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Secretariat of the Basel Committee on
Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

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Dear Sir / Madam,

Deutsche Bank response to the consultation on corporate governance principles for banks

Deutsche Bank ("DB") welcomes the opportunity to comment on the Basel Committee on Banking Supervision proposals for corporate governance principles for banks ("Principles"). We understand that this update reflects changes to the financial sector landscape and agree that ongoing awareness and effort is needed to ensure high standards in the financial sector. This proposal provides a helpful focus on accountability and the alignment between business strategies and good governance.

DB is broadly supportive of the updates to the Principles. We highlight some suggested areas for further refinement. These relate mainly to the following key themes:

- **Two-Tier Boards:** The introduction to the revised Principles makes clear that the intent is to encourage sound corporate governance under diverse board structures and not to advocate any specific structure. We strongly support that aim but believe where drafting revisions that there are places where changes are required to ensure that the guidelines encompass all board structures.
- **Consistency:** Some changes in terminology, clarification of definitions and alignment on wording would be helpful to ensure Member jurisdictions and banks have a correct understanding of what is expected under the Principles.

We have elaborated on these points in more detail below. Overall, this document provides a helpful resource for keeping in line with changes and developing greater awareness of key risks and warning signs in the financial services sector. We hope that you find these comments useful and we would be very happy to discuss them further.

Yours sincerely,

A handwritten signature in dark ink, appearing to read 'Daniel Trinder'.

Daniel Trinder
Global Head of Regulatory Policy



Deutsche Bank comments on Guidelines on Corporate Governance Principles for Banks

General comments

We welcome the fact that in the introduction the Committee explicitly recognises the need for the Principles to be applied in a way which reflects differences between jurisdictions and the diversity of board structures that currently exist.

As currently drafted, however, there appears to be an inconsistency between item 12, which states that, “the Committee recognises that there are significant differences in the legislative and regulatory frameworks across countries, which may restrict the application of certain principles or provisions therein” and item 14 which states that “the principles set forth in this document are applicable regardless of whether or not a jurisdiction chooses to adopt the Committee’s regulatory framework”. This second point risks undermining the flexibility captured in the first point and also could be read to transform the Principles into binding rules rather than guidance. To avoid any confusion, we would recommend revision of the drafting in item 14 to clarify the Committee’s intent and ensure jurisdictional differences can be accommodated.

Furthermore, although the principle of proportionality is expressed in item 13, it would be helpful if it were referred to more explicitly in the body text of the Principles so as to ensure that it is taken into account where appropriate.

In addition and notwithstanding the statement in item 16, there remain some places within the Principles where further clarification is required as to how they should be interpreted in relation to different board structures. Further details of these specific points are set out below.

Principle 1: Board’s overall responsibilities

The board has overall responsibility for the bank, including approving and overseeing the implementation of the bank’s strategic objectives, governance framework and corporate culture. The board is also responsible for providing oversight of senior management.

Item 22 makes reference to the duty of care of the members of the board. According to the second sentence of the definition of “duty of care” there is a reference to an OECD document stating that this is “[o]ften interpreted as requiring board members to approach the affairs of the company the same way that a ‘prudent person’ would approach his or her own affairs”. To prevent confusion over the relationship with the OECD language and avoid potential conflicts with other definitions and interpretations according to applicable law we suggest removing the second sentence and OECD reference from the glossary definition of “duty of care”.

In the board responsibilities set out in item 23 there is a reference to a requirement for the board to develop the bank’s risk appetite “along with senior management and the CRO”. This may suggest that the CRO would not be a member of the board, whereas for some institutions it would be entirely appropriate for the CRO to sit on the Management Board. To avoid any confusion we would suggest amending this point to clarify; “develop, along with senior management and the CRO (where not already a member of the board) the banks’ risk appetite...”

Overall, we welcome references to “risk culture” within the Principles. The importance of attitudes and behaviours related to risk awareness, risk taking and risk management could be further enhanced by including additional references to risk culture in the Corporate Culture and Values section of Principle 1. Specifically, we would propose the following amendments (marked in bold):

- **Item 27** – A fundamental component of good governance is a demonstrated corporate culture of reinforcing appropriate norms for responsible and ethical behaviour. These norms are especially critical in terms of a bank’s risk awareness, risk-taking and risk management (“**risk culture**”).
- **Item 30, first bullet point** - Employees should be encouraged and able to communicate, confidentially and without the risk of reprisal, legitimate concerns about illegal, unethical or questionable practices. This can be facilitated through a well communicated policy and adequate procedures and processes, consistent with national law, which allow employees to communicate material and bona fide concerns and observations of any violations in a



confidential way (e.g. whistle blower policy). This includes communicating material concerns to the bank's supervisor. **Such policies are unlikely to be sufficient in isolation and require the support by a robust risk culture that enables effective challenge.**

- **Items 39 - 41** - There should be explicit reference to discharging responsibilities in line with the bank's risk culture and for promoting a strong risk culture in guidance for second and third lines of defence as well.

