Institute
and Faculty
of Actuaries

CP18/15 – Corporate governance – Board responsibilities

IFoA response to the Prudential Regulation Authority

11 September 2015

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Institute and Faculty of Actuaries

Hugh Burns and Christopher Forster
Bank of England
Threadneedle Street
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11 September 2015

Dear Mr Burns and Mr Forster

PRA CP18/15 – Corporate governance – Board responsibilities

1. The Institute and Faculty of Actuaries (IFoA) welcomes the PRA's consultation paper CP18/15 "Corporate governance: Board responsibilities", and we support the general tone and content of the document. Members of the IFoA's Risk Management Board have led the review of this response.

2. The IFoA has identified a few places in the paper where we suggest the PRA could articulate its approach more clearly, and these are set out below.

3. In paragraph 3.1 (under Culture), the PRA states that boards should establish a culture of risk awareness. We believe it would be helpful to make brief reference to possible differences in the nature of a risk culture for different broad areas of risk – for example between internal risks to a firm's profitability, risks affecting customers, and risks affecting compliance with regulatory requirements.

4. The same paragraph refers to remuneration as one method of embedding a culture of risk awareness and ethical behaviour. We suggest that the paper should add that financial incentives must be carefully structured to ensure that they do not encourage unethical behaviour instead.

5. In paragraph 4.1 (under Risk appetite and risk management), the PRA could consider adding that when a board drafts its risk appetite statement, it should be careful to make sure that the statement would not allow the business to take on more risk in aggregate than it can bear.

6. Also referring to paragraph 4.1, the IFoA does not think that it is practical to produce a statement of risk appetite that is readily understood by employees. We suggest saying instead "The statement should be communicated to employees throughout the business and where necessary interpreted in its application to individual job functions."

7. It might be helpful for the PRA to add a further phrase at the end of the first sentence of paragraph 4.2: "and systematic processes for identifying and managing newly emerging risks as early as possible."

8. In paragraph 4.3, we suggest adding a new phrase at the end: "and an effective crisis-management system."

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9. The PRA could consider including a reference to the Financial Stability Board's 2013 paper on risk appetite as an excellent source of good practice for larger firms.[1]

10. We believe that the last sentence of paragraph 6.3 (under Respective roles of executive and non-executive directors) could be clearer. We suggest ending the sentence after "and escalate matters to them", and replacing the rest of the sentence with: "Boards should communicate clearly to the executive management that even where an area has been delegated to it, on occasions it must exercise its judgement to decide that a matter of particular significance should be escalated to the board."

11. Solvency II firms are now required to maintain a "governance map" of their organisation's key functional responsibilities and role holders (see Supervisory Statement SS35/15 para 2.29). To ensure that insurers do not have overlapping governance documents, we believe that the PRA could usefully extend paragraph 6.3 to articulate its position on which requirements in relation to board delegation are covered by the governance map.

12. Paragraph 7.1 (under Knowledge and experience of non-executive directors) says that the non-executive directors should 'between them' have sufficient sector experience to understand and provide challenge across the firm's business lines. The IFoA endorses this but we suggest the wording could be amended to avoid any suggestion that non-executive directors should be chosen based on a narrow matching of their areas of expertise to particular parts of the firm.

13. In the same paragraph the consultation paper says that the PRA will expect to see evidence that key decisions in particular have been challenged effectively by boards. We would welcome a reference here that it is good practice for boards to document alternative options which have been considered but not adopted.

14. Paragraph 8.1 (under Board time and resources) states that board meetings should be organised to ensure that there is enough time to deal with all the issues to be covered. We think that the wording could go further and state that it is good practice for the board to have an annual discussion about the schedule of meetings for the coming year, including relative priorities.

15. Paragraph 8.1 also talks of board meetings being genuine, open discussions and not stage managed. We note that auditors, other control functions within the organisation, and regulators are likely to be exposed to board meetings only through the minutes. The PRA might therefore consider stating in the paper that the minute taking process should be genuinely open.

16. Paragraph 9.1 (under Management information and transparency) states that the chairman and non-executives are responsible for managing the frequency and content of management information. It might be helpful to note here that this could involve frequent review of the information provided as there could be fast-moving changes in priorities. For example, if a major risk crystallises the board will need to devote significant time to it, but subsequently the board should not need to give it as much weight as the impact becomes better understood.

17. In section 11 (Remuneration), the paper refers to an expectation for boards to ensure that incentives within the firm's remuneration system are aligned with prudent risk taking. We would suggest making an explicit reference here that the remuneration system should be consistent with the firm's risk appetite.

[1] http://www.financialstabilityboard.org/wp-content/uploads/r_131118.pdf

18. Should you wish to discuss any of the points raised in further detail please contact Steven Graham, Technical Policy Manager (steven.graham@actuaries.org.uk / 0207 632 2146) in the first instance.

Yours sincerely

Fiona Morrison
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