Regulatory and Administrative Sanctions Unit

DILLON EUSTACE

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REGULATORY AND ADMINISTRATIVE SANCTIONS UNIT

Introduction

Dillon Eustace is one of Ireland's leading law firms focusing on financial services, banking and capital markets, insurance regulation, corporate and M&A, insolvency, litigation and dispute resolution, real estate and taxation. Headquartered in Dublin, the firm acts for many regulated financial services firms, particularly MiFID entities, life and general insurers, investment funds and their service providers and many others. The firm's other offices are in Tokyo (2000), New York (2009), Hong Kong (2011) and Cayman Islands (2012).

In response to the shift from a principles to a rules-based regulatory approach and the increased use of enforcement actions by Irish regulators and similar bodies, we have developed a dynamic cross-disciplinary Regulatory and Administrative Sanctions Unit, made up of specialists operating in our financial services, litigation and regulatory and compliance teams.

The Unit is active in advising regulated financial services providers and their management teams through all stages of the Central Bank of Ireland's ("**Central Bank**") administrative sanctions process under Part III C of the Central Bank Act, 1942, from examination to inquiry and in settlement discussions.

We also advise regulated firms and their executives regarding all aspects of the Central Bank's fitness and probity regime as well as corporate governance matters generally. We have also acted for D&O insurers of regulated entities involved in enforcement actions which included sanctions and proceedings under company law**.**

We have also represented individual executives dealing with the Office of the Director of Corporate Enforcement and have advised clients in relation to similar procedures involving other regulatory bodies such as the Chartered Accountants Regulatory Board.

This experience means that we can provide practical advice and guidance as well as legal analysis and representation to clients through the entire process and beyond, if necessary.

In conjunction with our Regulatory and Compliance Unit we also advise on day to day regulatory and compliance matters.

Background

Since the late 1980s, Ireland has developed as a leading international financial services centre for investment funds, cross-border insurance and re-insurance, asset management

and other MiFID investment services, banking, securitisation and SPV domiciliation and administration. These internationally focused activities sit side by side with Ireland's long established domestic financial services industries.

Both the international and domestic sectors have seen, particularly since the global financial crisis, ever increasing levels of regulation and inspection, the introduction of new corporate governance and fitness & probity requirements for those involved in executive type roles and, as one would expect, more intrusive and robust regulatory interventions.

Reflecting what might be described as a move from a "principles based" to a "rules based" regulatory approach, the industry has seen quite a marked increase in the use by the Central Bank, as primary regulator, of its administrative sanctions powers resulting in the levying of sizeable financial penalties on regulated firms concerning contraventions of regulatory requirements across a number of areas.

The Central Bank's Administrative Sanctions Procedure

The legislative framework governing the Central Bank's Administrative Sanctions regime is found in Part III C of the Central Bank Act 1942, as amended (the "**1942 Act**") and in the Administrative Sanctions Guidelines (the "**Guidelines**") issued by the Central Bank pursuant to the 1942 Act.

Section 33 AO (1) of the 1942 Act provides that

> "*whenever the Bank suspects on reasonable grounds that a regulated financial service provider is committing or has committed a prescribed contravention, it may hold an inquiry to determine whether or not the financial service provider is committing or has committed a contravention".*

The term "*inquiry*" is defined in Section 33 AN of the 1942 Act as:

> "*an inquiry held under Section 33 AO or Section 33 AR, and includes such an inquiry begun by the former Regulatory Authority and continued by the Bank".*

Section 33 AP of the 1942 Act provides that before holding an inquiry under Section 33AO, the Central Bank shall give notice in writing of the proposed inquiry to the financial service provider or other person concerned and the notice must specify the grounds on which the Bank's suspicions are based; and specify a date, time and place at which the Central Bank will hold the inquiry; and invite the financial service provider or person concerned either to attend the inquiry or to make written submissions about the matter to which the inquiry relates.

Examination phase

The 1942 Act provides a regime for the holding of inquiries by the Central Bank.

In its Guidelines document the Central Bank explains that process and what it refers to as the "*examination*" phase where the Central Bank seeks to establish whether it has reasonable grounds for its suspicion that a contravention has occurred.

In paragraph 2.1.2 of the Central Bank's other document titled "*Outline of Administrative Sanctions Procedure*", it describes the first step as being suspicion, the second step being examination and the third step can be one of a number of steps including an administrative sanctions inquiry.

The possible steps after the examination phase are as follows:

- Central Bank decides to take no further action;
- Central Bank decides to take other supervisory action;
- Central Bank decides to establish an inquiry;
- Parties agree to enter into a Settlement Agreement;
- Central Bank decides to initiate a criminal procedure;
- Central Bank refers matter to other authority or enforcement body.

The Outline document notes that in some cases, where it appears that a prescribed contravention has occurred, the Central Bank may decide that the case may most appropriately be dealt with by taking supervisory action only and that that may be particularly appropriate if the prescribed contravention has limited regulatory significance or can be fully dealt with without applying sanctions.

