ESBG feedback on the EBA Draft Guidelines on internal governance under Directive 2013/36/EU (EBA/CP/2020/20)

ESBG (European Savings and Retail Banking Group)

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**General comments**

Adapting the guidelines on internal governance to the current legal situation is basically reasonable. However, in some places the draft’s requirements go beyond Level 1 rules. From our perspective, some adjustments should therefore be made (see specific comments).

Definitions

On one side, the term “relevant institutions” has been introduced in the Fit & Proper GL and makes difficult to further differentiate between the categories of institutions that are now in scope (there are overall 6 categories: “institutions”, “CRD-institutions”, “relevant institutions”, “significant CRD-institutions”, “listed relevant institutions and listed institutions”, “consolidating credit institutions”); on the other side, the Internal Governance GL operates with the terms “significant credit institutions” and “listed CRD credit institutions”). We recommend reviewing the definitions and operate with one set of definitions for both GLs.

1. **Are subject matter, scope of application, definitions and date of application appropriate and sufficiently clear?**

Regarding section 11 (loans and transactions with members of the management body and their related parties), we suggest extending the date of application to 1 January 2022. This would allow institutions sufficient time for implementation and avoid having to make process-related changes within a financial year.

Section 19m has been added. A reference to the definition of “large institution” should be added to clarify that it refers to the definition provided in Article 4(1) 146 of Regulation 575/2013. In this regard, the reference to large institutions when considering applying the proportionality principle could make the rest of criteria to be considered inapplicable. Therefore, it should be clarified that the rest of the criteria included in Paragraph 19 of Title I can be considered when applying the principle of proportionality even though the entity is classified as a large institution.

1. **Point (d) has been added, throughout the Guidelines references to money laundering and terrorism financing and the institutions obligations have been added, are those references sufficiently clear? The Guidelines aims at clarifying that AML/TF measures form a part of institutions governance arrangements. The EBA is developing further separate work on AML compliance.**

The expectations regarding the internal governance framework with respect to AML/CTF should be questioned. The EBA should clarify if the intention is to include references to existing AML/CTF guidelines/functions or if additional frameworks/documents in this regard are expected? If the EBA is still working on further developments, it could be more reasonable to wait for the new guidelines/work to be in place.

In addition, under the current regulation, AML policies and procedures are already a key part of the compliance function and a fundamental pillar of the internal control systems and, eventually of the internal governance framework. In this regard, letter c already refers to the obligation of setting an adequate and effective internal governance and internal control framework. Taking into account that in title V of the Guidelines (Title V develops the internal control framework) a clarification related to AML has been added in Paragraph 208 referring to the compliance function “credit institutions should take appropriate action against internal or external behaviour that could facilitate or enable fraud, ML&TF or other financial crime (…)” as well as in paragraphs 140, 149, 166 164, we suggest to delete letter d and amend letter c of paragraph 23 as follows “And adequate and effective internal governance and internal control framework as defined in title V (…)”.

1. **Paragraph 24 regarding ESG factors has been added, is it sufficiently clear? The addition is thought as providing a link between the responsibilities of the management body and the aspect of ESG factors. Respondents should be aware that the EBA is developing further detailed work in the area of sustainable finance.**

No. ESG factors are, in contrast to money laundering risks, too vague of a concept and could be interpreted as pertaining to environmental or sustainability matters for the financial institution, or more broadly for the general public, environment, planet etc. Furthermore, it is only stated that the institution should “aim at”. The guideline would therefore benefit from the “additional work” of the EBA which is referred to in the consultation paper before this amendment is introduced. Currently, our proposal is that the amendment is removed, or alternatively, that a general reference to all material risks is included.

1. **Paragraph 84 and 86 have been amended to reflect changes to CRD. Are those paragraphs sufficiently clear?**

No comments.

