To the European Central Bank

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	BSBV 115/Egger	3137	20 January 2017

ECB Draft Guide on Fit & Proper

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the above cited consultation document and would like to submit the following position:

General remarks

The general concept behind independence/conflicts of interests and the distinction between these two concepts in the EBA Fit & Proper Draft GL and the ECB Fit & Proper Draft Guide but also in the Internal Governance Draft GL are not sufficiently clear. Some of the criteria mentioned in the ECB Draft Guide under Section 5.3 (Conflicts of interests and independence of mind) are treated as conflicts of interests ("The appointee or a close personal relation holds at the same time a management or senior staff position in the supervised entity or any of its competitors, or in the parent undertaking/its subsidiaries"), while in the EBA Fit and Proper Draft GL basically the same situation is considered an independence criteria ("a CRD-institution´s management body in its supervisory function should include a sufficient number of fully independent members that do not have a mandate as a member of the management body in its management function within the scope of prudential consolidation, are not employed by any entity within the scope of consolidation and are not under any other undue influence or conflict of interest …"). Referring to the above mentioned criteria, we are of the opinion that it neither constitutes a conflict of interest, nor does it indicate a lack of independence when members of the management body in its management function at the same time hold mandates in the management body in its supervisory function in group entities. In fact the right of the parent company to nominate members of the management body in its supervisory function in its subsidiaries represents one of the key instruments of group steering and should therefore not be prohibited or restricted (with this respect please see the explanations provided to Section 5.3 point b) below).

Reputation – (pending) legal proceedings (Section 5.2 - page 13)

In the ECB's view concluded legal proceedings may also have an impact against the appointee, even if the conclusion is in favour of the appointee. This approach is a clear breach of the principle of the presumption of innocence according to Article 6 (2) European Convention on Human Rights if the appointee has been absolved from all charges by the judicial decision of an

independent court. An administrative authority must not ignore or override these final judgements of courts to the disadvantage of the appointee.

Conflicts of interest and independence of mind (Section 5.3)

We appreciate that the presence of shareholder representatives in the management body is basically accepted (see page 15), but this is still not enough. As the Accounting Directive 2013/34/EU requires to prepare consolidated accounts when an enterprise has the right to appoint or remove the majority of supervisory board members (see Article 22 (1) b) a majority of shareholder representatives has to be accepted). This should be made clear, otherwise the ECB Guide would be in contradiction with the Accounting Directive.

In Chapter 5.3. it is stated correctly that it would be acceptable for a member to have conflicts of interest if these were mitigated or managed adequately. The problem is that it is necessary to differentiate between individual conflicts of interest and structurally different interests that have to be considered. The definition of a conflict of interest as given in the EBA Guidelines on Internal Governance (see page 14) concentrates on the conflict between the duty of a person and private interests of an individual which could improperly influence the performance of his or her duties and responsibilities.

This is a very wise approach because representing e.g. a shareholder always creates a need to legitimately take into account the dividend interests of all shareholders. At the same time for example being part of workers' representation in a supervisory board creates the need to consider also the interests of the employees when questions of remuneration or for example questions of a restructuring of an entity connected with mass dismissals are discussed. Members of the supervisory board always have to pursue the benefit of the entity first but it is typical that at the same time they have to consider the interests of shareholders, employees or other stakeholders.

It is impossible to require from shareholder representatives in the supervisory board to abstain from their voting right when decisions regarding the annual account and the possible dividends have to be made in the supervisory board. It is simply necessary to reconcile all these interests properly. Mitigating and managing conflicts of interests is a question for conflicts with private interests of a person.

This understanding should be explicitly expressed and made clear in the ECB Guide.