There are a number of available options in those circumstances. It may be appropriate to impose an enhanced supervisory regime to ensure adherence to the required standards and reduce the risk of future non-compliance. The Central Bank may also issue a supervisory warning where there are reasonable grounds to suspect a breach of statutory or regulatory requirements has occurred. The Outline states that supervisory warnings may be issued where full co-operation is received and the problem was rectified immediately and other considerations supporting enforcement do not apply. The Outline document notes that if it proves necessary to issue a supervisory warning, that shall form part of the compliance record of the regulated financial service provider or person concerned in its management.

Interestingly, Section 33 AO (1) (nor any other Section of Part III C of the 1942 Act) does not provide for an examination procedure. It only provides for an "*inquiry*". Furthermore, whilst Section 33 BD provides that the Bank may prescribe guidelines with respect to the conduct of inquiries under Part IIIC, it makes no mention of prescribing guidelines with respect to the conduct of examinations.

Central Bank Inquiries

Under the 1942 Act, where the Central Bank "*suspects on reasonable grounds"* that a regulated financial service provider is committing or has committed a prescribed contravention it may hold an inquiry to determine whether or not the entity is committing or has committed the contravention.

An inquiry is a formal hearing, normally held in public, before members of the inquiry made up of personnel from the Central Bank who are not meant to have been involved in the investigation of the matters alleged. Before it holds such an inquiry, the Central Bank is required to give notice in writing of the proposed inquiry setting out the grounds upon which its suspicions are based, setting out the date, time and place at which the inquiry will be held and inviting submissions/attendance at the inquiry.

The 1942 Act provides that, at the conclusion of an inquiry, the Central Bank shall make a finding as to whether the prescribed contravention was or is being committed and if it makes such a finding it can impose one or more of a series of sanctions including a caution or reprimand, a direction to pay a monetary penalty and directions to cease committing the contravention.

As an alternative, if the regulated entity acknowledges that it has committed or is committing the contravention then the Central Bank can, with the agreement of the regulated entity, dispense with holding an inquiry and proceed to impose a sanction or can proceed to hold an inquiry to determine what sanction, if any, should be imposed.

Settlement Agreement

The 1942 Act also provides that where the Central Bank has a reasonable suspicion as outlined above it is entitled to enter into a settlement agreement in writing. It can do so once it has that reasonable suspicion and at any time before an inquiry is completed.

Where a settlement agreement is reached this will be noted on the regulated entity's compliance record and can influence a decision by the Central Bank to bring other administrative sanctions procedures at a later date. It is important to note that the Central Bank will only enter into a settlement agreement where:

- the regulated entity admits at least some of the breaches;

- where the regulated entity demonstrates that it has acted promptly to take, what the Central Bank considers to be, the necessary remedial action to deal with its concerns;

- where the regulated entity agrees to a negotiated financial settlement (i.e. a fine), the terms of a settlement agreement and the publication of that settlement agreement.

Every settlement agreement appears on the Central Bank's website, and in practically every instance is reported in the Irish press and may in fact be disseminated by the Central Bank more widely – as it is normally accompanied by a publicity statement detailing the outcome of the settlement which, according to the Central Bank's own publications, are carried by media outlets giving European and global distribution, including traditional print outlets, online resource sites and financial and securities markets wire services (e.g. FT, Bloomberg, Reuters and NASDAQ). This has been publicly stated by the Central Bank's Head of Enforcement on several occasions.

It is also of note that under the new Fitness and Probity Regime applicable to directors / officers of regulated firms, where a member of the board or other senior officers were to seek to be approved as pre-approval controlled functions in other Irish regulated entities at a later date, they would be required to disclose to any proposed appointing company the fact that they were a director / officer of a firm which had been sanctioned.

Sanctions

Currently the Central Bank compose financial penalties of up to Euro 10 million in a case of a corporate or unincorporated body or 10% of the annual turnover of the regulated financial service provided in the last year, whichever is greater or in the case of a natural person an amount not exceeding Euro 1 million.

In 2012 the Central Bank entered into 16 settlement agreements with regulated entities resulting in fines totalling almost Euro 8.5 million being imposed.

Into 2013 the Central Bank also entered 16 settlement agreements with regulated financial entities and they have entered into 11 settlements so far in 2014.

The Office of the Director of Corporate Enforcement

The stated aim of the Office of the Director of Corporate Enforcement ("**ODCE**") is to improve the compliance environment for corporate activity in Ireland by encouraging adherence to the requirements of the Companies Acts and by bringing to account those who disregard the law.

Background

The conclusions of various review groups, courts, tribunals of inquiry and parliamentary committees revealed that provisions of Irish company law and other legislation were regularly being breached without the companies or individuals in question being held accountable. As a result various innocent parties bore the cost of this misbehaviour and the associated business risks.

These concerns led to the enactment of the Company Law Enforcement Act, 2001 and the establishment of the Office of the Director of Corporate Enforcement. Under the Act, the Director of Corporate Enforcement is legally responsible for both encouraging compliance with company law and with investigating and enforcing suspected breaches of the legislation.