1. **Are paragraphs 98 and 99 sufficiently clear? They have been added to reflect changes in CRD V and to link the Guidelines to Article 157 TFEU and Article 21 of the European Charter of Fundamental Rights.**

**Paragraph 98** provides that institutions should have anti-discrimination policies, with reference to Article 21 of the European Charter of Fundamental Rights. Neither the Charter of Fundamental Rights nor banking supervision law (CRD V) provide a legal basis for comprehensive anti-discrimination policies. The European Charter is already implemented by existing national law. In the context of proportionate implementation, institutions must be given leeway on how to ensure non-discrimination. It is not necessary for credit institutions to have their own anti-discrimination policies.

In addition, most EU Member States already have separate anti-discrimination and women’s promotion schemes in place. It should at least be made clear in paragraph 98 that plans for gender equality already drawn up on the basis of other regulations should be considered as policies within the meaning of these EBA guidelines. This would prevent institutions from having to draw up further internal policies in addition to those required by national or regional law.

According to **paragraph 99**, institutions should pursue a gender-neutral policy and take measures to ensure equal career opportunities for all genders and to improve the representation of the underrepresented gender in management positions. These objectives are understandable. However, in countries with a dual board structure, the management body in smaller institutions often consists of only two members, who usually hold this position for a longer period of time. A gender-balanced composition would mean that one board member should always be a woman. Though, application procedures show that women do not always apply for board positions. In this respect, we would like to point out that this objective cannot always be achieved for purely factual reasons.

We understand that some have objected to the inclusion of the word “birth” in this amendment, especially considering that “origin” is already added. Para. 98 is however clearly aligned with the wording of the European Charter of Fundamental Rights and the difference of birth and origin is well-established (consider e.g. “noble birth”), if somewhat vague and partly overlapping. Removing it would beg the question whether there was a particular reason for doing so and whether certain forms of discrimination prohibited under the European Charter of Fundamental Rights are acceptable.

1. **Point (c) of paragraph 101 has been amended to reflect the EBA’s work on dividend arbitrage schemes. Is point (c) sufficiently clear?**

It is clear, but it is not appropriate to specifically point out to one particular kind of tax evasion scheme in this context. Tax offences should be sufficient in this regard. Inclusion of this amendment would set a bad precedent as it would set an expectation of the guidelines being updated whenever a new tax evasion scheme emerges.

1. **Section 11 has been added to provide guidelines on loans and transactions with members of the management body and their related parties, reflecting changes to CRD. Is the section appropriate and sufficiently clear?**

First of all, we would like to express our criticism of extending the requirements to other transactions. Art. 88 (1) CRD V, which is to be specified, expressly refers only to loans and does not mention “other transactions”. The extension to "other transactions", especially since this term is not precise and is not defined, is therefore not legitimate. Thus, the GL creates new requirements, which are not covered by secondary law and go beyond the scope described by Art. 16 of the EBA Regulation No. 1093/2010 which stipulates that Guidelines” are to create consistent, efficient and effective supervisory practices and ensure a common, uniform and consistent application of EU law and move within the limits (i.e. within the explicit requirements) prescribed by the applicable secondary law (in this case Art. 88 (1) CRD). The GL should rather explain or specify the documentation requirements for loans (and not transactions) to management body members and their related parties. Furthermore, the regulation applicable to transactions of a company with its directors is already set in the related parties transactions regime in Directive (EU) 2017/828, amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement. Directive 2017/828 details the framework and procedures institutions should follow regarding transactions with its directors. Adding a reference to these transactions in the GL would lead to confusion.

As a general remark, the entire section 11 is in our opinion missing clarity and does not take sufficiently into consideration that certain requirements on loans to management body members and their related parties (for example, framework, decision-making processes, control procedures, materiality thresholds) are/could be already in place in the national law of Member States. Therefore, an interference with already applicable rules of the Member States on loans to management body members and their related parties should be avoided.

In our opinion, it should be further specified that only loans that are classified as mate-rial and have been concluded under better conditions than standard conditions are subject to increased documentation or approval requirements. It is not justified and rea-sonable from an administrative point of view in our view to apply the same requirements to non-material loans and loans that have been concluded under less favorable conditions since they do not represent a conflict of interest (para. 108, 109, but also 110, 112 and 113 should be amended with this respect).

