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Our ref.:

GBIC reference:
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**Comment by the German Banking Industry Committee
on the Consultative Document "Guidelines – Corporate
Governance Principles for Banks" (BCBS 294)**

9. January 2015

Dear Sir or Madam,

First of all, we would like to express our thanks for giving us the opportunity to comment on the consultative document indicated above. We welcome this opportunity, and would like to make the following statements:

We believe that the dual corporate governance structure, which strictly separates management and supervisory bodies, should be better reflected in these guidelines. The consultative document acknowledges that the "board of directors" may have different structures amongst member states (as reflected by a single-board vs. a dual-board system), and that the anticipated regulations would therefore require interpretation based on applicable national law. Nonetheless, from our perspective, the adoption of the paper in its current form would introduce standards leading to interpretation issues and considerable problems for national implementation, and would ultimately weaken the principle of mutual control between the management board (*Vorstand*) and the supervisory board (*Aufsichtsorgan*) in the German corporate governance system.

Moreover, the BCBS should be aware that governance regulations for institutions in Europe were comprehensively amended with the introduction of CRR and CRD IV regulations as at 1 January 2014. Hence, we do not find it necessary to introduce additional market standards or standalone regulations on the structure of compensation systems (Principle 11). In addition, time should be given for the European corporate govern-

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ance regulations to prove their worth and validity in practice.

We would like to point out the following ambiguities/inconsistencies within the consultative document as examples, particularly in view of the dual system of corporate governance:

I. Principle 1:

1. Responsibilities of the board (nos. 20-26)

The board's explicit responsibilities listed do not completely suit dual-board systems. Some of the responsibilities, e. g. strategies or internal organisation, are carried by senior management in dual-board structures. We therefore believe it would be useful to distinguish between management and oversight functions at this point of the guidelines.

2. Corporate culture and values (nos. 28-29)

We consider nos. 28 and 29 as particularly problematic. From our point of view, the responsibilities of the management bodies and employees result from the comprehensive legal and regulatory requirements and guidelines already in place on a European and national level. Additional regulations – particularly concerning the provision of concrete definitions of acceptable vs. unacceptable behaviour – cannot be sensibly implemented in our view, let alone the fact that such definitions would not be in line with the more abstract understanding of the regulations in Continental Europe. The general norms for responsible and ethical behaviour can also be derived from existing laws and regulations under civil, administrative and criminal law. Therefore, we respectfully request the deletion of these two items from the consultative document.

3. Whistleblowing process (no. 30)

Not all indications provided by employees through the whistleblowing process require the board's acknowledgement or action. From our perspective, it should be made clear that the competent office collecting employees' notices (for instance, the Compliance office) is authorised to evaluate the incoming information, and to decide on further measures to be taken. Involvement of the board should only be required in the case of potential major violations of regulations.

4. Selection of key members of senior management (no. 43)

According to the consultative document, the board in its oversight function has – in addition to the selection of the members of senior management – a duty to select the heads of the control functions. This contradicts the division of functions within a dual board structure, in which senior management is responsible for selecting executive staff below management board level. Hence, the proposed regulation on the selection of management members should reflect the conventions of a dual board structure to a larger extent.

5. Responsibilities of board and senior management (no. 44)

According to the consultative document, members of senior management are to be held accountable for their actions, based on predefined sanctions, should they not fulfil the requirements and expectations of the board. Again, the sanctions required in such an event are already defined by the existing laws and regulations under civil, administrative and – if need be – criminal law, from our perspective. Against this background, we believe it is unnecessary and difficult to establish any company-internal sanctions. Therefore, we kindly request deletion of the second half of sentence 2 from the consultative document.

Should the sanctions mentioned in the consultative document merely refer to the performance-based remuneration of the management, we kindly ask for a clarification in the text.

II. Principle 2:

Nomination Committee (no. 52)

The requirement to establish a nomination committee (or similar body) should depend on the size and internal organisation of a company, as well as the nature, scope, complexity and risk potential of a company's business activities, and should not be mandatory for all institutions. We kindly request to amend the text accordingly, in consideration of the principle of proportionality and of different jurisdictions (as mentioned in no. 48, footnote 12). A possible clarification of no. 52 could be geared to the requirements of no. 62.

