Investment Funds Update

December 2011 / January 2012

Irish Central Bank launches PRISM

The Central Bank of Ireland (the "Central Bank") has launched a new Probability Risk and Impact System ("PRISM"). The aim of this risk-based supervision framework is to supervise all financial firms using an approach that would make it materially less likely that a firm would fail, and less likely the firm would fail in a manner which would endanger financial stability or consumers. In addition to being a framework for risk-management, PRISM is also a software application and has taken over eighteen months of development.

In order to explain how the system works, the Central Bank has issued a paper entitled "PRISM Explained" to provide greater details on the system.

The paper is divided under the following main sections:

Risk-based supervision

The paper explains that risk-based supervision is based on the notion that all firms are of varying significance to the economy. A regulator can focus on the firms which are the most significant to the economy and on the risks that pose the greatest threats to financial stability or consumers.

A number of different risks can be identified and assessed under PRISM and those likely to result in failure or likely to cause damage to financial stability, can be mitigated.

How PRISM operates

Firms will be categorised based on their levels of impact. A higher level of supervision will be allocated to firms which would have the greatest impact to financial stability or consumers in the event of failure.

Regulated firms are divided into the following categories: high impact, medium-high impact, medium-low impact and low impact. The category applicable will be determined by regulatory returns and will not be subject to appeal.

A firm's risk probability will be based on the following criteria;

- Credit Risk;
- Market Risk;
- Operational Risk;
- Insurance Risk;
- Capital Risk;
- Liquidity Risk;
- Governance Risk;
- Strategy/Business Model Risk;
- Environmental Risk; and
- Conduct Risk.

If a firm falls under the category of medium-high or high, mitigating actions will be taken and a supervisor will open a Risk Mitigation Programme ("RMP") in order to determine actions to mitigate significant risks.

A system of quality assurance has been adopted to ensure appropriate judgements and actions take place.

What PRISM means for individual firms

PRISM was implemented for banks and insurers on 25 November 2011 and will be implemented in late May or early June 2012 for the following;

- credit unions;
- intermediaries;
- investment firms;
- trustees;
- administrators; and
- funds.

Banks and insurers which are not low-impact will be informed of their impact category by December 2011.