**Para. 107:**

There is no legal basis to prescribe arm’s length conditions for private-law agreements in general. The wording should be clarified as follows:

*“Such framework should include limits for loans and transactions (e.g. per product type) and ensure that they are either conducted at arm’s length or deviations are documented.”*

The requirement for a framework for granting loans and entering into other transactions with members of the management body and their related parties is generally covered by national laws and the banks´ internal process descriptions for transactions with management bodies and their related parties (including the decision-making process and the rules for dealing with conflicts of interest). In our opinion, it is not necessary to set any limits (“Such framework should include limits for loans and transactions…”) since loans to management body members are subject to risk assessments (see with this respect para. 110). The demand for the definition of limits and the assessment, if the transaction is in line with market conditions, goes not only beyond national requirements, but also beyond the new version of Art 88 (1) CRD V and should therefore be deleted.

In our opinion, no added value results from a further classification of materiality/immateriality by the EBA, since the regime for transactions with management bodies and their related parties could already be in place in national law of the Member States. It is important to highlight that the establishment of further thresholds (such as the threshold of € 200 000,- from the Fit & Proper regime) does not lead to an automatic qualification as a potential conflict of interest, especially due to the diversity of the members of the management body in their personal income and living conditions.

In general, it would be helpful to clarify, that transactions which are already qualified as immaterial on the basis of national provisions (and are therefore excluded from the approval by the Supervisory Board), are also not qualified as material under the EBA Internal Governance Guidelines (see also 109).

With respect to article 108, it could be added, “if allowed by national law”.

With respect to article 110, it is not clear what the required assessment should lead to. Should for example the loan or other transaction not be granted/accepted if it is not fair and reasonable?

**Para. 112 f**

Information that the loan is on arm´s length is sufficient for documentation purposes, it is in our opinion not necessary to refer here to “conditions available to all staff”.

**Paras. 112 g and 113:**

It remains unclear what the EUR 200 000 threshold is derived from. If this is kept, it should be clarified, that institutions are not expected to equate it with the term "material", as used in the other paragraphs of Section 11. Under proportionality aspects, corresponding classifications should be made individually for each institution. We suggest additional explanations or clarifications.

The requirements under para. 112 g i. and ii. extend illegitimately - as mentioned above at the beginning of our statement to section 11 – the scope of Art. 88 (1) CRD since they include into the calculation of the requested figures also exposures (exposures definitely go beyond loans). In addition, it is not sufficiently clear which types of positions shall be subsumed under aggregated exposures. This should be avoided, as it would lead to legal and practical uncertainties and we therefore request to completely remove para.112 g.

**Para. 114**

Considering the increased documentation requirements the present GL intends to impose and in some cases the complexity of loans to management body members and their related parties it will be extremely difficult from to make available all loans to the competent authorities without undue delay. We therefore recommend reformulating the paragraph, in order to allow institutions to have more flexibility when facing such information requests.

“*Credit institutions should ensure that the documentation of all loans to members of the management body and their related parties is complete and updated and the institution should be able to make available to competent authorities the complete documentation of a specific member or his/her related parties in an appropriate form upon request.*”

**Para. 115:**

This requirement should be deleted without replacement. Neither the CRD nor the CRR contain a legal basis for a reporting to the shareholders or owners of the institution. The provision of the Shareholder Rights Directive mentioned in the public hearing is obligatory only for listed companies. Many credit institutions in the EU operate under a different legal form, however. Extending this requirement to all institutions is not justified.

Furthermore, this requirement is incomprehensible in terms of its content, as the volume of corresponding transactions is likely to be minor at most institutions, and conflicts of interest are managed appropriately via the requirements above.