III. Principle 3:

1. Organisation and Assessment of the board (nos. 55 and 57)

The requirements of nos. 55 and 57 should also depend on the considerations mentioned in no. 48, footnote 12. We kindly request to amend the text accordingly.

No. 57 should only address banks of large size, risk profile or complexity.

2. Chair of the board (nos. 60 and 61)

No. 60 is another example of the fact that a number of the proposed regulations do not – or do not sufficiently – reflect the characteristics of a dual board structure. According to no. 16, the term “board” only refers to the oversight function. The chair of the board should be a non-executive board member, in order to promote checks and balances, according to the consultative document. However, the chair of the board in a dualistic system never exerts any executive rights when exercising his/her supervisory role. Thus, the proposed regulation would not have any effect.

No. 61 refers to regulations for jurisdictions where the chair is permitted to assume executive duties; these regulations also do not fit into the dual corporate governance structure that is in place in Germany.

3. Board Committees (no. 62)

The requirement to establish board Committees (audit committee, risk committee, compensation committee or other board committees) should depend on the size and internal organisation of a company, as well as the nature, scope, complexity and risk potential of a company's business activities and should not be mandatory for all institutions. We kindly request to amend the text accordingly.

4. Transparency of committees (no. 64)

This transparency requirement should be covered by Principle 12. It can therefore be deleted here.

5. Committee chairs (no. 66)

According to the consultative document, the committee chair should be an independent, non-executive board member. Regarding the question of independence of controlling shareholders' representatives, as stipulated in the EU Commission Recommendation, as well as the German Corporate Governance Code (section 5.4.2 s. 2), we clearly reject the proposed assessment. Following the provisions of these guidelines, representatives of controlling shareholders would be excluded from chairing any of the respective

committees. From our perspective, this cannot be in line with the controlling shareholder's legitimate intentions to exercise control over the institution.

6. Audit and risk committees (nos. 67 and 70)

The establishment of audit and risk committees is required for systematically important banks. For banks of large size, risk profile or complexity it is strongly advised. The requirement to establish audit and risk committees (or similar bodies) should depend on the size and internal organisation of a company, as well as the nature, scope, complexity and risk potential of a company's business activities and should not be mandatory for all institutions. Therefore we respectfully request the deletion of the sentence "For other banks it remains strongly recommended." in nos. 67 and 70 for smaller banks with less complex or lower risk business activities ("other banks").

The consultative paper proposes that the audit and risk committees should each have a chair who is independent, and who is not the chair of the board or any other committee. However, we believe that the chair of the board or a committee should be permitted to chair another committee. This would bring the advantage of gaining an extensive overview of critical issues to be discussed and monitored, and would facilitate the flow of information between committees. This would be particularly important to the chair of the board in exercising his/her central function. From our perspective, any attempt to derogate the chair's central functions would contradict the overall objective of enhanced control over the management board, and would simultaneously contradict European requirements for cross-links between different committees, including overlapping activities of committee members and chairs. No. 60 should be revised in this respect, too.

The consultative paper does not provide for the option of a joint audit and risk committee or a joint nomination and compensation committee. However, we believe that this option should be provided for non-systemically important institutions, in order to streamline organisational structures.

7. Disclosure of conflicts of interest (no. 83)

We consider the disclosure of concrete information on conflicts of interest to be critical in matters of confidentiality and privacy protection. We therefore request deletion of this section from the document.

IV. Principle 4:

Senior management

According to principle 4 senior management should carry out and manage the bank's activities ... "under the direction and oversight of the board". The term "direction" doesn't match with the responsibilities in dual-board systems. We therefore suggest to use another word like "orientation" or "bias".

V. Principle 5:

Parent company boards (nos. 94 et seq.)

The regulations proposed in nos. 94 et seq. regarding the responsibilities of structuring and steering a group of companies do not specify whether this role is to be assumed by the management board or the supervisory board, in a dual board structure.