Compliance Role

The Director of Corporate Enforcement encourages compliance with company law requirements by communicating publicly the benefits of compliance with the law and the consequences of non-compliance. The strategies employed include:

- the publication of information, via the printed and electronic media, on the legal duties and powers which exist under Irish company law,

- consultations with professional bodies to secure the conformity of their members with the requirements of the law, and

- discussions with government and other parties to facilitate and support the compliance role of the Director.

Detection Role

The Detection Unit of the ODCE has a twofold duty:

- to conduct initial assessments of complaints received of suspected breaches of company law, and

- to gather information on suspected breaches.

Its role includes company investigations, examining company books and documents and interviewing company directors, auditors and other individuals.

The Detection Unit identifies possible remedial options and takes steps to conclude or advance the complaints process. Having evaluated the information and corroborating material, the ODCE will determine what action, if any, is appropriate and what would be the most suitable means of legal redress or sanction.

The Enforcement Role

The investigative and enforcement role of the ODCE arises in the following areas:

- the initiation of fact-finding company investigations,
- the prosecution of persons for suspected breaches of the Companies Acts,
- the supervision of companies in liquidation and of un-liquidated insolvent companies,
- the restriction and disqualification of directors and other company officers,
- the supervision of liquidators and receivers, and
- the regulation of undischarged bankrupts acting as company officers.

Future Trends

In mid-February 2013 the Central Bank issued its Enforcement Priorities for 2013 indicating that it intends to pursue enforcement actions in the following enforcement priority areas for 2013 – retail intermediaries, payment protection insurance, client asset requirements, prudential requirements, AML/CTF, systems and controls, time lines and accuracy of information submitted to the Central Bank, errors and overcharging, payment services regulations and suitability requirements (Consumer Protection Code).

The Central Bank noted that where serious breaches of regulatory requirements occur:

> "*regulated entities and their management can expect vigorous investigation and follow through by the Central Bank*".

Separately to the administrative sanctions procedure, executives across the financial services industry are also having to deal with the Central Bank's fitness and probity regime which has caused a number of difficulties for executives, not only upon the introduction of the regime but also when moving positions internally and when moving to other firms with certain unusual consequences particularly around confidentiality.

Publications and Information Briefings

The Unit regularly publishes articles on matters related to the work that it is doing and reviews new or pending legislation and regulatory changes. These articles can be accessed on the Dillon Eustace website under the publications section www.dilloneustace.ie/Publications.

In addition, the Unit hosts regular briefings at our Dublin offices on topical areas. If you would like to be kept informed of these briefings please let any of those listed below know.

The Regulatory and Administrative Sanctions Unit

- **Andrew Bates**

Andrew is the Head of the Financial Services Department where he works primarily on asset management, investment funds and insurance regulatory matters. He has been recognized as a leading lawyer in these practice areas by Chambers, by the Legal 500, by IFLR and others.

He is the author of several publications including Guides on UCITS, on Hedge Funds and on Private Equity Funds as well as on MiFID and cross border insurance regulation and is a regular speaker on financial services related topics at domestic and international events. He most recently co-authored the Irish Chapter on Liabilities of Asset Manager (Oxford University press 2012). Andrew is a former Council Member of the Irish Funds Industry Association and is a member of the Investment Funds division of the IBA. He also sits on the boards of several investment fund platforms, asset managers and has previously sat on the board of a number of insurers.

- **Brian Dillon**

Brian has been a partner in the Financial Services Department since 2002 where he advises asset managers, fund administrators and promoters of Irish regulated funds. Brian established the firm's Tokyo representative office and managed it from 2000 until 2002, during which time he was admitted as a foreign member of the Japanese Bar Association. He is currently a committee member with the Irish Funds Industry Association and a member of the International Bar Association. Brian sits on the board of several client companies.

- **John O'Riordan**

John is a partner in the firm's Litigation and Dispute Resolution Department. He previously spent time in the firm's Financial Services Department. John also has also worked on secondment with an international bank operating in the fields of insurance, financial services and mutual funds.

John practises in the areas of commercial dispute resolution and has significant experience in representing national and international corporations, banks and financial institutions in the area of commercial and financial services litigation.

John has also advised a number of clients through the Central Bank's Administrative Sanction procedure up to and including negotiating settlement agreements with the Bank.

Breeda Cunningham

Breeda is a Chartered Accountant, having trained with PWC. Prior to joining the Regulatory and Compliance Unit in Dillon Eustace in 2007, Breeda was the Head of Compliance for one of the largest insurance brokers in Ireland she also has several years internal audit experience in the retail insurance sector having worked for a number of years in one of the largest life companies in Ireland. Breeda works closely with regulated entities assisting them in the authorisation process, with ongoing compliance obligations also in implementing action plans following inspections by the Central Bank.

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For more details on how we can help you, to request copies of most recent newsletters, briefings or articles, or simply to be included on our mailing list going forward, please contact any of the team members below.

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