in conjunction with all current operating outsourcing models. The Bank's view is that this level of outsourcing is likely to be at or close to the outer limit of what is appropriate for this industry.

The Bank has also committed to undertaking a review of outsourcing across all financial sectors.

Preparation for MiFID II Implementation

Considerable work was carried out in 2016 in preparation for implementation of MiFID II in January 2018 by ensuring firms have appropriate structures and controls in place. A comprehensive MiFID II implementation programme has been established with a particular focus on implementation analysis, training and development. Extensive stakeholder engagement including a MiFID conference in Q1 2016 and significant key note speeches at relevant industry fora were aimed at directing and guiding firms in their preparatory plans. MiFID II will continue to be a priority in 2017 within the Bank.

²¹ Requirements on Outsourcing of Administration Activities in relation to Investment Funds.



Gráinne McEvoy

Acting Director of Securities and Markets Supervision

3.5 Securities and Markets Supervision

Objectives

The Securities and Markets Supervision Directorate is responsible for the supervision and regulation of Ireland's primary and secondary securities markets. As part of its role, the directorate is tasked with ensuring the Bank meets its obligations under various pieces of sectorial legislation, the focus of which seeks to ensure orderly, fair and transparent markets. As such, the directorate plays a significant role in supporting the Bank's goals of financial stability, consumer protection and market integrity.

The directorate delivers on the above objectives through carrying out the following activities:

- Authorisation and supervision of investment funds established in Ireland;
- Approval of prospectuses of issuers making offers to the public and/or seeking admission to trading on a regulated market;
- Market monitoring and surveillance of regulated markets under (i) MiFID, (ii) MAR, (iii) Transparency Directive (TD), (iv) Short Sales Regulations, and (v) European Markets Infrastructure Regulation (EMIR); and
- Markets risk analysis of regulatory data reported by firms to identify firm and macro-level risks impacting primary and secondary securities markets.

Data analysis is integral to the successful delivery of the above objectives.

2016 Key Outcomes

Implementation of the Market Abuse Regulation (MAR)

In July 2016, Ireland implemented the MAR and related directives aimed at ensuring greater transparency and market integrity. The new legislation strengthens the detection and sanctioning of market abuse and covers new offences, such as attempted market abuse and inciting, aiding and abetting the commission of certain market abuse offences. The MAR increased the range of requirements to notify or report activity to the Bank which involved a number of modifications to reporting systems. Extensive engagement took place with external stakeholders

to ensure successful implementation of these legislative changes. The scope of the Bank's powers has been broadened to cover Multilateral Trading Facilities²², and over-the-counter trades, including in derivatives.

Improving Data Quality

The analytics capability developed was used to examine the quality of EMIR reporting to trade repositories. This included (i) regular review of rejection and reconciliation reports received from trade repositories and (ii) detailed review of the completion of a number of key EMIR data fields by significant users of derivatives. The Bank is represented in the ESMA Data Quality Action Plan which aims to improve the quality, consistency and usability of EMIR data reported to and by trade repositories across all EU member states. Where concerns arose, the Bank engaged with the relevant counterparty to ensure all data quality issues identified were rectified in a timely manner. A new process for the EMIR regulatory returns was introduced in 2016 (see Case Study 8 below).

Delivery of Intrusive Supervisory Engagement

The Bank is responsible for the supervision of c.6,500 investment funds authorised in Ireland; representing over €2 trillion in assets under management. In 2016, this included consideration of over 3,800 regulatory returns and of 565 individual supervisory triggers²³. Supervisors undertook six designated inspections during the year, including two deep dive on-site inspections of depositaries' oversight of investment funds. This was in addition to two thematic reviews on the use of the risk management process by UCITS and fees charged by investment funds. The findings of thematic reviews may inform future policy development and, where appropriate, good practices identified are communicated to the wider industry with the aim of improving overall compliance standards.

Case Study 8: Proper and Effective Supervision of Non-Financial Counterparties (NFCs)

Background and Context

EMIR was introduced following the financial crisis and imposed new requirements on all counterparties, both financial and non-financial, which enter into derivative contracts. These new requirements are designed to improve transparency and reduce risks associated with derivatives markets.

The supervision of NFCs' compliance with EMIR posed new and distinct challenges for the Bank as most NFCs have no experience of financial regulation and do not require authorisation to enter into derivative contracts. To overcome these challenges, the Bank required a number of large NFCs with significant derivative gross notional positions outstanding to submit an EMIR Regulatory Return (ERR). The NFCs selected included companies in the transport, pharmaceutical and energy sectors as well as special purpose vehicles and financial vehicle corporations. The ERR provides the Bank with information about the NFC, trade reporting information, details of risk mitigation techniques undertaken and supplementary information on its business activity.

Key Actions and Initiatives

The Bank undertook an in-depth review of the ERR submissions and compared the information provided with trade repository data directly available to the Bank. The purpose of the review was to assess the extent to which the data provided was complete, accurate and reliable. Where anomalies were identified, these were followed up with the relevant counterparties. In certain cases, it was apparent that the directors of the NFCs were not sufficiently aware of their responsibilities under EMIR and relied on service providers to execute the requirement without applying an appropriate level of oversight. The Bank issued an industry letter detailing its findings and recommendations in September 2016. The Bank will continue to review the EMIR data in order to identify cases of mis-reporting or poor data quality, and will use its powers, including enforcement action, where required to ensure the complete, accurate and timely reporting of details of derivative contracts.

²² A multilateral system, operated by an investment firm or a MO, which brings together multiple third-party buying and selling interests in financial instruments in a way that results in a contract in accordance with Title II of this Directive. Article 4(1) of Directive 2014/65/EU (MiFID II)

²³ Triggers include findings from depository and regulatory reports, internal referrals, PRISM alerts, protected disclosures and ONR alerts.

Building and Improving Analytics Capability

The directorate has undertaken considerable work in designing reporting and analysis tools to aid supervisors in their roles. Over the course of 2016, there has been an increased focus on utilisation of data to identify patterns, trends and themes across the broad spectrum of supervised Irish funds, including liquidity, leverage, market and operational risks. The initiatives in the utilisation of data have aided the intelligence gathering and sharing of expertise across the Bank including liaising with colleagues in Statistics, Market Risk Analysis, Financial Stability, Asset Management and EMIR Supervision.

Contribution to IMF FSAP

As part of the IMF FSAP the directorate carried out stress testing of Irish money market funds which fed directly into the asset management portion of the IMF's final report. Arising from this work was the first collection of daily redemption data from Irish investment funds, which will form the basis of joint research with the IMF on investment fund liquidity analysis. The directorate was also heavily involved with other IMF FSAP work-streams

Case Study 9: Improving the Efficiency and Effectiveness of the Funds Authorisation Process

Background and Context

The authorisation of investment funds is an important part of the Bank's role as NCA of the funds industry. In evaluating applications for investment funds seeking authorisation, the Bank applies a rigorous and high quality assessment of applicant submissions and engages extensively with relevant stakeholders. In 2016, the Bank was responsible for authorisation of 775 investment funds (including sub-funds).

Key Actions and Initiatives

Acknowledging that speed to market is an important consideration for industry participants, it has been the Bank's stated intention to improve the quality and efficiency of its authorisation processes. Substantial progress was made in 2016 on a project to deliver on this commitment for investment funds and fund service providers. An important sub-set of fund applications, namely Qualifying Investor Alternative Investment Funds (QIAIFs), are now being processed using the new automated system ORION. The next component of ORION went live in March 2017 delivering a new online authorisation service for funds and fund service providers. This will mean that approximately 80% of investment fund applications will be processed using this new system. It is important to note that processing applications through ORION does not change the standard or quality of approach to the applications process. Directorate staff will continue to perform an in-depth review of fund documentation, particularly for retail investment funds. What has changed, however, is that the new system improves the quality and efficiency of the authorisation process through the use of online applications and automated workflows, which is ultimately aimed at improving authorisation turnaround times.

Building on the success of this transition, the Bank will continue to review and streamline its processes to deliver a consistently high standard and efficient service to its stakeholders.



Gerry Cross
Director of Policy and
Risk

3.6 Policy and Risk Directorate

Objectives

The Bank oversees the development and implementation of regulatory policy in relation to banking, insurance, investment firms, investment funds, and securities and markets both domestically and internationally. Its core objectives in this area are:

- To develop and maintain the Bank's domestic regulatory and policy framework for prudential and markets supervision;
- To contribute to the formation and implementation of European and international regulation;
- To lead the development and maintenance of the Bank's risk-based framework for supervision (PRISM);
- To provide support and assurance for supervisors' implementation of the Bank's policy and supervisory frameworks; and
- To promote a high quality and effective policy environment across the Bank.

2016 Key Outcomes

Improving Fund Management Company Effectiveness

The Bank regulates approximately 400 fund management companies and aims to ensure that companies have the right governance arrangements, organisational structure and resources with a view to improving standards for fund management companies, which is important from an investor protection perspective. The Bank also aims to ensure that it effectively supervises the fund management companies it authorises.

In December 2016, the Bank published the final package of measures to improve fund management company effectiveness. This consisted of a small number of new rules targeted at areas where the Bank considered its rules should be strengthened. The Bank also published detailed guidance which sets out clearly how directors and fund management companies should operate.

Chart 3.7: Fund Management Company Effectiveness

<p>GOVERNANCE The way in which directors should perform their roles and guide the company</p>	<p>Chapter 1: Delegate Oversight</p> <ul style="list-style-type: none"> • Approach to management of delegation of the performance of tasks focusing on five key areas of delegation; investment management; distribution; risk management; operation and administration; and support and resourcing. <p>Chapter 2: Organisational Effectiveness</p> <ul style="list-style-type: none"> • Creation of new role with the obligation to proactively ensure appropriate organisation and resourcing. <p>Chapter 3: Directors' Time Commitment</p> <ul style="list-style-type: none"> • Establishment of reasonable time commitments and guidance on documentation of time allocation.
<p>COMPLIANCE Complying and demonstrating compliance with regulatory obligations</p>	<p>Guidance Chapter 4: Managerial Functions</p> <ul style="list-style-type: none"> • Management to be undertaken by board appointed designated persons engaging with the directors and actively monitoring and overseeing delegate service providers. • Performance of managerial functions by adequately qualified designated persons with allocation of regulatory obligations to one or more of the mandated six managerial functions. • Adoption of discrete suite of policies and procedures by the management company.
<p>SUPERVISIBILITY Ability to carry out engagement model without constraint</p>	<p>Guidance Chapters 5 and 6: Operational Matters and Procedural Matters</p> <ul style="list-style-type: none"> • Draft location rule mandates minimum director and designated person residency requirements depending on company's PRISM rating. • Draft record keeping and monitored email address rules enhance regulatory engagement and accessibility.

Setting Clear Expectations for Regulated Firms - Management of IT and Cyber Risk

With recently strengthened IT risk supervisory capabilities, the Bank has sharpened its focus on IT-related risks through a series of inspections and other engagements with regulated firms. Through this work, the Bank identified a number of common deficiencies across all sectors reviewed, in particular, insufficient levels of awareness, understanding and prioritisation of IT and cybersecurity risks by firms. The Bank was also concerned that firms were not doing enough to mitigate the potential impact of an IT failure on their business, reputations and the wider financial system.

In September 2016, the Bank published cross industry guidance in respect of IT and cybersecurity risks, for all regulated firms. The guidance articulates the Bank's supervisory expectations regarding the management of IT and cyber risks. It provides a set of standards and good practices for effective IT and cybersecurity governance and risk management, including IT outsourcing and business continuity management. It assists firms by highlighting inadequate practices identified by Bank supervisors.

The guidance is a tool through which to drive the actions necessary to raise standards of governance and management of IT-related risks across supervised sectors and to improve firm and sector resilience to disruption caused by IT failures or cybersecurity incidents. The Bank also sought to increase industry awareness of cyber risk through communications on the challenges facing the financial services industry in responding to this risk and the good practices that firms can adopt.

Enhancing Regulatory and Policy Frameworks - Banking and Insurance

During 2016 the focus, both at domestic and EU levels, was primarily on bedding down regulatory frameworks which had undergone substantial change in preceding years.

Solvency II was implemented within the EU with effect from 1 January 2016. Following significant changes to its policies and systems during 2015, additional measures were introduced in 2016 to maintain key aspects of

the domestic supervisory regime. These measures included guidance on the Domestic Actuarial Regime and revised Directors Certifications Requirements together with the introduction of external audit of key Solvency II regulatory returns. A common theme across these initiatives was the introduction of additional quality assurance or safeguards.

The oversight of branches of credit institutions authorised outside the EU (third country branches) is an area of banking regulation and supervision not currently covered. These branches are distinct from EU authorised subsidiaries of global banking groups. In June 2016, the Bank published a substantive policy document outlining its approach to the authorisation and supervision of these third country branches. It sets appropriately high benchmarks for authorisation and details the respective roles of the Bank and the home-state regulatory authority in the ongoing supervision of these branches

Influencing the EU and International Regulatory Framework

The directorate leads and coordinates the Bank's engagement with the ESAs with the aim of delivering high quality regulation both from prudential and consumer perspectives. It plays an important role in monitoring and analysing developments at EU level and ensuring there is an effective flow of information across the Bank²⁴.

For insurance, a priority in 2016 for the Bank at EIOPA was the development of a revised general protocol to strengthen the level of cooperation and information sharing among national regulatory authorities regarding insurance undertakings operating on a branch or cross-border basis. This work was concluded in 2016. Other EIOPA deliverables in 2016 ranged from a consultation paper to inform EIOPA's work on reviewing the Solvency Capital Requirement (SCR) and advising the European Commission on the EU-wide stress test of insurance undertakings which covered 236 firms and delivered a snapshot assessment of vulnerabilities and resilience to severe market developments.

For banking, EBA deliverables in 2016 ranged from a discussion paper exploring options for a more proportionate regulatory regime for various categories of investment firms to a Consultation Paper as a precursor to the development of guidelines on accounting for expected credit loss which will inform the implementation of the International Financial Reporting Standard 9 (IFRS 9).

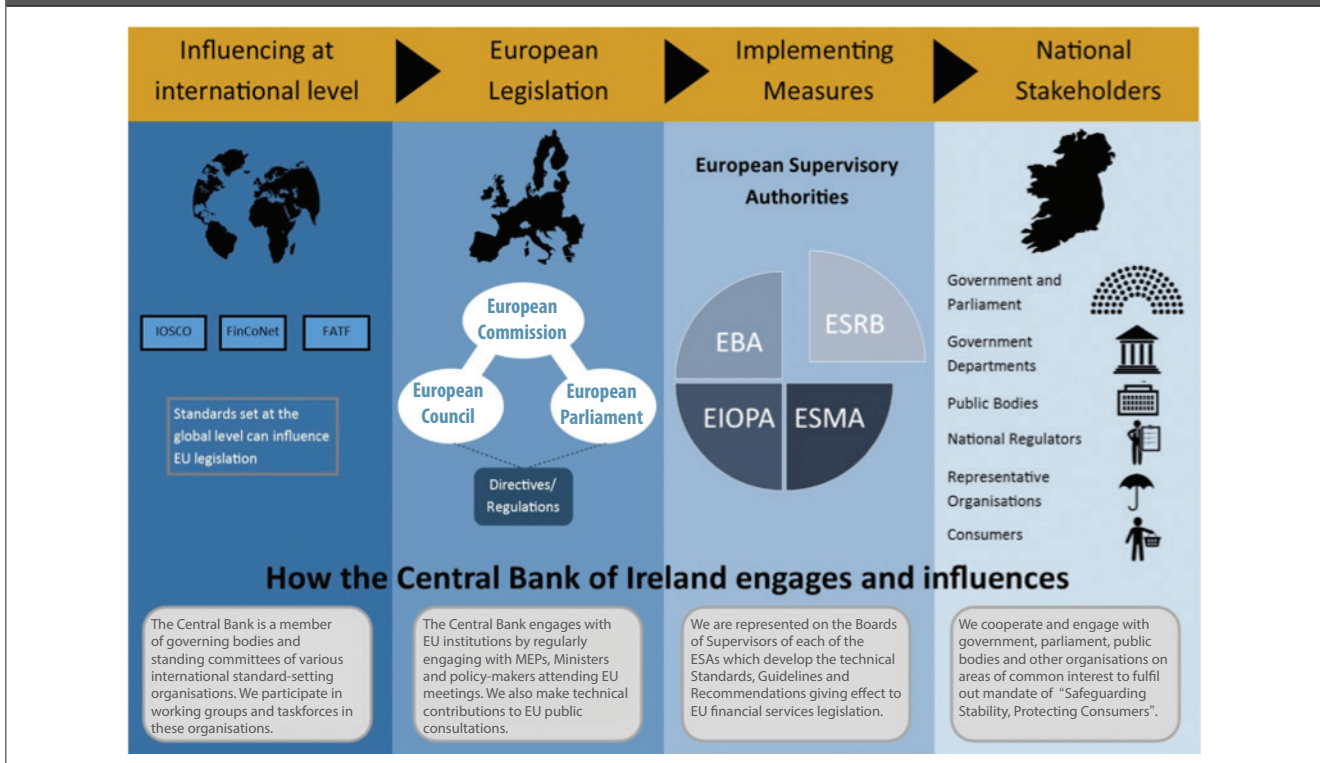
With respect to the Bank's engagement with the SSM, the directorate continued to provide technical and policy advice on certain high priority issues arising at the SSM Supervisory Policies Network and the SSM Supervisory Board throughout 2016. This included finalisation and development of the ECB's policy stance on the exercise of CRD IV/CRR options and discretions.

Work completed in ESMA in 2016 included:

- An opinion to NCAs in relation to UCITS Share Classes and UCITS Remuneration Guidelines;
- Advice in relation to the Alternative Investment Fund Managers Directive (AIFMD) third country passport and an opinion on loan origination;
- The development of Regulatory Technical Standards (RTS) on European long-term investment fund legislation; and
- Advice on the depositary frameworks of non-EU jurisdictions in the context of the AIFMD.

The chart below summarises how the Bank engages with, and influences, the EU and international regulatory framework.

²⁴ Further detail on deliverables across all three ESAs is set out in *Chapter 6*.

Chart 3.8: Influencing the EU and International Regulatory Framework**Case Study 10:** Influencing the EU and International Regulatory Environment: Shadow Banking

The Bank is an active participant in the international regulatory debate on shadow banking and market-based finance, leveraging its position as an integrated organisation bringing policy, supervisory and statistical knowledge and expertise to bear in international discussions. Shadow banking is relevant to the Bank's mission both in terms of safeguarding stability and protecting consumers given the size of the shadow banking industry that is domiciled here; though the majority of assets and liabilities are located overseas and not connected with the domestic economy. Details of the Irish shadow banking sector for 2015 are set out in the December 2016 Macro-Financial Review.²⁵

Globally, the work on shadow banking has been led by the Financial Stability Board (FSB), both in terms of policy development and measurement. In January 2017, the FSB published its final report on a policy recommendation to address structural vulnerabilities from asset management activities.²⁶ The Bank participated in this work, contributing specific knowledge accumulated from supervising the asset management sector in Ireland over a number of years. Similarly, the Bank participates in the annual publication of the FSB's global shadow banking monitoring review. This contribution to the FSB's work comes despite Ireland not being a member of the FSB.

The FSB works closely with the International Organisation of Securities Commissions (IOSCO) to operationalise many of their policy proposals from the structural vulnerabilities work. The Bank has played a key role in IOSCO's work in this area and chairs a working group in IOSCO on liquidity risk management practices of investment funds. The Bank was also appointed to the board of IOSCO as one of three members from the European Regional Committee, the first time the Bank has been represented on the IOSCO board.

25 <https://www.centralbank.ie/docs/default-source/publications/macro-financial-review/macro-financial-review-2016-2.pdf?sfvrsn=4>

26 <http://www.fsb.org/wp-content/uploads/FSB-Policy-Recommendations-on-Asset-Management-Structural-Vulnerabilities.pdf>

Case Study 10: Influencing the EU and International Regulatory Environment: Shadow Banking

The Bank has also been actively involved in shadow banking work in the ESRB and chairs an expert group on investment funds which is currently assessing the potential systemic risk from investment funds and how the European legislative framework is positioned to respond to this. This is in addition to the Bank's position as chair of the Policy Task Force of the ESRB's joint expert group on shadow banking, where work on investment fund systemic risk analysis and the potential use of margins and haircuts as macroprudential instruments has been carried out.

Managing and Monitoring Supervisory Risk

In 2016, the Bank continued to develop and enhance its risk-based supervisory framework and PRISM to assess risk appetite in respect of supervised firms. Following the implementation of Solvency II, amendments were made to the Insurance Supervision supervisory approach within PRISM to align with Solvency II changes.

Additionally, a bespoke Anti-Money Laundering (AML) Module has been designed and implemented within PRISM, which allows supervisors to identify money laundering (ML)/ terrorist financing (TF) risk and monitor all engagements with firms from an AML/ CFT perspective.

The PRISM framework includes the performance of regular quality assurance reviews to assess the Bank's supervisory engagement with regulated firms. The quality assurance work seeks to ensure that risks within firms are properly identified, understood and mitigated in a timely manner and consistency and quality of supervisory decisions and judgements are maintained.

The Bank completed a series of specific Environmental Risk Assessments (ERAs) on a sectoral basis. Environmental Risks are assessed using four lenses: the macroeconomic environment, the operating environment, the financial market environment and the regulatory environment. The ERAs are provided to senior management and supervisors to assist them in conducting their forward-looking risk assessments of supervised firms. The impact of negative interest rates, regulatory developments, financial technology, political instability, and the domestic and international economies were all key drivers for these environmental risk assessments in 2016.

