

**Law Reform Commission Conference 2016
Regulatory Powers and Corporate Offences
Thursday 3rd November 2016**

Remarks by Derville Rowland, Director of Enforcement Central Bank of Ireland

Introduction

1. Good afternoon members of the Law Reform Commission, regulatory colleagues, ladies and gentlemen. The Law Reform Commission issues paper and Professor Hodges' insightful presentation putting a focus on integrity and ethical regulation provides a vivid and compelling context for these discussions.

Objective

2. To my mind, ensuring that an ethically focused, graduated and responsive enforcement framework is in place is a critical endeavour. The existence of such a framework and its skilful deployment would significantly increase effectiveness and promote public trust and confidence in key areas of regulation.
3. I propose to focus my remarks on:
 - the role of Enforcement in the Central Bank of Ireland
 - an overview of some of the key enforcement powers
 - comment on how to ensure the continued enhancement of the Irish regulatory and enforcement framework

Approach and Regulatory Toolkit

4. The Central Bank operates an assertive risk based approach to supervision which is supported by a credible threat of enforcement. The aim is to safeguard the stability and sustainability of the Irish economy and to protect consumers and investors. The Central Bank seeks to ensure that the use of its enforcement powers contributes to the embedding within industry of core behaviours and standards. The enforcement strategy seeks to ensure that regulated firms and individuals are held to account where their behaviour fails to meet the required standards. This is essential to deter poor practices, achieve compliance and promote the behaviours we expect. Financial services firms and the individuals who run them must operate to high standards. Enforcement will make appropriate use of

all available enforcement and regulatory powers to pursue and promote these important outcomes.

5. Current regulatory thinking, informed by the financial crisis and the weaknesses it exposed, recognises that rules form only a part, albeit a critical part, of the wider toolkit needed to capture and address the dynamic and complex risks of the financial system. The regulatory toolkit for effective financial system governance is now recognised as being composed of a series of interlocking components whereby regulation i.e. the rules, ongoing supervision and enforcement interact effectively.
6. This model facilitates an effective regulatory system so that a regulator's powers are grounded in well-constructed, robust and enforceable rules and legislation. Supervisory processes are developed to ensure that a regulator keeps abreast of current sectoral practices; understands not only key risks but also the motivations behind poor practices. Enforcement measures will be deployed, where appropriate, to investigate why a breach has occurred, how it can be rectified and how to prevent it occurring in the future. This may involve the imposition of any one or combination of sanctions or other remedies.
7. With respect to the first part of this model, the legislative architecture within which a regulator operates, it is essential that the law and guidance promulgated by the legislature and the particular regulatory authority are well-crafted, consistently drafted and designed to be effective and enforceable.
8. With respect to the second part of the model, supervision, in order to effectively regulate an industry, we must understand the drivers in that industry, the business models adopted by those we regulate and the risks to which those firms or individuals and their clients are exposed including, in particular, emerging risks. To do so, regulators must foster an effective supervisory relationship which will also allow regulators to assess how the rules adopted i.e. the legislative architecture is working in practice and whether amendments are required to deliver a more effective regulatory regime. The Central Bank has a range of regulatory tools available to it in order to deliver on these objectives, which tools can be used in conjunction with other powers such as enforcement or as standalone measures.

9. It is imperative that a regulator, such as the Central Bank, has a toolkit of varied and adaptive methods of promoting a culture of ethical compliance by firms and individuals.
10. The third part of that model is enforcement. The Enforcement Division of the Central Bank is organised into multi-disciplinary teams made up of lawyers, accountants and investigative experts. Some key responsibilities and functions of Enforcement include:
 - advising supervisory divisions;
 - investigating and managing cases where decisions may be proposed to refuse applications i.e. for authorisation; in connection with fitness and probity or for proposed acquiring transactions, or where decisions may be proposed to revoke an existing authorisation.

These are core regulatory tools and are generally referred to as a gatekeeper role which affects entry to or continued operation in the regulated market. This gatekeeper role is an increasingly important aspect of our work.

