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FEDERAL MINISTRY
OF FINANCE

Comments regarding the Joint Guidelines on the assessment of the suitability of members of the management body and key function holders under Directives 2013/36/EU and 2014/65/EU.

Please find below the comments from the Austrian Ministry of Finance on the draft guidelines:

- **"Suitability assessment by competent authorities": Mandatory ex ante-assessment of the suitability of members of the management body (Title VII of the draft guidelines, p. 53-59):**

It is undisputed that members of the management body of institutions according to the CRD IV [and, limited to the requirements of good repute and possess sufficient knowledge, skills and experience as referred to in Article 91 (1) of the CRD IV, (mixed) financial holdings] must at all time comply with the requirements regarding their suitability which are stipulated in Art. 91 CRD IV. According to the wording of the CRD IV (and in line with the interpretation presented in para. 23 and 28 of the draft guidelines), compliance with these requirements is primarily within the competence of the respective institution or (mixed) financial holding company (as it is generally the case with all prudential requirements based on the CRD IV or the CRR). On the other hand, competent authorities are charged with the tasks of monitoring and assessing compliance with the requirements of the CRD IV and CRR, thus including Art. 91 CRD IV (Art. 4 paragraph 2 CRD IV). Concerning the latter, the CRD IV usually allows for a certain degree of discretion for competent authorities with respect to the approach to be chosen to ensure compliance with prudential requirements, including the appropriate point of time when to conduct assessments. Only in specific situations, compliance with the prudential requirements must be assessed by the competent authorities on an ex ante-basis; such situations usually are explicitly determined in level 1 or level 2-legislation (e.g. Art. 13 CRD IV; Art. 26 (2), 78 CRR).

Taking into account the aforementioned, we strongly advocate – as there is no legal indication which would justify a deviation from the general supervisory assessment principles in the context of corporate governance requirements – for maintaining administrative discretion in the area of corporate governance, especially regarding the question when the assessment of the suitability of members of the management body should exactly take place.

Thus, it should be ensured that competent authorities retain the right to decide whether they conduct the suitability assessment of members of the management body (and the management body as a collective body) before or after the (re-)appointment of a member[1]. This right must at least remain concerning members of the management body in its supervisory function.

Besides these legal aspects, practical problems (i.e. especially overwhelming administrative costs), which are of even more severe nature, could be prevented by maintaining the current procedural rules:

Competent authorities currently do not have to initiate formal proceedings in the context of every appointment of a member of the management body. Formal proceedings, which would always have to end with a formal decision by the competent authority (approval or denial) would require considerable additional administrative resources. Currently, such formal proceedings only have to be initiated if – according to the assessment of the competent authority – an appointed member is considered not suitable on an individual basis or if the appointment of a member results in the non-suitability of the management body as a collective body and the competent authority thus must take corrective measures to address these shortcomings. Mandatory ex ante-assessments would therefore lead to a significant enhancement of administrative costs compared to the status quo, an enhancement which hardly seems to be justifiable in relation to the possible additional value under proportionality aspects.

The additional administrative costs could become even higher when other aspects of the draft guidelines are taken into account: With a reference to para. 127 of the guidelines *("[…] where appropriate, the assessment [conducted by the institutions] should comprise different alternative compositions of the management body that can be introduced to the shareholders")*, it is possible that the competent authority would probably have to assess these different compositions if the shareholders have not already taken a final decision which particular person(s) to appoint several months before the shareholders' meeting. The result would be that competent authorities would have to assess (ex ante) the suitability of several

[1] With the exemption of the suitability assessment according to Art. 13 CRD IV, which explicitly requires an ex ante-assessment before granting an authorization.

persons (and their impact on the collective suitability) even though only one of these persons will finally be appointed by the shareholders' meeting. The other alternative would be that the decision concerning a concrete future composition of the management body in its supervisory function would have to be taken – on an informal non-binding basis, as a binding decision is not possible before the shareholders' meeting – approximately 9 months in advance of the shareholders' meeting to enable the institution to apply for approval regarding suitability (maximum period for the assessment and decision according to the draft guidelines: 6 months), to take the necessary decisions within the management body in its supervisory function and to publish the convocation and the agenda of the shareholders' meeting – according to national company law – one month in advance of the meeting at the latest. Such an extensive lead time would be practically unfeasible and hardly compatible with national company law from a legal perspective as it would considerably interfere with shareholders' rights with respect to the election of members of the management body in its supervisory function.

To sum up, **we strongly advocate for keeping the current assessment system (assessment before or after the appointment of a member of the management body, at the discretion of the competent authority), at least with regard to the assessment of members of the management body in its supervisory function,** as this system enables competent authorities to allocate their resources in a more flexible and cost-effective way and it would facilitate and accelerate the appointment procedures regarding institutions' members of the management body (in its supervisory function); in addition, national particularities with regard to the appointment of members of the supervisory board which result from national company law could be taken into account in a more appropriate way in the course of the assessment procedures by the competent authorities.

