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FITNESS & PROBITY REGIME

New Central Bank Fitness and Probity Regime for persons performing controlled functions and pre-approved controlled functions at regulated financial service providers ("firms").

Regulated financial service providers, (for ease of reference called firms) would include Banks, insurance companies, financial advisers, MiFID firms etc with the exception of credit unions.

The Central Bank Reform Act 2010 and related regulations (the Act) has together with a **Fitness and Probity Code** issued under s50 of the Act and a **Guidance** document¹, created a harmonised statutory regime for the regulation of persons performing Controlled Functions (CFs) and Pre-Approval Controlled Functions (**PCFs**) in regulated financial service providers (**firms**). In complying with the new regime, the new **Minimum Competency Code 2011** must also be complied with.

Persons occupying positions where CFs² (including PCFs³) are performed will be subject to the Central Bank's powers of investigation, suspension and prohibition. Firms need to act with urgency to ensure compliance with the new regime as the first deadline where action needed to have been taken was the 31st of December 2011 and the next deadline is the 31st of March.

What regulated financial services providers (firms) must not do:

- permit a person to perform a CF unless satisfied on reasonable grounds that the person complies with the Standards (s21 and the Code issued under s50 of the Act)
- appoint a person to perform a PCF unless the Central Bank has approved in writing the appointment (s23)

What regulated financial services providers had to do by 31st of December 2011:

- examine the definition of PCFs in Schedule of the Regulations
- create a record of persons performing PCFs in the firm as of 1st December 2011
- if unsure whether an employee is performing a PCF, contact a member of the firm's supervisory team in the Central Bank
- submit to the Central Bank by 31st of December 2011 a list of persons in PCFs as of 1st December 2011.

What regulated financial services providers must do by 31st of March 2012:

- CEOs of firms must confirm in writing, that they are satisfied that the persons on the list of persons in PCFs are compliant with the Standards and they have obtained each person's written agreement to abide by the Standards. Firms must document and record all due diligence and retain relevant documentation.

¹ the final version of which was published on the 24th of November.

² this is a significant influence function (CF1) or a compliance function (CF2), or customer facing function (CF3-9) or dealing in property function (CF10-11).

³ this would be a member of a board, the CEO, member of a partnership/sole trader (PCF10-11), senior management position (core) (PCF12-18), senior management positions (Industry specific -FSP)(PCF19-41) and non-EEA firm branches in the state (PCF42)

Fitness and Probity

A person to whom the Code applies must comply with the Standards set out in the Code. In order to comply with the Standards, the person must be:

- Competent and capable (s3 of the Code);
- Honest, ethical and to act with integrity (s4 of the Code); and
- Financially sound (s5 of the Code).

Relevant Dates for commencement of the new regime

From 1st December 2011 the new regime applies to new and existing PCFs

From 1st March 2012 the new regime applies to new CFs

From 1st December 2012, the new regime applies to existing CFs

General Obligations of Firms

Firms must:

- carry out certain levels of Due Diligence appropriate to the CF or PCF concerned and in the case of a PCF, the Individual Questionnaire (IQ) has to be completed and filed on line with the Central Bank as part of the pre-approval process
- be satisfied on reasonable grounds that persons performing PCFs and CFs comply with the Standards on appointment. This includes obtaining certain undertakings from them
- require staff to comply with the Standards throughout their employment
- establish systems and controls to comply with their obligations and retain supporting documentation

Standards of Fitness and Probity appropriate to the particular CF – levels of due diligence

The firm must satisfy itself on reasonable grounds that a person complies with the Standards. This would include considering the responsibilities linked to the specific function in the firm and determining the specific competencies and level of probity that should be expected of a person performing that specific CF in the firm.

The **level of due diligence** required from a firm in fulfilling its obligations may differ depending on the categorisation of the CF (e.g. CF1 and CF2 will attract higher diligence than CF3-11).

Guidance on determining the **standard of fitness and level of due diligence** appropriate to a particular CF are set out in s14 and s15 of the Guidance.

Guidance on determining the **standard of probity and level of due diligence** appropriate to a particular CF are set out in s16 and s17 of the Guidance.

Additional due diligence is required to be undertaken by a firm in the case of **CF1, CD2 and PCF functions**. The Guidance at s18 sets out what should be done.

