

# Corporate Governance - CEBS Guidebook on Internal Governance

Febelfin's answer – 14 January 2011

## Febelfin

Febelfin, the Belgian Financial Sector Federation, is the umbrella organization and shared voice of the financial sector. It defends the latter's views and interests and accepts the challenge of playing an important role as a bridge between its members and a range of national and European parties, including policy-makers, supervisory authorities, professional federations and interest groups.

Febelfin monitors trends and developments and helps its members position themselves accordingly. It informs and advises them on legal, tax, prudential and industrial relations issues, and on technical product matters.

Febelfin shares the values of the sector it represents:

-  Customer service
-  Trust and transparency
-  Dynamism and proactivity

Together with its members, Febelfin aims at expressing these values through the messages and viewpoints the sector communicates. By means of a proactive attitude and maximum openness, it tries to constructively and positively take part in the general social debate and to keep in touch with developments in society. At the same time, Febelfin takes full account of the priority issues of the different pressure groups and determines how best to respond to their views.

## General comment

The Belgian banking industry welcomes the opportunity to comment on the CEBS Consultation Paper regarding the Guidebook on Internal Governance (CP 44).

Referring to its response as for the Green Paper of the European Commission on Corporate Governance in the financial institutions, Febelfin considers Corporate Governance as a very important topic. Moreover, our members share the European Commission's goal of **promoting effective corporate governance for financial institutions** and consequently **support the policy intent underlying the principles laid down in the Green Paper**.

The CEBS Consultation Paper on the Guidebook on Internal Governance is **one of several initiatives at the European and national level that are currently being taken or already have been implemented**. Therefore, Febelfin would like to ask CEBS **to bear in mind the already existing or currently planned initiatives** before considering if further principles are necessary.

Moreover, Febelfin believes that **the concept of internal corporate governance depends on the structure, size and business model of the company concerned**. Given the fact that national provisions are very different one from another, the corporate governance provisions should be adequately flexible and formulated as 'comply or explain' principles. In this respect, Febelfin appreciates that the Consultation Paper states in **paragraph 22** that the **principle of proportionality** applies to all guidelines and that a "one size fits all" approach is impossible.

## Specific Comment

### Principles 1 & 2 – Group Structure

As for **the group structure**, it is important to note that local supervisors always refer to the social interest of the entity they control. Within this context, it is important to note however that if the liability of the management body of a parent company becomes bigger as for the structure, reporting lines and internal control, it is **necessary that the local authorities/supervisors take the group structure and reality more into account**.

**Paragraph 16** stipulates that **the Guidebook generally does not state whether a particular task or responsibility falls within the management body's management or supervisory function**. It states that this will vary according to the national legislation within each Member State. "The crux is that the task or responsibility is fulfilled."

Febelfin appreciates this solution, but one must not forget on the one hand that **laying down the general policy of the institution is first and foremost part of the competence of the**

**Board of Directors**, and on the other hand that **several matters eventually may not be regulated through national provisions and therefore implementation may be difficult.**

**Paragraph 33** emphasises **the role of independent members on the management body.** It goes without saying that Febelfin is well aware of the important role those members can play. However, Febelfin sees **no need to increase the number of independent directors** at the level of the individual entities of a group. Independent directors **do not always offer the best possible guarantee for a sound governance of the subsidiaries, because they are often not (or not sufficiently) familiar with the business nor with the operating procedures.**

The principal aim must be the effective, efficient and sound governance of the (operational) entities. There is however an unmistakable tendency to try to solve any problem by imposing formal conditions as well as structures, not taking into account the specificity of each individual company.

The conjunction of new requirements in terms of number, experience and independence of independent directors could result into a lack of candidates susceptible to respond to the required criteria and could therefore reduce the efficiency of the legal provisions in this respect.

Besides, the presence of a reasonable number of independent directors in the board of directors at the level of the parent company should be a sufficient and efficient guarantee taking into account the principles stated in paragraph 36.

**Paragraph 36** stipulates that **the management body of an institution's parent company should understand not only the corporate organisation of the group but also the purpose of its different entities and the links and relationships between them.** This includes understanding group-specific operational risks, intra-group exposures and how the group's funding, capital and risk profiles could be affected under normal and adverse circumstances. However, **the management body does not have all the tools to manage the problems related to funding, as the interest of the group is not recognized in national law.** Moreover, local supervisors tend to adopt a protective attitude towards the subsidiary under their control.

CEBS is trying to improve the exchange of information intra group and in particular between the parent company and its subsidiaries, but it does not provide the tools for doing so, for instance as for the managing of intra group funding.

**Paragraph 58** stipulates that **a minimum expected time commitment** for all members of the management body should be indicated in a written document (in the same way **paragraph 57** stipulates that the members of the management body should have only **a limited number of mandates** or other professional time-consuming activities ).

