EAPB position on the consultation on joint ESMA/EBA Draft Guidelines on the assessment of the suitability of members of the management body and key function holders (EBA-CP-2016-17)

General remarks

EBA/ESMA drafted guidelines (GL) on the basis of Art. 91 para. 12 CRD IV with the aim of harmonising the EU-wide assessment of the suitability of members of the management body and key function holders. EAPB welcomes these guidelines and the initiative by EBA / ESMA but believes that the draft goes beyond the legal mandate as the institutions are required to create various internal standards. For example, the requirement for a "suitability policy" will result in a strongly increased administrative burden (especially since it applies on a group wide basis). This effect will further increase due to the required monitoring obligation. In general, we think that the GL should not go beyond the scope of the mandate. From a first assessment, it also seems that the guidelines increase supervisory reporting requirements disproportionately asking for too many details. While it is necessary to inform supervisors about the functions of the management body, a situation should be avoided in which supervisors excessively intervene in corporate governance decisions of a bank weakening the decision-making powers of the board. Finally, this would also cause organisational challenges and legal uncertainties.

EAPB also believes that it would be desirable if the tables and templates part of the guidelines would only be used as supporting material for banks which could develop their own internal templates based on EBA's / ESMA's forms adjusting them to their internal needs and specificities. Such flexibility would be particularly important for public and promotional banks as represented by EAPB since these banks have very specific business models often based on public ownership, state protection mechanisms (implicit/explicit guarantees) and a public mission to support the economy. Therefore, a proportional application of the guidelines should be warranted and any new processes established by them should be aligned to the legal set up, risk strategy and ownership structure of the institution.

Finally, we would have preferred if the ECB and EBA/ESMA would have collaborated on a joint framework for fit and proper/suitability requirements as the some institutions will have to comply with two standards on the same subject.

Detailed remarks

Q1: Are there any conflicts between the responsibilities assigned by national company law to a specific function of the management body and the responsibilities assigned by the Guidelines, in particular within paragraph 23, to either the management or supervisory function?

The GL assume that the banks are able to influence the membership of the supervisory board and therefore have a certain discretion in terms of the people represented on the committee (in terms of adequate knowledge, skills, experience and diversity). However, this is not the case for all institutions. In certain cases, the supervisory body is exclusively occupied by employee representatives and the composition of the employee representation is determined by vote. The institution itself has no right, of any kind, to participate in the membership of the supervisory body. This has an influence on all the requirements that demand active control over the membership of the supervisory body.

Moreover, The distinction between supervisory functions and executive functions of the management body could cause uncertainties in some member state's legislations). As a matter of fact, in some cases, the nomination of an executive management body is not compulsory or the management body does not display of executive functions (e.g. limited companies with Board of Directors in France). Consequentially, the subject matter should be broadened reflecting also such specificities of national company law.

Q2: Are the subject matter, scope and definitions sufficiently clear?

Object matter, scope and definitions seem sufficiently clear. Nevertheless, a definition of the supervisory and executive powers of the management body and its members is missing One definition

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is available under point 17 on EBA's draft guidelines on governance. This definition, however, does not reflect all forms of company set ups as prevalent in the EU (please see response to question 1).

Q3: Is the scope of assessments of key function holders by CRD institutions appropriate and sufficiently clear?

The role of the supervisor in the nomination and assessment of key function holders still leaves room for further questions. Even if members of the management body need an authorisation from the supervisor, applying the same authorisation procedure for key function holders would only create ambiguity regarding the role of the supervisor in the internal governance of the bank and cause additional organisational burden and legal uncertainties concerning recruitment and contractual provisions of key function holders.

- Para. 21: Under national law the obligation to disclose to the supervisory authority the taking on of an additional directorship is usually the responsibility of the concerned members themselves. Particularly in the case of supervisory board members, an institution is unable to ensure, at all times, that these members are aware of the taking on of additional directorships. Accordingly, the regulation on the taking on of mandates should be limited to those of which the institution has been made aware.

