nestor advisors
A MORROW SODALI COMPANY

TRENDS IN FINANCIAL INSTITUTIONS' GOVERNANCE

20 October 2022

SUITABILITY

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In Europe, due to structural deficiencies in management oversight and board functioning, for 2022-24, the ECB plans to focus on the collective suitability of the board and management.

European Central Bank, Supervisory Priorities for 2022-2024, 2022;
Saudi Arabian Monetary Authority. Key Principles in Governance in Financial Institutions. 2021.

CYBER GOVERNANCE AND DIGITAL OPERATIONAL RESILIENCE

BCBS

Emphasizes the board's role on operational resilience with help from management.

Boards are expected to:

- Approve risk appetite and tolerance for disruptions to critical operations;
- Ensure bank's policies address barriers to meeting stated tolerance for disruption.

Management should provide timely reports on the bank's ongoing operational resilience approach in support of the board's oversight.

DIGITAL OPERATIONAL AND RESILIENCE FOR THE FINANCIAL SECTOR ACT ("DORA")

DORA pushes banks to fully understand how their ICT, operational resilience, and cyber risk management practices affect their most critical functions.

Under DORA, boards are responsible for:

- Setting clear roles and responsibilities for all ICT-related functions;
- Establishing appropriate governance arrangements to ensure effective and timely coordination among functions.

86%

*Of global banks identify cybersecurity and digitalization as material**

MAS Monetary Authority of Singapore

The Monetary Authority of Singapore requires financial institutions to have a comprehensive technology risk and cyber-security training programme for the Board.

BCBS, Principles for Operational Resilience, 2021; BCBS, Revisions to the Principles for the Sound Management of Operational Risk, 2021; Proposal for a Regulation of the European Parliament and of the Council on Digital Operational Resilience for the Financial Sector, June 2022;
BCBS, Cyber Resilience – Range of Practices, 2018; *Nestor Advisors 2022 Global Banking Study

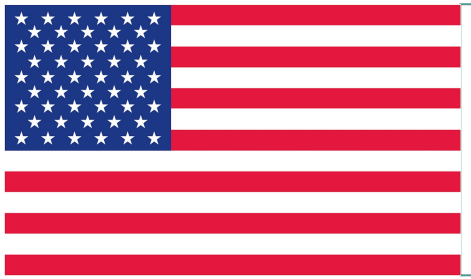
RESILIENCE: THIRD-PARTY RISK MANAGEMENT

WITH HEIGHTENED BANK OUTSOURCING, SUPERVISORS EXPECT BOARD AND MANAGEMENT EMPHASIS ON OVERSIGHT OF CRITICAL THIRD PARTIES

Banks should have review and approval processes for outsourcing bank functions.

The risk management function should provide input on the risks and on the outsourcer's ability to manage risks and comply with legal and regulatory obligations.

The UK recently laid out in *The Financial Services and Markets Bill 2022* a statutory framework for managing systemic risks from such providers e.g., cloud services and data analytics.

