

EBA consults on governance guidelines

The European Banking Authority (**EBA**) is developing guidelines setting out the criteria and processes that credit institutions and competent authorities should respect when assessing the suitability of members of the management body (in both its management and supervisory functions) and key function holders of a credit institution and including measures applicable to cases where such persons are not suitable for the position concerned.

Background

Article 16 of [Regulation \(EU\) No 1093/2010](#) empowers EBA to issue guidelines and recommendations addressed to competent authorities or financial institutions with a view to establishing consistent, efficient and effective supervisory practices within the European System of Financial Supervision (ESFS), and to ensuring the common, uniform and consistent application of the law of the European Union. On the basis of this delegated power, the EBA has just published a [consultation paper on draft guidelines for assessing the suitability of members of the management body and key function holders of a credit institution](#) (EBA/CP/2013/03).

EBA refers to Articles 11 and 22 para. 1 of Directive 2006/48/EC (**CRD**) (Articles 13 and 73 in the Commission proposal of CRD IV, [COM\(2011\) 453 final](#)) (**draft CRD IV**) as the rationale for its guidelines. Pursuant to these provisions (i) an institution may only be authorized if it is run by at least two persons of sufficiently good repute and with sufficient relevant experience and (ii) competent authorities shall require that every credit institution have robust governance arrangements in place.

EBA does not see its mandate limited by the current wording of the CRD. Instead, it refers to both the deficiencies found during the financial crisis on the one hand and to the proposed amendments to CRD by the draft CRD IV on the other hand to justify the broader scope of the draft guidelines.

The same regulation that empowers EBA to issue guidelines also requests competent authorities and financial institutions to make every effort to comply with such guidelines. Competent authorities need to confirm compliance or explain non-compliance issue within two months of the issuance of a guideline or recommendation.

Key issues

- Responsibilities and competent parties for assessing suitability
- Assessment by credit institutions
- Assessment by supervisors

Management body / key function holders

- **Management body:** Governing body of a credit institution, comprising the management and supervisory functions, which has the ultimate decision-making authority and is empowered to set the institutions strategy, objectives and overall direction.
- **Key function holders:** Employees outside of the Management body whose positions give them significant influence over the direction of the credit institution. These could include, e.g. senior managers, heads of internal control functions, heads of a significant branch or of a subsidiary.

Consultation topics

While interested parties are invited to comment on all matters of the draft guidelines, the consultation paper only contains two specific questions:

- one referring to the scope of the principle of proportionality and
- one on the assessment of credit institutions' policies for key function holders by competent authorities.

Responsibilities and competent parties for assessing suitability

The guidelines are addressed to both competent authorities and credit institutions. Whereas both are requested to assess the suitability of the members of a management body at different points in time, credit institutions have a primary responsibility for the initial and ongoing assessment. In addition, only credit institutions are obliged to assess the suitability of key function holders in line with the policy on the nomination and succession of individuals with key functions.

Assessment by credit institutions

Assessment pursuant to defined criteria

Credit institutions should assess the suitability of members of the management body taking into account the reputation, experience and governance criteria (see section on assessment criteria below) as well as the [EBA's Guidelines on Internal Governance](#), on the composition and functioning of the management body, pursuant to which policies should be in place for selecting, monitoring and planning the succession of the members of the management body.

Credit institutions need furthermore to assess the suitability of key function holders.

Point in time for the assessment

The assessment of the suitability of management body members should be made whenever possible prior to appointment or latest immediately thereafter. Re-assessments in connection with certain events (such as e.g. the extension of the mandate) may be necessary to verify the continuing suitability.

As far as key function holders are concerned, their assessment should be carried out prior to appointment.

Assessment of the board as a whole

When assessing the suitability of each of the members of a management body, credit institutions should also take into account the suitability of the management body as a whole. The fact that there are weaknesses in the composition does not necessarily mean that the individual members are themselves not suitable.

Documentation

The assessment and its results should be properly documented.

Policies on suitability

Credit institutions should have policies in place for selecting and assessing the suitability of members of the management body and for assessing the suitability of key function holders.

The policies for the **management body** must set forth, at least:

- cases where a re-assessment should be performed and measures to identify such cases;
- responsibility for performing the suitability assessment;

- competencies and skills leading to the assumption of expertise;
- internal procedure for the assessment of the suitability;
- information / evidence that candidates / members of the management body should provide for an assessment; and
- if the person is to be appointed by the shareholders, the measures taken to ensure that shareholders are informed about the requirements for the position and the relevant profile of persons before they are appointed.

The policies for the **key function holders** should forth, at least

- the positions for which a suitability assessment is required;
- who is responsible for performing the suitability assessment; and
- the criteria for reputation and experience required for the specific position.

Corrective measures by institutions

The lack of suitability may have the following consequences: either the unsuitable person may not be appointed or the institute has to take appropriate measures to ensure the future suitability.

