UPDATE

Central Bank of Ireland: Supervisory Priorities for 2022

On 8 February 2022, the Central Bank of Ireland ("Central Bank") published the "Securities Markets Risk Outlook Report - A Changing Landscape[1]" ("Report"). In it the Central Bank identifies the key conduct risks in the securities markets, and what it expects regulated firms should do to 'take concrete steps' to effectively identify, mitigate and manage risks. It also outlines its supervisory priorities for securities markets in 2022.

Key Areas

The Report sets out at a high level the following expectations in eight key areas:

Misconduct Risk (Market Abuse)

As the nature, scale and complexities of securities markets evolve, the risk of misconduct increases. Firms and issuers of financial instruments are expected to review and fully understand their obligations under the Market Abuse Regulations, in particular compliance with obligations under the Suspicious Transaction and Order Report regime by both firms and trading venues, and maintenance of insider lists. Trade surveillance systems should be appropriately configured to their respective products and activities to detect market abuse, and management information on trade surveillance needs to be formal, regular and effective. Also highlighted was the need for sufficient internal controls to address the operational risk of trading outside mandates, e.g. breaching limits or investing in assets not within the mandate.

Sustainable Finance

Greenwashing, i.e. inadequate or incorrect disclosure, which can mislead investors to buying products which do not meet their expectations, is damaging to sustainable finance goals. This will be a focus for the Central Bank and ESMA in 2022[2]. In addition to a firm's own statutory obligations on climate and sustainability issues, firms are reminded of the supervisory expectations in the Central Bank's November 2021 climate change and sustainability letter[3]. See our previous client update, "Central Bank of Ireland Signals Expectations on ESG / Sustainability to Irish Regulated Firms"[4].

Governance

Board oversight, clear documented governance structures and appropriate due diligence (of third parties) are highlighted as key components to secure better outcomes for investors and a well governed market. Fund management companies ("FMCs") provide "important infrastructure" for funds, and weak oversight could compromise stability in the sector.

The Central Bank notes that insufficient due diligence and *"the risks relating to ineffective Board oversight of delegates and third party*

[1] https://www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/securities-markets/risk-outlook-reports/securities-markets-risk-outlook-report-2022.pdf?sfvrsn=4

[2] Tackling greenwashing and promoting transparency is a priority for ESMA as announced on 11 February 2022 in its Sustainable Finance Roadmap 2022-2024 (ESMA 30-379-1051)

[3] https://www.centralbank.ie/docs/default-source/news-and-media/press-releases/governor-letter-climate-expectations-november-2021

[4] https://maples.com/en/knowledge-centre/2021/11/cbi-signals-its-expectations-on-esg

intermediaries remain a major factor in the regulatory deficiencies we see across our mandate …" Firms are referred to existing sectoral legislation, regulations and guidance on outsourcing as well as the Central Bank's Guidance on Outsourcing[5] and the Feedback Statement[6] on Consultation Paper 138 (December 2021). For further details see our previous client update, "CP138: Central Bank of Ireland Publishes Cross-Industry Outsourcing Guidance"[7].

The Report makes clear that appropriate due diligence is "essential" before entering into contracts with, and informs the decision to appoint, a delegate / third party, and should uncover issues, not just satisfy regulatory requirements. Funds and their FMCs are also expected to ensure any increase in the nature, scale and complexity of funds under management are considered and resourced appropriately, drawing attention to its findings from its thematic review of CP86[8], that some FMCs have not yet updated their governance frameworks to the expected standard. For further details see our client update "CP86 2.0: Welcome Clarity on Corporate Governance Issues"[9]. The Central Bank drew particular attention to a governance / oversight issue it has flagged previously, namely investment advisers acting as de facto investment managers (i.e. exercising discretion), and having a disproportionate role in the fund's operation. Fund boards and FMCs should provide a detailed rationale for the appointment and role that any appointed investment advisor will fulfil, and regularly scrutinise reports received from investment managers on portfolio management, including any interaction with investment advisors.

For further details see our client update, "CBI Clarifies Expectations on Non-Discretionary Investment Advisors"[10].

