

Prudential Policy Unit
International Credit Institutions
Financial Regulator
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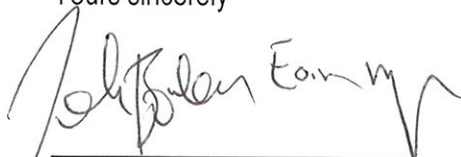
Re: Consultation Paper CP 41, Corporate Governance Requirements for
Credit Institutions and Insurance Undertakings

Dear Madam/Sir

Please see attached a joint submission of comments on the above consultation paper by German IFSC banks for your consideration.

The authors of these comments are the undersigned CEOs/Senior Officers. Please address any questions/comments for coordination purposes to Werner Schwanberg, WGZ BANK Ireland plc, 3, Harbourmaster Place, Dublin 1.

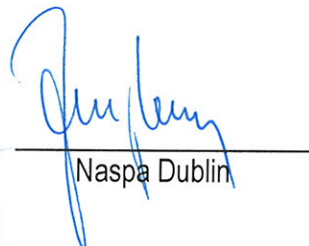
Yours sincerely


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Central Bank & Financial Services Authority of Ireland

Consultation Paper CP 41 (the paper)

**Corporate Governance Requirements for
Credit Institutions and Insurance Undertakings**

Joint submission of comments by the undersigned IFSC subsidiaries of German banks

1. General

The recent international financial crisis was exacerbated in Ireland by the property boom related softening of lending standards in the retail sector and the deterioration of governance standards in a small number of domestic institutions.

The proposals published for consultation are an understandable measure by the Financial Regulator to enhance corporate governance in relevant major financial institutions in the State. However, they do not clearly distinguish between these major institutions (mainly retail banks) and the typical IFSC wholesale banks and therefore fall short of the necessary proportionality which has been publically proclaimed by the Regulator.

The question is, how does the international (IFSC) business model fit in and is it warranted and wise to tar all institutions with the same brush. While the paper hints at differentiation between institutions with lesser economic significance and major institutions, the wording is unclear and the differentiation insufficient.

What may fit and work well for major systemically important institutions (mainly retail sector) could be counterproductive for international and non systemically important institutions (mainly IFSC banks).

It may, therefore, be prudent to look at the potential impact on IFSC institutions in more detail.

2. Wholesale banks in the IFSC

Since its inception the IFSC has fully achieved its objective of directly creating well over 20,000 jobs, supported the development of the dockland area and made significant taxation contributions, both corporate and personal to the Exchequer. Following high level marketing efforts a large number of small to medium sized banks from abroad located and invested significantly in the IFSC.

Most German owned IFSC banks have the following characteristics:

- established as a subsidiary between 1989 and 1999
- full Irish Banking Licence
- 100% owned subsidiary of German parent
- letter of comfort to the Irish regulator provided by parent company
- sufficiently capitalized
- 20-40 employees
- wholesale banking only, no retail banking
- balance sheet between 1 and 10bn €

How did the financial crisis in Ireland impact on these Banks?

- all banks were affected by the global crisis in the capital markets
- none suffered from the Irish 'home made' problems (real estate / governance deficits)
- none required any Irish state aid or cost the Irish taxpayer any money
- all were protected by the parent company if protection or additional capital was needed
- none showed any material weaknesses in corporate governance

The undersigned maintain that these banks at all times had appropriate and robust corporate governance structures in place which were fully compliant with all legal and regulatory requirements. We also feel that we were subject to an adequate level of supervision, in fact, our parent banks would not have sanctioned the establishment of subsidiaries in Ireland had this not been the case.

What is the average governance structure of an IFSC wholesale bank?

The board of directors of a typical German/Continental European IFSC Bank normally combines elements of a continental two tier board with elements of the Anglo-Saxon board structure as found in Ireland. In other words there is typically a strong shareholder presence on the boards. The chairman is in most cases a member of the parent company's board / senior management. Non executive directors (NED) often comprise of further shareholder representatives and Irish resident NEDs. The Irish NEDs generally are recruited according to their skills (legal, banking, insurance) which compliment those of the shareholder representatives on the board.

This inevitably leads to a lesser degree of NED independence than may be proposed by the governance codes. However, while the board has overall responsibility, strategy of such a bank/board is naturally integrated with the group strategy and, therefore, subject to a strong influence from the shareholder representatives together with the executive directors on the board. This somewhat lessens the importance of independence. The decision to prescribe the definition of independence in the paper causes significant problems for the banks and would necessitate major reshuffles of boards. Beside everything else, the natural limits on qualified resources, prohibition of cross board

membership and stringent limitations in directorship numbers would, in our view, threaten to diminish the quality of boards in such international banks.