Personal conflicts of interest

Table 1 on page 15 describes situations and lays down criteria where substantial financial interests/obligations or high political influence shall exist from the ECB's point of view which are deemed to be detrimental to the independence of a member of the management body. According to the ECB the substantiality depends on what (financial) value the interest or obligation represents to the financial resources of the appointee. A non-materiality of such a financial interest or obligation should exist in the following cases according to the guide:

- all non-preferential secured personal loans (such as private mortgages) that are performing;
- all other non-preferential loans under € 100,000, secured or otherwise, performing or non-performing;
- current shareholdings ≤ 1% or other investments of equivalent value.

At least this requirement must not apply for all performing loans no matter if they are secured or unsecured. In cases of an excellent creditworthiness of the borrower it is not always required to reserve collaterals. People with excellent creditworthiness would have no problem at all to switch to another bank. Therefore, there is no danger of losing independence of mind and of getting under economic pressure because of an unsecured loan.

Furthermore, in particular against the background of high real estate prices the given threshold of 100.000 Euro is much too low. A threshold of at least 500.000 Euro would be appropriate.

Apart from that it is inherent to the nature and the business model of cooperative banks and savings banks as self-help-organisations that their clients can also be their members and that their boards of supervisors are composed by their members. The ECB Guide should avoid everything likely to undermine the nature and the business model of cooperative banks and savings banks.

With respect to the proposed personal conflict of interest we propose to insert a significance threshold also for private businesses as a similar threshold applies to commercial relationships too.

Professional conflicts of interest

Regarding professional conflicts of interest, we understand that holding two directorships in two group entities at the same time represents a material conflict of interests and requires to be treated accordingly (detailed assessment and mitigating measure as stated in the Draft Guide).

This is inappropriate and impractical since the right of the parent company to nominate members of the management body in its supervisory function for its subsidiaries is one of the key instruments of group steering. In this context it should be mentioned with regard to stock corporations that the only way in which the group steering by the parent company can be exercised is through its representatives in the management body in its supervisory function of the subsidiaries, since according to the provisions of the Austrian Stock Corporation Act (Para. 70 sect. 1) the management body in its management function of the subsidiary is not bound by the instructions of the parent company. Furthermore, the Austrian Banking Act lays down certain supervisory requirements which consolidating institutions have to comply with on a consolidated basis and for the fulfillment of which they are responsible (Para. 30 sect. 6). For this purpose, the subsidiaries are legally required to provide the consolidating institutions with the necessary information and documents (Para. 30 sect. 8). The application of supervisory requirements on a consolidated basis and the legal obligations related thereto within group structures are also laid down by Art. 11 (1) CRR. Last but not least, the Draft Guide itself states that the presence of shareholders' representatives in the management body is acceptable.

Text proposal for Table 1

Material conflicts of interest

- Category of conflict: *Personal*
  Period: *Current*

  Degree and type of connection and, where applicable, threshold
  The appointee:

*Conducts **significant** business, in private or through a company, with the supervised entity or with the parent undertaking/ its subsidiaries.*

- Category of conflict: *Professional*
  Period: *Current or over the **last** years~~s~~*

  Degree and type of connection and, where applicable, threshold
  *The appointee or a close personal relation holds at the same time a management or senior staff position in the supervised entity or any of its competitors, ~~**or in the parent undertaking/its subsidiaries**~~*

According to Table 1 material personal and commercial relationships present a conflict of interest. In various national legislation frameworks (e.g. para 28 of the Austrian Federal Banking Act) it is regulated that certain business transactions with the management and related parties do require the approval of the management board in its supervisory function anyway.

Pursuant to Chapter 1.4 the NCAs have agreed to interpret and develop national law in line with these policies. Therefore, the requirements of Table 1 concerning material personal and commercial relationships have to be adopted in such a manner that they are in line with the national legislative requirements regarding the obligatory approval of certain transactions by the management board in its supervisory function.

Political influence or relationships

Without further substantiation Table 1 gives examples in which cases an appointee holds a position of high political influence.

It cannot be ECB's intention to consider every local politician (e.g. mayor, member of the municipal council), public employee (e.g. civil servants in ministries or other authorities) or state representatives as not independent. They do not have any material influence with regard to the legislative process for banking regulation on the European level.

