

Cyril Roux: Perspectives on financial regulation in Ireland

Speech by Mr Cyril Roux, Deputy Governor (Financial Regulation) of the Central Bank of Ireland, at the Institute of International and European Affairs (IIEA), Dublin, 1 December 2016.

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It is a great pleasure to be here today at the Institute of International and European Affairs, and I'd like to thank chairperson Brendan Halligan and director general Tom Arnold for the invitation.

The Central Bank has a broad mandate – to safeguard stability and protect consumers – but it's also one that is easily misunderstood as being all-encompassing. European and national laws give us a number of powers that we exercise, while also defining the limits of our role.

A core objective of the Central Bank is to be trusted by the public, whose interests we serve. It behoves us to explain clearly what we do and what we don't do. This is why we publish a performance statement every spring in relation to our financial relation function, come in front of the Oireachtas at its discretion, and explain our actions throughout the year.

Today, I'd like to explain a little more about our mandate and our work by offering concrete examples on three areas: residential mortgages, domestic insurance, and Brexit. These are three areas which may seem somewhat disparate at first, but in fact, all serve to illustrate the manner in which the Bank seeks to fulfil its mandate, as well as the roles the Bank doesn't play.

Let me start with residential mortgages.

The Central Bank is the national macroprudential authority for Ireland, meaning it is our role to limit risk to the financial system as a whole.

The mortgage measures, which we introduced in February 2015, are one of the tools by which we limit such risk. The measures also demonstrate the importance we attach to the protection of borrowers.

Borrowers should not over-extend themselves and borrow out of line with their income, nor should they risk entering into negative equity by leaving too little room for price reversals. Lenders for their part should not take excessive credit risk by lending at or beyond the circumstances of their consumers, and are required to ensure, under the Consumer Protection Code, that the mortgage is affordable for the borrower. That is why we impose the mortgage measures. Although we slightly recalibrated them this month, based on the evidence to date, we regard them as a permanent fixture of the regulation of domestic credit.

The Central Bank will shortly appear before the Oireachtas Finance Committee in public session to discuss the Variable Rate Mortgages Bill (2016), which proposes to give the Bank the power to cap variable mortgage rates charged by lenders.

Out of respect to the Committee and its deliberations, I don't intend to make extensive comment on the Bill here, other than to say that the Central Bank will fully explain its reservations about the Bill at the Committee hearing. In a nutshell, we believe that the Bill would conflict and interfere with our monetary and prudential mandates, while having counterproductive effects for borrowers.

Furthermore, the Central Bank has a prudential regulation and consumer protection mandate, but is not a competition authority, and that is an important distinction. There is a competition authority in the country, namely the Competition and Consumer Protection Commission, with which the Bank engages and exchanges to the fullest extent of our respective mandates. The same distinction applies at European level, where the European Commission is the competition

authority while prudential supervision of banks is entrusted to the European Central Bank.

Naturally, however, we will work both to the letter and spirit of any law the Oireachtas may ultimately pass.

In the meantime, it may be useful to explain precisely what our role is in relation to mortgage interest rates.

Our job is to ensure transparency for borrowers and facilitate switching.

This is why, earlier this year, we strengthened our disclosure requirements on lenders.

The Central Bank directed lenders to give sufficient notice when they change the interest rate they charge, to explain in layman's terms the rationale for such changes, and to facilitate their customers who are in a position to switch to a different mortgage or to a different lender.

When lenders do not honour these consumer protection obligations, when they fail to point out to their customers the options open to them, or worse, when they mislead or bring their customers to pay more interest than they should, the Central Bank acts forcefully.

And to emphasise that point, the Central Bank has driven all mortgage lenders to review their mortgage books to ensure that all borrowers who should have been on tracker mortgages *are* on tracker mortgages, and compensated accordingly if incorrect rates were applied.