VI. Principle 6:

1. Chief Risk Officer (no. 106 *inter alia*)

The requirement to establish an exclusive CRO – at management board level – in larger and complex institutions is included in the guidelines already. According to the principle of proportionality, this requirement should not apply to smaller banks with less complex or lower risk business activities, we believe. For such banks alternative solutions can be appropriate, either a senior manager that carries other responsibilities besides the risk management function or an executive below management board level. The term “CRO” is used throughout the guidelines, leaving the impression that an exclusive management board member with overall responsibility for the bank’s risk management is required for all institutions. We therefore recommend replacing the term “CRO” with the expression “head of the risk management function” in general.

According to no. 107 the CRO has primary responsibility for overseeing the development and implementation of the bank’s risk management function. Subject to no. 108 the CRO should not have management or financial responsibility related to any operational business lines or revenue-generating functions and there should be no “dual hatting”. In our view there should be a possibility to execute also other management functions as long as the CRO is not restricted in his essential function.

2. Access of the CRO to the board (nos. 108 and 109)

In our opinion, the establishment of an institutionalised, direct access of the head of the risk control function to the board is not necessary. It is proven practice in a dual-board system that the management body coordinates the flow of information towards the supervisory body. In addition, we would like to point out that the CRO has extensive competences (nos. 106 and 109). The CRO has to be independent from management, and advises the supervisory body regarding risk strategy and risk appetite, according to the consultative paper. Furthermore, the CRO reports directly to the supervisory body. Moreover in Germany the head of the supervisory body or the head of the risk committee is entitled to obtain information direct from the head of the risk control function.

This also applies to the requirements stated in no. 109 regarding changes to the position of CRO. In our view, the requirement of an approval from the supervisory body in the case of changes to the position of CRO, as well as the supervisory body’s review and approval requirement of the CRO’s performance, compensation and budget, should be mitigated into a requirement to merely inform the supervisory body of such an instance. In addition, the requirement to publicly disclose the removal of the CRO – and to discuss the reasons for the removal – should not apply to non-systemically important institutions. We kindly request amendment of the text accordingly.

VII. Principle 7:

Risk measurement (no. 112)

The requirement stipulated in the last sentence to measure “hard-to-quantify risks” is contradictory, we believe. We do approve the fact that an institution has to be aware of, and monitor reputation risk. However, we do not believe that this sort of risk can be measured by valid methodologies, and thus recommend deletion of this part of the requirement.

VIII. Principle 9:

1. Reporting of the Compliance function (no. 136)

We do not consider it necessary to establish the proposed separate reporting to the board. Instead, the information in reports submitted to the management body should be structured in a way appropriate and comprehensible to the supervisory body. We kindly request deletion of the word "separate".

2. Access of the Compliance function to the Board (no. 137)

In our opinion, the establishment of an institutionalised, direct access of the compliance function to the board is not necessary. It is proven practice in a dual-board system that the management board coordinates the flow of information towards the supervisory body.

IX. Principle 10:

Internal Audit Reports (no. 143)

We find it neither necessary nor appropriate to submit all internal audit reports to the board; this would produce an information overload. It is in fact sufficient to submit only significant or major findings to the board. As described above, concerning nos. 108 and 137, we recommend that the management body coordinate the information flow towards the supervisory body. However, direct access of the internal audit function to the board should be limited to major findings concerning the senior management itself.

Approval of compensation by the board (no. 146)

In dual-board systems, the compensation of executives below management board level, e. g. of the head of internal audit, lies within the scope of responsibilities of the senior management (management board). We kindly request amendment of the text accordingly.

Editorial note

Reference is made to Principle 9 (Compliance) at the end of no. 41. Given the context of the internal audit function, reference should be made to Principle 10 (Internal Audit) instead.

We kindly ask that our statements be taken into consideration.

Yours sincerely,
on behalf of the German Banking Industry Committee
Bundesverband der Deutschen
Volksbanken und Raiffeisenbanken e.V.

by proxy



Gerhard Hofmann



Thorsten Reinicke