- In para. 29-32, criteria for the suitability of "key function holders" are given. The requirements for an initial and recurring suitability assessment of "key function holders" may not (permanently) match the criteria for executive board members. The administrative burden seems disproportionate, particularly if, for all events involving "key function holders" (para. 30), an in-depth assessment must always be carried out at the assessment level of executive board members. In addition to this, the legal basis on which the requirements for the suitability of "key function holders" are based seems unclear. Art. 91 para. 12 CRD IV only refers to "members of the management body". We suggest not basing the assessment standard for "key function holders", for the events in para. 30, on the executive board assessment standard.

- Para. 37: The obligations regarding the sufficient time commitment of board members, which are anchored in national legislation, are directed predominantly at the members themselves. Institutions shouldn't be additionally be obliged to comply with this requirement as they only have limited knowledge of the additional time commitments of its board members - this is particularly true of supervisory board members. The assessment obligation, in accordance with para. 37, including the substantiations in para. 39, should therefore be restricted to the information available to the institution.

- Para. 42: The time commitment of board members - supervisory board members in particular - outside meeting times is generally unknown by the institution. In this case, the regulation should be limited to the available information. Para. 44 requires institutions to document and evaluate the other activities of their board members, provided that they are informed thereof or have found out via other means. This represents an excessive intrusion into the private spheres of board members. When assessing time availability, only professional aspects should be taken into consideration. The extremely vague reference to "all external professional, political and other functions and relevant activities" creates considerable legal uncertainly in terms of the institutions' potential documentation and evaluation obligation. The regulation should thus be removed.

Q4: Do you agree with this approach to the proportionality principle and consider that it will help in the practical implementation of the guidelines? Which aspects are not practical and the reasons why?

When applying the principle of proportionality, the special case of public and promotional banks as represented by EAPB should be considered. These banks can have a significant balance sheet size despite their very narrow business activities and limited mandates to operate in low risk sectors. Therefore, public and promotional banks often have a relatively small number of staff in proportion to their balance sheet totals. Thus, staff size should also be included in the list of criteria for the application of the principle of proportionality.

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Q5: Do you think that a more proportionate application of any aspect of the Guidelines could be introduced? When providing your answer please specify which aspects and the reasons why. In this respect, institutions are asked to provide quantitative and qualitative information about the size, internal organisation and the nature, scale and complexity of their activities to support their answers.

Para. 34: Section 4 of the draft GL describes the nature of the principle of proportionality. However, proportionality is not taken into account sufficiently in the other sections of the draft Guidelines. Specific links can only be found in two paragraphs of the draft Guidelines (paragraphs 141. a. and 169). The principle of proportionality should generally be applied to the whole assessment process. In particular, application of the principle of proportionality should not be barred automatically in the case of significant institutions since promotional banks in particular might be significant due to their size, but still have a risk adverse business model benefiting from a state guarantee while not maximizing profit, but rather promoting public policy objectives. Such business models of central, regional and local promotional banks should be reflected in the GL.

Therefore, para. 34 should read as follows: "Institutions should take into account their size, internal organisation, ***the degree of riskiness of the business model*** and the nature […]"

Para 36. should read as follows: "the underlying business model and strategy *(e.g. a **buy to hold strategy**), the* degree of riskiness of the business model, the nature and complexity of the business activities, and the institution's organisational structure".

Moreover, the size and the composition of the management body should be taken into consideration for a more proportionate application of the guidelines. Given specific legal provisions driving a bank's corporate governance and set up, it can become very difficult to fulfil all requirements as laid down in the draft guidelines. If justified, more flexibility should be allowed for.

Q7: Are the guidelines in Title II regarding the notions of suitability appropriate and sufficiently clear?

The notions of suitability are sufficiently clear. While they are very helpful, it would still be hard to implement them in their entirety (i.e. Annex II on Skills). Therefore, it would be adviseable to see the notions rather as guidance and not binding requirements. For this purpose, it would be useful to come up with a broader concept which should have leaner structures and be less prescriptive.