Department of Finance Cost of Insurance Working Group

In early 2016, the Department of Finance commenced a review to examine a number of issues across the non-life sector. The first phase of this work was focused on the current insurance compensation framework in Ireland (primarily in relation to motor insurance). The second phase of the Department's work on insurance is focused on the cost of motor insurance. The cost of insurance working group (CIWG) was established in July. The Bank is an active member of the CIWG and relevant sub-groups. The objective of the CIWG is to identify and examine the drivers of the cost of motor insurance and to recommend short, medium and longer-term measures to address issues arising. The CIWG's report was approved by the Cabinet on 10 January 2017 and subsequently published. The Report makes 33 recommendations with 71 associated actions to be carried out. The next phase of the CIWG's work will be the implementation of the individual actions and the Bank has been identified as the lead for a number of recommendations and actions.



Derville Rowland
Director of Enforcement

3.7 Enforcement Directorate

Objectives

Enforcement

One of the Bank's objectives is to seek to hold regulated firms and individuals to account where their behaviour fails to meet the required standards. Where firms and individuals fail to comply with their regulatory requirements, enforcement is an important tool to effect dissuasive and proportionate sanctions, achieve compliance and promote the behaviours we expect.

The Bank's powers to achieve these objectives include the following:

- Imposition of ASPs on firms and individuals who breach their regulatory requirements;
- Prohibition of persons, who do not meet the applicable F&P standards, from performing specified functions in the financial services industry;
- Revocation or refusal of firms' authorisations to carry out regulated financial services where those firms fail to meet their regulatory requirements, or where a firm fails to meet the authorisation requirements; and
- Summary criminal prosecutions.

AML/CFT

The Bank is the NCA for the monitoring and supervision of financial and credit institutions' compliance with their obligations under the Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 (CJA 2010).

The four key AML/CFT focus areas for the Bank are as follows:

- Effective risk-based supervision of AML/CFT/ Financial Sanctions (FS) compliance;
- Contribution and input into AML/ CFT legislative and policy developments;
- Authorisation of Trust or Company Service Providers that are subsidiaries of financial institutions; and
- Investigation of the provision of services by unauthorised firms/individuals.

2016 Key Outcomes

Enforcement

ASP Outcomes

The Bank imposed fines totalling €12,050,000 in 2016, the largest figure for fines imposed by the Bank in a single year to date. The public outcomes published in respect of the nine ASP cases concluded by way of settlement in 2016, highlighted the importance of compliance by financial institutions with important prudential, consumer protection and AML requirements.

Public statements in respect of fines imposed by the Bank in 2016 are published on the Bank's website. The publication of ASP outcomes informs financial services firms about issues identified by the Bank, how a firm or individual fell below the expected standard and why a particular regulatory response was adopted, which serves to improve compliance generally in all firms and sectors.

Case Study 11: Investigation of Springboard Mortgages Limited

Arising from an investigation by the Bank, a settlement agreement was entered into with Springboard for breaches of the Consumer Protection Codes 2006 and 2012. A fine of €4,500,000 was imposed on Springboard for serious failings in its obligations to tracker mortgage customers.

In addition to the fine and reprimand, the Bank required Springboard to implement a major redress and compensation programme under which Springboard has provided redress and compensation to customers impacted by the breaches of approximately €5.8m at November 2016.

The Bank's investigation found that Springboard failed to apply the correct interest rates to 222 customer mortgage accounts over a seven-year period between August 2008 and July 2015. In doing so, the investigation concluded that Springboard failed to:

- Act with due skill, care and diligence and in the best interests of its customers;
- Effectively employ adequate and/or appropriate resources and procedures; and
- Have adequate systems and controls in place.

The failures were significant and had serious consequences for impacted customers, all of whom had to make higher mortgage repayments than required. Further, the failures resulted in some impacted customers going into mortgage arrears and some being subjected to legal proceedings in respect of arrears on their accounts.

The imposition of a significant fine and reprimand, in addition to the comprehensive redress and compensation programme, clearly demonstrates that the Bank will take all necessary action in order to protect customers' best interests. The settlement served as a clear and timely warning to all regulated firms of their obligations to customers in the tracker mortgage area.

The first ASP case arising from an ECB instruction under Article 18(5) of the SSM Regulations was concluded by way of settlement with KBC Bank Ireland Plc in 2016. The Bank imposed a fine of €1,400,000 on the firm in respect of breaches of the Code of Practice on Lending to Related Parties 2010 and the Code of Practice on Lending to Related Parties 2013.

Progression of ASP Cases to Inquiry

In 2015, the Bank published announcements that eight cases had been referred to Inquiry; the case against INBS and five individuals who were concerned in the management of INBS and the case against two individuals who were concerned in the management of Quinn Insurance Limited (Under Administration) (QIL).

Following the referral of these cases to Inquiry a number of legal challenges were brought to the High Court by individuals concerned in the management of these entities. As at December 2016, the Bank had successfully defended each of the legal challenges brought before the High Court. Two additional High Court challenges are listed for hearing in 2017. The High Court judgments delivered to date with respect to the Bank's ASP uphold the very real and significant public interest in the proper regulation of the financial sector, the need to investigate suspected wrongdoing and the deployment by the Bank of its statutory enforcement powers. It was noted in one High Court judgment as follows:

"[The] evidence, which is uncontradicted, places considerable emphasis on the credibility of enforcement powers of financial regulators and the essential public interest in the underpinning of the stability of the financial system by credible administrative sanctions which provide a powerful deterrent against financial misconduct"

The Inquiry with respect to five individuals concerned in the management of INBS is proceeding. The Inquiry members are managing the Inquiry process and are currently addressing a number of preliminary applications. The Inquiry with respect to two individuals concerned in the management of QIL is also proceeding with preliminary applications being considered by the Inquiry members.

In 2016, a case in relation to the failure to hold adequate PII was also referred to Inquiry. This case was subsequently settled in July 2016, with the Bank imposing a fine of €2,750 on an insurance intermediary, Seamus Sutcliffe trading as the Mortgage Centre. Penalty decision factors taken into account in determining the appropriate fine included, amongst others, the firm's failure to settle at an early stage in the ASP and prior to the issuance of a Notice of Inquiry, which resulted in no discount for early settlement being applied by the Bank.

Fitness and Probity (F&P)

The Bank's F&P regime allows the Bank to investigate and, where appropriate, suspend or prohibit controlled function holders and to approve or refuse the appointment of people to certain positions.

Following an extensive investigation, in May 2016 the Bank issued a prohibition notice under the F&P regime in respect of Darren Gleeson, a former director of a retail intermediary. This prohibition notice prevents Mr Gleeson from acting in any controlled function indefinitely.

In February 2016, concerns were raised surrounding the alleged misappropriation of members' funds at Rush Credit Union which led to the Bank commencing an investigation into the former manager at Rush Credit Union. Thereafter, the Bank issued a suspension notice to this individual, using its powers under the F&P regime. In September 2016, the Bank successfully applied to the High Court for an order extending this suspension notice. This investigation remains ongoing.

Authorisations/Pre-approval Controlled Functions (PCFs)

The Bank holds interviews with applicants for PCFs when there are specific concerns about that individual's F&P. Following these interviews, the Bank may decide to refuse that individual's application. In 2016, this process resulted in:

- A decision to refuse an application for authorisation as a sole trader;
- A decision to refuse an application for approval of an individual to a number of PCFs; and
- The withdrawal of three applications for the appointment of individuals to PCFs.

In 2016, the Bank also successfully defended an appeal to IFSAT by Mr David Redmond of the Bank's 2015 decision to refuse his application for authorisation as a sole trader on F&P grounds.

Anti-Money Laundering

Enhanced Supervisory Engagement Model

During 2016 the Bank enhanced its supervisory engagement model and structures to better align with the risks of the supervised population and a bespoke AML module has been designed and implemented within PRISM. Firms with a higher level of risk are subject to more frequent and comprehensive supervision, comprising on-site and off-site measures. The Bank's supervisory engagement model also provides for responsive inspections based on specific intelligence or information, as well as spot check inspections. These inspections act as a deterrent for non-compliance by firms in sectors that are perceived to have lower levels of risk.

Effective Supervision of AML/CFT Compliance

The Bank carried out a range of supervisory activities in 2016, as set out below, aimed at effectively supervising firms' compliance with, and raising awareness of, AML/CFT compliance.

The Bank carried out 34 AML/CFT/FS on-site inspections in 2016. Firms from a broad range of sectors were inspected, including payment institutions, bureaux de change, credit unions, investment firms, banks and funds.

A report on AML/CFT/FS compliance in the life insurance sector was published in March 2016; a special AML edition of the Intermediary Times was published in August 2016 and a bulletin on Third Party Reliance was published in December 2016.

The Bank held 28 AML/CFT/FS review meetings and 40 AML/CFT/FS Risk Evaluation Questionnaires were completed by firms and assessed by the Bank.

The Bank participated in a wide range of speaking engagements around Ireland in 2016, aimed at increasing awareness of the Bank's expectations in relation to firms' compliance with AML/CFT/FS obligations; the Bank also updated its website to provide further advice and information in relation to AML/CFT/FS requirements and information for consumers.

Case Study 12: AML/CFT Supervisory College

During 2016, the Bank hosted a supervisory college for a firm authorised by it and passporting its services throughout Europe. The supervisory college, which focused exclusively on AML/CFT, was among the first of its kind in Europe.

Senior management from the firm attended part of the supervisory college to take questions from supervisors in relation to the firm's AML/CFT framework, as well as its operations and strategy. In addition, a number of countries presented on the nature of the AML/CFT supervision undertaken on the firm in their country.

The supervisory college, which was attended by representatives from 25 European jurisdictions, provided a platform for collaboration and information sharing among all of the European regulators responsible for the ongoing AML/CFT supervision of the firm.

Investigations of Unauthorised Activities

It is a criminal offence for an unauthorised firm/person to provide financial services in Ireland that would require an authorisation under the relevant legislation which the Bank is the responsible body for enforcing. Investigations into unauthorised activities by the Bank play a key role in consumer protection, as consumers who deal with unauthorised firms/persons will not have access to protections in place for regulated firms²⁷.

In 2016, the Bank carried out 237 investigations into unauthorised activities and published 19 warning notices, the majority of which related to unauthorised investment firms. The Bank has also been proactive in this area, by attending a number of Fintech seminars in 2016 to investigate if firms or persons are providing services that would require authorisation from the Bank.

²⁷ Investor compensation schemes, the services of the Financial Services Ombudsman, the F&P Regime, prudential requirements such as regulatory capital requirements or safeguarding of client funds.

Chapter 4: Our Strategic Priorities for 2017

The Strategic Plan 2016-2018 builds on work already underway in the Bank. The Bank's Mission Statement 'Safeguarding Stability, Protecting Consumers' remains at the heart of all that we do and encapsulates the dual priorities for the Bank in delivering on its mandate. The role of each of the directorates in achieving the Strategic Plan in 2017 is set out in this chapter. In the first instance, we have outlined some additional information on Brexit as it continues to be a significant priority which spans all of the directorates.

Brexit

The outcome of the UK referendum on the continued membership of the European Union (the Brexit Referendum) posed a number of material challenges for Ireland and the Bank. While the UK government invoked Article 50 of the Treaty on the EU by the end of March 2017, we do not know what the future arrangements between the UK and the EU will be, nor how the UK economy will fare once it has distanced itself further from the EU, and what the knock-on impacts will be for the Irish economy.

Against this background of significant uncertainty, and from a regulatory and supervisory perspective, the Bank's primary concern in the period leading up to the Brexit Referendum and thereafter has been to ensure that regulated firms with business models exposed directly or indirectly to the UK economy have addressed and planned appropriately for negative impacts that may result from the UK decision to leave. It remains a key part of the Bank's supervisory focus in 2017 to continue to engage with financial firms to ensure that they closely consider, and adapt for, the potential implications for their business models and revenue streams.

For firms seeking to establish for the first time in Ireland or for existing Irish regulated firms seeking to make material changes to their business strategies and scale as a result of Brexit the active debate about the implications of Brexit for the configuration of the European financial services sector continues. However, what determines where financial firms choose to locate themselves includes a wide array of factors. These include track records of different financial centres; national legal and tax environments; language and cultural factors; and infrastructure and quality of life attractiveness. The EU has a strong harmonised approach to financial regulation, and the Bank's approach to authorisation is firmly embedded in the overall European System of Financial Supervision (ESFS). The Bank does not have a role in seeking to attract business to Ireland. In determining an application for authorisation we have one central concern: to implement the Bank's mandate to safeguard stability and protect consumers.

The Bank expects to receive a number of applications from banks, insurance companies, investment firms, payment and e-money institutions. The Bank is committed to providing a clear, consistent, open and transparent authorisation process, while ensuring a rigorous assessment of the applicable regulatory standards. The authorisation gateway forms an important part of the Bank's supervisory model. There are a number of key elements which will form part of any Brexit related authorisation discussions in 2017 including:

- The Bank expects that the business will be run from Ireland, the board and effective management of the entity will be located here and that commercial and business decisions will be taken here. This flows through to the staffing that we would expect to see.
- The Bank will be focused on the firm's own understanding of the risks to its business, how they are managed by local management and mitigated.

Brexit

- The Bank will also seek to ensure that customer's interests are central to the business proposition.
- The Bank's focus in respect of outsourcing is on ensuring that there are strong controls and oversight in place and in line with sound practices. While the activity may be outsourced, responsibility may not and shall stay with the Irish firm.

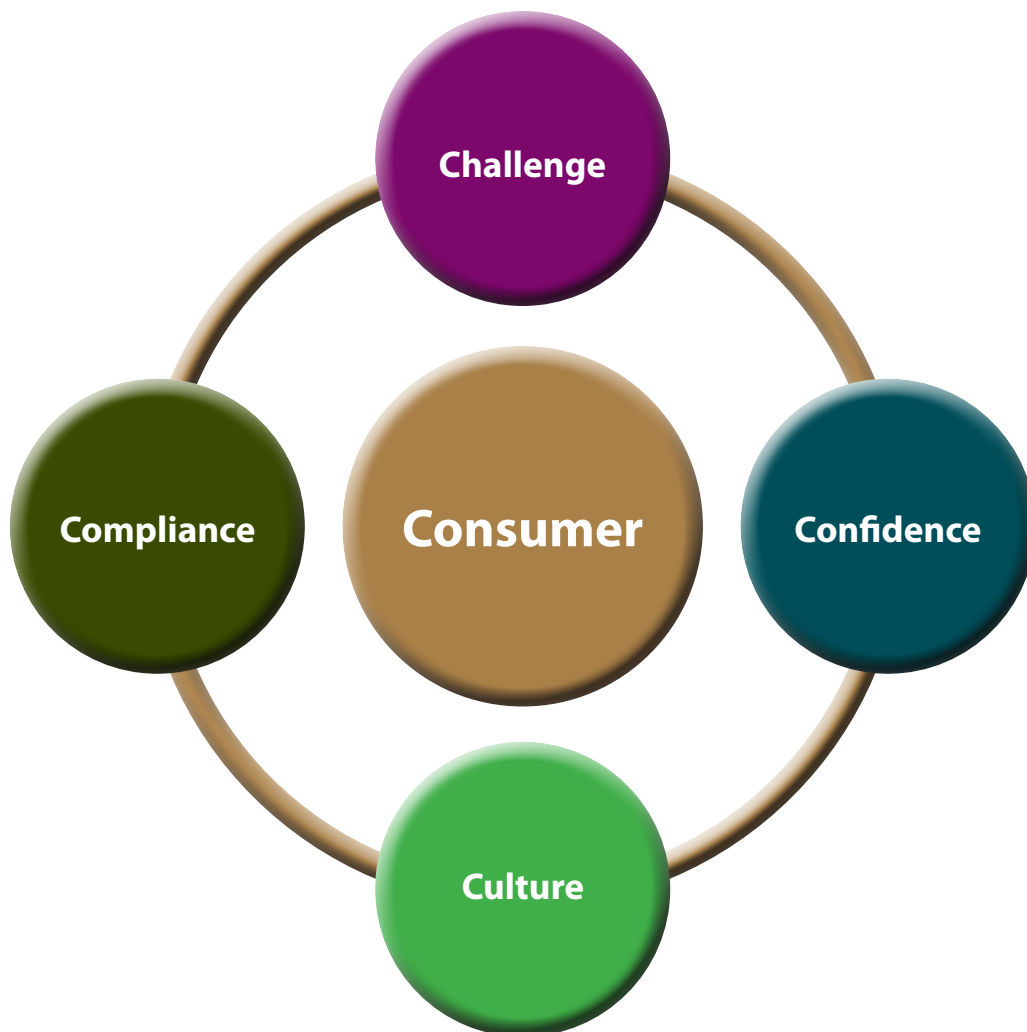
In short, firms that meet the Bank's regulatory standards can be expected to be approved.

In 2017, many firms will move to implement their group structural and geographical arrangements in response to Brexit. Although it is difficult to predict the full impact for the Bank, we are committed to deploying the required resources to deal with the potential increase in applications, and as such additional resources are included in workforce and recruitment planning.

4.1 Consumer Protection Directorate: 2017 Priorities and Challenges

Consumer Protection Directorate's 5Cs Framework Priorities

Chart 4.1: 5Cs Framework



The Consumer Protection Outlook Report, published in February, sets out under the 5Cs Framework, the key priorities for 2017.

Consumer: The Consumer Protection Framework

- The Bank will continue to support the Department of Finance with its work to implement key EU directives into Irish law, as well as working to review and update existing codes to reflect the changes arising from the new European legislation. The Bank will continue to commit resources to influencing and shaping the international and European agenda, including the work of the ESAs.
- In 2016, the Bank published a consultation paper on the review of the Minimum Competency Code (MCC). This review proposes a number of additional measures to raise standards as well as capturing changes required by European legislation and will be completed in 2017.
- Technology-driven innovation (Fintech) is having an impact on how products and services are being delivered to consumers in the digital age. In 2017, the Bank will publish a discussion paper on this topic as it relates to the Bank's existing Codes.
- As part of the Bank's ongoing monitoring of existing Codes, it is planning to review the Consumer Protection Code for Licensed Moneylenders to determine if the existing protections need to be enhanced.
- The Bank will continue its ongoing monitoring of market developments and will conduct consumer research to inform its work, including publishing this research and key trends observed in the market, in order to inform the wider discussion of consumer protection issues.

Culture: Consumer Focused Culture

- The Bank will publish details of its Consumer Protection Risk Assessment (CPRA) Model, which will help inform firms in developing or enhancing their consumer risk frameworks.
- The Bank will conduct a series of targeted CPRAs in a range of firms across the different industry sectors throughout 2017, with a particular focus on culture, performance management, sales incentives and product oversight and governance.
- The Bank will continue with its engagement with firms' boards and senior management to ensure that there is a clear focus from the top on embedding and measuring firms' own cultural change programmes.

Confidence: Consumer Confidence in Firms

- The ongoing Tracker Mortgage Examination continues to be a key priority for the Bank to ensure the fair treatment of tracker mortgage borrowers and is the most significant supervisory review that the Bank has undertaken in the context of our consumer protection mandate. Regular updates on progress were published during 2016 and we expect all relevant lenders to have identified and commenced engagement with most impacted customers by mid-2017, with the payment of redress and compensation extending beyond this point for some lenders. Further updates will be issued during 2017 as the Examination progresses.
- Following the publication of the discussion paper on the risks and benefits of the practice of product producers paying commission to intermediaries for selling their products in 2016, work will be progressed in 2017 to determine what measures, if any, need to be put in place to strengthen the protections for consumers.
- The Bank will conclude its research on mortgage switching and will bring forward any proposals for consultation, based on its findings.
- Systems failures and errors will continue to be monitored to ensure that firms are delivering on their obligations to ensure that consumers are kept fully informed of any issues, and that the impact on the consumer is dealt with in a timely and appropriate way.

Challenge: Firms and the Bank

- The Bank is currently reviewing applications from Credit Servicing Firms (CSFs) i.e. firms which service loans sold by regulated lenders to third parties. During 2017, these applications will be progressed to decision stage i.e. either authorisation or refusal.
- Applications for authorisation from other retail sectors including payment institutions, electronic money institutions, bureaux de change, retail intermediaries, debt management firms, retail credit firms and moneylenders will continue to be assessed in line with the relevant authorisation requirements and standards.

Compliance: Meet and Demonstrate Compliance

- In addition to the CPRAs which will be undertaken and the continuing Tracker Mortgage Examination, the Bank will conduct or commence a range of thematic reviews, including:
 - » Insurance companies selling niche/add on insurance;
 - » Payment institutions' safekeeping of client funds;
 - » Retail intermediaries' compliance with minimum standards; and
 - » Retail intermediaries which are acting as managing general agents on behalf of insurance companies.
- The Bank will also continue with its initiatives to facilitate smaller firms in better understanding their responsibilities, including hosting road shows around the country and the publication of newsletters for a number of industry sectors.

4.2 Credit Institutions Directorate: 2017 Priorities and Challenges

4.2.1 Banking Supervision

Supervisory Outcomes for 2017

In the execution of supervisory responsibilities during 2017, and to ensure that the right supervisory outcomes are achieved, the Bank will continue to require that credit institutions are properly governed and controlled with clear and embedded risk appetites; have sustainable capital generating business models over the economic cycle; have sufficient financial resources; and are resolvable in the event of a failure.

While a wide range of activities are planned for 2017, some of the key priorities that will be focused on to achieve the required supervisory outcomes include: continuing NPL resolution, Business Model and Profitability Analysis, IFRS 9²⁸ implementation, IT and Cyber Risk evaluation, Targeted Review of Internal Models (TRIM) and Brexit preparation.

NPL Resolution

As a result of the work carried out to date, there is evidence that there is much more to be done in the area of NPL resolution. The Bank will drive the banks to reduce their NPL ratios to an acceptable level, with sufficient provisions for remaining NPLs; while also assessing the restructuring in the Commercial Real Estate (CRE) and Small and Medium Enterprise (SME) portfolios. The Bank will challenge credit institutions in terms of their re-engagement strategies.

