

FINANCIAL SERVICES CONSULTATIVE INDUSTRY PANEL
Painéal Tionscail Chomhairligh na Seirbhísí Airgeadais



Financial Services
Consultative Industry Panel

Annual Report

2007

Industry Panel



Back row: Jonathan Goold, Sean Quirke, Pat McArdle, John O'Halloran, Tony Culley, Peter Keane, James Deeny, John Murphy, Gary Palmer, Liam Carberry, Robert Moynihan, Pat Farrell and Robert Richardson

Front row: Colette Clancy, Rachel Panagiodis, Sarah Goddard, Aileen O'Donoghue, Carmel O'Connor and Eimer O'Rourke

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Chairman's Statement

The provision of financial services domestically and internationally is a vitally important component of the Irish economy. The financial services sector employed some 59,500 people by the end of June 2007. The banking sector alone contributed an estimated 7% of GNP and 4% of the State's gross tax receipts, including some €0.8 billion in corporation taxes. IFSC companies are estimated to produce almost €1.0 billion in corporation taxes. Financial services is also a key export sector, accounting for over one third of all services exports.

Ireland has sought to position itself in the top quartile of well-regulated financial markets world-wide and this strategy has Industry's complete support.

The stated purpose of the Financial Regulator is to help consumers make informed financial decisions in a safe and fair market, and to foster sound dynamic financial institutions in Ireland. It is the case that with the full implementation of the Financial Regulator's Consumer Protection Code, the defined standards for the delivery of retail financial services in Ireland rank among the highest in the world.

The recent problems evolving from the global credit crisis have largely been avoided by the Irish financial services sector. The Financial Regulator is delivering on its mandate of fostering sound dynamic financial institutions in Ireland. In this it is to be congratulated.

The work of the Financial Services Consultative Industry Panel ("the Panel") has matured over the three years since its inception. In 2007, and indeed the same will apply again in 2008, the work of the Panel has been more concerned with evolving high-level themes rather than specific regulatory developments. At the same time, we have built on our strong working relationship with the Financial Regulator. We set a number of objectives for the Panel in 2007, and we have been largely successful in delivering these.

Stakeholder Protocol

Since inception, the Panel has been encouraging the Financial Regulator to address the question of its interaction with key stakeholders, and with Panel involvement and wide consultation, we are pleased that the Stakeholder Protocol was launched last July. This is a very progressive action by the Financial Regulator, and is highly innovative and possibly unique in a global regulatory context. It is also an important element in fostering innovation and competitiveness at the earliest stage of stakeholders' interaction with the regulatory process. The objective of the stakeholder protocol is to track the Financial Regulator's performance in meeting specified targets, recognising fully that success in this area also places demanding reciprocal obligations on industry. We look forward to the first annual review of the operation of the protocol, and the implications for all parties involved.

Survey of Unnecessary Regulatory Requirements

Following the invitation from the Financial Regulator to identify unnecessary regulatory requirements capable of being amended by the Financial Regulator, we have commissioned KPMG Consultants to carry out an appropriate review. This will be an important piece of research in its own right, and will also help inform the Panel's input into the larger scale review and consolidation of financial legislation being carried out by the Financial Legislation Advisory Forum.

We anticipate that the research will identify a range of sector specific issues which we will evaluate jointly with the Financial Regulator, recognising that not all of these will be susceptible to change.

Review of Income and Expenditure and Strategic Plan Update

The Panel participated actively with the Financial Regulator in the review of the Financial Regulator's income and expenditure budget for 2008. Full details are given later in this report, which shows that the Panel was able to identify the strengths and weakness of the proposed expenditure, in a robust and transparent process.

We are also pleased to report that our suggestions in respect of the Strategic Plan for 2008-2010 were generally well received, and in particular instances, adopted.

EU & International

The Panel Sub-Group was set up to facilitate increased industry engagement on EU & International affairs, and is comprised of the stakeholder industries in the international Financial Services industry sectors. The primary objective of the group is to consider EU and international developments, to ensure that there is early engagement with the Financial Regulator (or other relevant authorities), and to inform the Financial Regulator of emerging industry market issues/developments/trends. This Sub-Group will spearhead the work of the Industry Panel on the review of the Lamfalussy Process in 2008

Markets in Financial Instruments Directive (MiFID)

After long and complex negotiations, the MiFID was finally implemented in Ireland in November 2007. We are pleased to confirm that the transposition process was highly effective in Ireland driven by the MiFID Implementation Forum set up and operated by the Financial Regulator. The Forum brought together all the affected parties. The approach used was possibly unique in an EU context, and much credit is due to the Financial Regulator for the initiative.