It needs to be clarified that politicians, public employees and state representatives are generally considered as independent notwithstanding the possibility of singular conflicts of interest in certain questions that easily can be managed for example by not taking part in decisions regarding the local authority.

Beyond that, fulfilling the requirements laid down in para 77 point e) and f) also leads to pointless additional administrative burden for the institutions. A separate written justification has to be formulated and documented for every relevant borrower or politician.

Measures regarding conflicts of interests

The Austrian legal framework already contains both in the Banking Act and the Stock Corporation Act provisions regarding the treatment of conflicts of interests and mentions mitigating measures (voting abstention of the concerned member, disclosure requirements, etc). Thus, we do not consider it necessary to foresee additional requirements for the institutions in this respect.

Text proposal

When the materiality of a conflict of interest is determined the supervised entity must adopt adequate measures in accordance with national law. ~~***It must:***~~
~~***• perform a detailed assessment of the particular situation;***~~

~~***• decide which mitigating measures it will take based on its internal policy, unless national law already prescribes which measures must be taken.***~~
~~***The supervised entity should reply with a "Conflict of Interest Statement", explaining the above to the satisfaction of the supervisor***~~

Section 5.4: Time commitment

Counting of directorships (including "privileged counting")

According to its "restrictive approach to counting" the ECB is counting directorships in undertakings in which the institution has a qualifying holding and directorships within the group of undertakings separately without any further explanation (see figure 2).

The goal of interpretation should not be to take a strict or a less strict approach but to take an approach which meets the meaning of the regulation interpreted. So what is the meaning of Art 91 (4) CRD IV?

As the Recital 58 CRD IV gives no reasoning for the exemptions in Art 91 (4) CRD IV it may be helpful to watch out where this kind of exemption comes from and if it stems from the legislation of a certain Member State to take into account, how it is understood in this Member State. The exemptions in Art 91 CRD IV were not part of the original proposal of the Commission. They were entered into the discussion especially by Austria and by Austrian MEPs. There are similar exemptions in the German Public Limited Company Act for directorships in the same group but the combination of exemptions for directorships in the same group and for directorships in undertakings in which the institution has qualifying holdings only exists in the Austrian Public Limited Company Act.

The reason given in the Austrian legislation is simple: It is part of the job and a central responsibility of an executive director of the parent undertaking to control the subsidiaries and the undertakings, in which the parent undertaking holds a qualifying holding. There is no risk that directorships in the supervisory boards of these undertakings are handled with negligence. In fact, the whole staff of the parent undertaking delivers input for those members of the supervisory board that the parent undertaking has sent in these undertakings. There is no difference made whether the parent undertaking holds 51% or 49% of the shares. Therefore, in the Austrian legislation all these mandates are in the same bucket, when it comes to the calculation of the maximum number of mandates. A separate counting would not be reasonable in any way.

The same is true for the European version of mandate-calculation:

As it is part of one and the same job as an executive director of a credit institution to become member of the supervisory board of another undertaking, in which the credit institution owns a qualifying holding, the two directorships must be counted as one.

The separate counting as proposed in the ECB draft guide leads to strange distortions. An executive director of the parent undertaking would have to withdraw from a directorship he

rightfully held in a former subsidiary only because the parent undertaking sells some shares and loses the majority in another undertaking.

If there are more than one other undertakings, in which the credit institution owns a qualifying holding, and the executive director of the credit institution is non-executive director in all these undertakings even according to the ECB these directorships together would count as one single directorship. The strange thing is that the linking directorship in the credit institution above is not even part of the picture as seen by the ECB. This is not convincing.

The guide must not try to prevent persons from becoming members of the supervisory boards of central institutions whose mandates are otherwise privileged by CRD IV (see Art 91 (4) CRD IV). This would be a clear contradiction to the meaning of CRD IV.

We ask you to give our remarks due consideration.

Yours faithfully,

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