Building on the work of the NPL Task Force the Bank will push for better results, focusing at board level, including the strategy for and oversight of NPL reduction, in addition to continuing to examine the operational capability and execution of NPL resolution. Targets for NPL Resolution will continue to be a tool that the Bank utilise to

²⁸ IFRS 9 introduces a forward-looking impairment model based on expected credit losses and the allocation of loans to impairment stages based on increases in credit risk.

achieve better results. The Bank will also focus on IFRS 9 implementation across the relevant banks and will conduct a thematic review to understand their level of preparedness.

Business Model Sustainability

The Bank will continue to challenge the sustainability of banks' strategic plans, including participating in an SSM thematic review on the drivers of profitability. Additionally, the Bank will closely monitor the evolution of banks' risk appetite and cost reductions. The inspection programme for 2017 will also examine the business model and profitability of a number of in-scope institutions.

Inspection Programme including TRIM

It is planned that over 30 in-depth inspections will be performed across both SIs and LSIs in 2017 covering all risk areas. However, as has been the case previously, inspections are targeted to the areas of most concern, as informed by supervision and analysis findings. The inspections will be resourced by inspectors from the Bank, with inspectors from the ECB and/or other NCAs possibly joining/leading a small number of missions. The inspection programme will continue to ensure that the right emphasis is placed on credit and IT risk while also ensuring robust oversight of the governance of banks.

As part of the SSM, the Bank will engage in the execution of TRIM. This project was initiated within the SSM to assess whether internal models used by banks comply with regulatory requirements and are reliable and comparable. As part of TRIM the Bank will work with the ECB, other NCAs and external consultants to conduct on-site inspections on the application of internal models to determine regulatory capital requirements.

Authorisations Responsibilities and Impact of Brexit

During 2016, the Bank commenced engagement with banks that were considering the optimal location of their operations as a result of Brexit. The Bank will continue to engage with the SSM and other regulators to ensure the appropriate policy position is developed and understood. Preparations are well under way and the Bank has begun detailed engagement with institutions that have decided to either seek authorisation in Ireland or an extension of their current operations. While the ECB, with input from the Bank as the NCA, is the competent authority for the granting and revocation of licenses, the Bank has an established authorisations team that will work within the SSM Framework to complete the authorisations process.

During 2017, the Bank will prioritise expanding the authorisations resources in place. The Bank will engage with firms to ensure that those seeking authorisation have a good understanding of the supervisory expectations in the context of the original application and the post application operation of the business from a governance, control and risk management perspective.

The Bank will also work to examine and understand the impact of Brexit through the undertaking of cross sector analysis, engagement with firms through on-site inspections, and cooperation and collaboration with stakeholders within the Bank, and the wider SSM. The international banking sector in Ireland may undergo significant changes as a result of Brexit, giving rise to increased risks to the domestic banking sector from a macro-economic perspective. In the context of the Bank's Financial Stability mandate, comprehensive analysis of Brexit consequences and impacts on banks operating in Ireland. This will be done by contributing to the performance of macro stress testing to provide a thorough analysis of risk on a sector-wide basis, continued focus, monitoring and analysis of the macroprudential measures and their impacts, and the implementation of risk indicators for Other Systemically Important Institutions (OSII), to facilitate the identification of banks operating within Ireland that are of systemic importance at EU or Member State level.

Recovery Plans

The Bank undertook a considerable amount of work in 2016 in engaging with credit institutions on their recovery plans and participating in colleges. Many credit institutions still have further work to complete to ensure that they have effective recovery plans that are fit for purpose. Through ongoing review and engagement in 2017 the Bank will work to ensure that there are appropriate recovery plans put in place.

International Agenda

The Bank considers it important to effectively engage at a European and International level to ensure that we have an opportunity to influence important policy and supervisory decisions. Therefore, European engagement on supervision and banking policy matters will continue to be a priority with supervisors actively participating in a range of EBA and SSM Task Forces, Networks and Working Groups covering topics including Brexit, NPLs, IT risk, stress testing, crisis management, internal models and inspection methodologies. The Bank will continue to seek to deliver consistent, timely and effective supervisory outcomes working within the supra-national structures of the SSM.

Resourcing and Staff Development

The Bank will work to fulfil this broad and challenging mandate while faced with significant ongoing recruitment and retention challenges arising from high turnover levels. The Bank is working to address these challenges through the development of a comprehensive resourcing strategy.

4.2.2 Registry of Credit Unions

Supervisory Engagement

In 2017, the Registry plans to conduct quantitative and qualitative analysis to support the assessment of the credit union sector. The Registry will aim to enhance provision of technical input to supervisory activities through compilation of a Supervisory Manual for Supervisors. The Registry also plans to introduce a new Quality Assurance framework to ensure both the ongoing application and timely update of the Supervisory Manual for Credit Unions.

During 2016, the Registry developed a new engagement approach for credit unions, which will be implemented in 2017. This will involve performing risk profiling of the sector and the prioritisation of on-site inspections in line with the supervisory model. The Registry aim to undertake on-site engagements in line with the PRISM minimum engagement cycle and risk profiling. In particular, the Registry will target an assessment of post Transfer of Engagement (TOE) credit unions with a view to assessing the success or otherwise of the TOE and with a view to informing future strategy in this area. The Registry will also aim to conduct thematic inspections across a number of areas with a view to delivering sector-wide messages on the particular areas assessed.

The Registry will continue to review and enhance the credit union viability model as a basis for supervisory engagement priorities, taking into consideration the new regulatory returns (FRS102). Where relevant, it will liaise with the Enforcement Division with a view to taking enforcement actions against non-compliant credit unions.

The Registry will develop its storage and reporting tools, to improve access to and analysis of data received via online reporting from credit unions, with the aim of embedding analytics within the broader supervisory activity. The Registry will also develop improved Management Information on key sectoral performance areas and supervisory on-site activities. Where necessary, new reporting requirements e.g. more detailed information on investments and loans will be identified and developed.

Restructuring and Consolidation

During 2017, the Registry will continue to assist the consolidation of the credit union sector and will focus on a number of key areas to achieve this. The Registry will assess credit union post-restructuring cases with a focus on viability and performance compared with strategic and business plans provided. Supervisory engagement will include a focus on the embedding of governance, risk management and operational capabilities in post-merger credit unions. The Registry will also track progress on realising the benefits and synergies that were set out in business plans prepared by the credit unions prior to the transfer, with a view to ensuring that their increased scale is facilitating the objective of meeting the needs and expectations of members.

While the pace of restructuring will change, any further voluntary transfer proposals will be assessed ensuring that viability and governance is demonstrated through robust business cases and the risks clearly mitigated. The Registry will continue to encourage those credit unions that have not done so, to consider their strategic future and not to postpone unduly dealing with viability issues, as this will merely delay the necessary actions and have the impact of weakening their overall financial position, including reducing the level of reserves they hold.

The supervisory engagement model will include extensive focus on high risk credit unions to identify potential non-viability and determine mitigating actions. The Registry will ensure that appropriate and timely action taken to secure capital support to restore capital positions (immediately prior to the completion of a transfer of engagements process or on a standalone basis) or other intervention action.

The Registry will continue throughout 2017 to undertake and assist in the resolution of failing credit unions. The Registry will ensure proactive and collaborative engagement with third parties regarding the availability of private sector funds and the associated conditions. In those cases, where a credit union is not viable and/or there are egregious failures, the Registry will, and is prepared to, take whatever action is necessary to protect members' savings, once all appropriate supervisory options have been considered. In such cases, the Registry will work to ensure that any failure will be well-managed and completed in an orderly manner, so that financial loss or loss of service for members is avoided as far as possible. The Registry will collaborate and share information with the Bank's Resolution Division on individual credit union cases as appropriate and ensure that all supervisory matters/actions taken are documented to support cases where a resolution is taken.

Business Model Development

As part of the supervisory focus on business model analysis, the Registry will seek to enhance the focus of the credit union sector on business model transformation in 2017. The Registry will facilitate the development of proposals, via engagement, supervisory and other channels to ensure that proposals on business model development which are identified, will have the necessary regulatory assessment performed.

Where necessary the Registry will aim to make any changes required to the regulatory framework to facilitate prudent strategic business model development, ensuring that the appropriate changes are developed and implemented in accordance with internal and external consultation requirements.

Regulatory Framework Development; Safety Nets

The Registry will continue to develop and embed the credit union regulatory framework. In line with ensuring that regulations are kept up to date and appropriate, the Registry will review the investment regulations for credit unions in 2017:

- The Registry will review the regulations to consider whether it is appropriate and prudent to facilitate investment by credit unions in other investments, such as for example social housing, by broadening the permitted investment classes in the regulations.
- The Registry will undertake a review of the F&P Regime for Credit Unions in 2017 and plans to publish a Consultation Paper on potential changes to the Regime and subsequently publish the feedback statement and make any final changes to the Regime for credit unions.

- The Registry will develop Guidelines on NPLs / Provisioning for credit unions.
- The Registry will participate in the Implementation Group, established by the Department of Finance following the Credit Union Advisory Committee (CUAC) review of the implementation of Recommendations set out in the Report of the Commission on Credit Unions.
- The Registry will also contribute to the work on development of International Credit Union Regulators' Network (ICURN) Best Practices and Guiding Principles.
- The Registry will continue its proactive engagement/communication with credit union sector stakeholders. This will include issuing the biannual newsletter, information seminars, stakeholder meetings and other forms of engagement (e.g. credit union chapter meetings, other external events). The Registry also aim to publish high quality analysis.

4.3 Insurance Supervision Directorate: 2017 Priorities and Challenges

In 2017, the Bank will continue its risk-based approach to insurance supervision and will contribute to strengthening the regulatory framework by providing support to aid supervisors in understanding key macroeconomic risks. The Bank will do so through the production of comprehensive RMPs in accordance with PRISM guidance and by conducting on-site and off-site supervision of insurance undertakings to understand the key risks they face.

The specific 2017 priorities include the following:

- A focus on business model sustainability; how boards are recognising changing markets and the impact of Solvency II and building appropriate new strategies;
- Ensuring there is sufficient attention given to stress testing by firms through looking at the nature and strength of stresses and scenarios in the ORSA process, the understanding of group support and the undertaking of a focused stress test programme on the domestic Non-Life market;
- Continuing the embedding of Solvency II reporting through the online reporting of annual returns and new Solvency II reports such as the Solvency and Financial Condition Report and Regular Supervisory Report and ensuring they are built into the wider supervisory approach;
- Continuing to develop country risk reports on cross border business and building stronger links between actuarial work on reserving, capital and pricing.

Analytical Data

A priority for 2017 is the development of the use of analytical data across all supervision teams. This will include the development of triggers and alerts to highlight possible issues as well as access to reporting tools to allow more detailed analysis. A joint analytics/supervisory initiative has been established to develop analytics and to leverage more power from Solvency II returns, ultimately supporting supervisory oversight and decision making.

Branch On-Site Visits

The Bank will be increasing the number of (re)insurance on-site visits to increase the Bank's oversight of branches. A branch specialist will develop methodology and consistency of approach to branch inspections, to support the supervision team in completing inspections in 2017. As part of the branch visits controls, governance and risk management will be tested to ensure structures and processes are as detailed by head office.

Communication and Collaboration

Effective communication with industry remains a key priority for the Bank and plays an important role in support of the Bank's wider supervisory agenda. The Bank will continue to interact regularly with all stakeholders through regular publications, website update, colleges and meetings. Ongoing engagement with EIOPA via the Board of Supervisors (BoS) and other operational committee meetings will ensure the Bank contributes to the effective

development of EU insurance regulation. It is also important that the Bank continues to build relationships and collaborate with other regulators.

Authorisations Responsibilities and Impact of Brexit

One of the challenges for the Bank will be the potential impact and increased workload on the Irish insurance market arising from the outcome of the Brexit Referendum. There has been a material increase in the number of authorisation queries in Q4 2016 and Q1 of 2017. A significant volume of queries in relation to the authorisation process has been received from UK based insurance firms which are considering relocating their headquarters to Ireland.

4.4 Asset Management Supervision Directorate: 2017 Priorities and Challenges

The following have been identified as the priority areas of focus for the directorate in 2017:

Implementation of MiFID II

Implement the MiFID II legislation/Markets in Financial Instruments Regulation (MiFIR) regulatory framework and ensure firms have structures and procedures in place in readiness for meeting their obligations under the new legislation.

- The revision of MiFID II represents a significant change for the European financial markets. MiFID II is set to take effect from 3 January 2018 and includes a revision to the MiFID and a new MiFIR. There are several objectives of the revised legislation including: increasing investor protections; increasing competition across the financial markets and increasing supervisory powers.
- The Bank is engaged in multiple work streams and is committing significant resources to ensure the effective implementation of MiFID II in 2017. A complete analysis of the Directive, the Regulation, the Regulatory Technical Standards (RTS), the delegated acts and the ESMA guidelines has been completed. An IT project has been initiated, to deliver on the required system changes. From a staffing perspective this includes the delivery of staff training, updating all applicable policies and procedures, defining the supervisory priorities and liaising with all internal and external stakeholders.

Authorisation Responsibilities - Implementation of MiFID II and Impact of Brexit

- The authorisation process forms a key part of the Bank's gatekeeper role in relation to the asset management industry, this includes MiFID investment firms, FSPs and market infrastructure providers. Authorisation will become a particular focus for the directorate in 2017 as, in addition to business as usual, the area will be impacted by: the expected increase in applications for authorisation as a result of Brexit, and the changes being implemented by MiFID II.
- MiFID II introduces a number of new requirements for firms seeking authorisation, in addition to new entity types requiring authorisation; and a number of new financial instruments. Application forms and guidance are being updated to take into account these changes. As such, starting mid 2017 when MiFID II is officially transposed into national legislation, it will be necessary to assess all new applicants as MiFID II authorised entities given the six-month legislative timeframe for the approval of complete applications.
- The directorate will engage with all stakeholders during 2017 in preparation for new processes and their transitional timings.

Supervisory Engagement

Enhance supervisory engagement with supervised firms through implementation of findings from thematic reviews/inspections and enhancement of governance controls.

- The Bank will continue to mitigate risks of issues identified through intrusive supervisory engagements. In 2017 this will include FRAs, thematic reviews and focused reviews, in addition to the regular series of desk-top reviews and meetings.

- Ensuring effective implementation of supervisory findings is a priority for the Bank. Focused reviews will assess if issued RMPs have been fully embedded in the firm in order to achieve the required outcome.
- Building on the findings of the 2016 reviews, outsourcing arrangements will continue to be reviewed and robustly challenged to ensure that strong controls are in place concerning the governance of outsourcing arrangements.
- The protection of client assets is a key priority for the Bank. It is also at the core of the Bank's mission to protect consumers. The directorate has operated a Client Asset Specialist Team (CAST) since 2012, which ensures specialist supervisory resources are allocated to the supervision of client asset risk in relevant investment firms. This will continue to be a priority during 2017.
- During 2017, the CAST will prioritise supervision of investment firms to ensure tougher operational and governance requirements have been implemented to a high standard. The CAST will also continue its programme of engagement with FSPs in relation to implementation of new IMR introduced for the first time in July 2016.

International Agenda

Continue to assist the European regulatory colleagues by adding and contributing knowledge and expertise to enable the promotion of a common supervisory culture in Europe.

- The directorate continues to support the important work of ESMA. The Director sits on the Supervisory Convergence Standing Committee (SCSC). ESMA is mandated to take an active role in building a common supervisory culture among NCAs to promote sound, efficient, and consistent supervision throughout the EU. The SCSC helps in the coordination of this work.
- The Bank is also involved in ESMA Supervisory Convergence Work Programme through participation in a peer review on the compliance function guidelines. This review is to assess compliance by NCAs with the guidelines, identify good practices and potential areas for improvement. A final report will be published by ESMA in Q2 2017.

Staff Training and Development

Increased focus on staff training and development to mitigate against loss of experience and knowledge.

- The learning and development of staff is at the core of the directorates 2017 objectives, which will further enable the delivery of authorisation and supervisory objectives. The directorate will work closely with Human Resources to design training and development solutions that will unlock staff potential.
- The directorate will continue to prioritise the learning and development of staff through a combination of practical on-the-job training, structured training courses and supporting those who wish to pursue further education opportunities.

4.5 Securities and Markets Supervision Directorate: 2017 Priorities and Challenges

The following have been identified as the priority areas of focus in 2017:

MiFID II/MiFIR Framework Implementation

Implement the MiFID II/MiFIR regulatory framework, developing and enhancing supervisory structures to meet legislative and regulatory requirements.

- Changes introduced to the MiFID, represent a significant change for European financial markets and market participants. The directorate is impacted by this legislation through increased transaction reporting obligations and the increased monitoring and surveillance of market activity pre and post trade. The Bank is building and enhancing its systems to receive, validate and store greater volumes of transaction reports and to exchange transaction reports with other NCAs. Projects are in train to deliver these systems in time for January 2018.
- The Bank will establish a new team with specific responsibility for the increased surveillance of market activity. Collaboration with existing Bank-wide analytical capability will be imperative to assist in the design

and development of a model of supervisory engagement which best covers the scale and magnitude of data received from reporting entities. The Bank will commit additional resources to markets surveillance in 2017 to ensure the effective implementation of MiFID II and MiFIR including delivering training to staff within the directorates during the year along with ensuring all procedures and guidance are updated and publicly available. The Bank will also engage with external stakeholders, the purpose of which will be to educate and inform industry of the new legislative requirements.

Authorisations Responsibilities, Approvals and Impact of Brexit

Continued focus on ensuring all authorisation and approval processes meet the highest standards of regulation and comply with all applicable legislation.

- The Bank anticipates an increase in the volume of new applications and/or investment fund mergers from UK based firms who are considering their EU accessibility in light of the Brexit referendum. This trend is also expected from issuers of securities seeking the approval of prospectuses for offers to the public and/or admission to trading on a regulated market in accordance with the Prospectus Regulations.
- The Bank is committed to ensuring that all investment funds authorised by the Bank meet the highest regulatory standards. The authorisation/approval processes applicable to investment funds and issuers of prospectuses in Ireland form an integral part of the Bank's gatekeeper role and will continue to be a priority in 2017.
- The Bank will continue to contribute to the development of legislation applicable to investment funds and issuers of securities, and will ensure all authorisation/approval procedures comply with applicable legislative and regulatory requirements. All relevant application forms and supporting guidance will be available to new applicants through the Bank's website and the Directorate will continue to facilitate engagement with new applicants to assist with the authorisation/approval process.
- The Bank will undertake a review of charging structures applicable to investment funds/prospectus approvals to ensure that the cost of reviewing, authorising and approving these products is recouped and borne by the beneficiaries of the work undertaken by the Bank, rather than through firm levies or taxpayer subsidies.

Supervisory Engagement

Enhance supervisory engagement with investment funds through more intrusive themed inspections and use of newly developed analytical tools.

- In line with the PRISM supervisory engagement model for low impact entities, the directorate will continue with its programme of engagement throughout 2017 with a focus on depositaries' oversight of investment funds and will also perform FRAs on investment funds for the first time.
- The supervisory strategy for investment funds will be revisited and improved whereby the use of data will form an integral part of the Bank's supervisory engagement in 2017. Analytical tools and techniques will be used to identify market trends, monitor performance against such trends or benchmarks, and identify outliers which will be subject to further investigation and enforcement action where appropriate. Data will also inform supervisory judgements and identify investment funds to be included for thematic reviews. The directorate will seek to streamline and consolidate the reporting obligations of investment funds which will deliver efficiencies for both reporting entities and the Bank.
- Building on the thematic review performed in 2016 to examine the fees and expenses charged to investment funds authorised by the Bank, supervisors will be contacting the boards of specific investment funds to investigate concerns and request additional information in relation to their charging strategies.
- In accordance with the provisions of Omnibus II Directive, the Bank will undertake a thematic review comparing disclosure requirements in approved prospectuses with disclosures provided in advertising material. This is a new initiative and the first thematic review undertaken by the Bank in this area. The

findings of this review may result in further investigation of individual cases or, alternatively, an industry letter.

- The directorate will continue to regulate market activities through ongoing assessment of compliance with the Transparency Regulations, Short Selling Regulations, MiFID transaction reporting obligations, EMIR reporting requirements and ongoing surveillance of market behaviours in line with the recently amended MAR.

International Agenda

Continued contribution to development of legislation and enabling the fulfilment of the European agenda in regulatory development.

- The Bank actively contributes to the development of the EU legislative agenda and will continue to participate in the following ESMA committees: Investment Management Standing Committee (IMSC), Markets Data Standing Committee, Benchmark Regulation Task Force and Prospectus Regulation Task Force and its EMIR and MiFIR Task Forces.
- The directorate will take a lead role in transposing remaining parts of the TD II into domestic legislation in 2017 including collaboration with policy colleagues from across the Bank. This collaborative relationship will result in robust industry guidance and informed Q&As.

4.6 Policy and Risk Directorate: 2017 Priorities and Challenges

In addition to planning and responding effectively to the policy implications of Brexit across all the sectors of the financial services industry in 2017, the directorate plans to achieve the following key priorities:

Banking Policy

- Finalising proposed amendments to the CRD and the CRR: the directorate will work with colleagues across the Bank together with peers in the EBA and the SSM to analyse the implications of these proposals providing technical support and advice to the Department of Finance during critical negotiations at EU Council.
- Implementing IFRS 9: the implementation of IFRS 9 will also be a particular focus in 2017 driven by EBA and SSM work to assess the impact on banks, finalisation of the EBA guideline on Expected Credit Loss and consideration of the interaction of IFRS 9 with prudential requirements.