Conflicts of Interest

Firms are expected to consider conflicts as part of their daily business operations and have robust processes and procedures to identify any connected or potentially connected party transactions (noting the bespoke rules for funds). Firms should also ensure that all relevant parties understand their obligations and duties on these transactions, and engage rigorously with their fund depositaries and designated persons when such transactions are identified in order to ensure full compliance with all relevant obligations.

Financial Innovation

Funds and FMCs should maintain adequate oversight and due diligence over the selection of index provider for funds they manage and must ensure that dealing and settlement times are consistent with the liquidity profile of the funds managed.

Data

Firms can expect increased Central Bank engagement on data quality issues. Data submitted must be accurate, complete and timely. Any data quality issues should be managed quickly. Outsourcing of data submission must be overseen to ensure it is submitted correctly. Any automated technology used to submit returns must be fit for purpose,

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[5] https://www.centralbank.ie/docs/default-source/publications/consultation-papers/cp138/cross-industry-guidance-on-outsourcing.pdf
[6] https://www.centralbank.ie/docs/default-source/publications/consultation-papers/cp138/feedback-statement-cp138-cross-industry-guidance-on-outsourcing.pdf?sfvrsn=4
[7] https://maples.com/en/knowledge-centre/2021/12/central-bank-of-ireland-publishes-cross-industry-outsourcing-guidance
[8] https://www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/funds/industry-communications/dear-chair-letter---thematic-review-of-fund-management-companies-governance-management-and-effectiveness---20-october-2020.pdf
[9] https://maples.com/en/knowledge-centre/2020/10/cp86-welcome-clarity-on-corporate-governance-issues
[10] https://maples.com/en/knowledge-centre/2022/1/cbi-clarifies-expectations-on-non-discretionary-investment-advisors

appropriate and regularly checked to ensure complete reporting.

Cyber Security

Appropriate operational resilience is essential for firms to mitigate against the risk of cyberattacks, and is a key objective of the Central Bank and Cross Industry Guidance on Operational Resilience[11] published in December 2021. For further details see our client update "CP140: Central Bank of Ireland Publishes Operational Resilience Guidance"[12]. Firms are expected to understand their own specific IT related risks, ensure appropriate risk mitigation and have a risk analysis and oversight program to identify and minimise sources of cybersecurity risk. Automated systems must be reliable, secure and have adequate scalable capability. Regular staff training, emergency procedures, back-up facilities and disaster recovery plans should be established.

Market Dynamics

Funds and FMCs are required to have an appropriate risk management framework in place to identify, manage and mitigate the potential risks arising from use of leverage and liquidity risk within a fund's portfolio. Liquidity and leverage positions should be regularly stress tested and the impact on the fund's performance and redemption requests assessed.

Supervisory Priorities

Reflective of the risks identified, the Report concludes by outlining a non-exhaustive list of the Central Bank's 2022 supervisory priorities which include:

- Completing the common supervisory action ("CSA") on valuations in the funds sector.
- Following up on its 2020 thematic review of fund management companies' governance, management and effectiveness and CSA on UCITS costs and fees.
- Targeting risk assessments focussing particularly on governance, operational and capital risk for depositaries and fund administrators.
- Enforcing specific cases across its mandate and assessing and investigating suspected market abuse.
- Continuing planned supervisory review framework project for the Central Bank's Securities and Markets Supervision Directorate's mandates, and, in particular, reviewing the PRISM impact rating model for funds and related supervisory engagement.

In addition, further revisions to its 'Gatekeeper Approach' and application of its ROBUST principles to evaluate authorisation proposals and business expansion applications from a conduct risk perspective can be expected.

The Central Bank also highlights its close work with ESMA and other European colleagues to develop a more pan-EU approach to wholesale market conduct issues and supervision. International cooperation around conduct supervision will also be fostered with IOSCO members.

Further Information

For further information, please liaise with your usual Maples Group contact or any of the persons listed below.

[11] https://www.centralbank.ie/docs/default-source/publications/consultation-papers/cp138/cross-industry-guidance-on-outsourcing.pdf

[12] https://maples.com/en/knowledge-centre/2021/12/central-bank-of-ireland-publishes-operational-resilience-guidance

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