

Reform of Central Bank of Ireland's fitness and probity regime underway

Our analysis of this significant regulatory development



Introduction

In February 2024 the Central Bank of Ireland (“Central Bank”) announced it had commissioned an independent review of its fitness & probity (“F&P”) regime. The review was published in July and makes twelve recommendations, all of which have been accepted by the Central Bank. The implementation of these recommendations will lead to significant reform of the regime and how it is operated. This briefing contains our analysis of this important regulatory development, which will impact all firms and individuals that are subject to the F&P regime.



At a glance

Key potential changes

- Establishment of new core F&P team
- Reduction in number of PCF roles
- Increase in number of PCF interviews within funds sector
- 90-day time limit for processing applications
- Segregation of enforcement team from F&P team
- Establishment of new significant decisions committee

Background

Under the F&P regime an individual is prohibited from performing certain senior roles, known as pre-approval control function (“PCF”) roles, within firms regulated by the Central Bank unless the Central Bank has confirmed it is satisfied the individual is fit and proper.

This means the Central Bank must assess each individual wishing to take up a PCF role and decide whether, in its view, the individual is appropriately capable, honest, ethical and of integrity and financially sound.

Because of the serious consequences of this decision, the assessment engages the individual’s constitutional rights. A consequence of this is the assessment process must be fair and consistent with constitutional and natural justice requirements.

In January 2024, the fairness of the F&P assessment process was the subject of a hugely significant decision by the Irish Financial Services Appeals Tribunal (“IFSAT”) to uphold an appeal by an individual (known as “AB”) against a decision by the Central Bank to refuse to approve his proposed appointment to two PCF roles with a regulated entity, on the basis that he was unfit to

perform those roles.¹ In its decision, which focused on fair procedures, IFSAT found the Central Bank’s decision-making process was flawed, that it had denied AB fair procedures at each stage of the process, in breach of constitutional and natural justice requirements. For detailed analysis and commentary on the IFSAT decision, see our previous briefing [here](#).

In response to the IFSAT decision the Central Bank commissioned this independent review of the F&P regime.

¹ IFSAT decision dated 31 January 2024. Appeal No. 029/2022, AB and Central Bank of Ireland

Review

The review, which was carried out by Andrea Enria, a former Chair of the ECB Supervisory Board, involved extensive engagement with a range of stakeholders and analysis of the F&P practices of several other supervisory authorities.

It suggests that an effective gatekeeping function requires extensive reliance on supervisory judgement. It notes that given the severe potential consequences for firms and individuals arising from the exercise of that supervisory judgement, it must adhere to the highest standards of fairness and transparency.

The review examines the effectiveness and efficiency of the F&P process from the perspective of clarity of supervisor expectations, governance and process fairness and transparency. This identified five key themes which emerged as fundamental principles across all areas.

Themes



01. Supervisory judgement

Any proper assessment of an individual's fitness and probity to perform a specific role must involve both objective and subjective elements. The subjective element or supervisory judgement, is described as an indispensable component of the assessment process and the recommendations in the report are intended to improve the transparency, efficiency and fairness of the exercise of that supervisory judgement.



02. Fairness

Fairness and the perception of fairness is described as a pivotal principle in the F&P process. In AB and the Central Bank, IFSAT found the process had been unfair and several of the recommendations address steps in the process that were described by IFSAT as flawed, most notably those concerning the involvement of the enforcement division of the Central Bank and the interview process.



03. Efficiency

The report notes that "efficiency is a key component of fairness and an approval process that does not deliver timely decision is fundamentally unfair." It notes the negative impact on firms and individuals that flows from an absence of efficiency, a point which was made forcefully by IFSAT in AB and the Central Bank.



04. Proportionality

The report describes the importance of proportionality in the approval process and suggests this is achieved through a risk-based approach to the assessment process whereby higher risk roles, institutions or sectors receive greater scrutiny from the Central Bank, with others following a more streamlined process. This risk-based proportionate approach should also be applied to the due diligence expectations placed on regulated entities.



05. Culture

The report notes the importance of the culture prevailing amongst the Central Bank staff involved in the process in ensuring that the process is perceived as a fair and legitimate exercise of supervisory judgement. In considering culture it draws the distinction between an adversarial approach characteristic of an enforcement investigation and a more inquisitive approach appropriate for a gatekeeping process.

The review found that the conduct of the F&P process by the Central Bank is broadly aligned with other peer jurisdictions across several metrics but highlighted several areas in which the operation of the F&P process is "not always up to the requisite standards of fairness and transparency."² It notes the critical need to address this and puts forward twelve recommendations which flow from the themes identified and which it says "if implemented or clearly reiterated as key elements of internal practices, would go a long way in ensuring that in all cases the Central Bank will exercise the significant powers granted to them by the legislature with professionalism, integrity and respect for fair process."³

² Central Bank of Ireland, Fitness and Probity Review, Andrea Enria, July 2024, p.7

³ Central Bank of Ireland, Fitness and Probity Review, Andrea Enria, July 2024, p.12



Recommendations

01 Fostering industry role in gatekeeping

The Central Bank should provide greater clarity and guidance on its expectations as to the process a regulated firm engages in prior to submitting a PCF application. This should address due diligence and screening, background checks, documentation, and record keeping and monitoring of ongoing fitness and probity.