11. Enforcement's other important and core responsibilities include:
 - investigating and taking cases under the Administrative Sanctions Procedure ("ASP") (under Part IIIC Central Bank Act 1942, as amended) (the "1942 Act")
 - taking cases under Securities Markets legislation;
 - investigating fitness and probity cases in respect of persons '*in situ*'; and
 - Summary criminal prosecutions.
12. Other enforcement options include the imposition of supervisory warnings which are non-statutory tools, the imposition of conditions on authorisation and the issuance of directions. Referral of suspected breaches to other agencies also forms part of the regulatory framework. Enforcement also works with supervisors and firms to put in place redress schemes to redress customer loss, where appropriate.
13. An enforcement case taken by the Central Bank may be concluded by way of settlement, inquiry, assessment or other statutory decision. The range of sanctions which may be imposed depend on

the specific statutory regime utilised but can include monetary penalties, disqualification, suspension or prohibition of individuals and/or suspension or revocation of authorisation of a firm.

14. With respect to the ASP under the 1942 Act, where the Central Bank suspects on reasonable grounds that a breach has been committed, it may put in place an Inquiry panel to inquire into the matter, determine whether the breach did in fact occur and, if so, what (if any) sanctions to impose. On foot of such an Inquiry or where a case settles prior to a determination by the Inquiry, the Central Bank may impose a monetary penalty of up to €10million or 10% of turnover on a firm or up to €1million on an individual. As outlined above, in the case of an individual, the Central Bank may also disqualify an individual from being concerned in the management of a regulated entity. The Central Bank must apply to the Courts for confirmation of these sanctions.

Practical Examples

15. The protective gatekeeper aspect of our role is becoming increasingly significant with numerous refusals of authorisations and a growing number of acquiring transactions applications being made. In terms of fitness and probity, the evidence suggests that individuals prefer to withdraw from the process rather than run the risk of being refused. Approximately 31 specific interviews to challenge candidates have been conducted. These are very detailed enforcement led interviews. 18 candidates withdrew before the fitness and probity process reach conclusion. This is in line with the experience of other regulators.
16. The Central Bank has also ensured that a number of individuals can no longer participate in the provision of financial services. This is been done through the issuance of fitness and probity prohibition notices. We have also sought and obtained enforcement orders in the High Court to restrain poor conduct.
17. A good example of this diversified approach occurred in 2015. During the course of an investigation into the loss of tracker mortgages and options, the enforcement team ensured that Permanent tsb developed and deployed a comprehensive consumer redress program for impacted customers. Leveraging on

this experience, Enforcement continues to work with supervisory colleagues in the context of the wider tracker project.

18. These examples demonstrate the commitment of Enforcement to use all options to deliver appropriate outcomes.
19. Following the referral of a number of cases to inquiry pursuant to Part IIIC of the 1942 Act, an unprecedented number of legal challenges were brought before the High Court. In 2016, after a five day trial in respect of a Judicial Review application by Mr. Fingleton, Mr. Justice Noonan gave judgment for the Central Bank¹. This case is now being appealed.
20. Also earlier this year, Mr. Purcell challenged the constitutionality of the 1942 Act by way of Judicial Review and a plenary challenge. Following a six week trial, Mr. Justice Hedigan² found for the Central Bank and confirmed the constitutionality of the legislation.
21. These challenges necessitate considerable investment of resources by the Central Bank. We continue to progress these cases through the inquiry process and have successfully defended all of the litigation challenges to date.
22. Since the introduction of the Central Bank's ASP powers, over a hundred cases have been concluded by way of settlement. Financial penalties in the region of €49.7 million have been imposed and individuals have been disqualified from being a person concerned in the management of financial service entities. The longest duration of disqualification was for a 10 year period.