Principle 2: Board qualifications and composition

Board members should be and remain qualified, individually and collectively, for their positions. They should understand their oversight and corporate governance role and be able to exercise sound, objective judgment about the affairs of the bank

Our understanding is that Principle 2 focuses on the supervisory function and, therefore, would refer to the Supervisory Board under a two-tier-board system. This could be clarified at the beginning of Principle 2.

The requirement in items 45 and 52 for a "sufficient" number of independent directors could be problematic for banks embedded in a wider group structure. It is appropriate and common practice for the parent bank in these situations to have representatives on the Supervisory Board of subsidiary banks which is under its control. This also makes sense from an overall governance perspective as it ensures alignment with the business and risk strategy etc. To resolve this issue we would suggest clarifying the wording in items 45 and 52 to replace "sufficient" with "appropriate" in order to allow for flexibility for appointments at the subsidiary level.

Principle 3: Board's own structure and practices

The board should define appropriate governance structures and practices for its own work, and put in place the means for such practices to be followed and periodically reviewed for ongoing effectiveness.

As drafted, we are concerned that elements of this Principle may undermine the stated aim of the Principles not to favour any board structure over another and to allow for jurisdictional differences.

Item 60 and item 70 state that the chair of the board should not chair any committees, specifically not the risk committee, in order to promote 'checks and balances'. However, under a two-tier structure, this would affect the chairman's ability to perform duties as Chairman of the Supervisory Board. It is fairly common in jurisdictions where two-tier board structures are applied that the Chairman of the Supervisory Board chairs the Risk Committee and other board committees (except the Audit Committee). Also, the Chairman of the Supervisory Board represents the Supervisory Board to the Management Board. In this capacity, the Chairman of the Supervisory Board maintains regular contact with the Management Board and consults with it on corporate and strategic matters (including, but not limited to, risk situation, risk management and compliance of the company). We, therefore, would recommend that the language in items 60 and 70 be amended to clarify flexibility in their application to two-tier board structures.

Item 70 also states that the majority of members of the risk committee should be "independent directors". We note that in accordance with German co-determination rules, DB's Supervisory Board is composed of equal numbers of shareholder representatives and employee representatives. Given the participation of employee representatives in the risk committee (and other committees), we would welcome clarification that "independent directors" can include employee representatives, or the "majority" requirement should be relaxed. As general rule, the requirement of independence should be applied, as appropriate, for subsidiary banks embedded in a group structure (see in this respect our comments in Principle 2 in relation to item 45 and 52).

In the section relating to conflicts of interest, whilst we would strongly endorse the requirement for the board to ensure that appropriate policies are developed and monitored, we have concerns about the scope of the requirements, particularly as they relate to disclosure. There is a risk that the proposed public disclosure requirement would conflict with general confidentiality obligations



applied to the board (in both its supervisory and management functions). To remove this risk we would propose simply requiring the board to ensure “appropriate disclosure (taking, *inter alia*, into account the board’s confidentiality obligations under national law)” of conflicts in item 83. In addition, we would suggest that it be clarified in item 81 that the conflicts in scope as well as their management are “consistent with national law and supervisory standards” – at present the phrasing is ambiguous. Also, as the sixth bullet point of item 82 seems to assume that any transactions with related parties be made on an arm’s length basis, it should be made clear that any exemptions deriving from national law concerning groups of companies shall remain unaffected.

Principle 4: Senior management

Under the direction and oversight of the board, senior management should carry out and manage the bank’s activities in a manner consistent with the business strategy, risk appetite, incentive compensation and other policies approved by the board.

We are supportive of efforts to unite current strategies with the operational structure of the organisation and note that this is in concert with the approach already being taken within DB (such as by way of the House of Governance initiative aiming at promoting – as stated in item 91 – “accountability and transparency throughout the bank”). We also appreciate that this section is not prescriptive but instead focuses on a holistic approach, sharing best practice and ensuring that best practices are shared regularly and efficiently.

We would, however, want to propose one edit to item 92 to further highlight the importance of risk culture. This could be achieved by changing the text to read: “...consistent with the direction given by the board, risk management systems, **risk culture**, processes and controls...”

Principle 5: Governance of group structures

In a group structure, the board of the parent company has the overall responsibility for the group and for ensuring that there is a clear governance framework appropriate to the structure, business and risks of the group and its entities. The board and senior management should know and understand the bank’s operational structure and the risks that it poses.