Insurance Policy

- Supporting the ongoing embedding of Solvency II: As the Solvency II regime moves into its second full year in operation the directorate will work within EIOPA to review the SCR and further develop its supervisory handbook.
- Continuing to engage with Department of Finance CIWG: As outlined in **Chapter 3.6**, the Bank has been identified as the lead for a number of recommendations and actions arising out of the work of the CIWG and its report published in January. The recommendations propose that the Bank undertakes a consultation on proposed amendments to the existing Statutory Instrument which sets out the requirements for the provision of information in non-life renewal notices, and to amend legislation if required. The CIWG has recently embarked on the second phase of its work which will focus on the cost of public liability and employer's liability insurance. The Bank will continue to contribute to the work of the CIWG on these topics.

Markets Policy

- Successful MiFID II/MiFIR implementation including delivery of advice to the Department of Finance to assist in ensuring the implementing regulations are in place by May 2017 and preparation of the Bank's Investment Regulations to incorporate client asset and investor money rules.
- Completion of the exchange trade funds study and publication of a discussion paper.
- With respect to shadow banking, the directorate is working on: the development of a Bank framework governing the use of financial stability powers in markets legislation, together with other areas of the Bank; and the completion of relevant policy development work in the ESRB including delivery of the final report of the expert group on investment funds.
- Publication of the Alternative Investment Funds (AIF) Rulebook in the form of Bank Regulations.
- Implementation of Money Market Funds Regulation and Prospectus Directive III.
- Delivery of Market Abuse Directive and MAR and TD rules in the form of statutory instruments.

Outsourcing Review

The directorate will also lead work on a Bank-wide review of outsourcing across all regulated sectors focusing on current outsourcing arrangements and practices, future patterns and developments, how risks are controlled and supervisory experience to date.

IT and Cyber Risk Strategy

Building on the guidance issued in 2016, the directorate will continue work with colleagues across the Bank on the development and implementation of the Bank's internal IT and Cyber Risk Strategy in 2017.

PRISM and Quality Assurance

The review and evolution of the PRISM framework will be a priority in 2017 with particular focus on the delivery of enhanced reporting for both senior management and supervisors. Other areas of focus include the Bank's supervisory approach across the Registry, the Consumer Protection Directorate and the Asset Management Supervision Directorate. This will include a review of the PRISM guidance to reflect current supervisory practices and recent regulatory changes.

Through a range of thematic reviews, firm specific deep dives, and internal Risk Governance Panels, the Directorate will continue to provide quality assurance to senior management in 2017 on the effectiveness of the Bank's supervisory approach.

Further Strengthening the Directorate's Capabilities

The directorate plans to focus on further strengthening internal capabilities through:

- The development of future accredited phases of the Bank-wide technical training (One Bank Curriculum); and
- Expanding the activities of the Bank's Policy Network including through a series of in-house events on broader policy issues such as Brexit, Fintech, data protection and crowdfunding.

Brexit

In terms of policy implications, critical aspects include potential policy issues arising from individual applications for authorisation, the framework for engagement with supervisory authorities in the UK as a third country post Brexit and implications for firms currently authorised by the Bank operating in the UK or through the UK financial services infrastructure. As the details of Brexit become clearer, the ESAs will consider in more detail issues from an EU perspective and, given the close business connections between the Irish and UK financial services industry, the Bank will be an active participant in these deliberations and in any resulting decisions.

4.7 Enforcement Directorate: 2017 Priorities and Challenges

In 2016, the Enforcement Directorate was re-structured in order to further support the delivery of its strategic priorities. The directorate now comprises three divisions: Enforcement Investigations, Enforcement Advisory and the Anti-Money Laundering (AML) Division.

Enforcement

The strategic priorities for 2017 build on work carried out by the directorate over recent years in using the range of available enforcement powers to achieve credible enforcement outcomes.

Defence of Legal Challenges to the Bank's ASP and Assistance to Ongoing Inquiries

In 2017, the Bank will continue to defend legal challenges arising following the referral of cases in respect of individuals concerned in the management of INBS and Quinn Insurance Limited (under administration) (QIL) to Inquiry.

Two individuals who were involved in the management of INBS have taken three sets of High Court civil proceedings against the Bank relating to the Inquiry process and the constitutionality of the Bank's ASP. To date the Bank has been successful in defending all three sets of legal proceedings. One High Court decision, relating to a Judicial Review application, has been appealed to the Court of Appeal and this is expected to be heard in June 2017.

Judicial review proceedings have also been initiated by two individuals who were concerned in the management of QIL seeking to have the Bank's decision to refer the matters to Inquiry quashed. The proceedings are due to be heard by the High Court in April 2017. The Bank will continue to defend these proceedings and any related appeals, together with any other potential challenges to the Bank's powers, in 2017.

In 2017, the directorate will also continue to provide any assistance or information requested by Inquiry members as the Inquiry in respect of certain persons concerned in the management of INBS and the Inquiry in respect of certain persons concerned in the management of QIL proceed. Representatives from the directorate will attend Inquiry management meetings and Inquiry hearings in order to provide this assistance.

Tracker Mortgage Examination

Two other tracker mortgage related enforcement investigations are currently ongoing into Permanent TSB p.l.c. and Ulster Bank Ireland DAC and the Bank's investigation of these matters will continue in 2017. It is possible that other enforcement investigations may also be commenced in 2017, as appropriate, into other lenders and persons concerned in the management of such entities where there is evidence of non-compliance with regulatory requirements. Enforcement measures may be deployed as appropriate, including investigating issues and taking cases under the Bank's ASP together with the use, as appropriate, of the Bank's F&P powers. The Bank's enforcement activity in this area will be influenced by the outcome of the reviews currently being conducted as part of the industry-wide tracker examination.

Use of Enforcement Powers to hold Regulated Firms and Individuals to Account

The Bank will continue to use the range of its powers to carry out robust investigations of regulated firms and individuals. In order to foster and maintain a culture of compliance within the financial services industry, resources will continue to be committed to investigating individuals and seeking to hold them to account where their behaviours do not meet the required standards.

An important aspect of the Bank's enforcement work relates to the Bank's gatekeeper function, preventing those who do not meet the required standards of F&P from taking up PCFs. The Bank also has the power to investigate individuals to ensure that they consistently meet the Bank's F&P requirements. In relation to CFs, a wider selection of roles within the financial services industry, the Bank has investigative powers in relation to

those firms who engage individuals in CFs, to ensure that they have carried out the necessary due diligence on the F&P of those individuals.

Engagement with SSM

The Bank will continue to build and maintain co-operative and effective relationships with the SSM. In 2017 the Bank is participating in the Enforcement and Sanctions Network and contributing to two working groups of the network. The Bank is also participating in the Network of Authorisation Experts at the ECB and is co-chairing the F&P working group at that network.

AML/CFT

The Bank is responsible for monitoring the compliance of over 10,000 credit and financial institutions with Part 4 of the CJA 2010. The Bank has assessed the money laundering and terrorist financing risk of the supervised population and has adopted a risk-based approach to AML/CFT supervision.

The following are the Bank's priorities in 2017 for AML/CFT.

Supervision

In 2017, the Bank will continue with its risk-based programme of supervisory engagement. The engagement model provides for regular scheduled on-site and off-site supervisory engagements of higher risk firms, with reducing frequency and intensity of engagements for non-high risk firms. The Bank will monitor AML/CFT compliance of firms in sectors with a lower risk of money laundering and terrorist financing through random spot check inspections and through communications and outreach to industry.

On-site inspections will be supplemented by a comprehensive programme of AML/CFT/FS review meetings, which involve Bank inspectors meeting with key AML/CFT control function holders, to review and assess firms' AML/CFT/FS control frameworks.

In 2017, the Bank will roll out an online AML/CFT/FS return that will be submitted by credit and financial institutions to the Bank for review and assessment. The return will be submitted through the Bank's on-line reporting system.

Communications and Outreach to Industry

A key priority for the Bank is effective communication and outreach to industry to raise awareness of AML/CFT obligations and to set out the Bank's expectations regarding compliance with those obligations. The Bank will continue to interact regularly with its stakeholders through regular AML/CFT publications, website updates, as well as industry briefings and speaking engagements.

Risk Assessment/Use of Analytical Data

During 2017, the Bank will further refine and enhance its assessment of the money laundering/terrorist financing risk of the supervised population. The Bank will also seek to develop its use of data to assist in the supervision of firms by identifying outliers which will be subject to further investigation, where appropriate. The use of analytical tools and techniques will also be used to identify firms to be included in thematic reviews.

Authorisations Responsibilities and Impact of Brexit

The Bank is the NCA for the authorisation of Trust and Company Service Providers (TCSPs) which are subsidiaries of credit or financial institutions. The authorisation of TCSPs form an integral part of the Bank's gatekeeper role and will continue to be a priority for the Bank in 2017.

Authorisations more generally are a particular focus for the Bank in 2017 with the expected increase in applications for authorisation as a result of the Brexit referendum. One of the biggest challenges for the Bank in 2017 will be the potential impact and increased workload arising from the outcome of Brexit. Assessing firms' AML/CFT compliance frameworks as part of the authorisations process will be a priority area for the Bank in 2017.

AML/CFT Policy Development

The Bank will continue to actively participate at national and international AML/CFT fora, including the national AML Steering Committee and the ESA AML Committee and working groups. The Bank will also continue to play a key role at the FATF plenary sessions, which in 2017, include Ireland's mutual evaluation review.

Investigations of Unauthorised Activities

During 2017, the Bank will continue to investigate unauthorised activities and publish warning notices.

Chapter 5: The firms we regulate and how we regulate them

This chapter sets out the range and number of financial services providers that are regulated by the Bank; the tools, and methods that are implemented in order to effectively regulate, supervise and monitor them and the resulting outcomes; and measures of performance of the associated regulation.

5.1 Who we regulate

The Bank is responsible for the proper and effective regulation of financial institutions and markets. In 2016, the Bank had responsibility for the regulation of over 10,000 Financial Service Providers. Chart 5.1 below displays the range of providers, and Charts 5.2 and 5.3 the numbers and sector breakdown of regulated service providers.

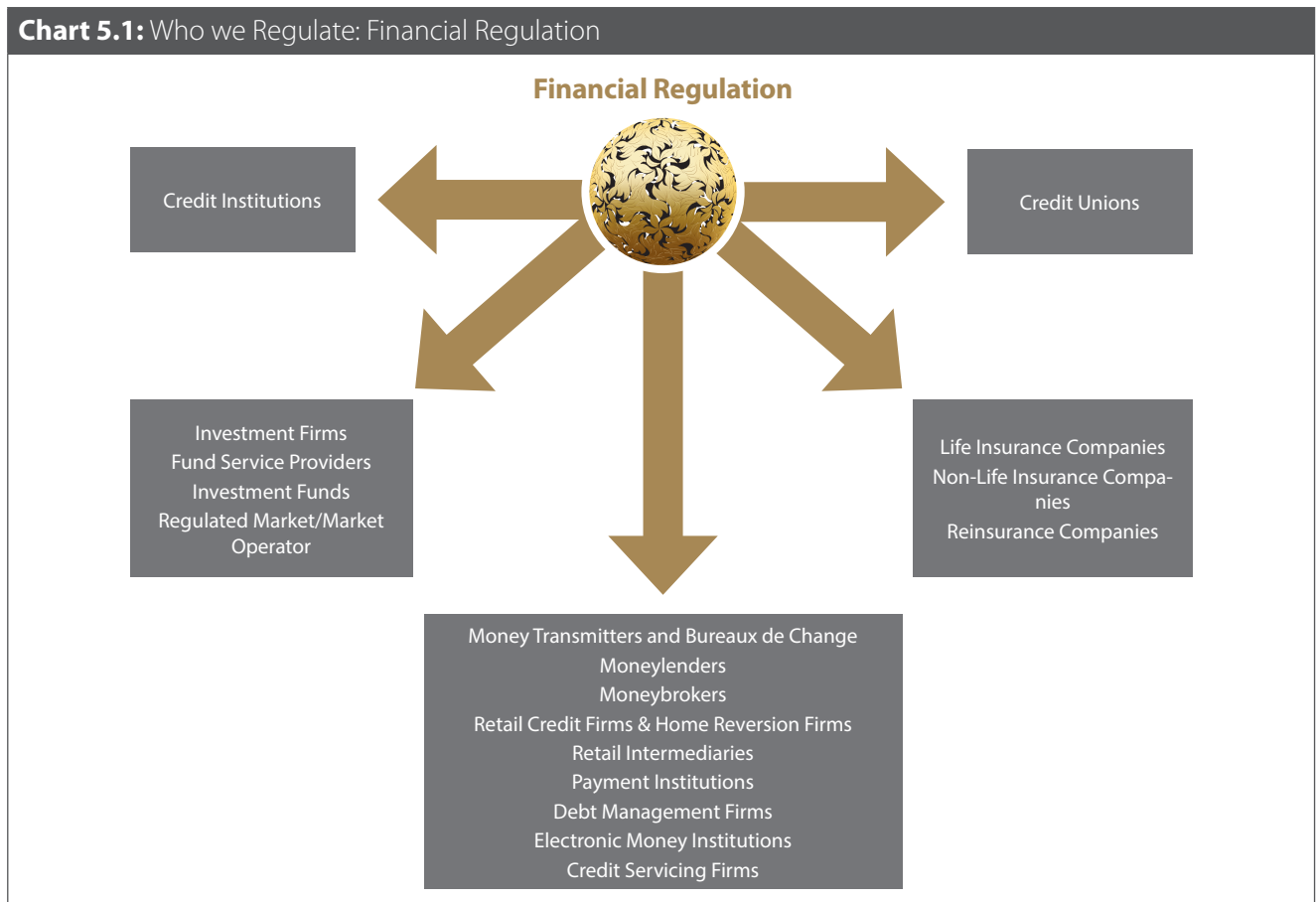


Chart 5.2: Total Financial Service Providers 2012–2016

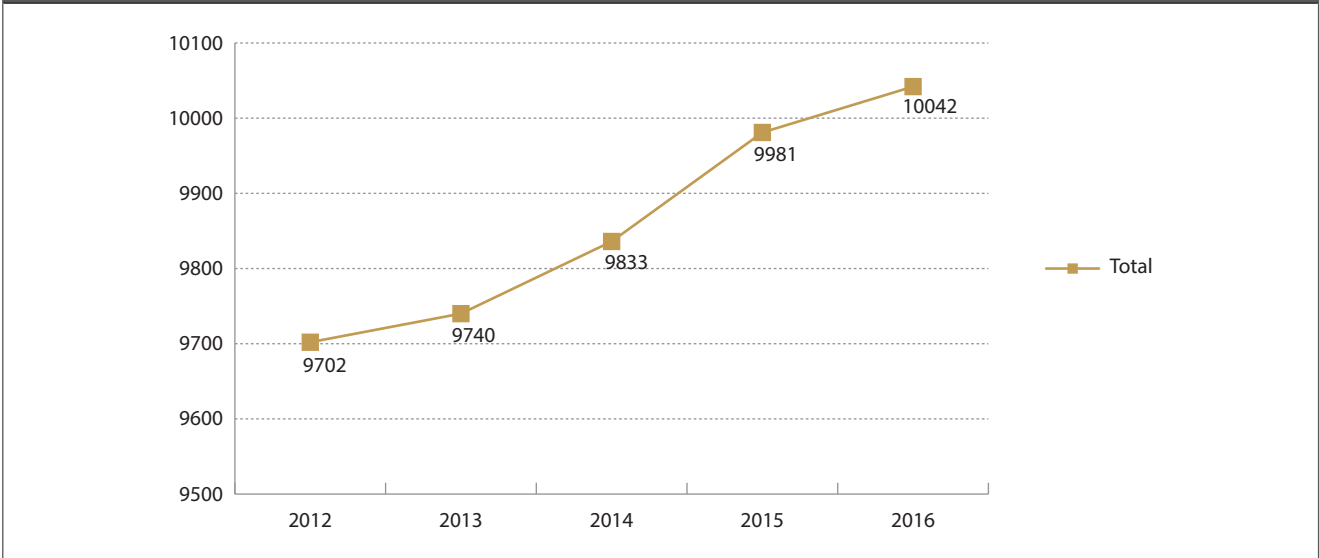


Chart 5.3: Breakdown of Financial Service Providers 2012–2016

Chart 5.3.1: Credit Institutions

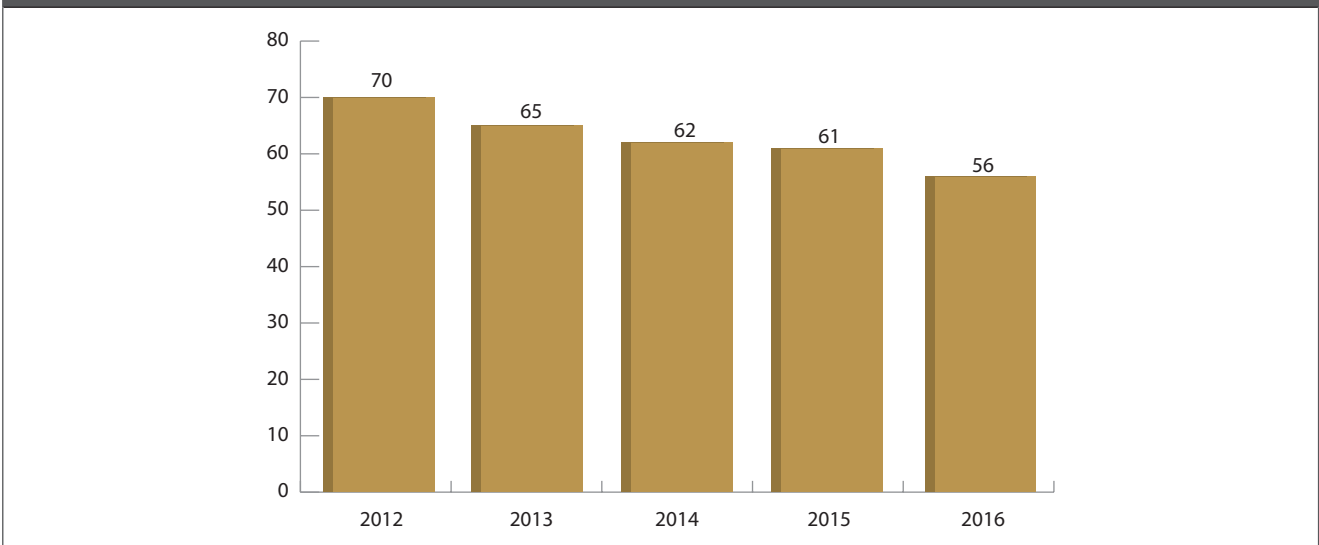


Chart 5.3.2: Credit Unions

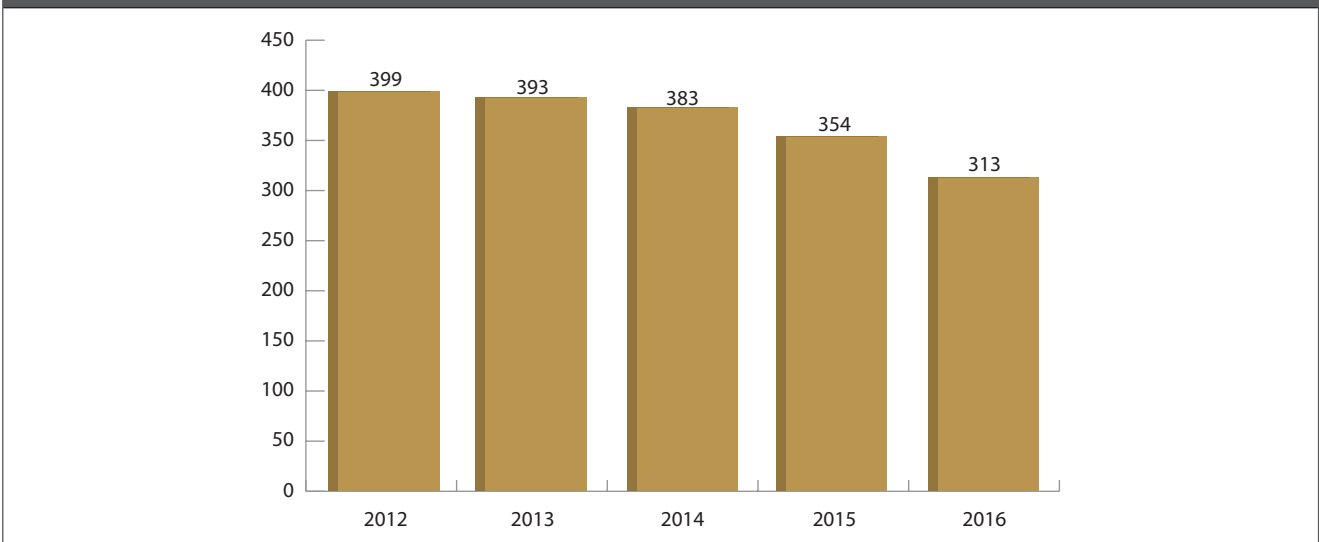


Chart 5.3.3: Insurance

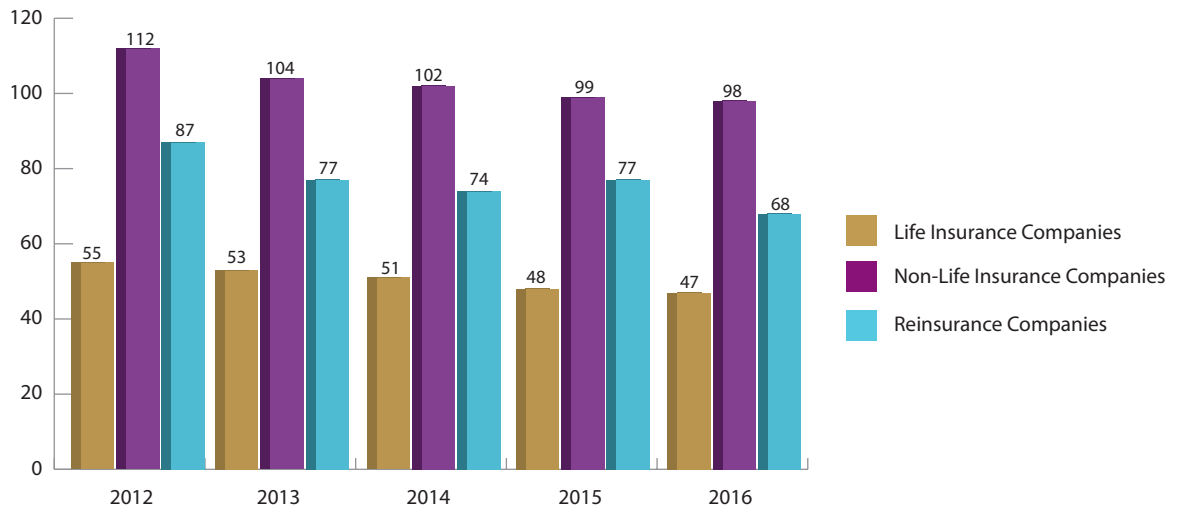
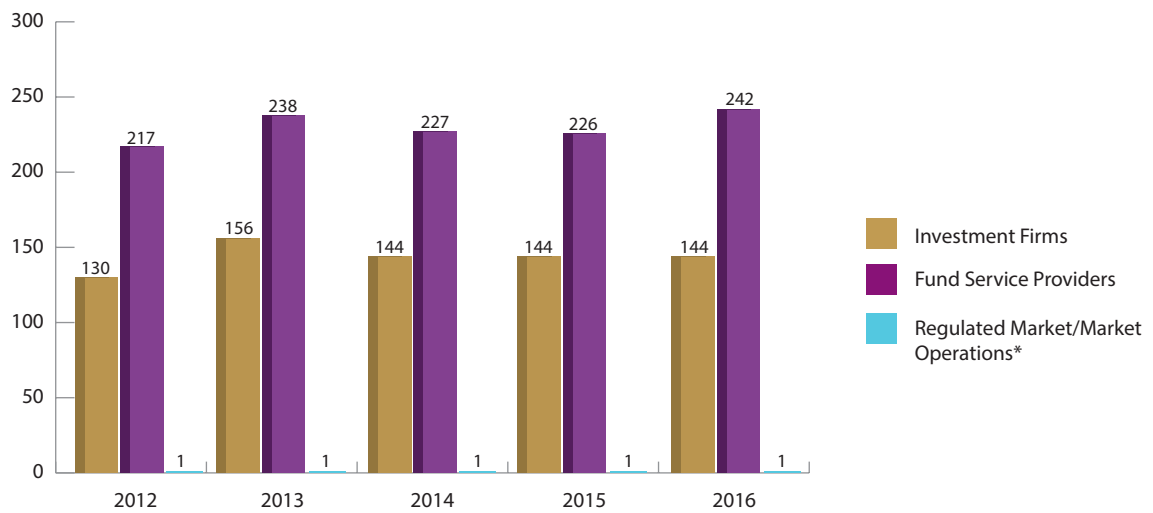


