



FEDERATION
BANCAIRE
FRANCAISE

The Director General delegate

Paris, June 18th 2010

French Banking Federation's Response to Consultative Document on *"Principles for Enhancing Corporate Governance"* BCBS 168

Dear Sir,

The French Banking Federation (FBF) is the professional body representing over 430 commercial, cooperative and mutual banks operating in France. It includes both French and foreign-based organizations.

The FBF welcomes the consultation process that the Basel Committee is using to help elaborating sound principles that strike the right balance between the supervisory objectives and operational issues that banks are confronted with. FBF concurs with the Basel Committee objectives of improving corporate governance and specifically risk governance that are priority areas on which both the industry and the regulatory community ought to focus.

We are supportive of the objectives sought with the revisions to the BCBS Corporate Governance Guidance and believe the consultative document represents an important step forward towards improvements in the area of risk governance.

However the respective role of the board of directors and the senior management is often a source of confusion in the international debate. There is no unique definition of these two bodies as laws, cultures and practices vary across jurisdictions. This is rightly outlined in the consultative paper but must be more systematically underlined. The FBF believes that more clarity should exist as to the roles of these different entities. Legal, organizational and practical considerations determine that management is more directly involved in the specific aspects of running the business of the banking group. The key distinction between the two roles is that of the "monitoring" and "oversight" nature of the role of the Board especially when there are very few executives directors on the Board as it is mostly the case in several European countries such as France. The guidance, in several instances, blurs this distinction, assigning to the Board roles and functions that by law and for practical reasons pertain more appropriately to senior management.

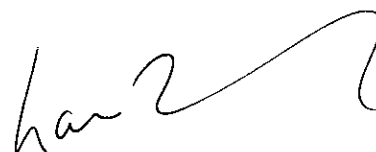
Mr Stefan WALTER
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH – 4002 Basel

To the extent that roles and functions are clearly assigned and separated, and that the Board performs its oversight function adequately, corporate governance can be robust and adequate and achieve the goals of the banking group.

The Basel Committee Principles usefully forestalls the enhancements of corporate governance regulation that may come up in jurisdictions. In particular we would hope that the planned European regulation be as close as possible to the final recommendation of the Basel Committee.

The French Banking Federation wants to see the instigation of healthy competitive conditions and believes the only way to do so is to establish appropriate regulation and sound, flexible principles that provide the same degree of oversight and governing standards and all financial institutions across all jurisdictions. FBF is looking forward to constructively working with the Basel Committee.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'han 2' followed by a long, sweeping flourish that ends in a small hook.

Pierre de LAUZUN

French Banking Federation response of BCBS Consultative document “Principles for enhancing corporate governance” BCBS 168

Recommendations Regarding Specific Principles

Principle 1 – Board’s overall responsibilities

Principle 1 of the Consultative Document, at paragraph 22, indicates that boards should take into account the “legitimate interests of shareholders, depositors and other relevant stakeholders” in discharging their responsibilities. In paragraph 11, it is noted that the Consultative Document will use the sentence “shareholders, depositors and other relevant stakeholders” while recognizing that banks’ responsibilities in this regard vary across jurisdictions and the legal system in a country determines which responsibilities a bank may have to its shareholders, depositors and other stakeholders. We believe the open-ended term “other stakeholders” is problematic as it could lead to overly broad interpretations. The primary role of the board is to ensure that the bank can survive outside shocks and prosper in good times. This is a responsibility it assumes on behalf of shareholders. Enlarging this responsibility to stakeholders, as the consultative paper tentatively does, is not appropriate. On the one hand, this does not fit with the legal responsibility of the board and, on the other hand, this concern is already indirectly addressed as the board is taking into account the long term interests of the institution. Going beyond this is taking the risk to raise unintended expectations and blur the fundamentals of the property rights.

Moreover the Board’s responsibilities should not encroach on the CEO role in “selecting” senior executives (§ 25), in setting standards for members of the management (§ 26) and in setting lines of responsibility and accountability throughout the organisation (§ 27). Finally we would like to specify that the role of the board in respect of organisational matters and processes is supported by the firm’s functions, including internal audit, risk management, finance and compliance.

Principle 2 – Board Qualifications

We recommend a more prudent approach when it comes to defining board members’ qualifications. Sound judgment, integrity, commitment are probably more critical than technical knowledge. Moreover a good mix of qualification and experience is the best mean to benefit from diverse origins and experiences and avoiding the danger of narrow “group think”.

As noted above, we also believe that the principle of proportionality is very important in the corporate governance context, especially as it is applied to smaller banking institutions or those institutions operating in smaller markets. We recommend that this aspect of Principle 2 be modified to better reflect the principle of proportionality as it applies to smaller institutions or those institutions operating in smaller markets.