As part of this programme of work, we have just reprimanded and fined Springboard and ordered it to pay redress for serious failings in its obligations to tracker mortgage customers. The fine of €4.5 million is amongst the largest ever collected by the Central Bank.

Other banks will shortly follow suit in offering redress to affected tracker mortgage customers at the direction of the Central Bank, as part of our wider tracker mortgage examination, which will lead ultimately to all lenders making their borrowers whole.

This critical multi-year project is a powerful example of the Central Bank exercising its mandate to protect consumers.

Let me now move on to a second case study, that of non-life insurance – typically motor and home insurance.

Whereas for many years' motor insurance premiums were low and falling, they have risen much of late.

This has led, understandably, to some people asking why the Central Bank, given its financial regulation and consumer protection mandates, is not doing more to cap, or drive down, premiums.

But while the questions are understandable, they arise from a misunderstanding of our mandate in a market-based economy where prices are set commercially. In the circumstances, they also fail to acknowledge that high premiums are driven by the high cost of claims.

The Central Bank has no role in setting or capping premiums or renewal rates, as that is strictly prohibited under EU law. Put simply, regulators cannot intervene on the *level* of premiums. As with the interest rates of mortgages, capping premiums would conflict with our prudential mandate, mix our role with that of the competition authority, and would likely be counterproductive for policyholders. Price *transparency*, on the other hand, is the area of pricing on which the Bank can intervene, and we do so to the fullest extent. We require insurers to disclose clearly their premiums, and to provide renewal rates sufficiently in advance for people to be able to shop around.

There have been calls for greater transparency around claims data and the Bank will continue to work with Minister of State, Eoghan Murphy and Department of Finance on this matter. The Bank will monitor from next spring the public provision of granular claims data by insurers, as required by the Solvency II directive. We will publish on foot of these disclosures more detailed aggregate claims data for all Irish insurers. However, the Bank is a public institution, with a specific mandate, and strict limits set in European law on its ability to collect and publish commercially sensitive or regulatory data.

More generally, our role in relation to protecting consumers in their dealings with insurance companies is threefold.

First, we monitor continuously and act to ensure the solvency of Irish insurers – so that they always have sufficient funds to pay claims in full.

Second, we set requirements for insurers to treat consumers fairly.

Third, we regulate the large and numerous retail intermediaries sector and root out those who are failing to meet minimum regulatory standards and shouldn't be acting as insurance intermediaries.

On the first point, the Central Bank has intervened forcefully in recent years. We oversaw a combined increase of the solvency capital of insurers in this sector by more than €750m in the past few years. In addition, we have ensured these firms have increased support from their parent companies and have put in place more extensive reinsurance cover in a number of cases.

As a result, all Irish insurers have remained solvent and open for business, despite their extensive losses. Their customers have been protected from the loss which failure of these insurers would have caused.

This in stark contrast to Setanta and Enterprise, which were regulated in Malta and Gibraltar respectively and who “passport” their services into Ireland without need for any further authorisation from the Central Bank. These insurers subsequently failed, leaving their customers without cover. Two more insurers based in Gibraltar have decided to enter the Irish motor insurance market this month, and people who choose to be covered by these insurers will have to rely on the prudential supervision conducted by the Gibraltar regulator for the continued solvency of their underwriters.

On the second point, our consumer protection code and the insurance regulations that we enforce require insurers to provide the correct information when buying an insurance product, and ensure these products are suitable for their consumers. When insurers sell unsuitable products, we mandate redress. This has brought Irish insurance consumers €70m in the case of mis-sold payment protection insurance, and close to €20m for mis-sold credit card insurance.

Our customer protection also covers how claims and complaints must be handled. In addition, insurers and brokers must employ sufficiently qualified staff. We have fined two insurance companies this year for breach of these consumer requirements, following similar fines in previous years.

