European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

European Banking Authority

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Consultation Paper on the Guidebook on Internal Governance (CP 44)

Ladies, Gentlemen,

The European Association of Co-operative Banks (EACB) welcomes the opportunity to comment on the Consultative paper on the Guidebook on Internal Governance (CP 44).

Please find our remarks on the following pages.

Do not hesitate to contact us should you have any questions.

We will remain at your disposal,

Yours sincerely,

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1. GENERAL COMMENTS

The members of the EACB appreciate CEBS/EBA's efforts to revise the internal governance principles to harmonise supervisory expectations and improve the internal governance arrangements, especially of large and complex institutions to overcome the weakness and superficial governance practices identified during the financial crisis.

We acknowledge that the principles should also apply to cooperative banking groups. Many of the principles in fact already apply to cooperative banks by virtue of legislation or governance codes following the Guidelines of 2006, the ICAAP and SREP. However, we consider that cooperative banks should not be put in the same context as other banks especially considering the fact that cooperative banks have not been subject to any bank failures or were dependent on state funds during the crisis. We consider that cooperative banks - with their specific features - who have been resilient during the financial crisis merit to be mentioned separately.

Specific Feature of cooperative banks

The cooperative business model has developed in different ways in the different Members States of the European Union. Today, the co-operative form of enterprise is common and is recognized in all Member States. At European level, the cooperative legal form as such is recognized by the Treaty of Rome. In addition, Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society underlines the efforts of the European Union to contribute to the economic development of co-operatives.

Co-operative banks serve more than 175 million customers in Europe with an average market share in SME financing of around 29%. They have naturally expanded the scope of their activities in recent years by moving into cross-border markets and rolling out new services. This expansion has respected their core values and promoted effective and prudent management. In fact, despite certain differences, co-operative banks share some common and defining features underlining a transparent and sound corporate structure

- ***Member-ownership***

The cooperative banks are effectively owned and controlled by their local customers who are at the same time the members through the membership concept. The member ownership concept is not only central to the co-operative approach but is also a unique aspect. It leads to a consensus-driven approach and hence more thorough, albeit conservative decisions suited to a long-term time horizon[1].

- ***Promotion of Members' Economic Interest***

Moreover, the statutory aim of cooperative banks is explicitly defined as promoting economic interest of its members rather than maximizing profit. This leads to a more prudent approach to banking, to a focus on retail banking and finally to a longer term perspective to business.

[1] Oliver Wyman, 2008. Co-operative bank: Customer Champion, p. 18, 22. see: http://www.oliverwyman.com/ow/pdf_files/OW_En_FS_2008_CooperativeBank.pdf.

- ***Democratic control principle***

Another feature that distinguishes corporative banks is the 'one person- one vote' principle. Due to the equality of voting rights of each member, the decisions taken by the General Assembly of the local banks illustrate democracy. There is thus in principle a control over management by the members/customers which fosters a better understanding, close to the grassroots level, of the bank's functioning and strategy. Moreover, the democratic principle leads to a consensus-driven approach and hence more thorough, albeit conservative decisions are made suited to a long-term time horizon[2]

- ***Democratic Elective system***

Most cooperatives have a democratic elective system to appoint directors. Local cooperative banks have a pragmatic approach that ensures adequate skills and a diversified supervisory board. This democratic elective system, which is a fundamental feature of the governance of cooperative banks, ensures that the enterprise will be controlled by its members in the General Assembly. Moreover, these General Assemblies from which the directors are elected are in itself source of diversity as they are composed of local entrepreneurs with diverse professions, skills and experiences, and diverse local backgrounds corresponding to the territories in which the local banks are located. This characteristic that board members are chosen among the members ensures that the composition of the board is suitably diverse.

We underline that the strength of cooperative banks lies in the fact that Board members have different backgrounds, are strongly involved in the activities and governance of their cooperatives and understand the cooperative's business model and the territories in which the local banks are located.

In addition to this democratic election system, due to the diversity of cooperative banks, some banks have ((non-)statutory) policies in place which specify criteria of professionalism and competences of board members and established specific training policies. The objective pursued by these programmes is clear: to strengthen the elected officials' initial skills in order to enable them to optimally discharge their office as directors. These requirements expressed by financial institutions themselves as regards the directors' banking competencies also make it possible to respond to the supervisory authorities' requirements.

