€3.8 million in fines and counting - what's behind the Central Bank's 2012 agenda

The fear of enforcement action by the Central Bank is currently having a considerable galvanizing effect on management teams at Irish financial services firms, but what is actually happening and what does the Central Bank hope to achieve by its enforcement actions, asks JOSEPH SHANNON.

The Central Bank has levied fines of €3,845,000 so far in 2012 in six published settlement agreements; this compares to total fines of €5,050,000 from ten settlement agreements in the whole of 2011. Half of these settlement agreements have been with IFSC firms and half with domestically-focused firms. While the insurance sector has borne the brunt of the bank's attentions in 2012, MiFID firms continue to feature in relation to transaction reporting infringements. Although the Central Bank has clearly set out its current enforcement priorities, the time delay involved in detecting, investigating and punishing infringements means that settlement agreements may reflect problems that first came to light in a previous year.


Joseph Shannon

So what is the Central Bank actually trying to achieve? The Central Bank has taken enormous steps since the arrival of Matthew Elderfield to promote broad changes in culture and mind-set in Irish financial services firms. Part of this agenda is promoting awareness of the 'credible threat of enforcement.' The first thing that firms facing into an enforcement action discover is that it's no longer just about them – an enforcement action has considerable 'educational value' in promoting compliance elsewhere in an industry or sector. This educational effect is an openly-admitted objective for the Central Bank when deciding whether to take an enforcement action.

The June 2012 settlement agreement for €65,000 with UBS International Life had the immediate effect of throwing focus for firms on the topic of anti-money laundering in particular. This settlement agreement is instructive as it does not even imply that there was a question of actual money laundering – the sanction was for failing to give training to staff on new anti-money laundering legislation for five months after it came into force (and even longer in the case of training the directors of the firm). UBS was also sanctioned for failing to demonstrate that it was meeting the conditions required for placing reliance on 'relevant third parties.'

The administrative sanctions regime used by the Central Bank caps the maximum level of fine that can be levied on corporate entities at €5 million. When the size of the problem dwarves this capped amount, the regulatory value of the sanction tool decreases significantly. The 2009 settlement agreement with Merrill Lynch International Bank related to losses incurred of $456 million – compared to such amounts a regulatory sanction of €5 million lacks serious behaviour-altering effect.

In extreme cases, where a firm is about to draw the wrath of regulators in more than one state for an event, the cynical approach of accepting the maximum €5 million sanction in Ireland and instead concentrating all resolution efforts on business lines in states where the regulator isn't constrained by a maximum fine is economically rational behaviour.

For reasons such as this, the Central Bank has previously sought to have the sanctions cap doubled to €10 million or 10 per cent of turnover for corporates and €1 million for individuals. The variable element would enable the Central Bank to effectively sanction large egregious breaches. However the Central Bank (Supervision and Enforcement) Bill 2011 has been with the Oireachtas Select Committee on Finance since October 2011 with little forward progress evident since that date.
Having said that, there are some other avenues also open to the Central Bank in seeking to mould behaviour - the 2010 anti-money laundering legislation provided for unlimited fines and market abuse legislation also provides for greater tariffs than the administrative sanctions regime - up to €10 million and ten years' imprisonment. However, the Central Bank's Enforcement Strategy document has stated its preference to utilise the administrative sanctions process rather than to use its powers to take summary criminal prosecutions.

It is noteworthy then that the Central Bank sought an order in the High Court in June 2012 against Baxter Financial Services Limited seeking revocation of that firm's authorisation as an investment firm. Baxter consented to the order and even the Central Bank's own press release notes that regulated business amounted to only 1 per cent of that firm's activities, which might indicate that the Central Bank had intended the court application to have a telegraphing effect for other firms of the bank's serious intent rather than being the most expeditious means of disposing with the particular matter at issue.

Most pertinently, with the introduction of the Fitness & Probity regime, having been 'subject to any disciplinary proceedings, issued with a warning, reprimand or other administrative sanction or its equivalent by a financial regulator' may now be a career-ending event for the aspiring financial services executive. This potential for career disruption is undoubtedly helping to concentrate minds and promote on-going focus on compliance matters. Although to date the Central Bank hasn't had a notable history of naming individuals other than sole traders in its settlement agreements, the prospect of irreparable damage to an executive's career by failing foul of Fitness & Probity might yet prove to be the most effective deterrent operated by the Central Bank.

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