1. **Paragraph 126 has been added, is it sufficiently clear?**

**Paras. 106 and 126:**

A detailed documentation and measures should not be required for every minor or merely theoretical conflict of interest. We ask the EBA to clarify this as follows:

**106** “If a notable conflict of interest is identified”

**126** “When mitigating identified notable conflicts of interests”

1. **Paragraph 140 has been added, is it sufficiently clear?**

Specific risk mitigation measures with regard to operational and reputational risks arising from ML/TF risks are not necessary for all institutions, as these depend largely on the nature and complexity of individual business activities. This should be clarified as follows:

*“and take mitigating measures to reduce those risks as well as, where relevant, their operational and reputational risks linked to them.”*

**As regards paragraphs 140 and 149:**

Does EBA aim for the integration of the AML/CTF check in the general risk management? If so, what effects would this have on the responsibilities within the credit institutions? In any case, the results of the AML/CTF check cannot have any impact on regulatory requirements, especially not on capital requirements; a negative result of the AML/CTF check can only result in the rejection or increased monitoring of the business relationship.

Some additional comments:

* **Paragraph 166.:** Are the control functions supposed to cover new/additional tasks (see also comments with respect to 140. and 149.) or shall AML/CTF aspects be integrated in the respective department.
1. **Other comments**

***Paragraph 21 (background)*:** Please see the proposed changes in red. *Combating money laundering and terrorist financing is essential for maintaining stability and integrity in the financial system. Uncovering involvement of a credit institution in money laundering and terrorist financing might have an impact on its viability and the trust in the financial system. Together with the relevant authorities and bodies [what bodies?] responsible for ensuring compliance with anti-money laundering rules under Directive (EU) 2015/849, competent authorities have an important role to play in identifying and tackling weaknesses. In this context, the guidelines clarify in line with Directive 2013/36/EU that identifying, managing and mitigating money laundering and financing of terrorism risks, is part of sound and prudent internal governance arrangements and credit institutions risk management framework.”*

***Paragraph 19 d*:** There is an errant “t” at the end of the row.

***Paragraph 32*:** The Directive 2015/849/EU should have been transposed to national law already. It seems a bit excessive to include references to other regulatory requirements.

1. ***Paragraph 51:*** *Credit institutions should consider the occasional rotation of chairs and members of committees, taking into account the specific experience, knowledge and skills that are individually or collectively required for those committees. This rotation should take into account the national specificities of Member States, as some already have laws to completely renew members after a fixed period of time.*

***Paragraph 129:*** *It is questionable whether there is any added value to insert a requirement to ensure that credit institutions are compliant with national law in one certain aspect.*

***Paragraph 139 and 140:*** Proposed changes in red in order to clarify. *Credit institutions should implement appropriate processes and procedures that ensure that they comply with their obligations in the context of combating money laundering and terrorist financing. Credit institutions should assess their exposure to the risk that they may be used for the purpose of ML/TF and take mitigating measures to reduce those risks as well as their operational and reputational risks linked to them. Credit institutions should take measures to ensure that their staff is aware of such ML/TF risks and the impact that ML/TF has on the credit institution and the integrity of the financial system. Proposed changes: “Credit institutions should implement appropriate processes and procedures ensuring compliance with applicable obligations relating to combating money laundering and terrorist financing. Credit institutions should assess the risk exposure of being used for the purpose of ML/TF and take mitigating measures to reduce those risks as well as their operational and reputational risks linked to them. Credit institutions should take measures to ensure that their staff is aware of such ML/TF risks and the impact that ML/TF has on the credit institution and the integrity of the financial system.”*

***Paragraph 149:*** *ESG-factors are too vague of a concept to be included in this manner without any clarifying information. It is very unclear how ESG-factors in and of itself constitutes a risk-type of its own. We suggest that the reference to ESG is removed. Please also see our comment to article 24 above.*

***Paragraph 164:*** Remove “their”, please see proposed changes in red: “*Furthermore, to comply with ~~their~~ obligations under Directive (EU) 2015/849, credit institutions should identify and assess the ML/TF risks associated with the new product or business practice, and set out the measures to take to mitigate those risks.”*

***Paragraph 166:*** Proposed changes in red: “*The responsibilities of control functions also include ensuring compliance with AML/CTF requirements.”*



**About ESBG (European Savings and Retail Banking Group)**

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