Solvency II

The new EU Solvency II regulatory regime for the Insurance Sector will come into force in 2012. The Financial Regulator is deeply involved with industry and their representative bodies in preparation for this. Quantitative Impact Study ("QIS") 3 which completed in June 2007 saw improved participation by Industry. QIS 4, which will run from April 2008 until July 7th for individual companies and until July 31st for Group results, will address a number of outstanding issues including proportionality, intra group transactions and different approaches for the Minimum Capital Requirement (MCR) formula. It is important there be widespread participation by the Insurance Sector in QIS 4 in preparation for the "sea change" in insurance regulation that is taking place.

Shared Services

I want to return again as in previous years to the subject of the IT and HR services provided to the Financial Regulator by the Central Bank and Financial Services Authority of Ireland, especially in the context of value for money, which I believe will be a keynote concern for financial service providers in this new, tougher, business environment.

The structure put in place in 2003 with the creation of the Financial Regulator has been in place for five years and it is timely that this arrangement should be reviewed.

In what I have to say, I must emphasise the Panel fully supports the fundamental legal structure which provides that the Financial Regulator be part of the Central Bank of Ireland. Given the experience over the last year with fragmented regulatory structures in Germany and the UK, the argument for our unitary regulatory model is compelling.

Within this structure, I nevertheless believe that incremental changes can be made to the delivery of shared services to better support the work of the Financial Regulator. By definition, there are fundamental differences in the type of IT and HR environments needed in the Central Bank and the Financial Regulator. The Central Bank is a mature organisation concerned with critical national and global macro-economic issues. The Financial Regulator is a young organisation with a dual consumer and regulatory mandate in what is a unique and complex market. For both operations to be effective, their respective IT and HR platforms and policies must, by definition, be fundamentally different. The Panel has long held the view that the senior management of the Financial Regulator should have more direct management and control over its IT and HR functions if it is to best meet the challenges it faces.

We therefore welcome the imminent opportunity to interact with the Central Bank to articulate industry requirements for both technology and human resources.

For IT, we recommend that the Financial Regulator be able to set its own priorities in the context of the Strategic Plan so that it has the capacity to deliver value for money while meeting all its statutory objectives.

For HR, we again recommend that the Financial Regulator develop its own HR strategy supported by a specific HR plan with tailored policies covering, inter alia, recruitment, promotion, secondments, succession, turnover and mobility, to address its own highly specialist needs.

The Financial Regulator experiences turnover at all management levels which the Panel sees as a continuing reality and a positive factor in populating industry with expertise in financial regulation. Feedback from a pilot personnel exchange initiative between the regulator and industry is encouraging, and the experience thus far would point to supporting an expansion of this programme and its establishment on a more formal footing

**Comment by Grainne Condon –
Senior manager from AIB on secondment to the Financial Regulator for one year**

'My secondment with the Financial Regulator was mutually beneficial and constructive, and I valued the opportunity to contribute to the achievement of the Financial Regulator strategic goals.

Working with the Financial Regulator provided me with a greater insight and appreciation of the regulatory approach being adopted in Ireland. I was impressed at the level of professionalism and commitment within the Financial Regulator and valued the opportunity of working with the team.

The current marketplace challenges are significant both for the Financial Regulator and the financial services industry and developing and fostering successful working relationships and partnerships between us are, I believe, critical to our continued mutual successes.

I am happy to encourage others to continue and develop this process."

Risk

The Irish regulatory structure has performed well during the recent and continuing turmoil in global credit and investment markets. However, with the extraordinary growth and global entanglement of financial markets and instruments, we believe it is an opportune time to review the need for a Strategic Policy Unit within the Financial Regulator to maximise insight and understanding of global market developments in framing appropriate regulatory policy responses. This is particularly relevant in today's uncertain climate and would act as a resource to the senior management of the Financial Regulator in evaluating the impact of international developments on the Irish financial market.

In this context, we are supportive of the business process review currently taking place in the Financial Regulator in relation to core functions such as business risk evaluation, and development of strategic planning. The Panel looks forward to participating in this process.

Comparisons with other jurisdictions

We return to the topic of benchmarking with appropriate regulators, and recommend that the business process review facilitates constructive comparisons. There are lessons to be learned where other jurisdictions get it right and where they get it wrong. The view of the Panel is that the relevant comparator jurisdictions should include the FSA in the United Kingdom and the Singapore Authorities. We suggest the former because of similarities both in a domestic and international context, and the latter because of a close similarity in scale and sophistication to the Irish market.

