

Address by
Mr. Frank Daly, Chairman of NAMA,
to the Corporate Governance Association of Ireland
Thursday, 22nd September 2011

Good morning and thank you for the invitation to address you today.

I propose first of all to give you an outline of NAMA's governance arrangements and to make some observations on corporate governance issues which may be of some interest or relevance to you.

NAMA, by now, is well established. We have recruited close to 200 staff with specialist skills and experience in property, banking, finance, law and related disciplines, mostly recruited from the private sector. Almost without precedent, the agency has had to be built from scratch over a short period of time. We have acquired a portfolio of over 11,000 property loans with balances in excess of €72 billion. These are secured by some 16,000 properties. Our loan book will shortly increase to €74 billion after we acquire a last residual tranche of loans from the participating institutions over the coming weeks.

We have acquired the loans of 850 debtors and we will manage the largest 180 of these debtors directly (their debts account for about 82% of the total). The other 670 debtors are being managed, under delegated authority from NAMA, by some 500 staff in the participating institutions. Most debtors, I should point out, are co-operative and are at various stages of discussion with us on their business plans which, in the majority of cases, will result in agreement on asset disposal schedules and debt repayment targets and, where appropriate, securing unencumbered assets and reversing asset transfers to relatives.

NAMA Governance

As with other statutory bodies, NAMA's governance structure is explicitly set out in legislation, which, in this case, is the NAMA Act 2009. The Board comprises nine members,

seven of whom were appointed by the Minister and two - the CEO of NAMA and the CEO of the NTMA – who are *ex-officio* members. As you can appreciate, the commitment required of the NAMA Board has been intensive: it met on 27 occasions between December 2009 and the end of 2010, during which time it made 219 key decisions. It looks as if it will exceed this number of meetings in 2011.

For the seven appointed members, the terms of office range from three to five years. This is to allow for a phased turnover of members in future. Somewhat unusually, but necessary given the nature of NAMA business, Section 19 (2) of the Act is quite prescriptive about the expertise and experience which Board nominees are required to possess. The section sets out fourteen disciplines, including finance and economics, credit management and accountancy, from which Board members may be appointed. The Minister is required to ensure that, in his opinion, nominees possess expertise or experience in one or more of the areas prescribed.

Committees

The Act is also prescriptive as regards committees of the Board. Again, somewhat unusually, Section 32 provides for the explicit establishment by the Board of four statutory committees: audit, credit, finance and risk. The Audit Committee is comprised of up to six members, of whom two may be external members appointed by the Minister for Finance. In the case of the other committees, all appointments are made by the Board from among its members and from officers of NAMA (the CEO and the seven senior executives).

Section 33 provides that the Board may establish advisory committees and two have been set up to date: the Planning Advisory Committee and the Northern Ireland Advisory Committee. The composition of these committees is again a matter for the Board and they include Board members, officers of NAMA and some external members. The Committees have also had a heavy workload: for instance, over the course of 2010, the Credit Committee met on 54 occasions and the other five committees met on 45 occasions between them.

The Act also provides that the Board may establish subsidiaries. Six subsidiaries have been set up to date, principally with a view to ensuring that debt issued by NAMA as consideration for acquired loans is not treated as part of the General Government Debt. NAMA Investment Limited (or NAMA IL) acts as the holding company for the five other subsidiaries and is the vehicle through which €51 million in shares has been invested by three private investors.

Under the terms of a shareholders' agreement between NAMA and the private investors, NAMA can exercise a veto over decisions taken by NAMA IL. As a result of this, the private investors' ability to control the financial and operating policies of the entity is restricted and NAMA has effective control of the entity. The other subsidiaries, fully owned by the holding company, provide for the legal execution of aspects of NAMA business such as debt issuance and loan acquisition.

Along with observance of the various governance and compliance requirements under the NAMA Act and other applicable legislation such as the Data Protection Acts and the Ethics in Public Office Act, NAMA has also adopted the Department of Finance's **Code of Practice for the Governance of State Bodies**, subject to a number of minor modifications to accommodate NAMA's particular governance structure and other provisions in the NAMA Act.

Commercial mandate

Many of you will know that NAMA is a hybrid which seeks to fuse the best of private and public – what we hope to achieve is to combine the commercial, hard-nosed approach of a private company with public sector accountability and control, very much in line with the trail blazed by NAMA's parent, the NTMA. I have spoken before about the challenge of achieving this and I have to say that the challenge is not getting any easier. NAMA's balance sheet of over €31 billion is very large by any standards and, not unreasonably, there is a huge appetite for information about the loans that constitute that balance sheet, the properties securing them and the debtors to whom they were advanced. The accusation that we are secretive and lacking transparency is one that is regularly, and sometimes lazily, flung in our direction.