- Para. 72 (b) should read as follows: "**extraordinary** financial and business performance of entities owned […]"

- Para. 77: The wording "political influence or political relationships" is rather vague. The same applies for paragraphs 123 and 124. In the case of public promotional banks in public ownership which have been founded by central, regional or local governments in order to pursue public policy objectives, certain members of the supervisory board are defined by the law or statutes establishing the institution, in part to make sure that the public policy objectives are achieved. Those ex officio members are members of the central, regional or local government holding political positions. There are always several representatives of the respective government present in the supervisory board of the promotional institutions with different political backgrounds and portfolios. Therefore, the fact that members of the supervisory board are holding a political position at the same time does not, per se, constitute a conflict of interest since the promotional bank has been established for the purpose of pursuing promotional policy purposes. Also, these ex officio members are linked to the government in its function as owner of the institution. This should not lead to the assumption that they are generally considered as being not 'independent'. When assessing the independence of members of the supervisory board, the founding purpose of public promotional institutions must be borne in mind. As laid down in the founding laws of these institutions, they have been set up in order to pursue public promotional objectives. The ex officio members are represented in the supervisory board in order to ensure that the strategy and business model of the institution are in line with these public goals. Due to the fact that the ex officio members come from different political backgrounds while being responsible for different portfolios as well, it has to be stressed that the composition of the supervisory board is complemented by other 'independent' members.

Q8: Are the guidelines within Title III regarding the Human and financial resources for training of members of the management body appropriate and sufficiently clear?

The guidelines are sufficiently clear but the requirements incorporated in them could cause a significant cost increase and are not justified given the competences of the members of the management body. EAPB would prefer if instead, the nomination committee could design the induction and training policy. Further to that, a 6 months period imposed on an individual member of the management body for completing all the requirements should be refrained from and instead, the requirements should be set more globally on the overall management body. Even if the guidelines are perceived as helpful on a bank level, they should not be too prescriptive and respect specific institutional set ups.

Q9: Are the guidelines in Title IV regarding diversity appropriate and sufficiently clear?

- Para. 96: Participation of employee representatives in the executive board is not common. It should therefore be clarified in the GL that the suggestion for participation by employee representatives in para. 96 refers to the "management body in its supervisory function".

- Para. 85 sets out the overall framework for an "induction and training policy". Responsibilities for the development of a "detailed training programme" should also be defined here. The specification of a training programme that includes members of the executive and supervisory boards must be appropriate. The specification for a detailed training programme seems excessive, especially since both the executive and supervisory board are permanently supported by their specialist divisions and various (specialist) committees (para. 87). Furthermore, the specification of an evaluation process to assess the training programme results in an additional administrative burden.

Q10: Are the guidelines in Title V regarding the suitability policy and governance arrangements appropriate and sufficiently clear?

Para. 117 should be phrased as follows: “The management body should, **as far as possible**, identify and select qualified and experienced members and ensure appropriate succession planning for the management body that is consistent with all legal requirements regarding composition, appointment or succession of the management body.”

The identification and selection of members of the management body in its supervisory function is limited to positions which are not taken by employee representatives as required by law and chosen by vote. Although the necessary consistency with legal requirements is stated, an additional clarification is suggested.

Other than that, the guidelines seem clear and useful but need further clarification. Since they regroup several aspects it would however be convenient if the respective bank could apply its own due diligence or followed more general, formalised procedures for the fulfilment of these guidelines.

Q11: Are the guidelines in Title VI regarding the assessment of suitability by institutions appropriate and sufficiently clear?

In accordance with para. 125, the nomination committee is responsible for ensuring the individual and collective suitability assessment of the members of the management body. In addition to that, the supervisory board is responsible for the final decision regarding suitability. This regulation is particularly problematic in terms of a suitability assessment of members of the supervisory board who are appointed at the decision of the general assembly. On the basis of para. 127, banks should inform their shareholders of the result of the collective and individual suitability assessment before the general meeting makes an appointment decision. Should the general meeting appoint a member who has not been assessed or proposed by the institution, the banks should assess suitability within three weeks of the general assembly at the latest and, in the case of a negative result, inform the supervisor and the shareholders. The individual suitability assessment of potential new members of the supervisory board by the supervisory board itself or its nomination committee, which is required in accordance with para. 127, would affect the legally, or otherwise, secured appointment powers of the shareholders. In particular for supervisory board members, who belong to the supervisory board on the basis of the owner's appointment powers based on the statutes or other regulations, considerable

conflicts of interest could arise through the inclusion of individual suitability assessment. Conflicts of interest should also be avoided for bank employees associated with the decision-making process. For these reasons, the assessment of individual suitability falls legitimately under the responsibility of the supervisory authority. The provision in para. 127 should thus be revised so that institutions, in particular, do not have to conduct any individual suitability assessments of supervisory board members. Such a prescribed suitability assessment and systematic review to it would also be too burdensome and should only be considered in rare cases or in the event of any substantial change or development.