I am grateful to all the members of the Panel, including Tom Healy, former Chief Executive of the Irish Stock Exchange, who stepped down during the year, for their energy and commitment on behalf of the Panel during 2007.

I also thank our colleagues in the Financial Regulator, at all levels, for their support. Our work is in reality a partnership in achieving the goal of a top quartile regulated market with a capability to compete internationally. We have made real progress together, and I am looking forward to further achievements in 2008.

James Deeny
Chairman
Financial Services Consultative Industry Panel

Panel Activity in 2007

The Panel was active in a number of areas during 2007. The most important issues from the financial services industry perspective were the evaluation of the Financial Regulator's Annual Budget for 2008 and its implication for the levy, the Panel's input into the update of the Financial Regulator's Strategic Plan for 2008, the commissioning of the review of unnecessary regulatory requirements, and the Panel's input into the development and launch of the Stakeholder Protocol. In line with its mandate, the Panel also made submissions to the Financial Regulator on a number of regulatory topics.

Strategic Plan Update for 2008

The Panel suggested the following high level issues for consideration by the Financial Regulator in developing its 2008 Strategic Plan, which is an annual update of the three year 2007-2009 Strategic Plan:

1. Strengthen capability for assessing of market risk and business exposure management in the domestic and international markets (e.g. hedge funds, sub prime, etc).
2. Support education in financial services including compliance and advanced quantitative analysis
3. Continue the input into the marketing of global financial services out of Ireland while recognising that the primary marketing function is the responsibility of industry and the Industrial Development Authority
4. Review operation and implementation of Capital Requirements Directive relating to new banking models and large exposures.
5. Improve knowledge transfer between the Authorisation and Supervisory departments.
6. Increase the internationalisation of Financial Regulator staff through secondments to other financial regulators and consultancies, and by espousing the cause of principles-based regulation in the regulatory regimes of developing countries.

The Financial Regulator was broadly supportive of the Panel's input, if not directly as in the case of items 2, 3 and 4, then by referring them for consideration in the imminent review of business processes

Evaluation of the Financial Regulator's Budget for 2008

The Panel reported to the Department of Finance on its consideration of the Financial Regulator's Budget for 2008, and confirmed the positive and constructive interaction between the Panel sub group and Financial Regulator finance personnel in relation to the composition of the various elements of the actual and budgeted expenditure, and in particular, comparing the budget for 2008 with actual results for both the year to date and the estimated outturn for 2007.

The Panel focused on three main issues in its evaluation of the budget expenditure for 2008, namely, the overall percentage increase in the budget, the significant increase in staffing costs, and transparency and accountability in relation to shared services.

Total budgeted expenditure for 2008 amounting to €55.8 million is projected to exceed the estimated outturn for 2007 by 11%, significantly in excess of inflation for the third year in succession. The Panel would like an indication from the Financial Regulator of what constitutes an appropriate level of expenditure for a "steady state" environment, and what constitutes incremental expenditure arising from, inter alia, growth in the number of regulated entities, or increased complexity of regulation, with a view to achieving lower year on year increases more closely in line with inflation.

Staffing costs are the most significant expenditure item of the Financial Regulator. Pay and pension costs amount to €29.9 million, an increase of 11% on 2007, and with headcount budgeted to rise to 380 by the end of 2008, 32 more than at December 2007, increased staff complement accounts for approximately half of the increase in staff costs.

The Panel appreciates where elements of the additional headcount are required to enable the Financial Regulator to deliver the requirements of regulated entities in highly complex areas (such as Insurance). However, we would also like to see efforts to redeploy people from areas which may be less busy or mission critical; the Panel would expect to see flexibility within the organisation in relation to moving staff around to fulfill strategic business needs.

In each of our budget submissions to date, the Panel has articulated its concerns over the size, scope and need for greater transparency in the arrangements for shared services provided by the Central Bank in respect of the human resources, information technology and physical infrastructural requirements of the Financial Regulator.

Shared service costs are budgeted to increase by 14% to €17.8 million. As previously indicated, the Panel is concerned that the Financial Regulator does not have the most effective means of controlling the quality, cost and method of delivery of the services to its operations in the absolutely critical areas of human resources and information technology in particular.

