Guideline Impact Analysis Statement

Corporate Governance Guideline

January 2013

I. Background

Corporate governance is the set of relationships between a company's Board of Directors (Board), management and other stakeholders. It provides the system through which the objectives of the FRFI are set and the means of attaining those objectives and monitoring performance are determined.

OSFI's *Corporate Governance Guideline* (Guideline), which was published in 2003, applies to all federally-regulated financial institutions (FRFIs) except the branch operations of foreign banks and foreign insurance companies. In 2010, OSFI established a dedicated Corporate Governance Division to review FRFI practices and to ensure FRFI compliance with the Guideline.

Corporate governance practices have evolved significantly over the past ten years. A number of domestic regulators, international standard-setters and various commentators have published reports highlighting industry best practices and standards with respect to the effective corporate governance of financial institutions. Notable among these are the *OECD Findings*, the *UK Walker Report*, the *G30 Report*, and the *BCBS Principles*. As a result, OSFI believes the time has come to update its own guidance in this area to incorporate changes that have taken place over the last ten years.

II. Problem Identification

OSFI's Guideline has not been reviewed or updated since its original publication in 2003. In light of the global financial crisis and the increasingly heightened attention regarding the corporate governance of financial institutions (by industry and regulators), the current version of the OSFI Guideline is no longer consistent with current industry best practices and international standards.

III. Objectives

The main objectives of the revised Guideline are to:

- Ensure that FRFIs have prudent corporate governance practices and procedures that contribute to their safety and soundness;
- Promote industry best practices in corporate governance;
- Be consistent with OSFI's *Supervisory Framework* (2011); and
- Address international standards, as articulated by organizations such as the Financial Stability Board (FSB), the Organization for Economic Cooperation and Development (OECD), the Basel Committee for Banking Supervision (BCBS) and the International Association of Insurance Supervisors (IAIS).

IV. Options and Assessment

Option 1 – Status Quo

Although the current version of the Guideline has served OSFI and the industry well in the past nine years, it is no longer consistent with current industry best practices and international standards. In particular, the current Guideline does not address key elements of risk governance (e.g., the development of a Risk Appetite Framework), a unique and crucial element of the corporate governance of FRFIs, which supports their safety and soundness.

Option 2 – Repeal Current Guideline

Repealing the Guideline altogether would provide FRFIs with operational flexibility with respect to their corporate governance practices. As well, it would reduce regulatory burden for FRFIs. However, this would pose significant operational risks for individual FRFIs, which may not adopt prudent corporate governance practices and procedures. This option would not be consistent with international standards (e.g., OECD, FSB, BCBS and IAIS standards).

Option 3 – Revise the Guideline

Under this option, the current Guideline would be revised to:

- Enhance the effectiveness of the Board of Directors (e.g., Board responsibilities and competencies);
- Strengthen the risk governance of FRFIs (e.g., the requirement to develop a 'Risk Appetite Framework' to guide FRFIs' risk-taking activities); and
- Bolster the overall internal control framework of FRFIs (e.g., the role of the Chief Risk Officer and Audit Committee).

Such changes would be consistent with OSFI's *Supervisory Framework*, revised in 2011, current industry best practices and international standards. As well, the revised Guideline would take into consideration the work undertaken by OSFI as part of a cross-system review (see next section). Based on the cross-sector review, it does not appear that revising the Guideline would impose significant costs on the industry, as the corporate governance practices and procedures of several FRFIs have evolved in the recent years.

V. Consultations

OSFI's dedicated corporate governance supervision team conducted a comprehensive cross-sector review of the corporate governance practices of the larger FRFIs in 2010/11. As part of these reviews, several FRFI directors and members of Senior Management were consulted with respect to evolving corporate governance best practices within the industry.

OSFI issued a draft guideline for public consultation from August 7, 2012 to September 14, 2012. Approximately 30 submissions were received from the public. The guideline was subsequently amended, as appropriate.

VI. Recommendations

Option 3 addresses all of the objectives outlined above, and is the most effective means to ensure that FRFIs have prudent corporate governance practices. The Guideline would be updated to be consistent with OSFI's Supervisory Framework, current industry best practices and international standards.

VII. Implementation & Evaluation

Full implementation of the Corporate Governance Guideline by FRFIs is expected by no later than January 31, 2014.