Q12 Are the guidelines with regard to the timing (ex-ante) of the competent authority's assessment process appropriate and sufficiently clear?

A suitability assessment period of 3 to 4 months seems too long. EAPB would suggest maintaining the flexibility of submitting information on a candidate before or after the nomination.

If all selection criteria are to be considered at once, finding a suitable candidate will become a lengthy process and a suitability assessment period o more than 3 months would unnecessarily prolong the process. Moreover, an ex-ante assessment process seems to be difficult to implement in cases when a member of the management body is elected. Moreover, another question also arises on how to proceed with contracts of already employed key function holders who would obtain a negative feedback after the competent authority's suitability assessment.

Q13: Which other costs or impediments and benefits would be caused by an ex-ante assessment by the competent authority?

Based on para. 161, supervisory authorities should conduct suitability assessments of new or reappointed board members before appointment (ex-ante assessment). Any deviation from this should only be possible in justified cases. The corresponding time specification for the assessment process by the supervisory authorities should be at least 3 and a maximum of 4 months (para. 166). In the question (Q13) it is already conceded that the currently used ex-post assessment (suitability assessment after appointment) reduces the amount of time between the start of the appointment process and the appointment, whereas an ex-ante assessment minimises risk. In this context, we would like to highlight that an ex-ante assessment undermines existing competencies and responsibilities in the appointment of members of the management body and would essentially challenge the procedures for the appointment of board members. From the experience of banking practices, there is the risk that appointment processes of this kind could easily take a year or more. Such a time span would considerably exacerbate the selection of otherwise committed candidates due to a lack of planning security and could essentially reduce the attractiveness of board membership at banks. Furthermore, periodic extension of the appointment period would lead to confidentiality risks associated with potential damage to reputation of the institution and the candidates. Thus, we think that an ex-ante assessment is not suitable in this context.

Q14: Which other costs or impediments and benefits would be caused by an ex-post assessment by the competent authority?

An ex-post assessment could become necessary in case of an «empty seat» situation. This is however rarely the case and can be prevented with lists of potential candidates.

Q15: Are the guidelines within Title VII regarding the suitability assessment by competent authorities appropriate and sufficiently clear?

The guidelines are clear. At the same time, it seems that they empower the competent authority with regards to governance issues. Following these guidelines, there would be greater interventionism, more concrete but also stricter and more formalised requirements set by supervisors. Therefore, it would be prefered if a more simplified approach is chosen offering banks a check list, templates and a limited amount o more general provisions.

Q16: Is the template for a matrix to assess the collective competence of members of the management body appropriate and sufficiently clear?

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The proposed template for a matrix is a possible starting point but too detailed. Banks should keep the flexibility to develop their own matrix following the criteria which seem most important to the individual institution.

Q18: Are the documentation requirements for initial appointments appropriate and sufficiently clear?

The documentation requirements are sufficiently clear but entail aspects to which it could be difficult providing further information (e.g. list of reference persons and their contact details). Other than that, it should be possible to fulfil the documentation requirements. A way to facilitate the process would be to display these requirements in a template style format which would have to be filled in a survey-style.

Q19: What level of resource (financial and other) would be required to implement and comply with the Guidelines (IT costs, training costs, staff costs, etc., differentiated between one off and ongoing costs)?

While it is not yet possible to assess the overall costs, the new requirements imposed by these guidelines would certainly cause a significant cost increase in the area of induction and training. Moreover, they would notably increase administrative costs and burden since most of the aspects linked to the guidelines would have to be prepared, analysed and submitted by additional staff. Some workload could be taken if the guidelines would offer precise templates and survey-like forms accompanied by explanatory texts so that they could be completed by the respective individual.

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