02 Clear fitness and probity standards

The Central Bank should establish a consolidated single location for standards which should be enhanced by:

- Incorporating more objective standards such as specific qualifications, certifications or experience requirements
- Developing the guidance on the role of executive and non-executive directors and on the specific expectations for independent directors
- Clarifying its approach to assessing collective suitability and diversity within boards.
- Agree a consistent approach to consideration of past events.

03 Governance

- A core F&P team should be established in the Central Bank with responsibility for the entire F&P process. This should include members with legal expertise, underscoring the significant legal nature of the process, but should not include members of the Central Bank's enforcement directorate.
- Consideration should be given to reducing the overall number of PCF roles, and to carrying out more interviews with PCF applicants in the funds industry given the increased size and systemic footprint of the sector in Ireland.

04 Decision making

- A Minded to Refuse Letter should be issued where significant concerns persist throughout the process.
- The Central Bank should establish a significant decisions committee, with responsibility for decision-making in significant decisions where the assessment is potentially leading to a refusal. A Chairperson should be appointed to that committee who is not routinely involved in the assessment stage and also be of sufficiently senior standing to allow for independent challenge. The Chairperson should be

accountable to the Central Bank Commission in respect of the decision-making process.

05 Communication and IT Platform

- An annual information session detailing and explaining the practicalities of the F&P process should be held by the Central Bank, and should be open to regulated entities and potential candidates.
- As a means of reducing the administrative burden on firms and improving the efficiency of the F&P process, ad hoc workshops should be organised to obtain feedback from regulated entities on the Online Portal and practical aspects of the application process.



06 Interview Stage

- An interview notification should be provided at least five days prior to an interview. This should specify the topics to be discussed and identify the Central Bank attendees and their roles.
- Central Bank attendees should be limited to three.
- The duration of the interview (which should be a single interview - see recommendation 7) should be limited to 90 minutes.
- Interviews should remain conversational rather than adversarial and minutes shared with the applicant within 1 week, allowing another week to provide comments. Individuals to be permitted to bring a note keeper or a lawyer as observers.
- Feedback should be provided to the applicant and the regulated entity following an interview.

07 Efficiency of interview process

- A "meet and greet" type interview should not form part of the fitness and probity gatekeeping process.
- A single comprehensive interview be conducted rather than conducting an initial interview followed by a specific interview, particularly when a specific issue is known in advance.

08 Withdrawals

- Feedback should be provided even where a withdrawal occurs as this would provide the individual with valuable clarity on the Central Bank's perspective on their F&P.
- Off-record discussions between the Central Bank and a regulated entity should not take place as a matter of practice, integrity and impartiality as this would ensure that all relevant information is documented and available for review.

09 Management Information

- The Central Bank should implement clear and comprehensive service standards covering all F&P applications. The same timeframe should apply across the board and there should be no exclusion from the service standards.
- The Central Bank should commit to a 90 day timeframe within which it will have concluded all F&P applications with limited opportunities to stop the clock.

10 Quality assurance

An external risk advisor to the Central Bank should oversee a robust quality assurance mechanism conducted by staff of the Central Bank. The output from the process should be provided to a senior Central Bank committee on an annual basis.

11 Complaints procedure

A F&P complaints procedure should be established to address grievances, issues or concerns that arise as part of the approval process or where a withdrawal has occurred. An external risk adviser should be involved to ensure independence, impartiality and to maintain confidentiality.

12 Training

All Central Bank staff involved in the F&P process should receive comprehensive training annually because it is imperative that those involved in the process from the Central Bank are well versed in decision-making elements, fairness of process, proportionality and the duty to give reasons.



Conclusion

In light of the Central Bank's acceptance of the review and its recommendations, it is understood the Central Bank has begun work on the establishment of a dedicated F&P unit and an overhauled F&P regime that reflects the range of recommendations put forward.



How KPMG Law LLP can help

Engagements with the Central Bank as part of a PCF assessment process can have profound professional, financial, employment-related and reputational consequences for firms and individuals. Any party preparing to engage with the Central Bank on a PCF application or on any other matter such as an investigation or enforcement action where they could be the subject of the exercise of a regulatory power, should approach those engagements with the necessary understanding of the relevant legal issues, including the operation of the principles of natural justice, and the requisite level of preparation and expert professional support.

Experienced lawyers from KPMG Law LLP's Financial Services Regulation team and its Employment Law team can provide firms and individuals with confidential legal advice on these issues, including assistance with preparations for interviews and representation at those interviews. Clients can also benefit from access to market-leading fitness and probity experts from KPMG Ireland with unique practical experience gained from the implementation and on-going assurance of clients' fitness and probity compliance controls.

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