We have been informed by the Financial Regulator that the CBSFAI is carrying out a major review of these services early in 2008. The Panel has been offered an opportunity to provide input into this process and looks forward to engaging actively with the CBSFAI in relation to its priorities in relation to the provision of such services.

The Panel has also been informed that the Financial Regulator will be embarking on a number of efficiency enhancing measures in 2008, as set out in the strategic plan, including reviews by external consultants of business processes, and benchmarking of key processes with other regulators and comparative businesses. We await the outcome from these initiatives, which we would hope and expect will lead to significant cost-saving opportunities to be identified and factored into a "steady state" zero increase budget for 2009.

Consideration of Formal Regulatory Documents

The busy period of consultations since 2005 stemming from the Lamfalussy Process, the Capital Requirements Directive, the MiFID and the Consumer Protection Code, slowed down significantly in 2007, and the Panel was invited by the Financial Regulator to consider only a small number of specialist issues relating to UCITS. The Panel also responded to the Department of Finance's consultation on the regulation of non-deposit taking lenders.

The Panel's submissions are available on the Consultative Panels section of the Financial Regulator's website.

Regulatory Issues Considered

During 2007, the Panel considered a number of regulatory concerns at length, both at its meetings, and through dedicated sub groups. Major issues considered included the implementation of the MiFID, competition and innovation in financial services, Solvency II, the funding levy, equity release, and the C&AG's VfM Report on the Financial Regulator. Key issues in the credit union movement were also addressed through a joint Consumer/Industry Panel "credit union day" in February.

Survey of Regulatory Requirements

The fourth High Level Goal set out in the Financial Regulator's Strategic Plan 2007-2009 states "Our regulatory approach will facilitate innovation and competitiveness". It further states that this Goal will be achieved by "fostering competitiveness and innovation through the adoption of international best practice and the Government's Better Regulation Principles".

In pursuit of this Goal, in Section 4.1 of the Strategic Plan 2007-2009, the Financial Regulator invited the Panel "to identify and prioritise regulatory requirements that they believe are unnecessary (and open to amendment by the Financial Regulator)".

In response to this invitation, the Panel sought tenders from regulatory specialists within the service providers to survey the regulatory landscape to achieve this objective, mindful of the restraint imposed by the need for any unnecessary regulatory requirements to be "open to amendment by the Financial Regulator".

Since the Panel is concerned with all aspects of the financial services industry, the survey will cover banks and building societies, insurance companies, investment firms, intermediaries, stockbrokers, credit unions and service providers (legal & accounting).

Preliminary results from the survey are expected during the second quarter of 2008, and will be shared with the Financial Regulator as soon as possible.

The Panel's Work Programme for 2008

Review of Unnecessary Regulatory Requirements

Following a request from the Financial Regulator in 2007 to comment on regulations which the Panel believes are both unnecessary and open to amendment by the Financial Regulator, the Panel commissioned KPMG to research this. Results will be available by end of the second quarter of 2008

Shared Services Working Group

A Panel sub group will monitor developments in the delivery of shared services by the Central Bank to the Financial Regulator, especially in the areas of IT and HR

Review of Panel Structure

Current appointments to the Panel expire in October 2008 and Panel members will evaluate the effectiveness of the current arrangements and make recommendations to the Department of Finance if appropriate.

Visit to London/Brussels

It is planned to meet the Practitioners Panel (the UK equivalent of the Industry Panel) to discuss regulatory issues of mutual interest. It is also hoped to meet EU officials and appropriate politicians in Brussels to aid understanding of the Irish regulatory approach

Review of Stakeholder Protocol

The Stakeholder Protocol will be in operation for a year by end June, and the Panel will participate with the Financial Regulator in a review of its achievements at that time

Annual Report 2007

The Panel's Annual Report will be finalised in the second quarter of 2008 and presented to both the Financial Regulator and the Department of Finance

Lamfalussy Review

Through its dedicated subgroup, the Panel will be fully engaged in this review process at EU level

Business Process Review

Panel members will be consulted by Mazars who are carrying out this project aimed at improving the operational efficiency and cost effectiveness of the Financial Regulator

Members of the Consultative Industry Panel

There was one change in Panel membership during the year with the resignation of Tom Healy, outgoing CEO of the Irish Stock Exchange. On behalf of the Panel, the Chairman expresses his appreciation of the contribution Tom made to the Panel's deliberations.