- Lack of suitability of a person to be appointed as a member of the management body **in its management function** → **No appointment**
- Lack of suitability of a person to be appointed as a member of the management body **in its supervisory function** → **No appointment or appropriate measures to ensure the person's future suitability**
- Loss of suitability (as per re-assessment) of a member or of the

management body as a whole → **Appropriate measures to rectify the situation and inform the competent authority accordingly**

- Lack of suitability of a person to be appointed as a **key function holder** → **Appropriate measures**

Assessment by supervisors

Notification procedure in place

Competent authorities should establish a notification procedure applicable to appointments and re-appointments of a member of a management body. The authorities decide, whether such notifications take the form of an application or may be simply a notification made prior to or even after the appointment.

Information for assessment

At the request of the competent authorities, credit institutions must provide accurate information necessary for the assessment of the suitability of the members of a management body. Both the credit institution and the member of the management body concerned are responsible for the verification of the accuracy of the documentation.

Termination of appointment

Credit institutions should notify the competent authority when the appointment of a member of a management body is terminated. This notification should also include the reasons for termination.

Assessment process

The process applicable to the assessment of the suitability of members of a management body should be publicly available.

The processes applicable for the initial assessment and for the re-assessment and the processes applicable to members of the management body in its management function and in its supervisory function must not be the same.

Assessment technique

When assessing the suitability, the competent authorities are not limited to the information provided but can ask for further evidence of reputation or experience and use interviews as a possibility of gaining the information. Assessment criteria may be weighted differently from case to case, taking into account applicable laws as well the specific policies and procedures of the institution.

While suitability assessments from other EEA authorities may be taken into account, local authorities must consider developments which may be relevant for its own assessment.

At the end of the assessment, which should be completed in good time, the credit institution should be informed of the results.

Competent authorities may also (but must not) assess the suitability of key function holders. In this case, the applicable processes and criteria are to be disclosed.

Corrective measures by authorities

If a competent authority considers a person to be unsuitable, it should request the credit institution to either not appoint or dismiss the person or to take appropriate measures to ensure future suitability. Furthermore, the authorities can also take corrective measures themselves, if the credit institutions do not react appropriately. Lack of good repute cannot

be cured and always leads to non-appointment / replacement.

General Assessment Criteria

Fit: Proportional

The experience required from the members of a management body and key function holders should take into account the nature, scale and complexity of the business as well as the responsibilities of the position concerned. Although all members of a management body need to show a certain degree of experience, the requirements differ as so do the respective tasks and responsibilities.

Proper: Constant

Members of a management body and key function holders should in any event be of good repute, regardless of the nature, scale and complexity of the business of the credit institution.

Specific Assessment Criteria

Reputation criteria

A person should be considered to be of good repute if there is no evidence or reason to suggest otherwise but should not be considered to be of good repute if the personal or business conduct gives rise to any material doubt about the ability to ensure a sound and prudent management of a credit institution.

EBA clarifies that all relevant information needs to be taken into account when assessing good repute and sets forth a long catalogue of issues to which particular attention must be paid. These include, inter alia, administrative or criminal records, circumstances for (potential) offences and measures against them, accumulation of smaller incidents, conviction or indictment of criminal offence, lack of

transparency / cooperation towards authorities, refusal (or termination or expulsion) of any registration, authorisation, membership or license to carry out a trade, business or profession, poor business performance, etc.

Experience criteria

The experience required will depend first of all on the nature, size and complexity of the business of the credit institution and the position at stake.

Both the theoretical experience gained through education and training as well as the managerial experience gained in previous occupations, taking into account the skills and knowledge acquired and demonstrated by the professional conduct of the member are to be reviewed in the course of the assessment.

A person to be appointed as a **member of the management body in its management function** should have served long enough in one management position (temporary functions should usually not be sufficient) and gained sufficient experience in a management position in a credit institution or similar firm. Particular attention is to be given to the length of service, the nature and complexity of the institution where the position was held, the scope of competencies,

decision making powers, and responsibilities and the number of subordinates.

The requirements for the appointment as **a member of the management body in its supervisory function** are not so tight: in this case, one should have sufficient experience to provide constructive challenge in relation to the management decisions. Such experience may be gained from managerial, academic, administrative or other relevant activities and both in or outside financial institutions.

When assessing the education, authorities should take into particular consideration the level and profile of the education and whether it relates to banking and financial services or other relevant areas. Education in the areas of banking and finance, economics, law, administration, regulation and quantitative methods can in general be considered to be related to banking and financial services.

Furthermore, for the assessment of the overall experience authorities must look at the knowledge and experience in financial markets, regulatory framework and requirements and management of credit institutions (with all its aspects).

In addition to the experience criteria, authorities may also want to assess

(but are not obliged to do it) whether a (potential) member has sufficient (soft) skills for the position, such as decisiveness, strategic vision, leadership, independence of mind, etc.

Governance criteria

In addition to reputation and experience, authorities also assess governance related criteria, such as conflicts of interest, ability to commit sufficient time, overall composition of the board, collective knowledge and expertise and ability to perform their tasks without undue influence.

EBA gives the issue of independence a great deal of attention and lists a number of situations to be considered when assessing the independence of a member: positions held in the credit institution or other firms; relationships with the members of the management body in their management function, in the same credit institution, in its parent company or subsidiaries and relationships with the controlling shareholders of the same credit institutions, with its parent institution and subsidiaries.

Next Steps

Interested parties are invited to submit any comments until 18 July 2012. The responses will be disclosed thereafter.

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