# Bank Governance Leadership Network

**January 2021**

SUMMARY of THEMES

# Bank board priorities for 2021

On January 21, 2021, Bank Governance Leadership Network (BGLN) participants, including non-executive directors and other banking leaders, were joined by EY's banking and capital markets leaders to discuss priorities for bank boards and management teams in 2021 and help to shape the network's agenda for the year.

## ESG will continue to be a primary focus for boards and investors

Participants expect climate and social issues to remain high on bank board and management agendas, with continued pressure from investors and regulators to improve governance and reporting.

### Climate risks and opportunities will demand further refinement of strategy, measurement, and reporting

Pressures for financial institutions to respond to environmental concerns have expanded drastically in recent years and significant work remains to be addressed. An executive said of the climate agenda, *"The discussion has really just begun and there is a lot for banks to decide and deliver that the world is now expecting. How can banks support the Paris Agreement? How can we align portfolios? How much investment is needed to deliver on these goals?"* Participants highlighted a number of issues for further exploration:

- **Embedding climate into all aspects of the business.** Further embedding climate change into banking operations will be critical not only to manage the risk, but also to identify opportunities. One participant suggested banks integrate climate into all aspects of transformation: *"We have to find ways to connect climate with technology and innovation…It's about doing things differently. We've seen with COVID the need for technology and digitalization in banking is key. Climate also needs to be at the center of that innovation."*
- **Continuing to improve measurement and reporting.** Many firms have made public commitments regarding climate and environmental impact and now must demonstrate progress towards achieving those goals. A director said, *"A lot is going to happen on the climate front this year. As boards, I think we'll be faced with some action and choices to get these results. Lots of judgements will need to be made in the middle to latter part of the year."* While several high-profile initiatives are focused on improving metrics and reporting, the lack of consistent standards and metrics continues to challenge banks. An executive

explained, *"The fundamental issue continues to be reporting. The climate agenda brings huge opportunities for banks to engage on society's challenges, but it also carries risks, and we must get it right. To get it right – not just for banks, for everyone – we need consistent reporting and measuring."* Participants expect more required disclosure.

## Making progress on social equality will require banks to redouble their efforts

The impacts of the COVID-19 crisis, along with a growing social justice movement in many parts of the world, is increasing pressures for companies to act. The spotlight on diversity, equity, and inclusion (DEI) is putting pressure on banks to demonstrate results. A participant said, *"This is not a new topic. Time has passed and the results are not there, and that's because we still lack conviction and a proper analysis of the root causes. Everyone is working on it, but progress is slow."* Another added, *"It's been 20 years and the numbers really haven't moved on gender. That is going to come to the forefront. Then coming out of the Black Lives Matter movement last year, CEOs and board made a lot of commitments and I think there will be a reckoning on that. How does it go from the nice-to-have discussions to actual change? It's going to be a closely watched issue."* Participants pointed to recent SEC rule changes regarding disclosures around human capital management as a potential indicator that regulatory pressures may also expand in this area.

Several noted the strategic importance of making progress. *"Gender and ethnic diversity still seem like a 'nice to have' for many banks. We need to strengthen the business case behind diversity and inclusion, and why it is a responsibility to have diverse talent to drive your organization,"* according to one executive. Another emphasized the potential revenue generating opportunity that increasingly large and important portions of the economy present to firms who think holistically about DEI: *"This is a strategic issue. It is about growth, not just diversity and inclusion for its own sake. There is a growing portion of sectors, with large companies, that are minority and women-owned and we need to effectively serve those populations."*

Some participants suggested banks' DEI initiatives should include efforts to promote socioeconomic mobility. One director said, *"We should also be focusing more on social mobility, understanding where the workforce comes from, and giving more opportunity to those who come from poorer backgrounds with less educational advantage. How can we give them a real chance and enable them? It goes beyond just gender and racial diversity and is a really important ingredient to creating a truly diverse company."* According to another participant, DEI initiatives should include workforce retraining: *"We need to actually link these efforts to skills. People's skills are becoming obsolete really quickly and if we can find a way to link DEI to the skills agenda it could be really valuable."*

### Banks' ESG efforts can extend to influencing customer behavior

A director said, *"I would expand our work on ESG beyond the bounds of our individual banks. Particularly, where you have an investment bank advising many other companies, what role can you play to drive change? For example, we have seen some banks change requirements for gender diversity on the board before taking a company public. Is there more that can be done to provide a leadership role as we touch so many sectors and industries?"* The sector's ability to influence client behavior places it in a unique position, one that raises challenging questions for business leaders. A director said, *"We have to be very careful that we define what banks should do and what they actually can do to contribute to development in this area. It's a clear problem and it will not just go away. But, if, you're a Polish bank, for instance, you can't just stop investing in coal because the whole economy depends on it."*

## Market risk is a growing concern

Participants raised concerns regarding a perceived disconnect between financial markets and the real economy and whether this reflects underlying structural changes to markets. Central bank efforts to bolster economies and smooth market volatility caused by the global impact of COVID-19 raise questions about the extent to which the financial system is now propped up by monetary policy and central bank liquidity. A director said, *"The markets were heading for dislocation and the Fed basically flooded them with liquidity as did other central banks. We have today a starker difference between market behavior and the real economy."* Others worried about the potential for unintended consequences. *"The growth of shadow banking and the growth of central bank balance sheets was already a concern years ago and it's obviously gone much further since. Central banks are extremely levered, can they restore confidence if you have a crisis?"* asked one director. Another participant wondered, *"The question is whether this is sustainable or not? What might we expect in the short term and the longer term?"* A director added, *"This new hyper-monetary policy where people think we can just further increase debts across the board and everything is just working and everyone is happy, I just do not believe it's going to work, and I wonder about the risks of such political trends. Everyone is just buying up debt and hoping it's going to work out fine."*

