

Comments  
on the Basel Committee on Banking Supervision  
Consultative Document  
“Principles for enhancing corporate governance”

The Association of German Banks welcomes the review of the Basel Committee’s principles, which were last revised in 2006. The financial crisis has made it necessary also to examine corporate governance practices for signs of weakness. We share the Basel Committee’s view that it is especially important for the members of bodies exercising an oversight function to be suitably qualified for their positions. If the principles are revised, it must be ensured that – as at present – they are formulated as guidance only rather than legally or de facto binding rules.

The key areas identified by the consultative document as requiring special action – i.e. board practices, senior management, risk management and internal controls, compensation, complex or opaque structures, disclosure and transparency – are already covered by existing or recently implemented regulation at international or national level. In April 2009, for example, the European Commission issued principles on the remuneration of risk-taking staff in financial institutions and on 15 February 2005 it adopted its Recommendation on the Role of Non-executive or Supervisory Directors of Listed Companies and on the Committees of the (Supervisory) Board. April 2009 also saw the Financial Stability Board issue Principles for Sound Compensation Practice, which were followed in September 2009 by accompanying implementation standards. Among the measures taken at national level in Germany, for example, the Act for the Strengthening of Financial Markets and Insurance (*Gesetz zur Stärkung der Finanzmarkt- und der Versicherungsaufsicht*) of 29 July 2009 requires financial regulators to set higher capital and liquidity requirements, report risk concentrations within groups and tighten qualitative requirements. Persons appointed to a bank’s supervisory or administrative board have to satisfy certain criteria concerning, among other things, their expertise. To avoid conflicts of interest, moreover, no more than two former senior managers of a bank are permitted to sit on its supervisory or administrative board. Listed companies also have to comply with a rule inserted into the German Stock Corporation Act pursuant to the Act on the Appropriateness of Management Board Compensation of 31 July 2009 (*Gesetz zur Angemessenheit der Vorstandsvergütung*). This stipulates that a former member of a listed company’s management board may only be appointed to its supervisory board after a “cooling off” period of at least two years unless the appointment is made at the suggestion of shareholders who together hold more than 25% of the voting rights in the company. In

addition, the German Act to Modernise Accounting Law of 25 May 2009 (*Bilanzrechtsmodernisierungsgesetz*) reemphasises, among other things, the supervisory board's duty to monitor the company's risk management system. The Basel Committee's guidelines should therefore apply only in areas where no equivalent rules are already in place.

Against this background, the proposed revisions and related comments are too detailed and define requirements too specifically. We see a real danger of the revised principles ending up as a box-ticking exercise instead of a process-oriented approach. While regulatory frameworks and board systems differ widely from one jurisdiction to another, this is not clearly addressed in the paper. Though paragraph 10, for example, recognises the distinction between a supervisory board and a management board, the following paragraphs fail to take account of the precise nature of this distinction. A supervisory board in a country with two-tier boards would not run day-to-day operations, for instance, or have "ultimate responsibility" (see paragraph 20).