In view of the limited scope of independent strategic development by a subsidiary due to its close links with the group, a frequent turnover of directors does also not necessarily enhance corporate governance in those cases, nor does the provision that the Chairman must be independent from the group to name but a few examples from the consultation paper. In fact, we cannot envisage a German financial institution handing over the chairmanship or voting majority of an Irish subsidiary to independent directors after capitalising it with, for example, €300m and issuing a letter of comfort.

3. Summary

It seems, therefore, that the provisions of the consultation paper on corporate governance for banks and insurances are geared towards holding companies and not towards the typical IFSC subsidiary of an international bank. If that is the case, it should be made clearer in the document. Proportionality should be risk based and applied by categorising licenced institutions and by significantly down-scaling the demands on the smaller IFSC wholesale banks and clearly differentiating them from large systemically important institutions. Furthermore, we note that the Financial Regulator's new supervisory structure clearly distinguishes between retail and wholesale banks, which supports the case for alternative corporate governance rules for wholesale banks.

We understand that it is not the responsibility of the Financial Regulator to market Ireland as a Financial Centre, however, throughout the years different governments have stressed time and time again the importance of the Centre. In the interest of the Irish economy it is essential to strike the right balance between attracting investment and having a robust but reasonable supervisory regime.

We strongly believe that the vast majority of this type of IFSC bank will reconsider their investment in Ireland if the goalposts were moved now and the proposed governance rules were to be enforced. The marketing of the IFSC is at present a difficult task. Perceived overregulation would make it impossible. We would run the risk of creating regulatory arbitrage in the wrong direction, i.e. away from Ireland.

The following are comments on specific provisions in the consultation paper:

**Comments on the provisions of the
Consultation Paper CP 41
'Corporate Governance Requirements for Credit Institutions and Insurance
Undertakings'**

Page 4 para 3.0 'Scope'

It should be considered to reduce the requirements for non systemically important subsidiaries of holding companies regulated in a member state of the EU. This should enable relevant institutions to continue in business in Ireland with an appropriate level of supervision.

Page 5 para 4.3 'compliance statement'

This requirement is reminiscent of proposals for company law a few years ago, albeit on a wider scale. Those proposals were dropped for various reasons. In order to enable institutions to comply with the now proposed compliance statements it is firstly necessary to establish exactly the extent of requirements imposed in wholesale banks after applying proportionality. Secondly, further guidance from the Regulator as to the format of these compliance statements would be advantageous.

Page 9 para 1.4 'applicability'

We consider that further clarification on the scale and nature of proportionate application is needed. (see also Page 4 para 3.0 'Scope')

Page 10 para 1.5 'Major institution'

The definition is not quite clear. What are large international activities?

Page 10 and 11 para 1.5 'Director Independence'

It is, in our view, problematic to prescribe what constitutes independence rather than, for instance, give recommendations. Having to strictly adhere to these criteria would upset the board compositions of all of our banks. It could be counterproductive and potentially lead to a dilution of quality and skills in the current boards. As mentioned before, there is typically a strong and deliberate shareholder presence on those boards (including the chairman).

In addition, the boards benefit from legal and financial local expertise coming from Irish NEDs. The fact that those NEDs may not be regarded as independent because they might supply some small professional services through their companies would rule them out of the equation and force changes to the boards of our banks which could be detrimental for the companies involved.

Insisting on these criteria in conjunction with the further requirements for board composition would unjustifiably decimate well performing boards and generate a 'scramble' for directors whose main virtue would be their independence.

Pages 15 – 17 4.0 'Composition of the Board'

The following sub paragraphs are impractical as outlined below:

4.1

For foreign owned subsidiaries the investors/shareholders will always want to see a strong shareholder representation on their boards, including the chairman.

4.5

Given the requirements especially for foreign subsidiaries to supplement skills with local experts does lead to, for example, partners of law firms or other advisors being appointed to several boards. In the case of the IFSC wholesale banks this should not be a disadvantage or reduction of corporate governance standards. The professionals who are appointed to our boards have shown to commit sufficient time and resources to their roles on our boards.

4.6

Please see 4.5

On a more general note, we don't think the prescription of numbers of directorships is necessarily beneficial. A director can well manage a number of funds or Special Purpose Companies, whereas a position on the board of a major financial institution, or, indeed, a major company may not leave time for other directorships. Company law prescribes a maximum of 25 directorships which does not even include Plcs. The qualifications of an individual director should be taken into account. To retrospectively force a director to give up directorships, some of which may have been approved by the regulator through the fitness and probity process previously, could force those directors to neglect their duties to those companies. It would also create uncertainty amongst investors, fund promoters etc.

