The independently functioning supervisory board: the Dutch Central Bank updates its position

Connecting today, shaping tomorrow

Introduction and background

Good governance is seen as an essential part of what defines a solid and sound financial sector. In the Netherlands, limited liability companies have a management board, which is responsible for the day-to-day management of the company, determining the company's policies and strategy. In addition, a company may have a supervisory board, which is responsible for supervising the policy determined and pursued by the management board and the company's general course of affairs and advising the management board in respect of its duties. Generally, having a supervisory board is optional, but for large companies and for certain financial institutions, a supervisory board is mandatory in the Netherlands. Prioritising ethical behaviour and proactive risk management enables institutions to meet their duty of care amidst changing ESG dynamics.

Scope of the independence-requirement

Not all Netherlands-based financial institutions are required by law to have a supervisory board. For banks, insurance companies and clearing institutions, a supervisory board consisting of at least three members, is mandatory. For payment institutions, electronic money institutions, currency exchange institutions and premium pension institutions, the law does not require a supervisory board. Having said this, these institutions are legally required to maintain a clear, balanced and appropriate organisational structure. Based on this, the Dutch Central Bank (DNB) often requires that a supervisory board is put in place.

Whilst for significant banks the European Central Bank is the competent supervisory authority, the guidance from DNB discussed below also applies to those banks in the Netherlands.

Background of independence requirement: suitability screening

For financial institutions, if there is a supervisory board, regardless of whether the supervisory board is mandatory or not, the supervisory board must consist of persons that are suitable for the performance of their duties. The suitability assessment relates to the duties and tasks of the supervisory board member and takes into account that person's knowledge, competences and professional conduct. DNB recently also updated its policy with respect to what it regards as "suitable" and what aspects it considers when assessing management and supervisory board members.

A fundamental part of the suitability assessments made by DNB is the assessment of independence. In order to pass the assessment, the members of the supervisory board must be able to make autonomous, objective and independent decisions.

DNB updates its position

Based on the Guidelines on Internal Governance, published by the European Banking Association (EBA) in 2018, DNB formulated its position in 2019 on what it considers to constitute an independently functioning supervisory board (or similar supervising body). In its guidance of 2019, DNB generally followed the criteria and guidance of the EBA guidelines but deviated on some points. On 1 May 2023, DNB announced that it would update its position. On 26 February 2024, DNB published its updated views in this respect. This briefing sets out the most important updates compared to the previous position from DNB.

2019: previous DNB position – applicable to all types of financial institutions

In its guidance of 2019, DNB made a distinction between three elements of independence with respect to the independence of the supervisory board:

- *Independence in mind*: supervisory board members must act with independence in mind. The supervisory board member must have the courage, power and conviction to critically assess the management board's policy and proposals, without being guided by for instance group thinking. It must be avoided that the independence and objectiveness of supervisory board members is prevented by conflicts of interest.
- *Independence in appearance*: the appearance of conflicts of interest must also be prevented and managed. The supervisory board must have policies in place to handle situations in which a (potential) conflict of interest occurs. Supervisory board members are not permitted to be involved in certain decision making in case they have a personal conflict of interest.
- *Formal independence / independence of state*: the supervisory board must consist of a sufficient number of formally independent members. A formally independent member does not have (or has not recently had) a relationship with the financial institution that could impact its decision making. DNB applies a minimum requirement of 50% of the supervisory board members that must be formally independent.

2024: updates in DNB position – mainly focused on independence of state

The update of DNB's position mainly entails additions or refinements with respect to the independence of state of the supervisory board. This is particularly relevant with regard to the number of formally independent supervisory board members that is required.

Number of formally independent supervisory board members
For banks, DNB states that it will follow the EBA Guidelines on Internal Governance with respect to the independence of state of the supervisory board of banks on the following points:

- Significant or listed banks must have a "sufficient" number of formally independent supervisory board members. DNB does not explicitly state what it considers to be a sufficient number, but it seems to be maintaining its current view that this is in principle at least 50% of the supervisory board.
- Non-significant and non-listed banks must in principle have at least one formally independent supervisory board member.
- Banks that are fully owned by another bank in the same member state are under certain circumstances not required to have formally independent supervisory board members.

With respect to financial institutions other than banks, it is DNB's view that a "sufficient" number of formally independent supervisory board members is required to ensure effective safeguarding of controlled and sound business operations. In response to questions from market participants, DNB has stated that its prior view that a "sufficient" number is in principle at least 50% of the supervisory board, will no longer apply as such. According to DNB, the relevant circumstances could entail that less than 50% of the supervisory board are independent.

Circumstances that may require a higher or lower number of formally independent supervisory board members

DNB states in respect of all types of financial institutions that it will take into account all relevant circumstances when assessing the independence of the supervisory board, which could lead to a higher or lower proportion of the supervisory board members being required to be formally independent. In this regard, DNB highlights four circumstances that it will in any event take into account to determine the minimum amount of formally independent supervisory board members:

1. The nature, scale, risks and complexity of the activities of the financial institution.
2. Group structure / different services: the independent role of the supervisory board becomes more important if the interests of the financial institution deviate from the interests of its parent company because the parent company provides different regulated services.
3. Majority shareholder: where the financial institution has a majority shareholder, the independent supervision of the supervisory board is of additional importance to ensure a balanced representation of the interests of all stakeholders.
4. Parent company outside of the European Economic Area (EEA): in the event that the financial institution has a parent company that is located outside of the European Economic Area (EEA), the parent falls outside of the scope of European regulatory supervision. In such case, additional importance is attributed to an independent supervisory board that is able to ensure a balanced representation of interests.

Intra-group relationship risks are of DNB's concern

Most of the circumstances set out above relate to intra-group relationships and the risks that those could bring for a financial institution's soundness. These risks are receiving particular attention from DNB. DNB's position with respect to the supervisory board's independence, must be seen within the context of the broader set of guidance by DNB, such as its recent consultation with respect to the management of intra-group risks by electronic money institutions and payment institutions.

Impact

Financial institutions licensed in the Netherlands which have a supervisory board as part of their internal governance, are advised to assess whether the independence of their supervisory board remains in line with DNB's updated view and should take into account the updated position when appointing, reappointing and replacing supervisory board members.

Want to know more about this topic?
We are happy to help you.

Larissa Silverentand
+31 6 53 95 93 61
larissa.silverentand@nautadutilh.com

Charlotte Sonneveld
+31 6 51 64 35 32
charlotte.sonneveld@nautadutilh.com

Published in the April 2024 issue of Butterworths Journal of International Banking and Financial Law