The continuing obligations imposed on firms by the Act

- Firms must bring the Standards to the attention of every person performing a CF on its behalf and obtain a signed copy of an undertaking in a certain form
- As part of ongoing performance monitoring, the firm should ask persons performing CFs to certify that they are aware of the Standards and agree to continue to abide by those Standards at least on an annual basis
- Firms should require persons performing CFs to undertake to notify the firm of any material changes in respect of initial due diligence carried out

- Firms should carry out an audit of persons performing CFs on an annual basis by asking persons in CFs to confirm whether they are aware of any material developments in relation to their compliance with the Standards of which the firm ought to be aware
- Where a firm becomes aware that there may be concerns regarding the fitness and probity of a person performing a CF, the Central Bank expects the firm to investigate such concerns and take action as appropriate without delay and this would include notifying the Bank

The finalised version of the Guidance on Fitness & Probity contained a number of significant changes to the draft version. Some of these are not in line with the Regulations and may require further amending regulations

- Three further exemptions to the application of the Standards were listed to add to the “call centre” exemption. The first of these is where a person is performing a CF or a PCF on behalf of a firm from another EEA country and which provides services in Ireland on a **cross border or branch basis**. The second exemption is for a person performing a function in a **separate legal entity but in a group structure of companies**, who may exercise significant influence over a CF or PCF in an Irish registered firm which is part of the same group. Thirdly, where an Irish firm **outsources** CF and PCF functions to another regulated firm under a written agreement, whether in Ireland, elsewhere in the EEA or elsewhere in the world, an exemption exists. This was included in the Central Bank Reform Act, 2010 (Sections 20 and 22) (Amendment) Regulations, 2011 brought in on the 30th of November last year
 - Firms were originally to have disclosed the identities of persons carrying out PCFs (at the 1st of December) and to have confirmed that the firm was able to demonstrate that they were Fit and Proper by the 31st December 2011. The new guidelines state that the CEO of the Firm still needs to submit a list of the persons in PCFs (at the 1st of December) by the 31st December 2011. It is now not until **31st March 2012** that CEOs have to confirm they have completed all related due diligence. Legally all firms need to be able to justify satisfaction with persons in PCF roles, but the Central Bank has indicated that it will not seek to police this until April 2012
 - The position of Company Secretary was removed from the list of PCFs. However a Company Secretary may be captured under CF-1 if he/she exerts a significant influence
 - Where **unregulated entities** propose themselves to perform **outsourced activities** for the CFs of a firm, the Central Bank has indicated that they should comply with Fit and Proper standards and Part 3 of the CBRA. The outsourced service provider should provide written confirmation to the firm that those individuals performing CFs are compliant with the F & P Standards and have agreed to abide by them. Sample documentation as to how compliance with the F & P Standards is adhered will need to be provided. If a service level agreement (SLA) is in place, it will be necessary to amend the SLA to comply with the Fitness and Probity standards regime when the SLA is updated or within 12 months, whichever comes sooner
 - The new Guidance provides that all **reasonable efforts must be made to obtain references** from former employers or other relevant persons and all evidence of correspondence must be maintained. If unable to obtain a reference the firm must record the steps it has taken to obtain the reference and demonstrate how it satisfied itself that the person is competent to perform the CF. Another change is that references are not required for persons in situ at the 1st December 2011 where the person is in the same position for at least a year
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Minimum Competency Code (MCC or Code)

The Central Bank of Ireland's revised Minimum Competency Code 2011 came into effect on 1st December 2011 and replaced the Minimum Competency Requirements, issued in 2006. The MCC requires regulated firms to ensure that persons exercising any of the relevant functions on behalf of the regulated firm comply with the Standards set out in Part 1 of the Code.

The Minimum Competency Standards

A person subject to the Code must either:

- a) have completed a recognised qualification and be compliant with the CPD requirements, or
- b) be a grandfathered person, or
- c) be a new entrant participating in a training process under supervision of a qualified or grandfathered person, or
- d) be performing a prescribed script function and

New entrants must participate in training programme and detailed supervision requirements apply on an ongoing basis with an obligation to keep written records. A register must be kept of all **accredited persons** acting as for or on behalf of the regulated firm.

A regulated firm that has carried an assessment for grandfathering purposes must ensure that the assessment and the certification of the individual's compliance with the experience requirement are complete and accurate. By 1st January 2013 each regulated firm must complete and retain on file a statement of grandfathered status.

Continuing Professional Development (CPD)

A regulated firm must ensure that it has procedures in place to ensure that qualified persons and grandfathered persons are in compliance with the CPD requirements on an ongoing basis. The main points are as follows:

- Change from three-year cycle to annual requirement
- 15 formal hours per year or as per professional body's requirements
- At least one hour for each function undertaken
- At least one hour relating to ethics
- Person who is qualified and grandfathered – 15 formal hours
- Surplus hours may not be carried forward
- Shortfall may be made up by end of following year provided no other shortfall within previous five years
- Firm must have procedures to ensure compliance with CPD requirements

Further Requirements

The MCC contains further requirements in relation to Outsourcing Agreements, annual certification and audit of relevant persons and to investigate any concerns regarding the fitness and probity of an individual and take action as appropriate without delay and notify the Central Bank of any action.

How McKeever Rowan can help

- We can provide a detailed manual outlining the practical steps to be implemented by firms to comply with new regime
- conducting searches and providing advice on due diligence
- advice on ongoing compliance with the regime
- advice on submissions to Central Bank
- advice and representation in relation to Central Bank investigations and appeals
- restructuring employment contracts
- advice on employment termination arising from new regime (including giving of references)