1. **Liam Carberry** Insurance and Mortgage Broker, nominated by the Professional Insurance Brokers Association.
2. **Tony Culley** Associate Director, Allianz Insurance.
3. **James Deeny (Chairman)**, Former CEO of HSBC Ireland and a Director of Hartford Life, PFPC and Finaref
4. **Billy Doyle** CEO Credit Union Development Association.
5. **Pat Farrell** Chief Executive, Irish Banking Federation.
6. **Sarah Goddard** Chief Executive, Dublin International Insurance & Management Association.
7. **Jonathan Goold**, Finance Director and Actuary, Acorn Life, representing the Irish Insurance Federation
8. **Tom Healy**, Chief Executive, the Irish Stock Exchange (to June).
9. **Pat McArdle**, Chief Economist, Ulster Bank Group.
10. **Paul O'Connor**, Head of Wholesale Banking and Risk, Irish Banking Federation, and Secretary of the Federation of International Banks in Ireland
11. **Robert Moynihan** Independent provider of compliance training and consulting services under the brand "Irish Regulatory Training & Consulting".
12. **John Murphy** Head of Regulatory and Operational Risk, Bank of Ireland.
13. **Carmel O'Connor** Partner, PricewaterhouseCoopers.
14. **Aileen O'Donoghue** Director, Financial Services Ireland.

15. **John O'Halloran**, Head of Legal & Secretariat, Irish League of Credit Unions.
16. **Eimer O'Rourke** Head of Retail Banking, Irish Banking Federation, and Secretary of the Irish Mortgage Council.
17. **Gary Palmer**, Chief Executive, Irish Funds Industry Association.
18. **Rachel Panagiodis**, Managing Director, Hansard Europe Limited and Member of the Board of the Irish Insurance Federation.
19. **Sean Quirke**, Qualified financial adviser with New Ireland Assurance Company and an independent Mortgage Intermediary.
20. **Robert Richardson** Chairman of the Irish Association of Investment Managers, and Chief Executive Officer, Pioneer Investment Management Ltd.

Functions of the Panel

Section 57DB of the Central Bank Act 1942 (as inserted by the Central Bank and Financial Services Authority of Ireland Act 2004) sets out the functions of the Consultative Industry Panel as follows:

- a) when the Regulatory Authority so requests, to comment on a policy document or regulatory document, or a proposed policy document or proposed regulatory document, prepared by that Authority;
- b) to provide that Regulatory Authority with comments on levies and fees that that Authority proposes to prescribe under section 33J or 33K;
- c) to provide the Regulatory Authority with comments on that Authority's draft estimate of income and expenditure for each financial year;
- d) to provide the Regulatory Authority with comments on the impact that the conditions and restrictions imposed by that Authority on financial service providers have on the competitiveness of those providers;
- e) to provide the Regulatory Authority with comments with respect to changing trends within the financial services industry that have implications for the functions and responsibilities of that Authority.

Section 57DB above should be read in conjunction with Section 57DF of the Central Bank Act 1942 (as inserted by the Central Bank and Financial Services Authority of Ireland Act 2004), which is set out below.

Section 57DF

- (1) Before making or issuing a policy document or a regulatory document, the Regulatory Authority shall consult each Consultative Panel, unless that Authority believes that the document must be made or issued without delay. In that case, the Regulatory Authority shall consult each of the Panels as soon as possible after the document is made or issued.
- (2) In making or issuing a policy document or regulatory document, the Regulatory Authority shall take into account the advice (if any) provided by a Consultative Panel on any aspect of the document. If the Regulatory Authority declines to give effect to any particular advice provided by the Panel, it shall provide the Panel with a written statement setting out its reasons for declining to give effect to the advice and shall, if the Panel so requires, publish the statement.
- (3) The Minister shall consult each Consultative Panel before approving the Regulatory Authority's draft estimate of income and expenditure for a financial year.

- (4) If the Regulatory Authority makes or issues a policy document or a regulatory document, a failure of that Authority to comply with subsection (1) in relation to the document does not of itself invalidate the document.

It is important to point out that the Panel neither duplicates nor replaces existing industry / representative body relationships with Financial Regulator, but may be seen to stand alone as a "lender of last resort" in a regulatory context for the Financial Services industry in its dealings with the Financial Regulator.

Cost of Panel

Panel members attend meetings and sub-groups on a voluntary basis, and are not paid to participate in Panel work. Limited travel and subsistence allowances are paid in certain cases, and secretarial functions are provided by the Financial Regulator. The direct cost of the Industry Panel for 2007 was € 64,640.

The Panel met 8 times in 2007 (no meetings in July August and December and a briefing session in April).

The average attendance was 15 members (out of an average of 19.5 members)

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