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Re: FEE Comments on EBA Consultation Paper on draft Guidelines for assessing the suitability of members of the management body and key function holders of a credit institution (EBA/CP/2013/03)

FEE (the Federation of European Accountants) is pleased to provide you with its comments on the EBA Consultation Paper on draft Guidelines for assessing the suitability of members of the management body and key function holders of a credit institution.

We welcome your consultation as we believe that assessing the suitability of candidates for the management body and key function holders should be treated with care and is an important topic that has been recognised as one of the key issues within corporate governance systems in the recent financial crisis.

FEE represents European accountancy and auditing professions. Those of our members not in public practice include members of management bodies or hold key function positions in various credit institutions. Members of the auditing profession deal with such members during their external audit engagements.

Our responses to the specific questions posed by EBA in the Consultation Paper, as well as additional suggestions on how the guidelines could be improved, are included as the Appendix to this letter. Our responses, which in some instances address the circumstances of financial institutions in general, can be summarised as follows:

- (a) Individual competences and general understanding of the complexity of the business model and its societal impact are essential, especially in credit institutions. Additional guidance on this matter, taking note of the lessons that can be learned from the financial crisis, is therefore appropriate and timely. Competences assigned should be well-balanced between the members of the management body given the subject matter that it deals with. This will support the aim of having an adequate level of collective competences in the management body as a whole.
- (b) Collective competence of the management body vs. individual competences of its members should be elaborated upon in the guidelines.

- (c) The guidelines should be more specific regarding the selection process of management body members as this is the main governing body of any credit institution that is responsible for the relationship with the competent authorities. In particular, we would advise EBA to expand the guidelines in respect of Article 15 *Governance Criteria*.
- (d) EBA is encouraged to closely cooperate with EIOPA to develop coherent assessment principles which can be applied in a practical and proportionate manner throughout the financial sector.

For further information on this letter, please contact Lotte Andersen or Sylwia Kujawa, Project Managers from the FEE Secretariat via email at lotte.andersen@fee.be or sylwia.kujawa@fee.be.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Philip Johnson', with a long horizontal stroke extending to the right.

Philip Johnson
President

Attachments: Appendix

General comments

General

- (1) Current laws, regulation and practice in relation to the role of supervisory authorities in the internal governance of financial institutions (including credit institutions) differ significantly from one EU Member State to another. Enhancement with the aim of a level playing field for supervision would address cross-border considerations and harmonisation. Therefore, FEE fully supports the joint initiatives of competent authorities in charge of assessing the professional skills as well as the collective and individual competences of members of management body in credit institutions. In this context, EBA is encouraged to closely cooperate with EIOPA to develop coherent assessment principles which can be applied in a practical and proportionate manner throughout the financial sector.
- (2) Due care should be given to the proper appointment, competences and composition of the management body as a whole in addition to assessment of the suitability of individual members. It is important that the board works to its full potential and reaches maximum efficiency in its operations. This could be elaborated upon in article 6 of the Guidelines.
- (3) When drafting the guidelines, EBA could more extensively use *the EC Recommendation on the role of non-executive or supervisory directors in listed companies*. Paragraph 11 addresses the qualifications of the non-executive or supervisory directors on issues such as proper balance in terms of qualifications in the board of directors, induction programmes for new members, and disclosures of competences upon appointment and yearly review. These generic requirements are also appropriate for management body members of financial institutions.
- (4) In this context, FEE agrees that the primary responsibility of assessing the initial and ongoing suitability of members of the management body should rest with the credit institution (as highlighted in article 4 and further explained in article 6 of the Guidelines). In addition, it could be further highlighted that choice of candidates for either management body or key function holders should be a matter of sound judgement rather than a matter of fulfilling a list of requirements based on practical and theoretical criteria.
- (5) The guidelines could highlight that the credit institution could carry out the assessment of its functioning as a collective unit on a regular basis through self-assessments as well as external assessment facilitated by an external evaluator. This would be in line with the general 2005 EC recommendation or self-assessment of non-executive directors in listed companies. Such regular self-assessments would also ensure that gaps in current collective competences of the management body and the need for new competences are identified in parallel with the developments in the business model and activities of the credit institution.

Involvement of competent authorities in the selection process of management body members vs. key function holders:

- (6) FEE finds the split between policies for assessment of the management body and the key function holders as set out in article 7, paragraphs 1 and 2, respectively, appropriate. However, it is important that article 7 more clearly explains the differences in the role of the competent authority in the two situations.