Finally, we monitor and root out unsuitable retail intermediaries. We turn away unfit or improper applicants and revoke intermediaries that run afoul of our rules. We have also issued prohibition notices in several cases, so that in total, citizens can avail of the service of insurance intermediaries in Ireland in the knowledge they are fit for the role, competent and solvent.

Mention of passporting brings me neatly to my third case study, on Brexit.

Since the UK referendum, there has been a material increase in the number of authorisation

queries from UK-authorized entities. Many of these engagements have been preliminary in nature. But several have moved into the pre-application or application phase, and this is likely to continue in the coming months as UK firms prepare for the possibility of a loss of passporting rights into the EU.

As the Governor stated to this institute in August¹ the Central Bank is committed to providing transparency, consistency and predictability with regard to our regulatory and supervisory responsibilities.

Potential applicants will find the Central Bank to be engaged, efficient, open, and rigorous.

In determining an application for authorisation, we follow clear, published rules and processes derived from EU law, and are guided by our mandate to protect consumers. We are mindful of the fiduciary role of financial actors, and the need to safeguard deposits, premiums, or client assets from loss stemming from incompetence, mis-governance or outright failure.

In authorising a firm, we will want to be satisfied that we are authorising a business or line of business that will be run from Ireland and which we will be effectively supervising. We will expect there to be substantive presence.

Outsourcing and insourcing are acceptable – up to a point. One may outsource activities, but one may not outsource responsibility. A firm may not outsource to the extent that it is effectively hollowing out its regulated activity.

It has been said that the Central Bank does not want to see investment banking or trading in Dublin.

I want to be clear: we do not have such a position. We have not sought to dissuade any such entities from seeking authorisation nor are we planning to do so.

Such applicants, of course, like any other applicant, can expect a rigorous process where we will expect to understand clearly the risks inherent in the business and how they are managed and mitigated. We will need to be satisfied that this is done appropriately and well.

This is no more and no less than would be expected by any applicant for any type of business.

In this regard, it is important to note the collective commitment of supervisors in the EU to safeguard the integrity and the homogeneity of rules and our determination to avoid regulatory arbitrage.

The Irish financial sector is set to grow, and quite possibly to a significant extent. The Central Bank is committed to meeting the challenge. Our workforce planning for next year reflects the additional resources needed to deal with applications that will come our way, and we have built in contingency should the need arise.

As Governor Lane has indicated, due to an expanded universe of regulated and supervised firms, further resources are necessary, and the Central Bank will staff-up as required.

But it's important to note that the Central Bank no longer has a mandate to promote the development of financial services in Ireland. We did have such a mandate in the past and it was judged that this compromised our authorisation and supervisory stance. There is good reason this has been removed from the Act that defines our role. Rather, we have a clear mandate to promote stability and protect consumers.

Conclusion

Residential mortgages, insurance and Brexit have helped me to illustrate, in different but related

ways, the nature of the Central Bank's work.

Our mission – to safeguard stability and protect consumers – is a wide-ranging and critical one. And in my remarks, I've tried to give a flavour of our powers under that mandate, and how we exercise them in the people's interest.

We are a public body. And the public is our first priority.

At the end of a year such of this, it is important to convey that. Citizens need to feel that public institutions are acting in their interest. More so, public institutions need to demonstrate as much.

Part of that process means conveying what we are and what we are not. The Central Bank is the monetary authority, the prudential regulator, the financial consumer protection authority, the macroprudential authority and the resolution authority of Ireland. We are fully committed to fulfilling our wide-ranging duties under these mandates, while recognising that responsibility for many policies that affect the financial conditions facing households and firms lies with the Oireachtas and executed by a range of State bodies. We interact, cooperate and collaborate with the relevant State agencies and a range of national and international bodies, while ensuring we both confine ourselves to our mandate while fully respecting the individual mandates of each organisation.

I hope I have given you a useful perspective on the Central Bank and welcome your questions.

¹ www.centralbank.ie/press-area/speeches/Pages/Macro-FinancialPerspectives.aspx