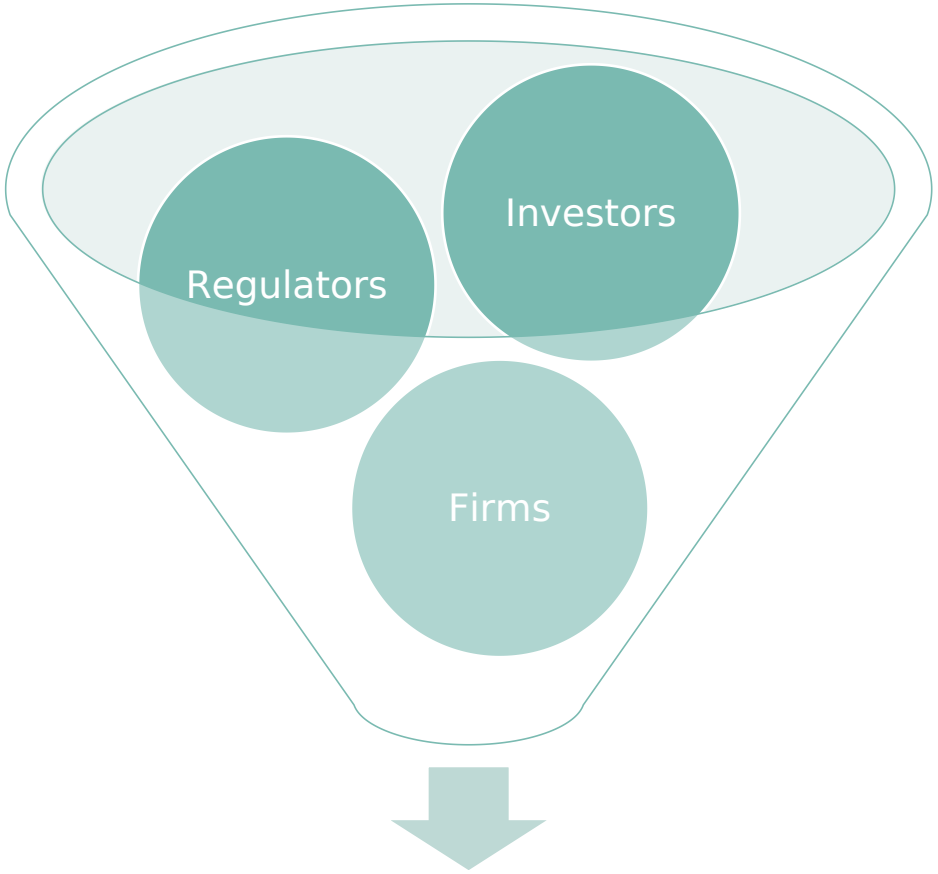


The US Federal Reserve and other agencies issued a joint proposal advising bank boards, with the support of management, to approve policies that govern third-party management, approve contracts with third parties involved in critical activities, and review management reports on ongoing monitoring of critical third-party relationships.

Basel Committee on Banking Supervision. Guidelines corporate governance principles for banks. 2015.
Federal Reserve System, Federal Deposit Insurance Corporation, and Department of Treasury, Office of the Comptroller of the Currency, Proposed Interagency Guidance on Third-Party Relationships, Risk Management. 2021;

THE DRIVERS OF SUSTAINABILITY

INSIGHTS FROM OUR BANKING STUDY



Sustainability

	Strategy		Risk	
	US / UK	Europe	US	Europe / UK
Firms	2	2	2	2
Investors	3	2	2	2
Regulators	1	2	1	3
Total	6	6	5	7

Key:

1 = low push / pull

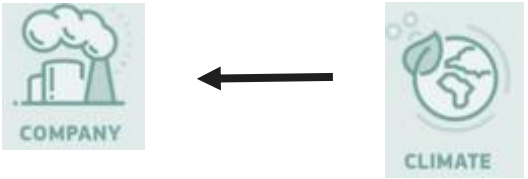
2 = medium push / pu

3 = high push / pull

CLIMATE: GREEN FINANCING OPPORTUNITIES

FINANCIAL MATERIALITY

To the extent necessary for an understanding of the company's development, performance and position



Climate change impact on company

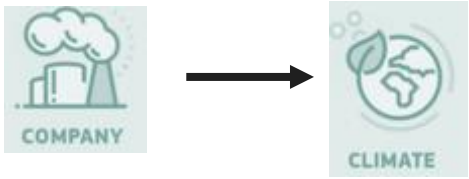
Primary audience:
INVESTORS

RECOMMENDATIONS OF THE TCFD

Company impact on climate can be financially material

ENVIRONMENTAL & SOCIAL MATERIALITY

… and impact of its activities



Company impact on climate

Primary audience: **CONSUMERS, CIVIL SOCIETY, EMPLOYEES, INVESTORS**

EUROPEAN COMMISSION

NON-FINANCIAL REPORTING DIRECTIVE

% 1.8 TRILLION

EU Commission estimate of financing required for the green transition in the EU

Financial institutions can contribute to the green economy by:

- Investing in projects focused on renewable energy and energy efficiency, circular economy initiatives;
- Investing in green bonds; and
- Investing in innovative technologies, such as carbon capture and storage (CCS), green and blue hydrogen, sustainable aviation fuels and green amm

WORLD ECONOMIC FORUM

Examples of banks embracing opportunities:

BARCLAYS

Bank of America

EU Commission, Guidelines on reporting climate-related information
World Economic Forum. What is green finance and why is it important. 2020. and Financing the Transition to a Net Zero Future

CLIMATE: CLIMATE GOVERNANCE

THE BOARD AND SENIOR MANAGEMENT SHOULD CLEARLY ASSIGN CLIMATE-RELATED RESPONSIBILITIES TO MEMBERS AND/OR COMMITTEES AND EXERCISE EFFECTIVE OVERSIGHT OF CLIMATE-RELATED FINANCIAL RISKS

BCBS published 18 principles covering corporate governance, internal controls, and capital adequacy for effective management of climate-related financial risks.

Global banks' board-level sustainability governance practices:

Board structures	Average
(A) Dedicated committee ***Where the company has a standalone sustainability committee that reaches decisions and makes recommendations for whole board approval***	48%
(B) Sustainability fully integrated ***Where sustainability is an integral part of board deliberations and decisions and is fully integrated into the organisation's long-term strategy.***	28%
(C) Added to an existing committee ***Where sustainability is formally added to the responsibilities of an existing committee, which has responsibility for making recommendations and decisions for the whole board to approve on most sustainability issues***	24%

Global banks' executive-level sustainability governance practices:

Executive structures	Average
(A) Senior Management committee on sustainability chaired by member of ExCo ***In these cases, on average 22% of Heads of Sustainability sat on ExCo.***	46%
(B) No senior management committee on sustainability – Full ExCo responsibility ***In these cases, on average 43% of the Head of Sustainability sat on ExCo.***	29%
(C) Management committee on sustainability not chaired by member of the ExCo ***In these cases, on average 43% of the Head of***	25%

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