If NAMA were a public body, without a commercial remit, there would be far fewer restrictions on its capacity to disclose information about its business. The fact that NAMA is dealing with 850 individual debtors and that those debtors are entitled to the same rights as debtors in any other institution was recognised by the Oireachtas when it enacted Sections 99 and 202 of the NAMA Act. These provisions prohibit us from disclosing confidential information, including information relating to debtors.

But even if we leave aside those legislative constraints on disclosure, there is still the matter of the commercial mandate which has been handed to us by the legislature. NAMA has been given the task of realising the best achievable financial return on its acquired assets and, at the very least, of breaking even over time. This mandate is in direct conflict with full transparency. On a daily basis, we are in discussion with international investors, private equity firms, large property companies and others who are, by and large, sharp operators whose track record suggests that they do not miss too many opportunities. The suggestion seems to be that NAMA should show its hand openly, including showing it to those with whom it is negotiating the sale of loans or facilitating the sale of property. This would be commercial folly, the business equivalent of scoring an own goal from the half-way line – a spectacular, generous but self-defeating gesture.

However, the fact that this debate is still continuing, almost two years after NAMA's establishment, shows how difficult it is to marry a commercial mandate with the transparency that is expected of a public body. I reiterate a point I made recently to the Joint Committee on Finance, Public Expenditure and Reform: NAMA can be a fully commercial operation focused on maximising the return to the taxpayer or it can be a fully transparent public body but it is difficult to see how it can be both.

There is, however, a distinction to be made between transparency and accountability. I know of no other entity where the requirement to be publicly accountable is as extensive as it is in the case of NAMA:

- We are subject to regular scrutiny by two Oireachtas committees and I, as Chairman, and Brendan McDonagh as CEO must appear before the committees whenever called.
- Our accounts are audited by the Comptroller and Auditor General who has full access to all our records and has a permanent presence at our offices. In addition to his conventional audit, the C&AG published a Special Report last November based on his examination of NAMA's acquisition of bank assets.
- Under Sections 13 and 14 of the Act, the Minister for Finance may issue guidelines and directions to NAMA concerning the achievement of the purposes of the Act.

- Section 53 provides that NAMA must submit an Annual Statement to the Minister three months before the beginning of each financial year outlining its proposed objectives, strategies and activities for the year ahead – our Annual Statement for 2012 is to be submitted shortly.
- Section 55 requires NAMA to submit to the Minister, on a quarterly basis, a report on its activities and those of its subsidiaries, including a set of quarterly accounts.
- Under Section 56, the Minister may require NAMA to further report to him on the performance of its functions, incorporating any information or statistics required.

This is very robust accountability framework and we have no difficulty with any of it. Given the scale of NAMA's balance sheet and its importance to the revitalisation of the Irish economy, that level of Oireachtas and Ministerial oversight is justifiable and appropriate.

Corporate Governance

As you will all appreciate, NAMA would not exist if it were not for some momentous failures of corporate governance in Irish financial institutions over much of the past decade. Much has been written about these failures and much remains to be written but it would be well to bear in mind that the lessons that can be learned are not exclusive to the financial services sector and have wider applicability.

Nor is Ireland alone in this respect. In a paper produced for the OECD in 2009, entitled *Corporate Governance Lessons from the Financial Crisis*, Grant Kirkpatrick draws together some of the common cross-national failures in corporate governance which contributed to the crisis we continue to face: insufficient safeguards against excessive risk-taking, inadequate accounting standards and regulatory requirements and the existence of Boards which were ill-equipped, in terms of competency and skills, to understand their business and its attendant risks sufficiently to enable them to challenge executive management. One of the unfortunate aspects of the crisis was the manner in which financial institutions and indeed regulatory regimes tended to mimic their counterparts in other jurisdictions with the result that the root causes of the financial crises in different countries tend to be quite similar.

Closer to home, Mr. Peter Nyberg's report on the banking crisis in Ireland, published in April of this year, provides some food for thought for all institutions, both public and private. He points to a number of lessons to be drawn from his analysis of the banking crisis: the need for professional vigilance, particularly when times are good, and the need to ensure that pay and incentivisation arrangements are structured in such a way as to constrain excessive risk-taking.

An additional interesting point is his emphasis on the need to ensure that there are opportunities and incentives for senior managers and staff to openly discuss and challenge corporate strategies, to the extent that it must become respectable and welcome to express contrarian views which are argued professionally and cogently. This requires an enormous cultural change but, as the events of recent years have shown, it is a vital and necessary change. We know that there were some dissenting voices in the banks during the past decade but they were silenced or sidelined by a culture fixated on short-term profits. We also now know that the gravity-defying profits turned out to be ephemeral but one can understand why a dissenting banker would have become frustrated with being ignored or dismissed as a crank and would have accepted the attractive redundancy or retirement package which was specifically designed to make the exit door particularly appealing for him.

