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Insights

STRENGTHENING YOUR CORPORATE GOVERNANCE FRAMEWORK TO WEATHER THE STORM

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SUMMARY

There has been a significant increase in the level of regulation concerning corporate governance since the last financial crisis. But what exactly are the regulators looking for, and how high should it be on your regulatory priority list for 2021?

In recent times, there has been a significant increase in the level of regulation concerning corporate governance. Against the backdrop of the current pandemic, with firms facing previously unimaginable commercial challenges with a scattered workforce, strong corporate governance is arguably more important than ever.

Regulators have expressed a desire for strengthening corporate governance in key areas. These include:

1. **Strong subsidiary board governance within UK-authorised firms sitting within large international groups**. There is a concern on the regulators' part that the boards of subsidiary undertakings may not be sufficiently independent from the firm's parent company or shareholders to be able to take the right decisions from the perspective of the UK subsidiary (or branch).
2. **Better governance in relation to non-financial misconduct and other 'people-related' risks**. The regulators are keen to see more consideration being given at board level to how the firm's staff behave, and what motivates them in doing so (with remuneration and performance management being two key examples).
3. **Greater diversity on the boards of authorised firms**. Regulators have repeatedly made their views clear in relation to this area: the messages are now getting stronger and have crystallised into a settled regulatory view that lack of diversity on boards is a risk management issue, given the risk of 'groupthink' that such lack of diversity can engender.

From a regulatory perspective, these objectives matter now for three key reasons:

1. Effective corporate governance operates as a protective mechanism for firms against regulatory risk.

2. Sound corporate governance is essential for the development and embedding of a sound corporate culture.

3. PRA review evaluating the effectiveness of the SMCR regime on a “multi-sector” basis.

It is clear that strengthening your corporate governance framework to meet the regulators’ evolving expectations should be kept high on your list of priorities for 2021. Not only will the regulators be happy to see you doing this, but it will also improve your regulatory risk profile.

Polly James, Ariel White-Tsimikalis and Siân Cowan wrote about this in our Emerging Themes in Financial Regulation 2021 publication.

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