Chart 5.3.4: Investment Firms & Funds Service Providers



*Irish Stock Exchange

Chart 5.3.5: Investment Funds

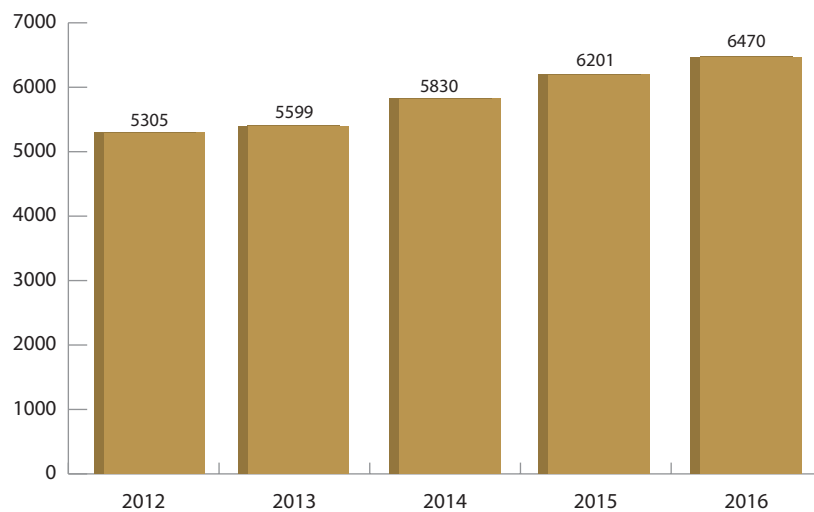


Chart 5.3.6: Retail Intermediaries

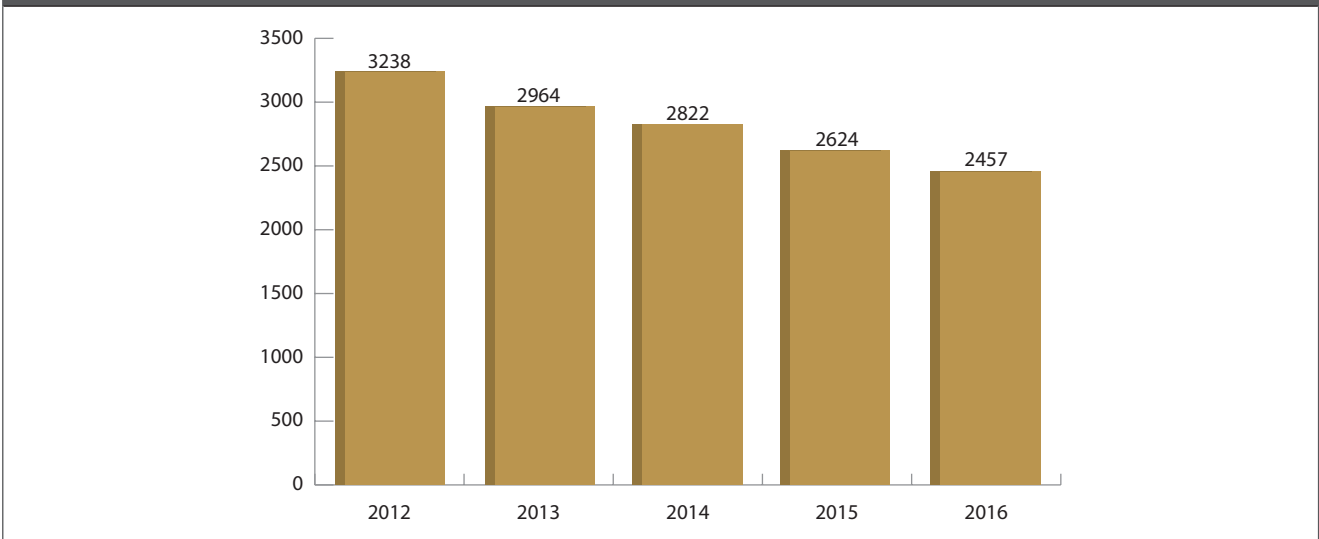
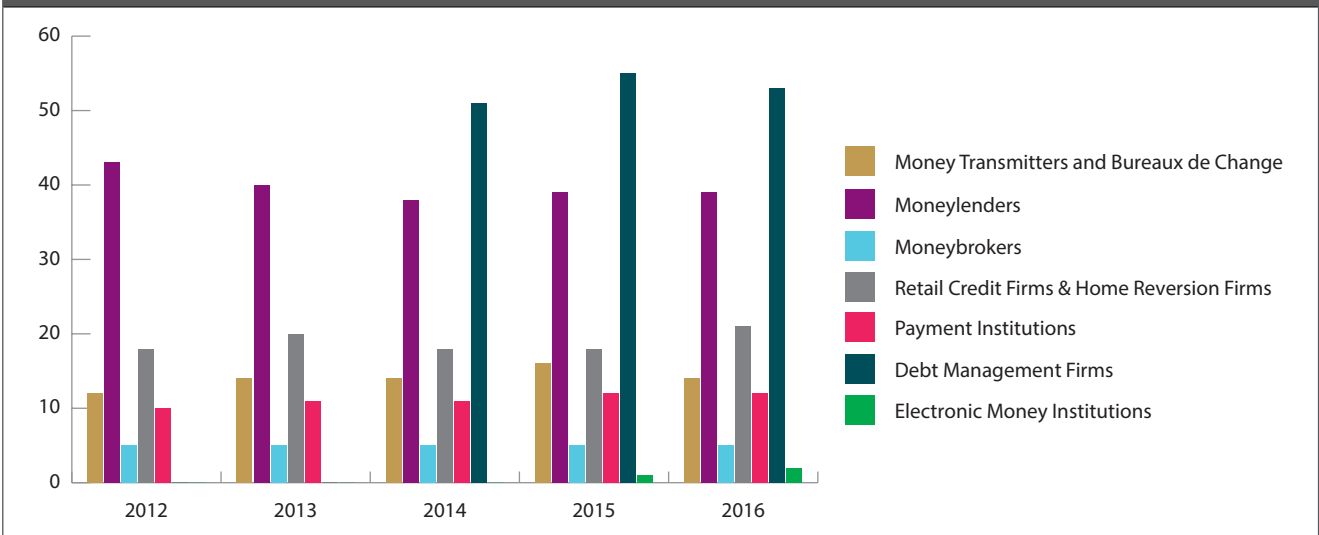
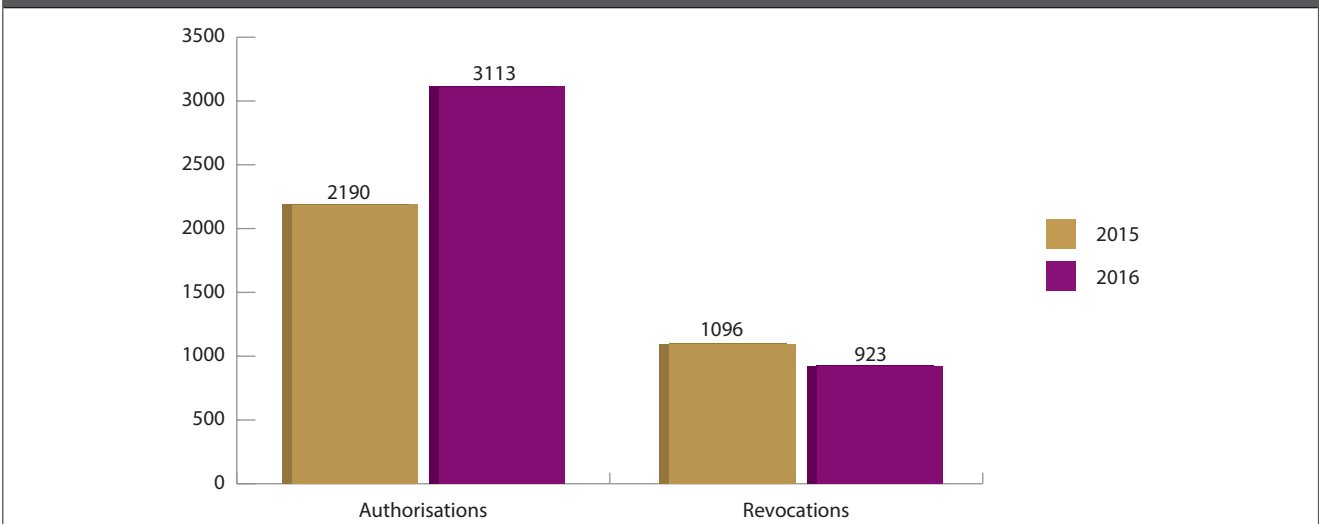


Chart 5.3.7: Other Financial Service Providers



A total of 3,113 authorisations were made in 2016. Compared to 2015, authorisations processed increased by 42% and revocations processed decreased by 16% in 2016 as set out in Chart 5.4.

Chart 5.4: Volumes of Authorisations and Revocations 2015, 2016

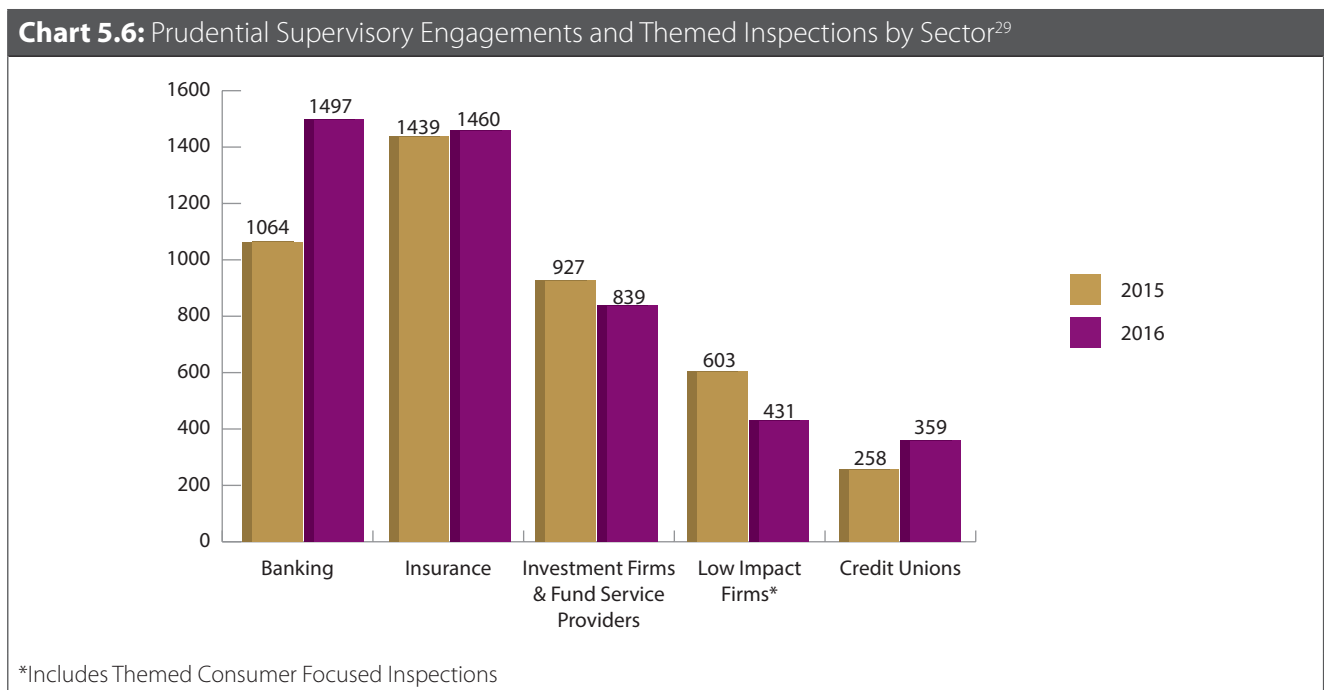
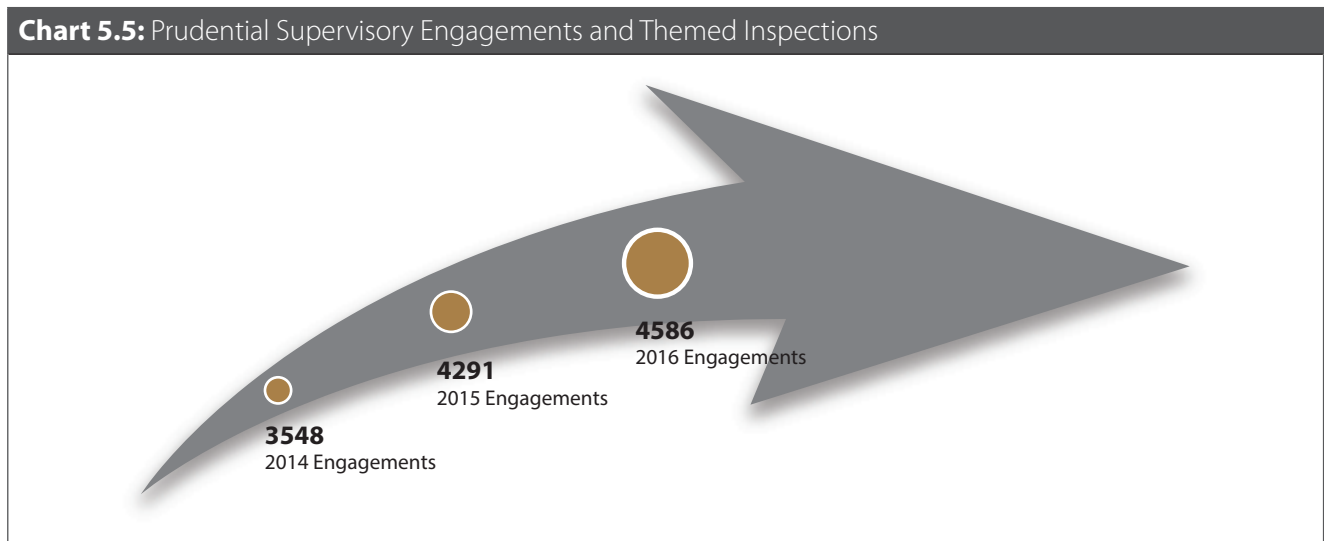


5.2 How we regulate

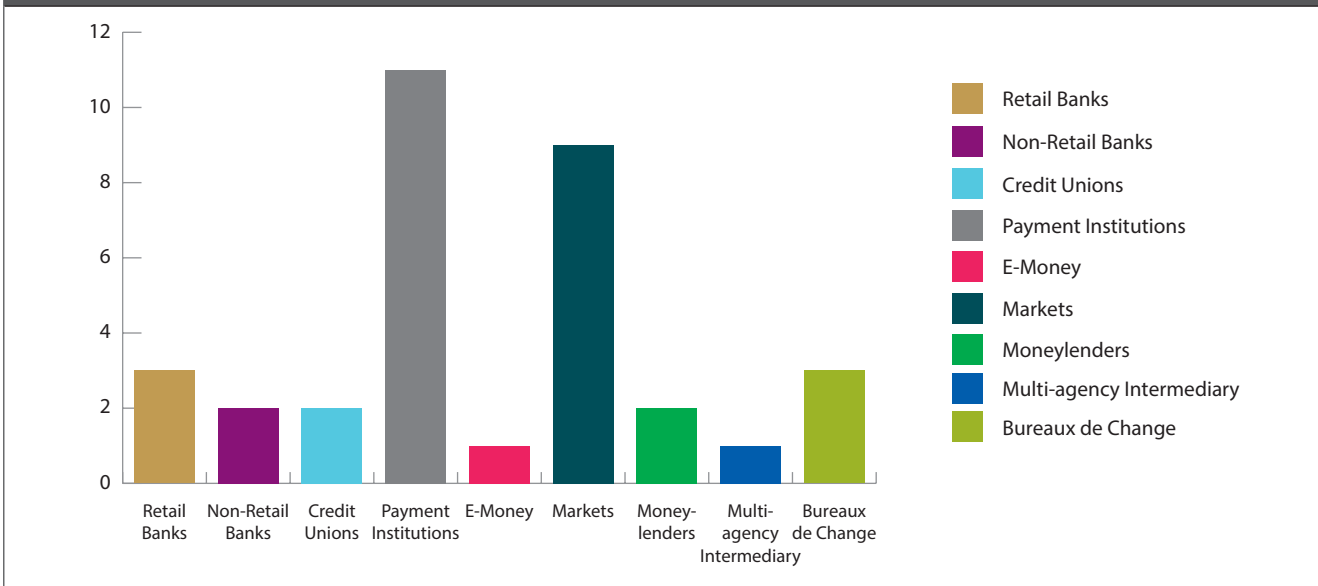
The Bank’s supervisory activities and outcomes across all financial sectors continued to be underpinned by its assertive risk-based approach to supervision, coupled with the credible threat of enforcement. Central to those activities is the Bank’s focus on its strategic and statutory objectives of *Safeguarding Stability, Protecting Consumers*.

5.2.1 Prudential Supervision Engagements

Charts 5.5 and 5.6 set out the volume of supervisory engagements conducted across the following sectors: Banking; Insurance; Consumer Protection; and Investment Firms and Funds Supervision. Chart 5.7 sets out the number of AML/CFT/FS inspections during 2016.

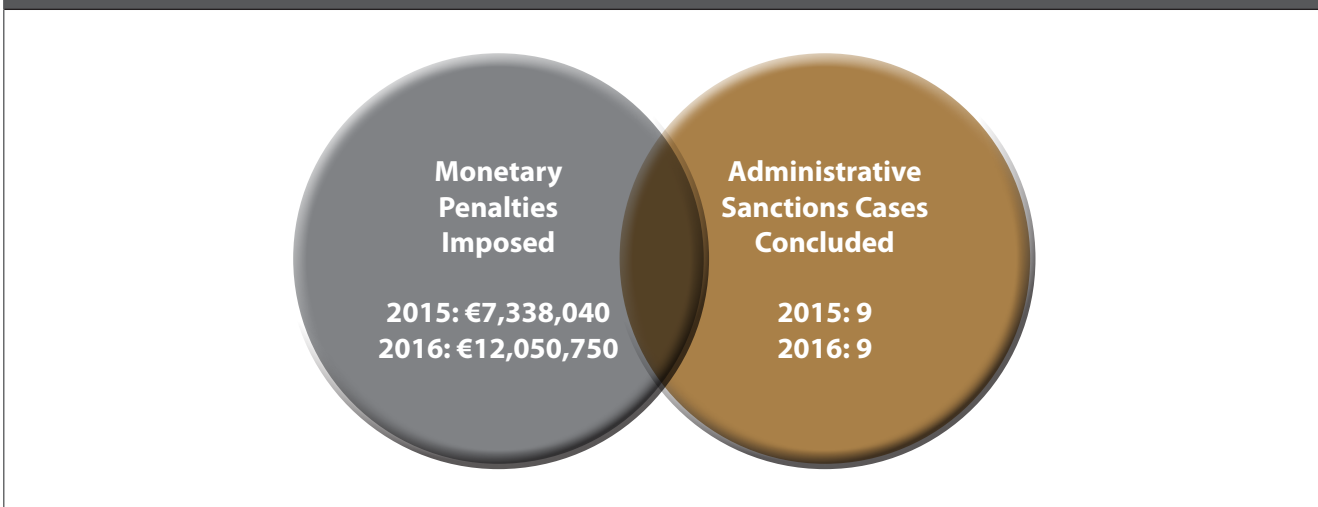


²⁹ Low Impact firms include payment institutions, retail intermediaries, moneylenders, credit servicing firms, debt management firms, e-money firms and bureaux de change firms.