- **Independent members of a CRD-institution's management body in its supervisory function (p. 45-46 of the draft guidelines):**

Whereas the draft guidelines regarding the requirement of „independence of mind" (para. 74 to 81) for members of the management body are clearly based on and comprehensively covering the requirements of Art. 91 (8) CRD IV, such a clear legal basis does obviously not exist with regard to the draft guidelines concerning "independent members of a CRD-

institution's management body in its supervisory function". Comparing the requirements of the CRD IV with the governance requirements in other regulatory legal acts, it appears that the co-legislators recently very consciously and explicitly took the decision respectively expressed their will whether a certain number of members of a company's supervisory board must be "independent members" or not. For example, Art. 27 (2) of Regulation (EU) No. 648/2012 ("EMIR") expressly stipulates – in contrast to the governance arrangements of the CRD IV – that "*[…] one third, but no less than two, of the members of that board shall be independent."* In addition, Art. 2 No. 28 EMIR provides with a definition of *"independent member of the board".* Since such explicit requirements are lacking in the CRD IV, it is **generally questionable if there is a sufficient legal basis in the CRD IV (or the Regulation (EU) 1093/2010) which would justify the introduction of a requirement for "independent members" of the supervisory body** by means of joint ESA-guidelines in the given context.

Taking into account the aforementioned, it appears appropriate to us that, if such a requirement is nevertheless introduced "only" by means of guidelines, this requirement should not be designed in an excessive way, i.e. the definition of "independent member" should not be too broad. Moreover, it must be clearly explained in the guidelines why certain constellations/situations shall be inclined to, at least potentially, cause conflicts of interest or other undue influence and are therefore "as a general principle" considered as "not independent". Such explanations are currently omitted in the draft guidelines, para. 124 (a) to (g) only lists several situations which should not be considered independent without further reasoning. Just to mention some of these examples, it is not comprehensible without an additional clarification why a 12 years-career as member of the management body within the group per se should exclude independence; the same applies to having been "a principal of a material professional advisor or consultant to the CRD-institution or another group entity (!) within a period of three years" or being "otherwise associated with a substantial shareholder of the CRD-institution". In particular, shareholders' as well as employees' rights to be represented in the supervisory board according to national company and labour law must always be considered in context of specific prudential requirements concerning the composition of the management body in its supervisory function. Equally, it has to be taken into account that actual conflicts of interests in many cases can be addressed by appropriate mitigating measures, e.g. abstention from voting on specific matters.

Finally, some definitions used in this chapter of the draft guidelines appear to be too vague, e.g. the expression "substantial shareholder". In connection with EMIR for example, the definition of an "independent member" refers to "controlling" shareholders, a wording which we would consider more suitable also in context of the draft guidelines.

- **Scope of (parts of) the draft guidelines: Application of governance requirements to (mixed) financial holding companies (see definitions of "institutions" and "significant institutions", p. 18 of the draft guidelines):**

The CRD IV clearly differentiates between requirements for "institutions" on the one hand and requirements for (mixed) financial holding companies on the other hand: With regard to (mixed) financial holding companies, Art. 121 CRD IV limits the application of Art. 91 (1) CRD IV to the requirement for members of the management body to be of "*sufficiently good repute and possess sufficient knowledge, skills and experience as referred to in Art. 91 (1) to perform those duties, taking into account the specific role of a financial holding company or mixed financial holding company*".

This interpretation is confirmed by para. 21 of the background of the draft guidelines, stating that „*In accordance with Article 122* (Correct reference would be Art. 121) *of Directive 2013/36/EU, members of the management body of a financial holding company or mixed financial holding company* ***should be of good repute and possess sufficient knowledge, skills and experience as referred to in Article 91 (1)*** *of that Directive to perform those duties, taking into account the specific role a financial holding company or mixed financial holding company*."

Currently, there are several areas in the draft guidelines which do not appropriately reflect this distinction. This is especially odd with regard to requirements which are only applicable to "significant institutions" as defined in Art. 91 (3) and (4) CRD IV (see para. 45 to 53 of the draft guidelines: calculation of the number of directorships): It is not foreseen in the CRD IV to classify (mixed) financial holding companies as "institutions" or as "significant institutions", since the classification as "significant" is limited to "institutions" as defined in the CRD IV (i.e. credit institutions and certain investment firms, see Art. 3 (1) No. 3, 76, 77, 88, 91, 95 CRD IV). Therefore, even the possibility to classify financial holdings as "significant institution" (as

currently foreseen on p. 18 of the draft guidelines: definition of "significant institutions") seems to be inappropriate from a legal perspective. We would therefore **advocate for a better distinction between governance requirements relating to (significant) institutions as defined in the CRD IV and governance requirements relating to (mixed) financial holding companies.**