¹ Mr. Justice Noonan said "*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*" (**Fingleton v. The Central Bank of Ireland [2016] IEHC 1**)

² Mr. Justice Hedigan said "*the evidence of Professor Niamh Moloney and indeed of Dr. Constantine Gurgdiev demonstrated very clearly the overwhelming public interest in maintaining the integrity of the financial sector of society ... It is something that requires... effective forms of regulation and enforcement. The Oireachtas has provided that those functions should be carried out by the Central Bank ... and have established complex and sophisticated administrative machinery for doing so. The courts have manifestly never been involved in this area of financial regulation*". He also said, "*the collapse of [INBS] left this country with liability for a colossal sum of money. The exact sum may never be precisely defined but it is a liability in the vicinity of €5 billion. That fact alone would be enough to outweigh any particular burden on anyone*". Mr. Justice Hedigan went on to say "*the evidence of Professor Moloney .. was compelling on the need to investigate what actually happened and to fix the blame for any contraventions that may have occurred. The very essence of reasoning was that the highly dynamic financial system needs constant in-depth surveillance of anything like the crash that occurred in 2008 is to be avoided. Its very dynamism demands highly adaptable mechanisms of control. The personal responsibility of persons in this highly complex structure is an essential part of that control system. It is to be hoped that a thorough enquiry of the kind proposed... Will illuminate the mistakes, both corporate and personal, that brought about this collapse which was a national financial disaster. The public interest in knowing what happened is overwhelming*". (**Purcell v. The Central Bank of Ireland & Others [2016] IEHC 514**)

23. The sanctions which can be imposed are, however, only a small part of the enforcement story. Enforcement is not simply a tool designed to achieve targets, to punish firms or to generate publicity. It is, instead, an integral part of a firm's engagement with the Central Bank, a complimentary strategy to regulation and supervision. The enforcement process has a more significant impact on the regulated industry than its financial cost. Rather, the intrusive investigative techniques adopted by the Central Bank in an enforcement case contribute to an overall regulatory strategy of improving behaviours within the regulated industry. The capacity to call individuals for interview, to require them to answer for their conduct or that of their firm, to conduct detailed investigations to understand why a breach has been committed and to tailor our response to the specific issues we encounter is fundamental to delivering on the Central Bank's objectives of ensuring the effective regulation of financial markets and protecting consumers of financial products. The proper deployment of these powers and the dissemination of lessons learned from these cases also promote public confidence in the financial industry, both nationally and internationally.
24. The ASP is, therefore, about a robust investigation to identify what went wrong in a regulated actor, stopping that harm from continuing, and ensuring that it doesn't happen again (within that organisation and the wider industry by warning against these bad practices).
25. As you may already be aware, the Central Bank issues public statements at the conclusion of enforcement actions that conclude by way of settlement. We believe that it is vital to the delivery of the Central Bank's strategy of credible deterrence and to ensure that enforcement operates in a transparent manner, informing the financial sector and consumers about the issues identified, how a firm or individual fell below the expected standard, why a particular regulatory response was adopted and what lessons are available generally from the particular case. These public statements are, therefore, a valuable method of deterring misconduct within the financial sector, of signalling to the market what practices and/or behaviours are not acceptable and the consequences of breach.
26. The effective operation of these component parts, namely, regulation, supervision and enforcement can assist any regulator in the fulfilment of their statutory objectives. I don't believe, however,

that you can simply look at enforcement in isolation but rather it must be looked at as an inherent part of a regulatory strategy to improve behaviours, imbed ethical standards and deter misconduct.

Closing Remarks

27. Taking a regulatory regime as a whole, it is vital that regulators are afforded the necessary tools to respond to issues arising for them in a proportionate, measured and strategic manner. These must be comprehensive, coherent and well drafted. Additional benefits of efficiency and effectiveness would also flow from such an approach. One size may not fit all regulators but variation could be accommodated. Public trust and confidence in a model of enforcement would be boosted by a well-crafted and ethically focused enforcement framework. It is worth considering, embedded within this law and guidance, certain core standards which could guide regulated firms and the individuals who run those firms.
28. By way of example, the embedding of the basic requirements for regulated entities and individuals such as requirements:
- to conduct themselves with honesty and integrity;
 - to have the competence and capability to conduct their business;
 - to act in the best interests of their customers;
 - to be financially sound;
 - to manage conflicts of interest; and
 - to co-operate with the relevant regulatory authorities.

may place the desired outcomes at the centre of focus of regulatory regimes. By starting with the end in mind high standards may be encouraged.