Chart 5.7: AML/CFT/FS Inspections 2016

5.2.2 Regulatory Actions

Where a financial service provider fails to comply with their regulatory requirements, enforcement is an important tool to affect deterrence, achieve compliance and promote the behaviours expected.

Chart 5.8: Enforcement Actions

Markets Supervision

The Bank is responsible for the monitoring and supervision of the primary and secondary markets in Ireland. In this regard it is responsible for (i) monitoring compliance by market participants with the Market Abuse Directive; (ii) approving prospectuses issued under the Prospectus Directive; (iii) monitoring Transaction Reporting under MiFID; and (iv) reviewing company disclosures under the Transparency Directive.

Chart 5.9: Monitoring Compliance of Market Participants against Market Abuse Directive

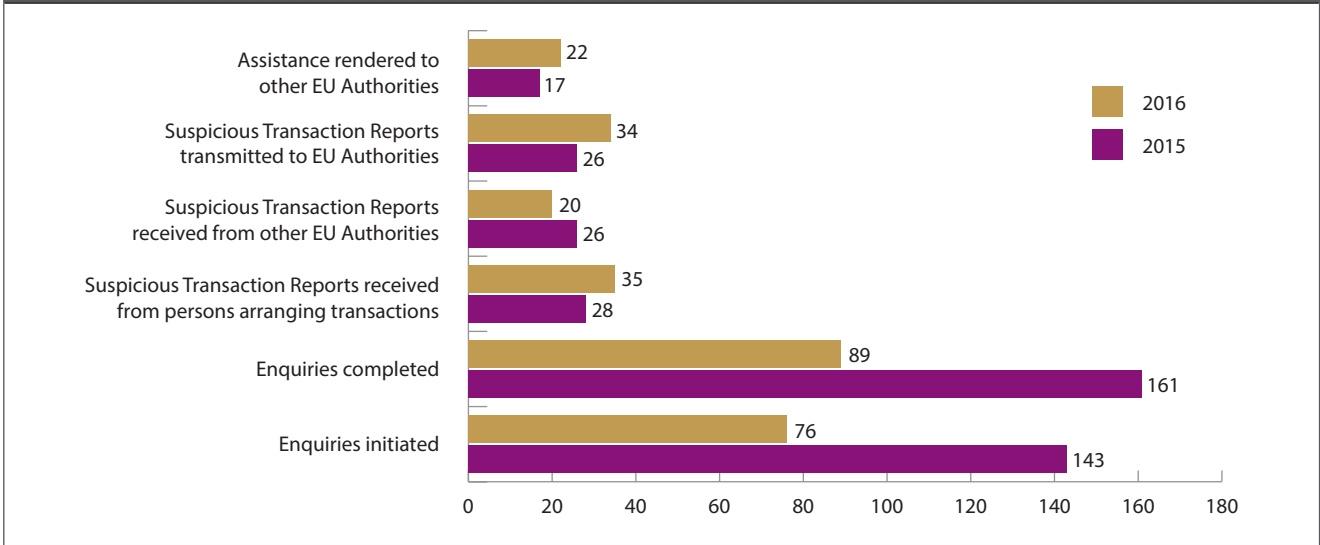


Chart 5.10: Approving Prospectuses issued under the Prospectus Directive

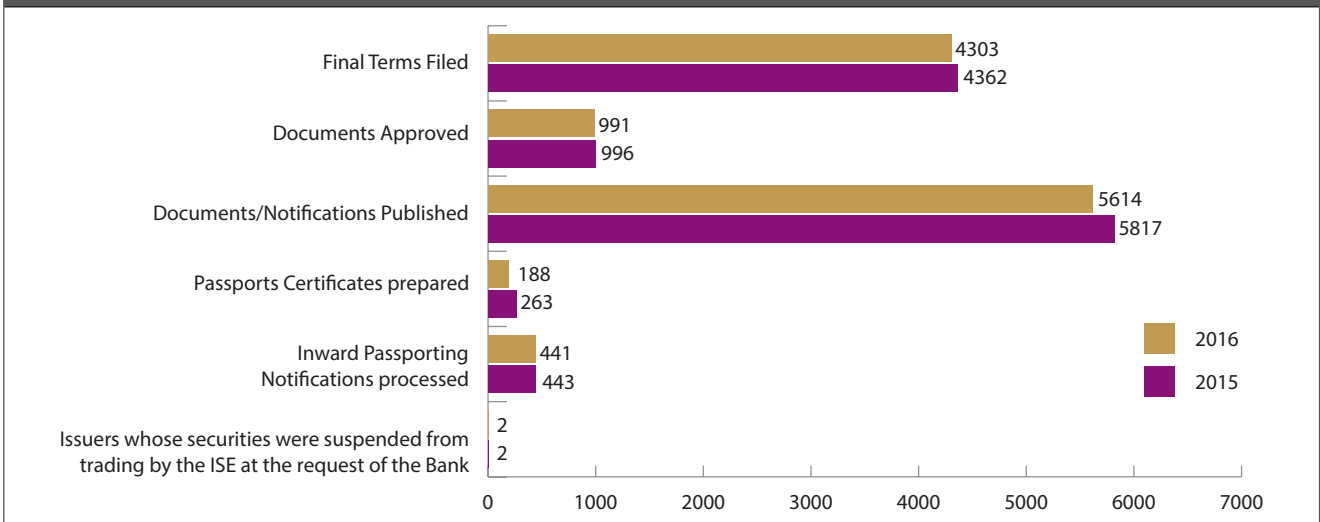
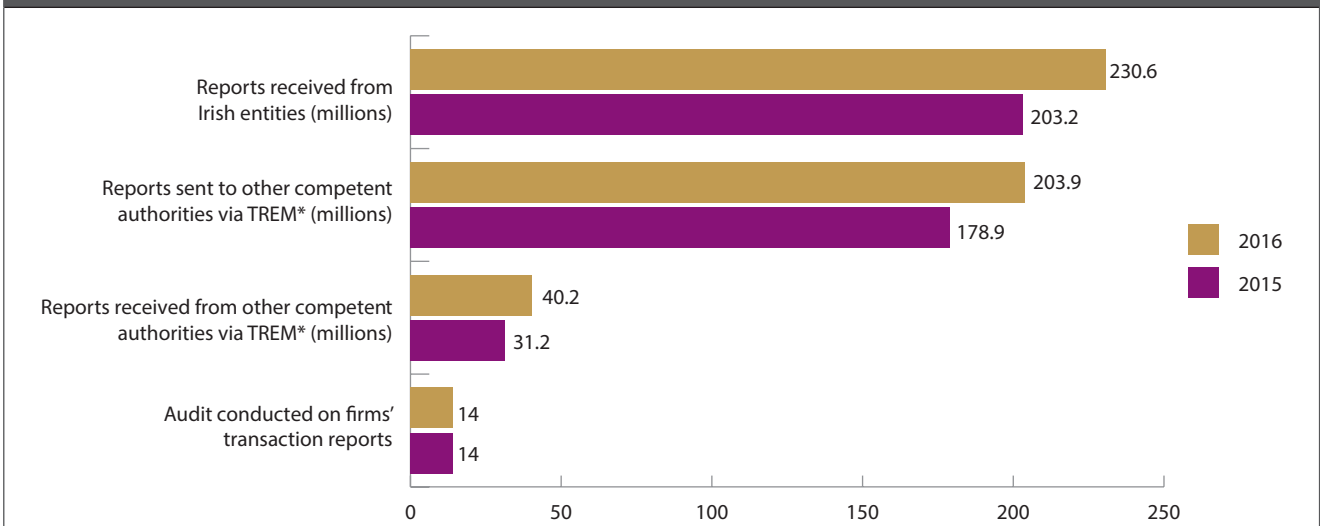


Chart 5.11: Monitoring Transaction Reporting Under MiFID



*Transaction Reporting Exchange

Chart 5.12: Reviewing Company Disclosures under the Transparency Directive



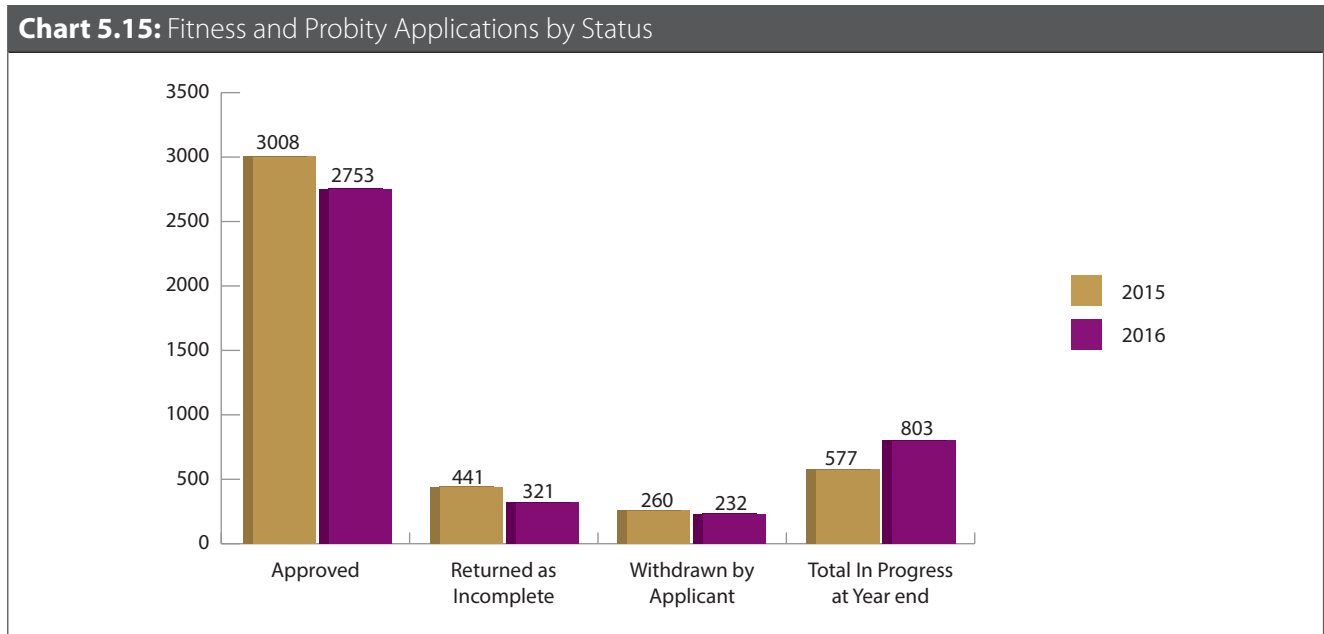
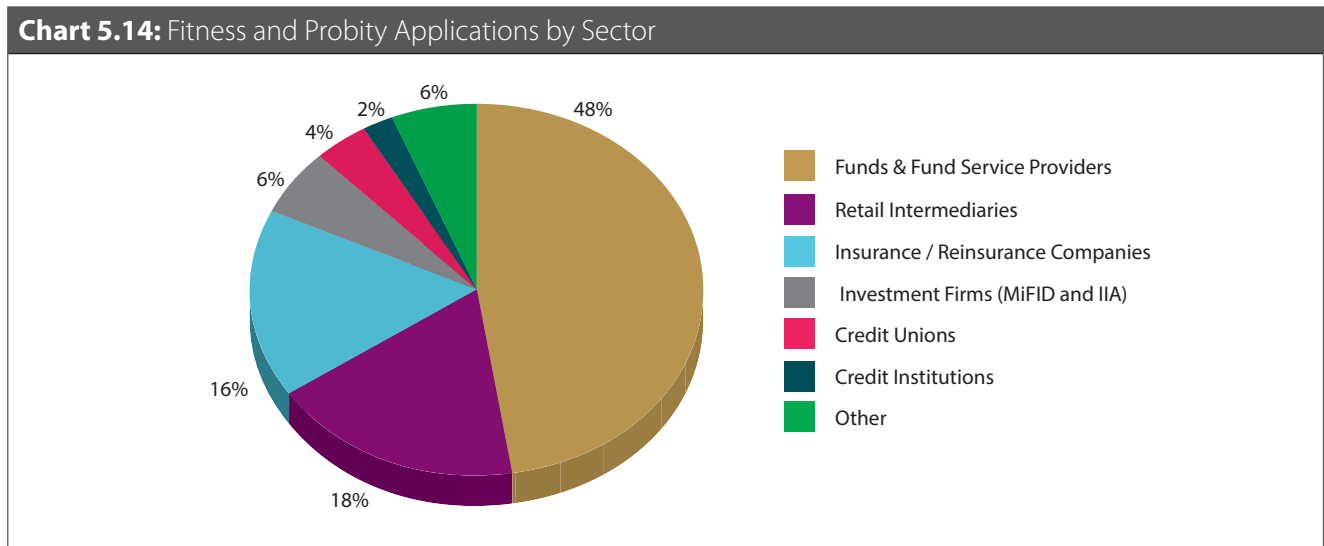
Chart 5.13: Online Reporting by Sector



5.3 Performance Metrics

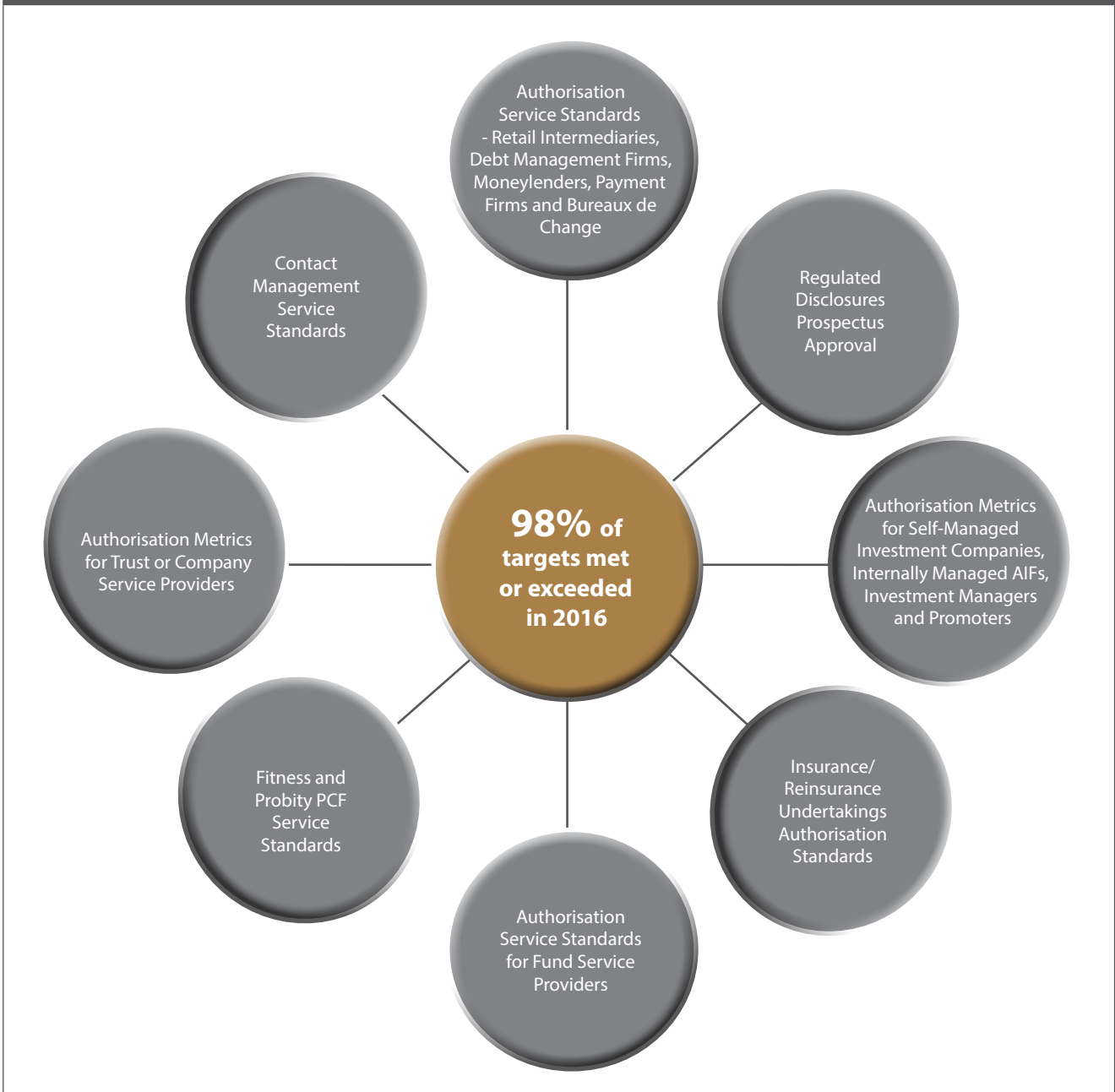
5.3.1 Fitness and Probity

The Bank’s mandate to deliver proper and effective regulation of financial institutions and markets is effected through a range of tools, one of which involves the assessment of applications for approval of persons under the fitness and probity standards. Charts 5.13 and 5.14 below set out the volume of applications by sector and by status. In 2016, when compared with 2015, there was a reduction in the number of applications both returned as incomplete (27%) and withdrawn by the applicant (11%).



5.3.2 Performance against Targets

Chart 5.16: Overall Performance against Targets



Authorisation of Investment Funds, Financial Service Providers and the processing of Fitness and Probity PCF Individual Questionnaire (IQ) applications is a significant operational activity of the Bank. The Bank is committed to providing a clear, open and transparent authorisation process while ensuring a rigorous assessment of the applicable regulatory standards. On a biannual basis, the Bank publishes its performance against Service Standards that it has committed to in respect of (a) authorisation of FSPs and Investment Funds, (b) processing of PCF IQ applications and (c) contact management. The service standards were met or exceeded for 98% of the targets for which applications were received.

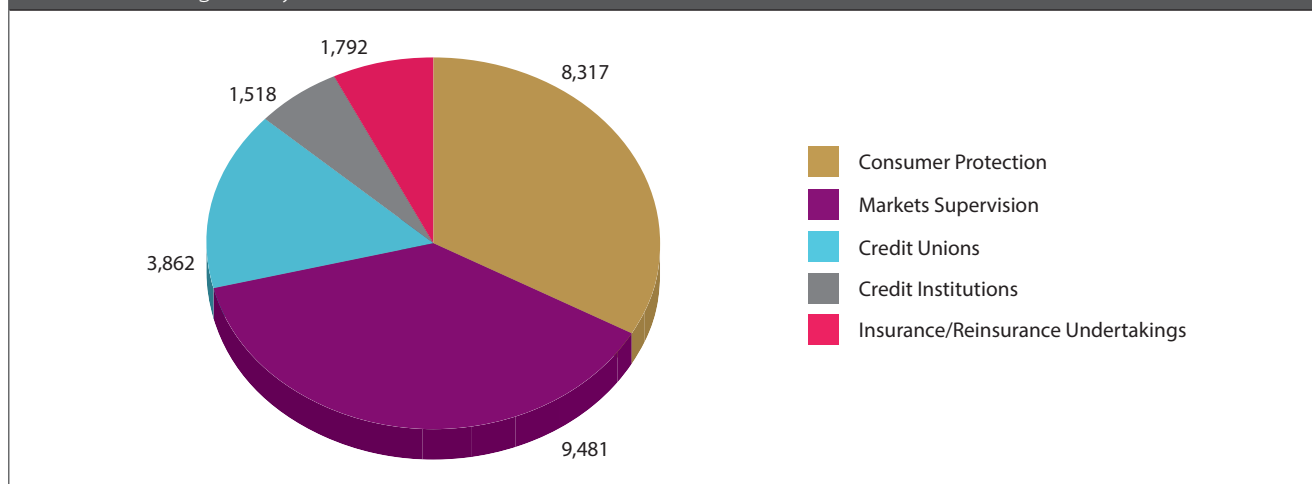
The Service Standards for Retail Intermediaries, Debt Management Firms, Moneylenders, Retail Credit Firms, Home Reversion Firms, Payment Firms and Bureaux de Change were amended midway through 2016 so that

they align with the new authorisation processes for these sectors and aim to ensure a clear, straightforward and facilitative process. Links to the service standards reports are below:

- [Service Standards for H1 2016](#)
- [Service Standards for H2 2016](#)

The new service for managing queries from Regulated Financial Service Providers (RFSPs) was enhanced in April 2016. The Contact Centre phone query service was extended to include e-mail and online queries. In addition, new Services Standards for the Contact Centre were introduced in July 2016 and are reported on biannually. A caller satisfaction survey was conducted in November 2016, with 93% of callers either satisfied or very satisfied with the service.

Chart 5.17: Regulatory Queries Dealt with in 2016



Chapter 6: Achievement of the Strategic Responsibilities of the Bank

The Central Bank Acts, 1942-2013, which set out the Bank's statutory objectives, also specify the framework for the Bank's Strategic Plan, including the planned objectives, the nature of activities undertaken, achievement of objectives and the means to measure the Bank's performance. The structure of the 2016-2018 Strategic Plan differs from the previous Strategic Plan 2013-2015. For that reason this chapter is presented in a different way to last year's Annual Performance Statement to align closer to the Priorities and Strategic Responsibilities within the Bank's current Strategic Plan.

The Bank's Strategic Plan 2016-2018 Framework, as illustrated below, demonstrates the independencies between the achievement of the Bank's mission and vision, and the achievement of the desired outcomes we have specified for its Strategic Enablers and Strategic Responsibilities.