Regarding the composition of the board, as paragraph 38 does not deal with issues in relation to conflict of interests (dealt in Principle 3) we suggest to delete the second sentence of paragraph 38.

Principle 3 – Board’s own practices and structure

Paragraph 45 of Principle 3 provides that, where the chair of the board is an executive, the bank should be prepared to explain as necessary why this is the case and to have measures in place to minimize its impact on the bank’s checks and balances of such a situation.

We believe that this guidance incorrectly presumes that placing an executive as a chair is undesirable from a risk and governance perspective. The combination of the roles is very common especially in smaller institutions and other measures such as independent directors or committees can improve the Board efficiency.

In large banking groups it is unrealistic and indeed counterproductive to flood the audit committee with all the audit reports produced (§ 48).

Paragraph 50 implies that the risk committee should be distinct from the audit committee. While a board committee should oversee risks, it should be left to the board's discretion to decide whether this is best left to a separate committee or should be assigned to the audit committee. Indeed, there are good reasons for having a single committee: overlaps between risks, internal control and financial accounts, practical problems of staffing separate committees in addition to other board committees depending on the size, the expertise and the availability of non executive board members. We are not in favour of alternative sources of decision such as the recommendation to access to external experts advice in relation to strategic decisions such as M&A and therefore ask to delete the end of paragraph 50 (after ("Principle 6")).

Principle 4 – Group structures

In paragraph 61 the draft expects too much from the board of a parent company especially in very large groups. We suggest the following changes:

"The board of the parent company should:

- approve (not establish) a governance structure... (rationale behind this change in wording is that the governance structure is proposed by the senior management. Its design requires a detailed knowledge of the organisation that the board may not have in case of large and complex groups) ;
- approve (not set and approve) a corporate governance policy.../...meet all applicable governance requirements and to have enough resources for each subsidiary to meet both group and local governance standards ;
- require the internal functions to verify that subsidiaries effectively comply with these governance structure and policy."

Principle 5 – Senior management

It should be the senior management's responsibility to define the bank's risk tolerance/appetite and the board to approve it. Senior management should ensure that the bank's activities are consistent with the business strategy, risk tolerance/appetite and policies approved by the board. Senior management is responsible for operating the bank's activities on a day-to-day basis and should be accountable for this.

Principle 6 – Risk management and internal controls

Paragraph 67 should be redrafted to take into account the assessment of risk decision conformity with the bank's risk appetite/tolerance in particular. Also in order to specify more precisely their respective role we believe that capital planning is a finance duty and not one of the risk management function. We suggest the following amendments to this paragraph as follows:

“67. Risk management generally encompasses the process of :

- defining adequate risk decision process and governance process with the risk originators;
- Assessing the conformity of risk decision with the bank's risk appetite/tolerance
- identifying key risks to the bank;
- measuring exposures to those risks;
- monitoring risk exposures and determining, generally in liaison with the Finance function, the corresponding capital needs on an ongoing basis;²³
- contributing to control or mitigate risk exposures; and
- reporting to senior management and the board on all the items noted in this paragraph.”

Paragraph 72: the removal of the CRO from his position should not require prior approval of the board; it should be enough to require information of the board.

Principle 7 – Risk management

Paragraph 83: the language here is too strong regarding the role of subsidiary management and boards. Some subsidiaries, especially in corporate and investment banking, are fully integrated in the parent company's risk management structure and this generally ensures a much better quality of risk management than the establishment of distinct risk management organisations. While the subsidiary management and board remain legally responsible for the risk management of their company, it is entirely appropriate for them to delegate its day-to-day management in whole or in part to the parent company. We are unclear as to why operational management is mentioned. The operational management may be delegated by the subsidiary to a third party and in particular to a function within the group, while the responsibility may not. Therefore we suggest deleting the following words: ~~“Irrespective of the use of the parent company models and systems, the daily operational management of risks cannot be delegated away from the subsidiary.”~~

The subsidiary should also rely and accept the systems spread out in the group, not validate them. We then modify the following sentence “If group risk management systems and processes are prescribed, subsidiary management, with subsidiary board oversight, is responsible for ensuring the proper **acceptance** of these systems “

Paragraph 87: requiring the risk management function to report its findings on risks arising from mergers and acquisitions directly to the board seems excessively burdensome, as “directly” could imply without informing the CEO. We would like to insist that some findings and or acquisitions may be of minor importance, and a principle of proportionality should be respected. We suggest changing the last sentence as follows: “...mergers and acquisitions, and or its specialised committee in charge according to the relevance of the matter”

Principle 11- Alignment of compensation policy

Page 24, footnote 34: it is again unrealistic to expect that, especially in large banking groups, the board should “develop and issue” the compensation policy for the bank as a whole; this is typically part of senior management responsibility; rather, the board should “approve the principles of the compensation policy...”