As prepared for delivery

Corporate governance: a building block for financial resilience

G20/OECD Seminar on Corporate Governance:
Corporate Governance in Today's Capital Markets
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Remarks by Dietrich Domanski, Secretary General, Financial Stability Board[1]

Thank you for inviting me to speak today.

Poor corporate governance as a driver of the financial crisis

Failures in corporate governance were one of the factors that contributed to the financial crisis. Inquiries found many examples of poor governance at the firms at the centre of the crisis.

Corporate governance failures were also an issue in the significant misconduct with benchmark setting and in foreign exchange markets. Misconduct in these markets was sufficiently severe and pervasive that it threatened to undermine activity in key global financial markets.

Common governance failings at financial institutions came in many forms: a lack of challenge of senior executives by board members with insufficient experience; a lack of independence for risk functions; poorly aligned incentives created by compensation frameworks with only up-side for senior executives; and employees taking actions which were clearly against the interests of their clients.

Given the systemic nature of the inappropriate behaviour, these issues were not only of interest to conduct regulators, but also prudential regulators. In terms of responses, one angle was to strengthen governance frameworks, the other to improve practices in financial institutions. These two angles have also been reflected in the work of the FSB.

Two strands of FSB work: misconduct workplan…

In May 2015, the FSB launched its misconduct workplan. The overall objectives of the work were, first, to reduce the opportunities for misconduct and, second, to strengthen the ability to contain associated risks.

The work progamme was completed last year. Outputs from the workplan included: a toolkit for firms and supervisors to tackle the causes and consequences of misconduct; the development of the *FX Global Code* by the Bank for International Settlements; a toolkit to address misconduct in wholesale markets from the International Organization of Securities

[1] The views expressed are those of the speaker and not necessarily those of the FSB or individual FSB members.

Commissions; and additional guidance by the FSB on the implementation of the FSB's standards on compensation.

Common to all of these was a focus on improving corporate governance at financial institutions. As such, these tools and guidance complement the G20/OECD Principles.

…and work on compensation

The second strand of FSB work pertinent to our discussion today is related to compensation practices. Work on compensation has been on the FSB's agenda for a decade now following the publication of the FSB's Principles and Standards on compensation in 2009.[2] The principles and standards promote sound compensation practices and align compensation with prudent risk-taking, so that compensation provides the right incentives to maintain a healthy financial system.

Through peer reviews, progress reports and engagement with the industry the FSB has continued to maintain a focus on this issue. In the coming days the FSB will publish the latest of its progress reports on the implementation of the principles and standards. The report highlights progress on implementation of the reforms for significant banks but also the need for continued vigilance to ensure risk alignment.

The principles and standards have significantly strengthened governance and rigour around compensation decisions at banks. However, further work remains to assess the effectiveness of the regimes put in place and to ensure that outcomes are aligned with the intended policy objectives. And, there needs to be more consistent implementation of the P&S across the financial sectors since implementation is more advanced for significant banks than it is for other financial sectors.

Global standards to ensure effective corporate governance

Global standards provide a basis for international consistency on corporate governance. The G20/OECD's *Principles of Corporate Governance* have been designated as one of the FSB key standards for sound financial systems. The World Bank benchmarks member countries' corporate governance frameworks and company practices against the Principles.

In 2017 the FSB published a thematic peer review which considered the implementation of the Principles for financial institutions.[3] On the positive side, the review found that, while all FSB member jurisdictions have a comprehensive corporate governance framework. On the less positive side, its effectiveness can be impacted if the division of responsibility among financial sector authorities is unclear or if the various requirements overlap, leave unwarranted gaps, or are otherwise not well aligned with each other. The peer review set out a series of recommendations to address these issues.

[2] FSB, *Principles for Sound Compensation Practices*, April 2009; *Implementation Standards for the FSB Principles for Sound Compensation Practices*, September 2009

[3] FSB, *Thematic Review on Corporate Governance*, April 2017

Robust minimum international standards have a role to play in fostering better corporate governance. But it is the implementation of those standards at the level of individual jurisdictions that determines their effectiveness. Like in other areas of post-crisis reforms, this is where continued effort is needed.

I look forward to our discussion.