Supplementing the outcomes detailed by each Directorate in **Chapter 3**, this chapter provides a summary of Bank-wide outputs and results that were achieved in 2016 in relation to the four Financial Regulation strategic responsibilities set out above; specifically:

- Consumer Protection;
- Supervision and Enforcement;
- Regulatory Policy Development; and
- Recovery and Resolution³⁰.

³⁰ Notably under the Strategic responsibility, Recovery and Resolution, significant aspects to this responsibility lie with the Central Banking pillar, namely where the Bank acts as the National Resolution Authority and Macroprudential Authority under the BRRD.

Strategic Responsibility



Desired outcome: Regulated firms act in the best interests of consumers

As regulator of financial service providers and markets, the Bank must ensure that consumer interests are protected. The Bank's mission of "getting it right for consumers" is delivered through the "5Cs Framework"; consumer, confidence, compliance, challenge and culture. This framework encourages regulated firms to deliver consumer-focused outcomes.

Key actions and activities undertaken in 2016 to achieve this desired outcome:

The Bank prioritised the themes set out in the CPOR under the 5Cs Framework by:

1. Working to develop a positive consumer-focused culture within regulated firms;
2. Ensuring the consumer protection framework remains effective by reviewing, developing and enhancing the protections in place and by influencing and shaping European and international developments; and
3. Monitoring and enforcing compliance with the required standards through themed reviews and inspections.

Consumer

- The Bank continued to increase its level of involvement at consumer protection committees at the EBA, EIOPA, ESMA and the Joint Committee, while also continuing to provide technical support to the Department of Finance on the negotiation and transposition of EU legislation into Irish law. This included the transposition of the Mortgage Credit Directive (MCD) and the Payment Accounts Directive (PAD), the related implementation into authorisation processes and consequent changes to Bank Codes.
- The Bank contributed to the work of FinCoNet, the international organisation of financial consumer protection supervisory authorities, through chairing the organisation and developing guidance to supervisors on standards in relation to sales incentives and responsible lending in 2016.
- Following a review of the existing protections for SMEs, new regulations came into effect³¹ which enhanced the protections for SMEs when dealing with lenders. In order to help SMEs understand the protections available, the Bank published a short Guide for micro and small enterprises and guarantors, and has been working with stakeholders representing SMEs to promote greater awareness of the protections in place.
- The Bank introduced, by amending the Consumer Protection Code 2012, a number of increased protections for variable rate mortgage holders, enhancing transparency for those borrowers on the variable nature of their rate and providing more information on other products.

³¹ Effective 1 July 2016 for all lending institutions except credit unions where they came into force on 1 January 2017.

- Three Consumer Protection Bulletins were published in 2016. They covered personal lending, the Code of Conduct on Mortgage Arrears and current account switching.
- In order to inform the Bank's policy and supervision work, a number of consumer research projects were undertaken: the results of consumer research into health insurance renewals (March 2016), complaints handling by regulated firms (May 2016) and consumer experience of motor insurance damage claims (February 2017) were published.

Culture

- The Bank continued to challenge boards and senior management of firms to demonstrate how they are managing risks and delivering the right outcomes for their customers. In 2016, 11 meetings were held with CEOs and/or Boards of banks/insurers/investment firms to discuss current and emerging consumer risks and culture. The Bank also re-iterated an assessment of current and emerging risks to its consumer protection objectives in a number of external speaking events throughout the year.
- The Bank developed its Consumer Protection Risk Assessment (CPRA) supervisory model during 2016 which will allow for better testing and monitoring of firms' progress in embedding fit-for-purpose consumer protection risk management frameworks. The CPRA model was tested in specific areas (including governance and culture) in six firms.
- The Bank reviewed the internal audit reports received from firms based on their implementation of the 2014 Guidelines on Variable Remuneration Arrangements for Sales Staff. The Bank will continue to engage with firms on this issue.

Confidence

- See **Chapter 3.1** for information on the ongoing Tracker Mortgage Examination.
- The Bank pursued to resolution all of the issues identified as part of the comprehensive themed review in 2015 of how lenders are delivering on the important consumer protections prescribed by the statutory Code of Conduct on Mortgage Arrears for borrowers in arrears and pre-arrears.
- In July 2016, the Bank published a discussion paper on the risks and benefits of the practice of product producers paying commission to intermediaries for selling their products.
- Systems failures and errors have and will continue to be monitored to ensure that firms are delivering on their obligations to guarantee that consumers are kept fully informed of arising issues and that any impact on the consumer is dealt with in a timely and appropriate way.

Challenge

- During 2016, the Bank commenced reviewing applications from Credit Servicing Firms (CSF). This has included the assessment of those firms against the detailed Authorisation Requirements and Standards introduced by the Bank on foot of the legislation. During 2017, these applications will be progressed to decision stage, i.e., either authorisation or refusal.
- New Authorisation Process Models for a number of industry sectors were rolled out in Q1 2016. This followed the introduction of enhanced authorisation process models for Payment Institutions and Electronic Money Institutions in October 2015. New internal tracking and reporting mechanisms were also introduced to track applications' performance against the new authorisation process models' targets on an ongoing basis.

Compliance

- A thematic inspection of high risk investment products (structured retail products) was completed and the findings were published on 1 September 2016.
- The findings of a thematic inspection into how health insurers handle the annual renewal process were published in March 2016 together with the results of supporting consumer research. The inspection focused on how providers were engaging with and/or advising their consumers.
- A themed inspection of motor insurance providers, focusing on the handling of motor damage claims was completed, with the inspection and consumer research findings published in February 2017.
- A significant thematic inspection continued throughout 2016 to target retail intermediaries that were not meeting the minimum standards in terms of complying with reporting and other obligations to the Bank. The Bank's objective was to target a culture of non-compliance, which can often signal other issues in those firms, which can impact negatively on consumers. As of 31 December 2016, of the original 325 firms in-scope of this inspection, 297 of these firms had either submitted their annual returns or revoked their authorisation.

Strategic Responsibility

Supervision and Enforcement

Desired outcome: Regulated firms are financially sound and safely managed

Regulation of financial institutions and markets is undertaken using assertive risk-based supervision, which is underpinned by credible enforcement deterrents. This mandate is delivered through a range of tools which include:

- Supervisory assessments of individual firms according to the engagement cycles set out under PRISM;
- Monitoring of regulatory returns filed with the Bank;
- Reactive supervisory work on foot of triggers including regulatory returns, market intelligence and whistleblowing complaints;
- Approval of persons under the F&P standards;
- Processing of requests for authorisation and acquiring transactions;
- Supervising banks within the SSM framework; and
- Enforcement actions.

The Bank, at all times, aims to take a proportionate approach to its actions as an intrusive and assertive regulator. Importantly, the Bank does not strive to ensure a 'zero-failure' system of regulation and supervision, but seeks to ensure that where a firm fails, this happens in a way that avoids significant disruption to financial services or consumers.

Key actions and activities undertaken in 2016 to achieve this desired outcome:

Enhancing supervisory engagement, processes and tools in light of new powers, new mandates and upgraded international standards and use enforcement powers effectively to achieve credible deterrence.

Enhancing Supervisory Engagement, Processes and Tools

- The Bank completed a review of macroprudential measures. This resulted in a slight recalibration, with the Bank committed to monitoring compliance with the regulation, as well as the evolution of mortgage market lending standards;
- Significant support for the SSM NPL Task Force was provided by the Bank with NPL guidance issued for consultation in 2016. This was complemented with robust on and off-site engagement with credit institutions in relation to distressed portfolios;
- The Bank commissioned the external auditors of credit institutions and insurance companies to conduct auditor assurance work under the powers of the Central Bank (Supervision and Enforcement) Act, 2013;
- An enhanced supervisory engagement model was implemented for credit unions and a risk-based approach to AML supervision has been adopted in line with international best practice and standards;

- Further development of the Banks' analytics capability across a number of Directorates in 2016. Enhanced engagement with supervisory teams is positively impacting the quality of supervisory processes such that supervisors can better and more efficiently utilise data to generate resource efficient supervisory outcomes;
- The Bank carried out stress testing of Irish money market funds which fed directly into the asset management portion of the IMFs final FSAP report. Arising from this work was the first ever collection of daily redemption data from Irish investment funds which will form the basis of joint research with the IMF on investment fund liquidity analysis;
- A sector stress test on the financial position of credit unions was completed in 2016 and results were presented to the Bank's FSC. The work included projecting credit losses, investment returns and capital shortfalls over a three-year horizon. Follow-up actions based on the projections are planned for 2017;
- A significant level of restructuring and consolidation activity occurred during 2016 within the Credit Union sector. In this regard the Registry has worked closely with the Credit Union Restructuring Board (ReBo) and individual credit unions with a continued focus on adequate risk management and delivery of business improvement. A dedicated unit has also been created with the Registry whose primary focus is to drive initiatives for the sector; and
- Material progress on improving the quality and efficiency of the investment fund authorisation process has been delivered through the use of online applications and automated workflows.

Using Enforcement Powers Effectively

The Bank has continued to commit resources to robust investigations of firms and individuals, seeking to hold them to account where their behaviour does not meet the required standards:

- Following the conduct of enforcement investigations, the Bank, under its ASP, referred cases in respect of certain persons concerned in the management of both the INBS and QIL to Inquiry in 2015. Following the referral of these cases to Inquiry a number of legal challenges were instituted by certain persons concerned in the management of these entities and during 2016, the Bank successfully defended a number of legal challenges brought before the High Court.
- The Bank continued to play an active role in networks and working groups to share knowledge and experience across the SSM, including:
 - » The Network of Enforcement and Sanctions Experts, which provides a forum for communication, collaboration and cooperation within the SSM in relation to enforcement and sanctions. The Bank has been active in sharing its knowledge and experience with the Network and also seeks to influence the direction of enforcement policy through the Network.
 - » The SSM Fitness & Probity (F&P) working group, which comprises representatives of the ECB and National Competent Authorities (NCAs) and works to develop policy stances to ensure a higher level of harmonisation of F&P assessments across the SSM.

More information on the 2016 key outcomes are detailed under **Chapter 3.7**.

Implementing the Solvency II regulatory framework for Insurance Undertakings.

Since 1 January 2016, insurers in Ireland have operated under a new EU regulatory regime - Solvency II. A key focus of the Bank in 2016 was to ensure that the new regime was embedded effectively, both within the Bank and in regulated insurance firms.

The most significant changes within the Insurance Directorate have been centred on the introduction of a revised engagement model, dedicated analytics team, increased on-site supervisory capability and the introduction of the F&P process.

As part of its work to support embedding Solvency II the Bank:

- Prioritised early feedback on areas such as systems of governance, capital management and regulatory capital calculations, with robust assessment of new control function holders under Solvency II;
- Issued a number of policy papers on topics such as outsourcing arrangements, look-through of Collective Investment Undertakings (CIUs) reporting and directors' certification;
- Introduced additional measures to maintain key aspects of the domestic supervisory regime which the Bank considered an essential complement to the Solvency II regime. These included guidance on the domestic actuarial regime and revised directors' certifications requirements together with the introduction of external audit of key Solvency II regulatory returns.

The Bank initiated a proportionate, bespoke engagement model for less complex insurance companies which results in increased levels of supervision under Solvency II and brings the engagement model for these companies in line with international standards. This model resulted in a combination of proactive supervisory activities, including a thematic inspection focused on governance, risk management and internal control frameworks. Further refinement and embedding is required in 2017, with the Bank actively engaged in identifying key trends and issues in the insurance industry and the wider regulatory environment.

Extending on-site inspection activities to further sectors of the industry.

On-site inspection activities represented a core supervisory activity in 2016 across sectors of the financial services industry. Such activities comprised thematic reviews and intrusive on-site inspections.

Thematic Reviews Focus 2016

- Credit institutions – regulatory reporting and IT Risk;
- Credit Unions – outsourced activities and F&P due diligence requirements;
- Insurance undertakings – governance and oversight of private motor pricing;
- Asset management - depositary oversight, sub-fund governance, risk function oversight, outsourcing arrangements, conflicts of interest and client reporting;
- Markets - use of the risk management process by UCITS and investment fund fees.

On-site Inspections Focus 2016

- Credit institutions – credit risk; capital; liquidity risk; operational risk; IT risk; governance; and business model analysis;
- Insurance undertakings – reserving; claims management; and underwriting discipline;
- Markets - depositary oversight of investment funds;
- AML/CFT/FS inspections across a broad range of sectors including: payment institutions, bureaux de change, credit unions, investment firms, banks and funds.

Strategic Responsibility



Desired outcome: Regulatory frameworks are appropriate and effective

A high quality and effective regulatory framework is essential in requiring financial firms to operate to high standards. It provides the basis for supervising and enforcing the key principles of organisational and financial soundness, consumer protection, and effectively functioning markets.

The Bank engages actively in the European regulatory policy process, contributing to the development of sound rules and supporting the work to transpose those rules into Irish law.

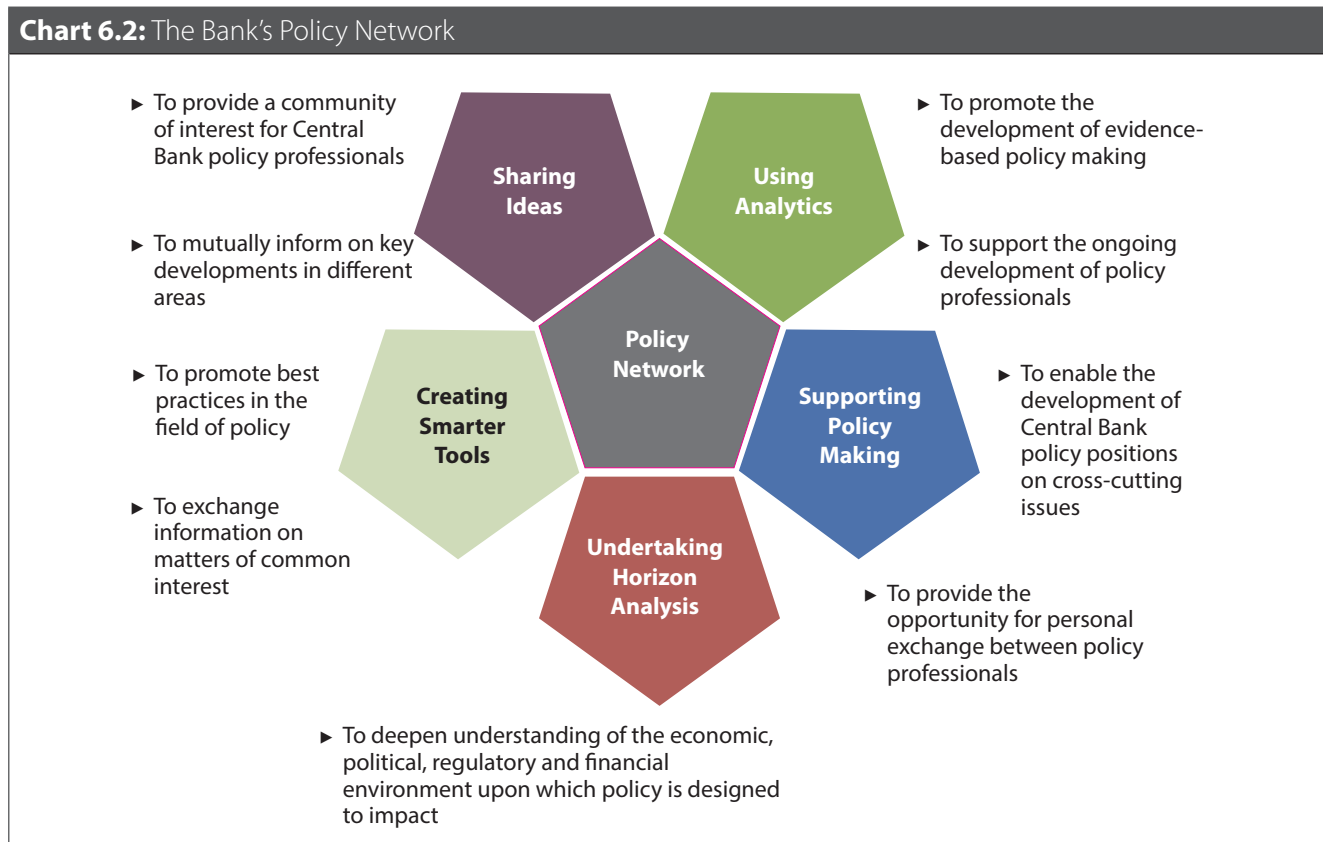
The Bank ensures that the rules and regulations are maintained and implemented in such a way that their spirit and purpose is achieved on an ongoing basis, having regard to the changing environment and new activities and products developed by financial firms and markets.

Key actions and activities undertaken in 2016 to achieve this desired outcome:

Actively contributing to the development of relevant laws, regulations and technical standards in Europe and provide the necessary guidance for regulated firms and markets in Ireland

- The Bank continued to support the work of the SSM by participating in a number of working groups to develop a range of aspects of the SSM methodology, support the work on NPLs and SSM TRIM initiative - a multi-year review of Pillar I internal models used for purposes of regulatory capital estimation of credit institutions;
- In terms of IT risk, the Bank contributes to IT Expert groups at both the EBA and the ECB/SSM. Output included the development of guidelines on the assessment of IT risk in the context of the SREP and cyber-risk inspection methodologies for use across all SSM banks. For regulated firms in Ireland, the Bank published IT and cyber risk cross industry guidance in September 2016;
- The Bank has been actively engaged in the development of EBA Reports, guidelines and technical standards (e.g. leverage ratio, liquidity, securitisation and covered bonds, large exposures, credit risk management) and in the impact assessment of IFRS 9;
- The Bank continued to influence the international policy agenda on securities and markets issues through participation on the NCA prospectus peer review, contributing to work on Prospectus Directive III, ESMA initiatives, Transparency Regulations amendments and ESMA Guidelines;
- In terms of AML/CFT policy:
 - » At the national level in 2016 the Bank contributed to the National Risk Assessment on Money Laundering and provided technical assistance to government departments on the transposition of the Fourth Anti-Money Laundering Directive (AMLD IV);
 - » At the international level, the Bank has been an active contributor at the ESAs and FATF.

Providing and maintaining the policy framework to support effective supervision of regulated firms and markets.



- On 1 January 2016, the remaining sections of the 2012 Credit Union and Cooperation with Overseas Regulators Act and Regulations commenced. The Credit Union Handbook was updated in 2016 to reflect the revised Guidance for the new sections of the Act and Regulations;
- Following the introduction of the cap on savings over €100,000, as provided for in the Credit Union Act 1997 (Regulatory Requirements) Regulations 2016, an application process was developed to facilitate credit unions in seeking approvals;
- The Bank ensured the smooth implementation of new legislative requirements by successfully implementing UCITS V requirements;
- Considerable work was carried out in 2016 in relation to preparation for implementation of MiFID II in January 2018 and ensuring firms and funds have appropriate structures and controls in place. For further information on this see *"Preparation for MiFID II Implementation"*, 3.4 Asset Management Supervision;
- Throughout the year the Bank had extensive and ongoing interaction with the Department of Finance, e.g., in relation to the transposition of key European legislation and a review to examine a number of issues across the non-life insurance sector;
 - » Following the publication of the new European Union (Market Abuse) Regulations 2016³² by the Department in 2016, the Bank published its revised Market Abuse Rules and Guidance.
- In July and November respectively, the Bank published Feedback Statements in relation to Consultation Paper (CP 100) and Consultation Paper (CP 97) on Central Bank Investment Firms Regulations. These Regulations consolidate the conditions and requirements which the Bank imposes on certain investment firms.

32 Published by ESMA on 29 April 2016.

During 2016 the Bank actively participated in the work of the ESAs as follows:

EIOPA:

- Consultation Paper on the SCR designed to inform EIOPAs work on reviewing the SCR and advising the EU Commission;
- EU-wide stress test of insurance undertakings which covered 236 firms and delivered a snapshot assessment of vulnerabilities and resilience to severe market developments;
- Report on Long Term Guarantee and Measures on Equity Risk which was the first in a series until 2021 of similar reports to assess the impact on insurers of certain measures in Solvency II, including the volatility adjustment and the matching adjustment; and
- Advice to the EU Commission to enhance the asset class for high quality infrastructure investments under Solvency II by extending the asset class which could benefit from the differentiated treatment.

EBA:

- Discussion Paper on the Prudential Regime for Investment Firms exploring options for a more proportionate regulatory regime for various categories of investment firms;
- Consultation Paper as a precursor to the development of Guidelines on Accounting for Expected Credit Loss which will inform the implementation of IFRS 9;
- Impact Assessment on the potential interaction between IFRS 9 and prudential regulatory requirements;
- Report on the Leverage Ratio calibration recommending the introduction of a Leverage Ratio minimum requirement in the EU to mitigate the risk of excessive leverage;
- EU-wide stress test covering 51 European credit institutions designed to support ongoing supervisory efforts to maintain the process of repair of the EU banking sector;
- Guidelines on remuneration policies and practices related to retail banking products and services aimed at reducing conduct risk and mis-selling; and
- Guidelines specifying the definition of default across the EU and an RTS on the materiality threshold of past due credit obligations aimed at improving consistency and comparability of capital requirements.

ESMA:

- An opinion to NCAs in relation to UCITS Share Classes; UCITS Remuneration Guidelines; ESMA advice in relation to the AIFMD Third Country Passport; and an Opinion on Loan Origination for the European Commission all delivered from the IMSC, which the Deputy Governor (Financial Regulation) chairs;
- The IMSC also developed RTS on European Long-Term Investment Fund Legislation and ESMA also delivered advice to the European Commission on the depositary frameworks of non-EU jurisdictions in the context of the AIFMD;
- Drafting of further Implementing Technical Standards (ITS) and RTS on the MiFIR/MiFID II, for example the RTS on packaged orders;
- Development of technical standards under the EMIR, including the bilateral exchange of margin between parties, the indirect clearing provisions which arise under EMIR for over-the-counter derivatives, and under MiFID II for exchange traded derivatives; and
- The publication of the first EU-wide stress tests of Central Counterparties³³.