- (7) Appointment and assessment of key function holders should be the responsibility of the management body. Generally, the competent authority should not perform the function of a management body by taking responsibility for business decisions that rightfully belong to the credit institution itself.
- (8) With regard to this individual assessment of candidates, competent authorities should generally be more involved in the assessment of suitability of the individual members of management bodies than of key function holders.
- (9) We find the approach of transparency with regard to the assessment techniques used by the competent authority appropriate, as referred to in paragraph 8 of article 11 of the Guidelines. Article 11 should be clarified in order to state that the competent authority will only make general information publicly available. Criteria and/or assessment applicable to particular individuals should not be published.

Governance principles, including diversity in composition of the management body

- (10) Guidelines in respect of general corporate governance criteria are addressed in article 15 “*Governance Criteria*” by inclusion of a reference to the EBA Guidelines on “Internal Governance”. For the general applicability of the Guidelines on assessment of the suitability of the management body, which is core to corporate governance, supplementary guidance on these general corporate governance criteria should be included. Particularly, additional guidelines regarding the following issues could be added in article 15:
 - a. The overall composition and competence of the management body,
 - b. Issues related to independence of the members (which would be the same whether or not the entity is a credit institution) would be relevant to highlight in conjunction with the assessment criteria,
 - c. The time commitment of individual members.
- (11) The key point is balancing skills and experience so that the management body as a *whole* has strong expertise relevant to the activities of the respective credit institution to be able to sufficiently challenge the key function holders in their discharge of duties. Therefore, all members of the management body shall have a collective responsibility for the decisions taken by such body, also in areas they may not have specialist knowledge of. The composition of boards should be based on the principle of “*the best person for the job*”.
- (12) These collective competences should be those that are needed to discharge the duties of the management body. This can be ensured by an appropriate composition that has sufficient diversity among the members. The diversity should be with regard to not only gender, but also background, age, ethnicity etc.
- (13) Within this overall composition of the management body, individual members perform their tasks in the various areas of speciality assigned to them. This will ensure a composition of the management body that possesses a variety of experience and knowledge relevant to the activity of the credit institution in question.
- (14) Depending on the governance structure decided upon by the individual credit institution, subjects discussed by the management body should be further debated by e.g. audit committees and other committees established by the management body. Proper cooperation between the subcommittees is therefore important.

- (15) Appropriate continuous training of individuals who hold responsible positions that deal with complicated risk matters that credit institutions face, e.g. valuation of sophisticated derivative financial instruments, expected losses on loan portfolios, future scarcity of liquidity scenarios, etc., should be ensured. This will facilitate the development of a sufficient pool of talent for selection as members of the management body or key function holders in the future. This issue could be addressed in conjunction with article 15 of the Guidelines.

Definition of key function holders

- (16) Key function holders are defined in article 2 as employees outside the management body whose positions give them significant influence over the direction of the credit institution. This could include senior managers, heads of internal control functions, or the head of a significant EEA branch or third country subsidiary.
- (17) The definition is quite general and needs to be more specific. It should explicitly refer to “management”, having regard to the hierarchy of the credit institution. Furthermore, it should incorporate any function that has the possibility to influence the implementation of the strategy and business model decided by the management body, including those individuals that report directly to the management body or the Chief Executive Officer.

Question 1:

While the principle of proportionality is a general principle within European legislation, it may be desirable to spell out this principle in more detail for the application of the Guidelines. Which criteria could be applied by institutions and competent authorities to differentiate the assessment process and the assessment criteria regarding the nature, scale and complexity of the business of the credit institution and how should such a differentiation look like?

- (18) Yes, due consideration should be given to the impact on small and medium-sized financial institutions to avoid imposing requirements on them that are not proportionate to the size and complexity of their business.
- (19) The criteria could for instance relate to the nature of the credit institution with regard to retail only, retail and corporate, corporate only, investment; stand-alone, parent company with numerous subsidiaries (special care if including other types of financial institutions such as insurance undertakings, investment firms, funds, leasing companies) or subsidiary of a national or foreign parent.

Question 2:

Should competent authorities be required by the Guidelines to assess the policies of institutions for assessing the suitability of key function holders aiming to ensure that institutions have appropriate policies in place ensuring that key function holders would fulfil the suitability requirements?

- (20) No, assessment of policies for suitability of the candidates for key function holders should always remain the primary responsibility of the credit institution. Basically, selection of key function holders should be an autonomous decision of any credit institution. It should be noted that sometimes involvement of supervisory authorities in the selection process of operational personnel may slow down the recruitment process and actual appointment of a favourite candidate who can be targeted by other potential employers.



Appendix – FEE response to specific questions in EBA CP on draft Guidelines for assessing the suitability of members of the management body and key function holders of a credit institution (EBA/CP/2013/03)

- (21) Even though the competent authority is not taking on responsibilities of the management, it may be appropriate to retain the right to veto the proposed appointment of a key function holder or a member of the management body. This situation currently exists in several Member States.