Febelfin does **not see the usefulness of imposing this kind of limitations as for the minimum expected time commitment or the number of mandates** at the European level. The existing set of Belgian laws and regulations is sufficient for guaranteeing the required level of the directors' availability and competence and for giving companies enough room, more particularly

in the standing orders of the body concerned, for determining the number of mandates acceptable in those particular circumstances.

**Paragraph 65** states that the members of the management body **need to acquire, maintain and deepen their knowledge and skills to fulfill their responsibilities**. Institutions should ensure that members have **access to individually tailored training programmes** which should take account of any gaps in the knowledge profile the institution needs and members' actual knowledge.

It seems only natural for the members of the management body to keep up and develop the knowledge that pertains to their level of responsibility. **In the opinion of Febelfin, this does not necessarily have to result in cost and time consuming "individually tailored training programmes" that can even lead to misuses.**

#### **Paragraph 72 (Specialised committees) – 75 (Audit Committee) & 78 (Risk Committee)**

The purpose of Principle 10 is to provide for the **organisational functioning** of the institution, in that it states that **the management body should define appropriate internal governance practices and procedures for its own organisation and functioning**. Paragraph 72 ff pertains more particularly to the various specialised committees that can be created.

Within this context, Febelfin would like to point out that the Board as a whole (collegial body) should continue to be in charge of risk management, but indeed with **the possibility (no obligation) to set up a separate risk committee or a similar committee within the Board**.

A number of financial institutions have created separate committees (Risk Committee, Audit Committee, ...), whereas others combine Audit and Risk (and compliance as well, in some cases) into one Committee, because, in their opinion, these aspects are closely interwoven and should better be dealt with together in one single Committee. Other institutions have split up the Audit Committee into a Risk Committee and an Accounts Committee.

According to Febelfin, this should be a **possibility rather than an obligation** given the principle of proportionality and the specific characteristics of each institution. More than ever before, the Board must pay special attention to risk management. However, it should also be pointed out that it is up to the **chairman of the Board of Directors to speak on behalf of the Board as a whole**, as well as **on behalf of** the special Committees which prepare the decisions to be made by the Board. The Board's joint liability towards the general assembly must be maintained. **The role of the Committees within the Board is and must stay a purely advisory role exclusively towards the Board** even if this latest can delegate some less material tasks to committees. Taken into account that the Committees have solely a role towards the Board, they should not intervene at the general assembly unless the Chairman of the Board at its sole discretion decides otherwise.

The Board of Directors must (1) lay down the general risk policy (risk policy, willingness for risk taking, ...) and (2) ensure the follow-up of its application. Defining and drawing up the risk profile is part of corporate strategy and consequently, belongs to the competence of the Board of Directors.

**Paragraph 81-83** impose to **establish, implement and maintain effective policies to identify actual and potential conflicts of interest** so they can be prevented. Without the intention of questioning the usefulness of policies such as these, Febelfin draws the attention to the difficulty of drawing up a list with the maximum number of potential conflicts of interest.

In this respect, Febelfin also wants to stress the huge number of “written policies” institutions must comply with including, among other things:

- the responsibility of the management body (paragraph 43)
- the conflicts of interest within the management body (paragraph 60)
- a general policy for conflicts of interest (paragraph 81)
- the outsourcing policy (paragraph 86)
- the remuneration policy (paragraph 90 & 101)
- a new product approval policy (paragraph 113)
- the compliance policy (paragraph 148).

Febelfin does not contest the need for nor the usefulness of policies such as these, but this will make it difficult for the financial institutions to ensure a systematic coordination and update.

In **paragraph 113**, it is important to point out that **it is not the task of the Board of Directors to approve new products and subsequent changes**. This should be **left to the management body**.

Febelfin welcomes the general principle of strengthening Risk Management.

**Paragraph 132** states that **before any decision is taken by the management body, the Risk Control Function should be addressed**. This rule **does not tie in with the independent managing of the company by the management body**. More particularly as for a change of senior management (see paragraph 132), one cannot understand why a change of person in charge of Human Resources can have an impact on the risk management of the bank. It should be clear that **the management body can be held liable for the decisions of the company** (see paragraph 129 – “the accountability for the decisions taken remains with the business and support units and ultimately with the management body”). So, the management body should involve risk management before taking any decision. A mandatory involvement of the risk management in the decision process does not match with the legal situation in some Member States, as **the management body must manage the company independently and holds the monopoly on decision taking**. The independence in the decision process also extends to the independence to decide who is involved in the process and who is not. For these reasons, **the decision making process in the consultation paper should be reconsidered**.

**Paragraph 144** deals with the **Chief Risk Officer's potential right to veto** within the framework of the decision taking process. This provision does not tie in with some Member States' legal provisions that allow the majority principle concerning Management Board voting. **Febelfin is not in favour of a veto right. A more appropriate measure seems to procure the CRO the right to contact directly the Chairman of the Board.**