The regulator should in each individual case through the fitness and probity test determine a director's ability to fulfill his role adequately and maybe impose a duty to inform the regulator of any new directorships. This would give the regulator the possibility to review their position on a case by case basis.

4.12

This point is in our view sufficiently covered in company law and Memos and Arts. It is questionable if these additional requirements add any value for the governance of IFSC wholesale banks.

Page 18 5.0 'Chairman'

The following sub paragraphs are impractical for small IFSC banks and should not apply to them:

5.6

The chairman of a fully owned subsidiary will always be nominated by the shareholder for approval by the board of directors and, therefore, not be independent in the spirit of the paper. Enforcement of this rule will be a major stumbling block for Ireland when strategic decisions in respect of location are made at group level.

5.8

As explained before (see also introduction), subsidiaries of foreign banks generally have a shareholder representative as chairman. The shareholder will in his own interest ascertain that the person nominated to guard their interest has sufficient time to do so. These are normally senior representatives with a dedicated staff of their own in the parent company. It would not add any value to corporate governance standards to force these individuals to apply for permission from the Irish regulator before taking up a directorship outside Ireland. On the contrary, it may negatively influence further strategic decisions at group level.

5.10

This requirement is not practical for group companies.

Page 19 6.4 'Renewal of CEO contract'

As with the chairman, the recruitment and nomination of the CEO is in the first instance carried out by the shareholder of the subsidiary and then ratified by the board of directors. The employment of a CEO is normally based on a legally binding contract between the institution and the CEO. These contracts do not necessarily have fixed terms. If a board fulfills its duties correctly, the performance of a CEO is under constant review. This point does not add value to the corporate governance structure of IFSC wholesale bank subsidiaries.

Page 20 para 7 'Independent Non-Executive Directors'

The independence requirements do not take into account the well working governance structures of foreign owned subsidiaries as described above. In general, please see our above comments (in relation to page 10 and 11 para 1.5 'Director Independence').

Page 21 para 8 'Role of the Board'

The role of boards is exhaustively documented in law and numerous publications including the UK Combined Code. In Ireland, the Director of Corporate Enforcement has issued excellent guidance notes in relation to the role of directors. In our view it would create potential for confusion and deterioration of standards, if each board would separately define and document its role again. Therefore, 8.2 should be deleted for all institutions.

Page 22 para 9.0 'Appointments'

9.1 and 9.2

Which senior positions should be endorsed/appointed by the Board?

9.4

The responsibilities of directors are laid down in law and further in the Memos and Arts of a company. All directors are equally responsible. Additional definitions of directors' responsibilities could lead to confusion and misunderstandings.

This is different in the case of Board Committees to which the board delegates powers. Here it is appropriate to have Terms of Reference or Charters.

9.5

This requirement should be viewed proportionately and formal, documented reviews are not practical for small wholesale institutions.

9.6

This requirement does not lend itself to formal documented procedures in the case of small IFSC banks.

Page 24 para 11.0 'Meetings'

11.1 The frequency of meetings for IFSC subsidiaries of international banks should be determined in the spirit of proportionality and practicability. In practice there are informal contacts between management and among directors on an ongoing basis between the scheduled board meetings. We regard a minimum of 4 meetings per annum for IFSC subsidiaries as being sufficient.

11.4 A conflict of interest policy for small IFSC banks should not be necessary as potential conflicts of interest are noted in the board minutes.

Page 27 para 14.0 'Committees' and page 31, para 18.0 'Risk Committee'

In a number of cases the role of the Audit- and/or Risk Committees are covered by the board of directors. The nature of the business, the frequent reporting and close communication between management, board, auditors and shareholders has in the past and will in future ensure adequate governance and controls in those institutions.

It is hoped that principles of risk based proportionality will be applied in the case of small IFSC banks.

Page 28 para 15.0 'General Requirements of Committees'

15.1 b)

We assume that the recording of 'discussion' in the minutes does not literally mean word for word records of conversations, which would necessitate taping the meeting. In our view the standard of minutes of board meetings in our banks is high and sufficient. We would ask the regulator to review and confirm or comment on it further. We ask the Regulator to clarify this requirement.

Page 30 para 17.0 'Audit Committee'

Please see comments on **Page 27 para 14.0**

Page 34 para 21.0 'Compliance Statement'

Please see comments on **Page 5 para 4.3**

In order to enable institutions to comply with the proposed compliance statements it is firstly necessary to establish exactly the extent of the requirements imposed on wholesale banks after applying proportionality. Secondly, further guidance from the Regulator as to the format of these compliance statements would be advantageous.

Signed:

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