³³ Published by ESMA on 29 April 2016.

Strategic Responsibility



Desired outcome: Frameworks are in place to ensure failed or failing regulated firms go through orderly resolution

One of the key lessons from the financial crisis was the absence of a robust framework to deal with the failure of financial institutions without recourse to the taxpayer. The EU policy response was to implement a single rulebook to deal with failed or failing firms, the BRRD.

The Bank acts as Ireland's NCA, National Resolution Authority and Macroprudential Authority under the BRRD. This requires us to ensure that:

- Banks and investment firms, within scope, prepare recovery plans which set down the measures they would adopt in the event of their financial deterioration;
- Feasible and credible resolution plans are put in place by the Bank for those firms requiring:
 - » A preferred resolution strategy to be determined;
 - » A resolvability assessment to be conducted examining the impediments to the preferred strategy; and
 - » A resolution plan to be documented.

The Bank works in close cooperation with the Single Resolution Board, which assumed responsibility, from 1 January 2016, for resolution matters concerning the significant and cross-border institutions.

Key actions and activities undertaken in 2016 to achieve this desired outcome:

The Bank continues to implement all aspects of the BRRD and embed the recovery and resolution planning regime domestically

- During 2016, the Bank conducted assessments to evaluate bank recovery plans against EBA and SSM guidelines and criteria, together with recovery plans relevant for investment firms;
- As part of this work, the Bank engaged to ensure risk management frameworks include effective, embedded recovery plans, requiring retail and international banks (SIs and LSIs) and investment firms to remediate any issues identified as a result of an assessment to ensure compliance with all aspects of the regulations;
- In terms of resolution planning the Bank has been engaged in the development of executable resolution plans for the SIs and, in the case of LSIs, in ensuring that clear resolution strategies are agreed and are being progressed in line with supervisory and resolution priorities;
- The Asset Management Supervision Directorate worked closely with the Bank's Resolution Division to review the recovery plans relevant for asset management firms. This was a new role for the directorate involving extensive engagement and training by the supervisory practices and regulation team, to familiarise supervisors with the legislation and allow an informed review and interrogation of recovery plans. Procedures and checklists were implemented to ensure compliance with all aspects of the

regulations and enable peer comparison of the recovery plans submitted. Of 11 plans submitted by firms deemed in scope, four were materially deficient, requiring redrafting and resubmission by end- November 2017. The remaining seven firms submitted plans which were deemed sufficient, but these firms were given additional feedback on how future plans could be improved.

Fulfil Single Resolution Mechanism (SRM) responsibilities working closely with the SRB

The Bank has continued to fulfil its SRM responsibilities by participating in colleges for SIs.

Chapter 7: Internal Audit

The objective of Internal Audit is to act as the independent 'third line of defence' within the Bank's governance framework. It is the responsibility of the Bank's operational management to establish appropriate systems of internal controls. Thus, operational management acts as the first line of defence. The risk management, control, compliance and oversight functions established and deployed by management represent the second line of defence. Internal Audit provides independent, objective assurance and consulting activities designed to add value and to improve the performance of the Bank's tasks and activities. In doing so, it assists the Bank in accomplishing its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

During 2016, Internal Audit conducted audits across a number of financial regulatory areas including: the Authorisation and Revocation Delegations Framework; inspections in the Insurance Supervision Directorate; inspections in the Consumer Protection Directorate and the AML Supervisory Framework and Inspection Model. All issues identified are routinely followed up by the Internal Audit division to ensure that approved action plans are implemented.

As part of its information gathering and to ensure that Internal Audit keeps abreast of developments and risks within the organisation, Internal Audit regularly attended a number of executive committee meetings and also held meetings with a large number of divisions across the organisation.

Internal Audit submitted regular reports to the Audit Committee on the outcome of all audits including progress in implementing recommendations from previous audits. A three-year plan is prepared on a rolling basis which is approved by the Audit Committee annually.

The Internal Audit Committee (IAC) is the internal audit function for the SSM. One of the responsibilities of the IAC is to conduct audit assurance work as stipulated by the audit plan and as a result, the Bank participated in the SSM audit of Information Management in 2016, and is participating in the audit of ongoing supervision – planning and monitoring in 2017.

Chapter 8: International Peer Review

8.1 IMF FSAP

During 2016 the Bank participated in the IMF FSAP. This is a comprehensive and in-depth analysis of a country's financial sector to gauge the stability of the sector and to assess its potential contribution to growth and development, and is a mandatory part of Article IV surveillance³⁴. The FSAP involves an assessment of a country's financial sector in the following areas:

- The resilience of the financial sector (risk and vulnerabilities assessment);
- The quality of the regulatory and supervisory framework; and
- The capacity to manage and resolve financial crises.

The IMF has identified 29 jurisdictions with systemically important financial sectors, including Ireland, that are required to undergo financial stability assessments under the FSAP every five years. The FSAP was set as a priority for the Bank for 2016, as it is the first FSAP since the financial crisis³⁵ and is a public examination of the current situation in the Irish financial sector and the competency of the Bank in delivering on its financial stability and supervisory mandates. The FSAP, which commenced in September 2015, was a substantial and complex project which involved resources and input from most of the divisions in the Bank, as well as input from, and coordination with, other Irish and European authorities.

The IMF FSAP culminated in the publication in July 2016 of the FSSA for Ireland, followed in September 2016 by publication of technical notes on the following areas:

- Macroprudential Policy Framework;
- Stressing the banking system;
- Non-bank sector stability analyses;
- Insurance sector and update on the assessment of observance of the Insurance Core Principles;
- Banking Supervision and update on the assessment of observance of the Basel Core Principles;
- Asset management and financial stability;
- Update on the assessment of implementation of the IOSCO objectives and principles of securities regulation; and,
- Financial safety net, bank resolution, and Crisis Management Framework.

The assessment found that the Irish financial system has strengthened significantly since the financial crisis and has undergone major structural changes. While recognising the considerable progress that has been made, the IMF noted that vulnerabilities remain, including those related to highly indebted households and smaller domestic firms, and the likely negative effects on the Irish financial system of the UK vote to leave the EU. The global scale of the international funds industry in Ireland was also noted, with recommendations that the Bank continue the innovation, collaboration with other agencies, and monitoring already established in this area.

The Bank welcomed the recognition by the IMF of the progress made since the financial crisis and the recommendations made, in particular those that support the Bank's previous actions and current priorities, including the recommendations to:

³⁴ Country surveillance is an ongoing process that culminates in regular (usually annual) comprehensive consultations with individual member countries, with discussions in between as needed. The consultations are known as "Article IV consultations" because they are required by Article IV of the IMF's Articles of Agreement.

³⁵ The last FSAP for Ireland was conducted in 2006.

- Maintain, and in due course review LTV and LTI limits;
- Transform LTI limits into more comprehensive debt-to-income limits once the Central Credit Register is operational;
- Close data gaps on cross-border and inter-sectoral exposures, the non-financial corporate sector, and the CRE market; and
- Further develop stress test capability.

8.2 FATF

The FATF is an intergovernmental agency that sets the international standard for combating money laundering and the financing of terrorism and proliferation of weapons of mass destruction. FATF regularly monitors the progress of its members (Ireland has been a member since 1991) in implementing its recommendations through the MER process.

The last MER of Ireland was carried out by FATF in its third round of mutual evaluations in 2006. Ireland received partially compliant ratings for certain core and key recommendations and was placed into the regular follow-up process. FATF removed Ireland from the follow-up process in June 2013 based on its 11th follow-up report, which acknowledged the country's significant progress in addressing the deficiencies identified in the 2006 MER.

As part of the fourth round of evaluations, FATF is, for the first time, assessing the effectiveness of national AML/CFT systems. This is an assessment of the adequacy of the implementation of FATF recommendations and will identify the extent to which Ireland achieves a defined set of 11 immediate outcomes that, according to FATF methodology, are central to an effective AML/CFT system.

The on-site element of FATF's fourth round evaluation of Ireland took place between 3-17 November 2016. During the on-site visit, FATF assessors met with a wide range of bodies including government departments, public agencies, representatives from the financial services sector as well as the non-financial services sector. The Bank met with FATF assessors as part of the review of a number of areas including immediate outcome 3 (supervision) and immediate outcome 4 (preventative measures).

A draft evaluation report was provided by FATF to Ireland in January 2017 for review and comment. Following a period of engagement between Ireland and FATF, the report will be finalised after the plenary session of FATF in June 2017, and then published by FATF. During 2017, the Bank will carefully consider any recommendations arising from the review.

8.3 ESMA Peer Reviews

- In December 2014, the ESMA BoS mandated the Supervisory Convergence Standing Committee (SCSC), to carry out a peer review regarding compliance with the MiFID suitability requirements. During 2015 and Q1 2016, the Bank participated in the assessment group for this peer review on the suitability of investment advice provided to retail clients. The review involved a desk based assessment of a suitability questionnaire completed by all NCAs followed by on-site visits to seven CAs. The Bank participated in two of the on-site reviews. The final suitability peer review report was published on 8 April 2016 and found that there was room to improve in relation to CA supervision of investment advice for retail clients.
- In 2016, the Bank was subject to a Peer Review by the ESMA on the prospectus approval process under the Prospectus Directive. The review was carried out by peer regulatory authorities with the overall findings published in June 2016. It found that the Bank has strong experience with debt securities, asset-backed securities and base prospectuses. It was also found that the Bank has efficient procedures, tools and practices in place which allow efficient use of resources and ensures a consistent prospectus review and approval process.

8.4 EIOPA Peer Review

EIOPA's review panel conducts regular peer reviews to enhance supervisory convergence within the European Economic Area.

In Q4 2016, the review panel launched a peer review on the application of the proportionality principle in governance requirements regarding key functions. The key objective is to assess how the proportionality principle is applied and identify best supervisory practices towards supervision of fit and proper requirements. On conclusion in 2017 the Bank will consider any necessary changes to supervisory processes.

Glossary

AML	Anti-Money Laundering Anti-money laundering refers to a set of procedures, laws or regulations designed to stop the practice of generating income through illegal actions.
ASP	Administrative Sanctions Procedure Where a concern arises that a prescribed contravention has been or is being committed, the Bank may investigate. The Administrative Sanctions Procedure provides that, any time before the conclusion of an Inquiry, the matter may be resolved by entering into a settlement agreement.
AIF	Alternative Investment Fund All investment funds that are not already covered by the European Directive on Undertakings for Collective Investment in Transferable Securities (UCITS). This includes hedge funds, funds of hedge funds, venture capital and private equity funds and real estate funds.
AIFMD	The Alternative Investment Fund Managers Directive 2011/61/EU An EU directive that looks to place hedge funds, private equity and any other alternative investment firms into a regulated framework in order to monitor and regulate their activity.
BoS	Board of Supervisors The Board of Supervisors is the main decision-making body. The main role of the Board of Supervisors is to take all policy decisions of the relevant Authority, such as adopting draft technical standards, guidelines, opinions and reports.
BRRD	The Bank Recovery and Resolution Directive This Directive establishes a common approach within the EU to the recovery and resolution of banks and investment firms.
CET1	Common Equity Tier The Tier 1 common capital ratio is a measurement of a bank's core equity capital compared with its total risk-weighted assets.
CF	Controlled Function Persons in senior positions within Regulated Financial Service Providers are known as Controlled Functions.
CFT	Countering the Financing of Terrorism Measures to be taken to prevent terrorist financing are set out in the Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 as amended by the Criminal Justice Act 2013. Credit and financial institutions are obliged to take measures to prevent the financing of terrorism such as carrying out customer due diligence, ongoing monitoring, reporting of suspicious transactions, training and having in place effective policies and procedures.
CIWG	Cost of Insurance Working Group The group was established by the Department of Finance in early 2016 to identify and examine the drivers of the cost of motor insurance and to recommend short, medium and longer term measures to address issues arising.
CJA 2010	The Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 (See CFT above)
CPOR	Consumer Protection Outlook Report The Bank publishes an annual CPOR which sets out in more detail its consumer protection objectives, current and emerging risks to those objectives, as well as a number of key themes to address those risks.

CPRA	Consumer Protection Risk Assessment This is a supervisory model introduced in 2016 which allows for better testing and monitoring of firms' progress in embedding fit-for-purpose consumer protection risk management frameworks.
CRE	Commercial Real Estate Commercial real estate is property that is used solely for business purposes and that is leased out to provide a workspace rather than a living space.
CRR	Capital Requirements Regulation The Capital Requirements Regulation (EU) No. 575/2013 is an EU law that aims to decrease the likelihood that banks go insolvent.
CSFs	Credit Servicing Firms Firms which service loans sold by regulated lenders to third parties.
CUAC	Credit Union Advisory Committee The Credit Union Advisory Committee was established under section 180 of the Credit Union Act 1997 and acts as an adviser to the Minister for Finance on matters relating to credit unions.
EBA	European Banking Authority The European Banking Authority is an independent EU Authority which works to ensure effective and consistent prudential regulation and supervision across the European banking sector.
ECB	European Central Bank The European Central Bank is the central bank of the 19 EU countries which have adopted the euro.
EIOPA	European Insurance and Occupational Pensions Authority EIOPA was established to support the stability of the financial system, transparency of markets and financial products as well as the protection of policyholders, pension scheme members and beneficiaries.
EMIR	The European Market Infrastructure Regulation EMIR is a body of European legislation for the regulation of over-the-counter derivatives. It established common rules for central counterparties and trade repositories.
ERR	EMIR Regulatory Return In order to fulfil its responsibilities under EMIR the Bank may require counterparties that are not exempt from the requirement to complete an EMIR Regulatory Return on an annual basis.
ESA	European Supervisory Authorities These Authorities work together in a network, interacting with the existing national supervisory authorities, in order to ensure the financial soundness of the financial institutions themselves and to protect users of financial services.
ESCB	European System of Central Banks The ESCB comprises the ECB and the national central banks (NCBs) of all EU Member States whether they have adopted the euro or not.
ESMA	European Securities and Markets Authority An independent EU Authority that contributes to safeguarding the stability of the EU's financial system by enhancing the protection of investors and promoting stable and orderly financial markets.
ESRB	European Systemic Risk Board The ESRB oversees the financial system of the EU in order to prevent and mitigate systemic risk.

F&P	Fitness and Probity The core function of the Fitness and Probity Regime is to ensure that persons in senior positions within RFSPs are competent and capable, honest, ethical and of integrity and also financially sound.
FATF	Financial Action Task Force FATF sets standards and promotes effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.
FS	Financial Sanctions Financial sanctions are restrictive measures imposed on individuals or entities in an effort to curtail their financial activities.
FSAP	Financial Sector Assessment Program The goal of FSAP assessments is twofold: to gauge the stability and soundness of the financial sector, and to assess its potential contribution to growth and development.
FSB	Financial Stability Board The FSB is responsible for macroprudential actions aimed at preventing and mitigating systemic risks to financial stability.
FSC	Financial Stability Committee The FSC coordinates and assesses financial stability issues and advises the Governor in this regard in relation to Ireland and the euro area.
FSPs	Fund Service Providers Funds service providers is the collective term used to describe the parties providing services to a fund/collective investment scheme.
FSSA	Financial Sector Stability Assessment An FSSA is a comprehensive assessment which focuses on issues of relevance to IMF surveillance and is discussed at the IMF Executive Board.
ICAAP	Internal Capital Adequacy Assessment Process A process through which the firm assesses the risks and their mitigation for its business, and determines an appropriate level of capital for those risks.
IFRS 9	International Financial Reporting Standard (IFRS 9) Financial Instruments IFRS 9 is a reporting standard issued by the International Accounting Standards Board (IASB). It contains three main topics: classification and measurement of financial instruments, impairment of financial assets and hedge accounting.
IMF	International Monetary Fund The IMF is an international organisation which is governed by and accountable to 189 member countries.
IMR	Investor Money Regulations The Investor Money Regulations apply to Irish fund service providers, including fund administration firms who own and operate bank accounts for the collection of investor subscription and redemption monies.
IMSC	Investment Management Standing Committee The committee is responsible for fostering supervisory convergence among national competent authorities, implementation of new rules and providing guidance on existing requirements for the investment funds sector.

IOSCO	International Organisation of Securities Commissions The International Organisation of Securities Commissions (IOSCO) is the international body that brings together the world's securities regulators and is recognised as the global standard setter for the securities sector.
JST	Joint Supervisory Team JSTs are formed of staff of the ECB and the relevant national supervisors, including the competent authorities of the countries in which credit institutions, banking subsidiaries or significant cross-border branches of a given banking group are established.
LCR	Liquidity Coverage Ratio The LCR is designed to ensure financial institutions have the necessary assets on hand to ride out short-term liquidity disruptions.
LSIs	Less Significant Institutions LSIs continue to be under the direct supervision of the National Competent Authorities.
MAR	Market Abuse Regulations MAR aims at enhancing market integrity and investor protection.
MCC	Minimum Competency Code Minimum professional standards for staff of financial service providers when they are dealing with consumers in relation to retail financial products.
MER	Mutual Evaluation Review These are peer reviews conducted by FATF, where members from different countries assess another country.
MiFID	Markets in Financial Instruments Directive MiFID is the EU legislation that regulates firms who provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment schemes and derivatives), and the venues where those instruments are traded.
MiFIR	Markets in Financial Instruments Regulation The MiFIR encompasses the rules and guidelines on execution venues, transaction execution, as well as pre- and post-trade transparency.
MO	Market Operator A market operator means an entity that manages and/or operates the business of a regulated market and may be the regulated market itself.
MPCAS	Member Personal Current Account Service A service for credit unions who wish to provide current account services and payment instruments such as debit cards to their members.
NCA	National Competent Authority The NCA is the legally delegated or invested authority that has the power to perform a designated function.
NFCs	Non-Financial Corporations NFCs are corporations whose principal activity is the production of market goods or non-financial services.
NPLs	Non-Performing Loans A non-performing loan is a loan that is in default or close to being in default.
ORSA	Own Risk and Solvency Assessment A set of processes constituting a tool for decision-making and strategic analysis.
OSPs	Outsourcing Service Providers External service providers that effectively deliver a business process, application service and infrastructure solutions for business outcomes.

PAD	Payment Accounts Directive The objective of the Payment Accounts Directive is to improve and develop the internal market for retail banking, through the removal of barriers to a fully integrated market.
PCF	Pre-approval Controlled Function These are positions whereby prior approval must be sought from the Bank prior to appointing an individual to that role or function.
PII	Professional Indemnity Insurance PII provides cover if you become liable to a member of the public following an error or omission in the professional advice or service you have provided your client and as a result have suffered a financial loss.
PRISM	Probability Risk and Impact System The Bank's risk-based framework for the supervision of regulated firms.
PSP	Payment Service Providers A PSP offers shops and online services for accepting electronic payments by a variety of payment methods including credit card, bank-based payments such as direct debit, bank transfer, and real-time bank transfer based on online banking.
QIAIFs	Qualifying Investor Alternative Investment Funds The QIAIF is a regulated investment fund targeted at sophisticated or institutional investors.
ROSC	Report on Observance of Standards and Codes ROSC summarise the extent to which countries observe certain internationally recognised standards and codes.
RMP	Risk Mitigation Programme A document that is prepared by the institution to foresee risks, estimate impacts, and define responses to issues.
RTS	Regulatory Technical Standards These are standards developed by the European Commission and define the way in which NCAs and market participants must operate.
RWAs	Risk Weighted Assets RWAs represent is a bank's assets or off-balance-sheet exposures, weighted according to risk.
SCR	Solvency Capital Requirements The SCR reflects a level of eligible own funds that enables insurance and reinsurance undertakings to absorb significant losses and that gives reasonable assurance to policyholders and beneficiaries that payments will be made as they fall due.
SCSC	Supervisory Convergence Standing Committee The SCSC helps build a common supervisory culture among NCAs to promote sound, efficient, and consistent supervision throughout the EU.
SIs	Significant Institutions A significant institution is a bank to which such importance is attached that it is directly overseen by the ECB.
SME	Small and Medium Enterprise This category is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding €50m, and/or an annual balance sheet total not exceeding €43m.
SREP	Supervisory Review and Evaluation Process SREP is an annual exercise conducted by the SIs within the SSM which shows where a bank stands in terms of capital requirements and the way it deals with risks.

SRP	<p>Structured Retail Products</p> <p>Structured products are generally a type of fixed-term investment where the return depends on the performance of a specific market or specific assets.</p>
SSM	<p>Single Supervisory Mechanism</p> <p>The SSM refers to the system of banking supervision in Europe. It comprises the ECB and the national supervisory authorities of the participating countries.</p>
TCSPs	<p>Trust and Company Service Providers</p> <p>A Trust or Company Service Provider is any firm or sole practitioner whose business is to: form companies or other legal persons. act, or arrange for another person to act, as a director or secretary of a company. act, or arrange for another person to act, as a partner (or in a similar position) for other legal persons.</p>
TD	<p>Transparency Directive</p> <p>The Transparency Directive improves the harmonisation of information duties of issuers, whose securities are listed at a regulated market at a stock exchange within the EU.</p>
TF	<p>Terrorist Financing</p> <p>Terrorism financing refers to activities that provide financing or financial support to individual terrorists or terrorist groups.</p>
TRA	<p>Targeted Risk Assessments</p> <p>Assessments developed for each firm under each risk category which outlines on-site inspection activity.</p>
TRIM	<p>Targeted Review of Internal Models</p> <p>A project to assess whether the internal models currently used by banks comply with regulatory requirements, and whether they are reliable and comparable.</p>
UCITS	<p>Undertakings for Collective Investment in Transferable Securities</p> <p>UCITS is a mutual fund based in the EU and can be sold to any investor within the EU under a harmonised regulatory regime.</p>

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