From the perspective of Board-Executive relations generally, the crisis has reminded us of the need to ensure, more than ever, that a Board's role is to be challenging yet supportive of its Executive and that it should focus its energies on strategic oversight rather than on operational meddling. Board meddling in operational matters is wasteful of Board and Executive resources and can be demoralising in its impact. A Board must ensure that a framework is in place which appropriately reserves high-level decisions to itself while specifying the powers and functions delegated to the Executive so that the organisation can operate in an efficient and effective manner. A Board needs also to be mindful of the maxim that good corporate governance is not only about implementation of the required policies but also about ensuring that they are monitored and reviewed. Corporate governance failures often occur, not because of the absence of policies, but because of ineffective implementation and monitoring.

Composition of Boards

The composition of Boards, in both the public and private sectors, has been the focus of some comment in recent times. In the financial institutions, it appears that the appointment process for Boards was a factor in the level of challenge they exerted on executives. In the public sector, the suggestion is made that appointments have tended to be based on political allegiance rather than on suitability and competency. This is changing. In the public sector, it is increasingly the case that expressions of interest are sought for Board positions in agencies under the aegis of various departments. On a personal level, I would suggest that it may be worth reviewing the experience of jurisdictions such as Scotland where a Public Appointments Commissioner regulates appointments to state bodies. However, this is a personal view and a matter for the Government and the Oireachtas.

A particular issue highlighted by Nyberg was the role of auditors and their failure to draw attention to the risky lending practices being adopted by Irish banks. There has been some discussion since of the restricted view that auditors have adopted towards their own role, their contribution to the crisis and the lessons that may be learned from it. I am pleased to see that the European Commission is focusing some attention on this and that it published a Green Paper on the role of statutory audit late last year. The audit profession needs to have a fundamental review of its role in the context of what has happened. As the Nyberg report noted, in focusing on the accuracy of historic accounts, auditors primarily look backwards. This is surely no longer adequate and it seems to me that the profession must reinterpret its role to include a forward-looking focus on business sustainability, long-term business strategies, ethical behaviour and underlying business risks. Huge reliance is placed on their work and, while there is a so-called 'expectations' gap between the statutory role of audit and the public expectation of the level of assurance that audit should offer, I would have thought that the prudent strategic response for the profession would be to move in the direction of fulfilling the public expectation of its role.

Conformance and Performance – a perennial dilemma

Most organisations, certainly those whose core rationale is commercial, are faced with a constant tension between the demands posed by conformance and those posed by performance. Over the past decade, the pendulum swung too far in the direction of performance, with disastrous consequences. A natural reflex reaction now would be to force

the pendulum back too much towards conformance. But we should be vigilant about this. Too much emphasis on conformance and on pointless box-ticking drains enterprise and initiative. While corporate governance failures in the public and private sectors have invariably and rightly focused attention on rule creation and tightening, there is an appropriate balance to be struck between control and initiative. Performance should be aligned with, but not subordinate to, conformance.

Public organisations, in particular, face a plethora of compliance obligations, ranging from statutory requirements to ‘soft law’ Codes. Indeed, the Code of Practice for the Governance of State Bodies incorporates approximately 100 specific compliance requirements. Taken in conjunction with obligations imposed by data protection and FOI legislation, reporting requirements in the form of strategy statements, annual reports, audits and scrutiny by parliamentary committees, there is a risk that some organisations exhaust so much energy on compliance or conformance that they lose sight of their *raison d’etre*. More importantly, there is a risk that a culture of atrophy will develop whereby the prevailing attitude becomes ‘if I do nothing, I can do no wrong’. I say this because, in the difficult economic vista before us, we need more than ever to ensure that our public service is focused on finding innovative and creative responses in circumstances where budgetary resources are much reduced; in other words, we need our public service to make less go further.

Performance, competence and innovation are the way forward for both private and public sectors in Ireland. In our desire to ensure that there will never be a repeat of the trauma we are now experiencing, we must be careful not to stifle the energy and creativity which can hasten our recovery. We need strong, competent and confident people in the public service now more than ever. A focus on costs is entirely understandable but I would caution that there are considerations of performance and quality which are also important. In general, there is a delicate balance to be struck between the demands of conformance and the demands of performance and the challenge for us, in our various organisations, is to find that golden mean.

Thank you for your attention.