Cooperative Banks and Crisis

These specific features of the cooperative model as well as cooperative banks' contribution to financial stability during the crisis are largely recognized. More specifically, the report prepared by the International Labour Organisation concerning the cooperative economic model's resilience during times of crisis, as published in 2009, concludes that "future regulations that might result from this crisis must clearly recognize that cooperative financial institutions were not the source of these problems, were materially less affected by the economic crisis, and should not be punished by being included in a series of new rules adopted in order to correct a problem that they did not cause"[3].

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2 Ib idem.

[3] International Labour Organisation, 2009. Resilience of Cooperative Business Model in Times of Crisis, p. 35. Online available at: http://www.ilo.org/wcmsp5/groups/public/---ed_emp/---emp_ent/documents/publication/wcms_108416.pdf.

We therefore appreciate that CEBS recognises in paragraph 7 that sound internal governance practices in some institutions helped to manage the crisis significantly better than others. The diversity of business and internal governance models enhances the stability in banking. However, we consider that CEBS guidebook on internal governance should therefore more specifically distinguish between the different existing internal governance practices.

The proportionality principle

The proportionality principle should be a central element in examining internal governance rules.

In that respect, we fully share the position of CEBS that the practical application of the principles should be proportionate and may vary depending on nature, scale and complexity of the institution as referred to in paragraph 22. However, for the proportionality, the legal form, size, the focus of activity and relevant financial and legal model should also be taken into account especially as regards paragraph 71 and 77. This approach seems essential given that each institution has its own corporate structure. In this respect, CEBS is requested to concretely take into account the proportionality principle in its broadest sense in any future guidance for internal governance principles.

Convergence existing and future internal governance regulation

Finally, the revision of the "Guidebook" should be consistent with existing national legislation and also timely with any future regulation following from the Green Paper on corporate governance in financial institutions and remuneration policy, in order to avoid duplication and redundancies.

2. SPECIFIC REMARKS

The principles set out by the CEBS are considered as important elements of a sound and transparent corporate structure and organisation. However, the principles are rather focused towards Member States with a monistic corporate system rather than Member States which have a dualistic system.

Corporate Structure and Organisation

As regards the principles for a transparent, effective and prudent corporate structure and management of the institution, in co-operative banks, the power of all bodies originally emanates from the members which exert influence through the General Assembly. The General Assembly, as the body representing all members, is the body that controls the orderly conduct of corporate governance as a whole. The democratic participation of the members in the General Assembly very efficiently maintains the balance of power between the members and the directors as owners and the management body of co-operative banks.

Directors in cooperative banks are independent of any shareholder or group of shareholders and protect the members' collective interests. Unlike the situation observed in joint-stock companies, the directors of cooperatives are not the representatives of a given shareholder or a group of shareholders. As such, the directors of cooperative banks are, by definition, the representatives and guarantors of the members' collective interest. The said collective interest corresponds to the quality of the service to clients, which is by nature different from an exclusively financial interest. In addition, the directors of regional banks have a highly diversified social and geographic profile, which has no equivalent among listed companies, in which the social cross-breeding of directors is often criticized. [4]

As such the management and oversight function of most cooperative banks consist of their members who have approved the operational structure, and decisions to operate in another jurisdiction and should therefore 'know' and 'understand' their structure and the risks it poses.

Especially, in cooperative banks, whose statutory purpose is explicitly defined as promoting the economic interest of its members, certain strategic decisions are often taken by the general assembly. In some instances, the General Assembly of a cooperative bank can equally take up any question as the Board[5], or has to decide on the commencement or giving up of any area of operation[6].

Management Body

- ***Use of term Management Body***

First, we acknowledge that CEBS is aware of the different governance structures in the Member States. However, the principles in the Guidebook are still too much based on a

[4] No director of a regional bank may be at the same time a director of another regional bank, and may therefore not be subject to the reproaches very often made as regards the composition of boards of directors of listed companies. The presence of external directors in cooperative companies is contrary to the co-operative spirit. Therefore, the recent discussions among the various supervisory authorities aimed at increased transparency and improved governance rules among listed companies converge in many ways with these features that mutual organizations have been embodying and enshrining for a long time. Only members and therefore the holders of a share may be members of the various representative bodies.