We are supportive of this Principle and agree that a clear understanding by boards and subsidiary boards of operational structure is crucial to the long term health and stability of an institution. However, in item 95 the current drafting of the requirement in the second bullet point could usefully be refined in order to ensure effective focus: “... which takes into account the different **material** risks to which the group, its business and its subsidiaries are exposed...” Likewise in item 100, we would suggest amending the phrase “unnecessarily complicated structures” to “**disproportionately** complicated structures”.

Also, item 97 refers to the “independent” corporate governance responsibilities of subsidiary banks. As a consequence of the top-down / bottom-up standard for the governance of banks under the EBA Guidelines on Internal Governance, a recently introduced provision under German law now provides that the group-wide business and risk strategy need to be aligned between parent and subsidiary companies. This requires, on the one hand, an own view of the subsidiary and, on the other hand, alignment with the parent. Therefore, as such term is more neutral; we believe that the term “own” corporate governance responsibilities would be more appropriate.

Principle 6: Risk management

Banks should have an effective independent risk management function, under the direction of a Chief Risk Officer (CRO), with sufficient stature, independence, resources and access to the board.

Whilst we strongly support the aim of this Principle, in the context of (a) a two- tier board structure (b) a large, global bank, it would be important for the CRO to be a member of the Management Board in order to effectively secure independence and maintain influence on board decisions, in



particular, from a risk perspective. It is understood that the provisions are drafted to be applied to a range of board structures. In this specific instance, however, there would be value in a specific note clarifying that the CRO being a member of the Management Board does not conflict with the requirement of independence in terms of Principle 6.

In addition, in [item 103](#), we propose adding a point stating, “promote Risk’s role in influencing, shaping and leading change by reviewing, approving and leading appropriate components of the enterprise-wide risk” to highlight and clarify expectations for Risk.

Also, the requirement in [item 109](#) to disclose publicly if the CRO is removed from his or her position seems to be disproportionate (at least in respect of non-listed banks) and should, therefore, be deleted.

Principle 7: Risk identification, monitoring and controlling

Risks should be identified, monitored and controlled on an ongoing bank-wide and individual entity basis. The sophistication of the bank’s risk management and internal control infrastructure should keep pace with changes to the bank’s risk profile, to the external risk landscape and in industry practice.

We support the positive approach outlined in Principle 7 and welcome the fact that it sets out to avoid a “tick-box” approach through the use of qualitative and quantitative analysis of risk ([item 118](#)).

To further support this focus on both “quantitative and qualitative analysis”, we would propose an amendment to [item 118](#) to clarify that, “Banks should leverage stress testing to develop reviews of the risk appetite, the capital adequacy assessment process, the capital and liquidity planning processes and budgets”.

Principle 9: Compliance

The bank’s board of directors is responsible for overseeing the management of the bank’s compliance risk. The board should approve the bank’s compliance approach and policies, including the establishment of a permanent compliance function.

By way of clarification it would be useful for the Committee to confirm in [item 135](#) which “compliance laws” are being referred to. It is not clear whether this phrase is intended to refer only to specific national legislation concerning the set up and operation of bank compliance functions, or whether it refers to compliance *with* laws, or regulation.

This clarification is also important for understanding the scope of the proposed reporting requirements captured in [item 136](#), which itself could be refined to make clear that compliance reporting should not duplicate existing reports where those already capture the required information. Also, [item 136](#) should ensure that there is no perceived conflict between the requirements for the compliance function to be “independent from management” and to provide reporting to “the board”. We would suggest this could best be achieved by clarifying whether in this instance “the board” refers to the Management or the Supervisory Board. Under a two-tier board structure, the compliance function would principally report directly to the Management Board, even though certain direct reporting obligations to the Supervisory Board are current law. As to the latter, however, it would be a fairly new concept to apply the same standard of reporting to the Management Board as well as the Supervisory Board.

[Item 138](#) seems to require that money laundering is necessarily part of the compliance function. The wording should, however, be refined in order to allow for flexibility where money laundering is intended to be taken care of by a separate unit.



Principle 11: Compensation

The bank's compensation structure should be effectively aligned with sound risk management and should promote long term health of the organisation and appropriate risk-taking behaviour.

We support the Principle that a bank's compensation structure should be aligned with sound risk management and the longer term health of the organisation. As with the approach taken with the implementation of CRD IV in Europe, however, we would suggest that certain requirements with regard to the compensation structure and the compensation system, in particular relating to 'long term performance' as outlined in [item 149](#) and the deferral and clawback requirements pursuant to [item 151](#) would be more appropriate if imposed on "material risk takers" rather than generally covering the whole employee population.

We would also recommend including a specific reference to risk culture in [item 149](#). This will help further cement the importance of developing an overall risk culture within an institution to guard against "promote appropriate risk-taking behaviour and encourage a sound **risk culture** in which risk taking behaviour is appropriate and which encourages employees to act in the interests of the company as a whole.

END