[5] Article 27, Genossenschaftsgezets

[6] Article 30(m), Mustersatzung fűr Volksbanken und Raiffeisenbanken mit Vertreterversammlung (ohne Warengeschaft) [Standard Statutes of German Cooperative Banks].

monistic system. The exclusive reference to 'management body' is confusing, unclear and could lead to misunderstandings. The term management body refers to both the board in its supervisory and executive function. This is not efficient and practical. It is essential to make a clearer distinction between the decision-making and supervisory functions. We therefore consider that the term 'management body is misplaced.

We therefore suggest in the first place referring to a dualistic system i.e. separating the supervisory and management function and specify the principles accordingly. Especially given that both supervisory and management function can be fulfilled by a Board of Directors in a monistic system. Secondly, we also recommend using another term for 'management body' which is more neutral and objective and which does not pose for problems from a perspective of a dual system such as 'board of directors'. This term was used in the Commission Green Paper on Corporate Governance.

- ***Responsibilities of the Management Body***

In the second place regarding the responsibilities of the management body, in cooperative banks certain decisions are made under the auspices of the general assembly. In the statutes of cooperative banks the powers and responsibilities of the members of each of the governing organs is included. The responsibilities of the Supervisory and management board are therefore already described in detail in the different national rules. We do not consider it necessary to have any additional documentation.

- ***Composition appointment and succession***

Furthermore, we appreciate that CEBS acknowledges in paragraph 52 that it should be sufficient for the board to collectively dispose of adequate knowledge and experiences. . Instead of defining a rigid profile for individual candidate board members in recruitment policies, which would not allow necessary diversity within a board, we agree with the approach to adopt a principle by which it is to be ensured that board of directors have the ***collective*** knowledge, skills and understanding of the business to enable them to contribute effectively. We would like to underline that the strength of cooperative banks lies in the fact that Board members have different backgrounds, are involved in the activities of their cooperatives and understand the cooperative's business model

Regarding the selection and re-appointment of members it should be taken into account that due to the core values of cooperative banks: member–ownership, 'one person - one vote' principle and the democratic election procedures, local cooperative banks have a pragmatic approach that ensures adequate skills and a diversified supervisory board as mentioned above.

- ***Commitment and mandates of board members***

We think the time commitment is a good general principle We share the idea that the aim must be to ensure that members of the supervisory board dedicate sufficient time to their mandates. However, one should see that the time commitment is one of the indicators/factors to take into account.

Therefore, it is necessary not to rely blindly on a given minimum expected time commitment and cumulative calculations. In reality, expectations of the minimum expected time may not correspond with the real commitments and arrangements to a certain mandate. Furthermore, there are on the one hand 'internal' mandates which are positions within the same banking group and to which other positions are linked, and on the other hand 'external' mandates which are positions outside of the banking group for boards in different institutions. As such the mandates of a director for all the different (technical, major subsidiary specialized in one area of banking) subsidiaries of the cooperative bank group must not be counted in the time commitment. Therefore, all the internal mandates within the same group which are linked to the position of the director should be considered as one internal mandate. As mentioned, in cooperative banks certain decisions are made under the auspices of the general assembly.

In addition, the number of boards in which a director can sit depends very much on the individual circumstances. For others who perform other professional activities, even five supervisory board mandates in large companies may be excessive. In each individual case a threshold based on a cap of board mandates could be too high or too low; thus it seems advisable to rely on the time commitment approach.

Nevertheless, any criteria for limiting mandates should be subject to the proportionality principle, since there is a difference between the mandate of a non- executive director of a small bank and between the non-executive director of a large bank. Therefore, the mandates on the supervisory board of an international large investment bank cannot be compared to supervisory board mandates of local or regional credit cooperatives , which do not appear on the capital market [see Art 39 Directive 2006/43/EC], but mainly engage in traditional retail business.

Therefore, the time commitment should be used as an indicator to ensure a sufficient commitment of board members to a certain position.