## Firms are monitoring shifts in regulatory policy and supervision

With a new administration in the US expected to bring significant policy change, participants wondered about the ramifications for regulation and oversight, particularly as relates to consumer protection. A director said, *"Obviously the Consumer Finance Protection Bureau is going to have a very different outlook for the next four years. It will be interesting to see what their priorities are and what approach they take to achieving them."* Some participants expressed concern that the CFPB would establish policy via precedent, using strict enforcement and steep fines to send a message, what one described as *"supervisory arbitrariness,"* as opposed to legislation. These concerns extend beyond the US as well. In the

UK, the Financial Conduct Authority (FCA) is also facing pressure to step up enforcement and European Commission officials have expressed intent to closely monitor collections and support for vulnerable customers coming out of the pandemic.

Participants discussed whether the financial pressures of the pandemic could make banks a target for cash-strapped governments. A director said, *"We're in an environment where no deep pocket goes unplucked …Given the deficits we have right now at the local, state, and national government levels around the world – and the fact that the banking industry appears to have come through the crisis in decent shape so far – I think this could be a situation where regulators get more aggressive and penalties become larger."* Bank leaders should ensure any potential issues are being addressed now: *"If you have potential points of vulnerability today you should probably think about doubling resources or doing whatever needs to be done to solve the issues,"* advised one participant.

## Artificial intelligence carries risk, but also vast potential

Expanded adoption of AI is increasing discussion of additional use cases and scrutiny of the potential for bias in the technology's application.

- **The benefits and risks of AI warrant greater board attention.** A participant said, *"The reputational risk of AI is worth considering due to the potential for discrimination. As we worked with big tech and other tech companies, we found so many tools and data that banks have not harvested yet. Many are great at isolating credit-worthy customers, but the problem is that we discovered it is heavily discriminatory. It's a major social issue we need to discuss."* Another added, *"It's going to be a big deal as you look at the work each of our institutions is doing. AI is a big topic that has not taken up a lot of time in the board room yet, but it's going to."*
- **AI has much broader application than many often consider.** Participants agreed that oversight and understanding of the risks in AI and machine learning warrant close inspection, but also stressed that the industry should not be shortsighted about the technologies' vast potential in a variety of areas. A director said, *"I think there's a risk that people jump to the use-case of credit and fair lending and responsibility around decision making, but the applicability of machine learning to so many other aspects of banking is so useful we should talk about it more."* Banks have not yet harvested their data effectively, while some fintechs and tech companies have adopted advanced tools allowing them to identify data signals most banks cannot. Another director highlighted that the technology's ability to analyze and manipulate large swaths of data could lead to new ways of examining and categorizing risks and gleaning new insight from existing sources of management information: *"We all received enormous decks that are hundreds of pages. Can AI transform the way we think about risk? Could it break down traditional siloes to allow for better understanding of correlations? AI could be a way to improve the information reported to the board by presenting things in very clever ways."*

Participants also noted that technology could enable industry collaboration to create more efficient compliance processes, particularly in areas like anti-money laundering and know-your-customer, where there is shared interest and minimal competitive concerns. A director said, *"Everyone has tried to think through how to create industry utilities around these processes that are extraordinarily expensive with a ton of downside risk to institutions. We are looking into how AI can help that ability. It seems very exciting and has real potential to build something more efficient and effective."* Another said, *"There are a few opportunities where this technology is potentially going to allow us to work together. AML is one, cyber could be another, where we have information-sharing mechanisms, but they are not automated or fast. Working collectively and pooling our knowledge in a way that is not littered with litigation and liability is something that a lot of companies are thinking about."*

## Appendix

The following individuals participated in this discussion:

### Meeting participants

- Kent Andrews, Senior Vice President, Regulatory Risk and Risk Capital, TD Bank
- Nora Aufreiter, Corporate Governance Committee Chair, Scotiabank
- Michelle Caturay, Associate General Counsel, Corporate Secretary, and Chief Privacy Officer, CIBC
- Bill Connelly, Chair of the Supervisory Board and Nomination and Governance Committee, Aegon and Risk Committee Chair, Société Générale
- David Conner, Non-Executive Director, Standard Chartered
- Martha Cummings, Former Head of Compliance Strategy & Operations, Wells Fargo
- Lara de Mesa, Group Executive Vice President, Head of Responsible Banking, Executive Chair's Office, Santander
- Terri Duhon, Risk Committee Chair, Morgan Stanley International
- John Finneran, Corporate Secretary, Capital One
- Morten Friis, Risk Committee Chair, NatWest Group
- Tobias Guldimann, Audit Committee Chair, Commerzbank
- Brad Hu, Former Chief Risk Officer, Citigroup
- Sebastian Jost, Chief Editor, Head of Strategy Communications, Deutsche Bank
- Tom Killalea, Non-Executive Director, Capital One
- Christine Larsen, Non-Executive Director, CIBC
- Richard Meddings, Audit Committee Chair, Credit Suisse, and Chair of the Board, TSB Banking Group
- Wim Mijs, Chief Executive Officer, European Banking Federation
- Marty Pfinsgraff, Risk Committee Chair, PNC Financial
- Juan Pujadas, Non-Executive Director, Wells Fargo
- Philip Rivett, Audit Committee Chair, Standard Chartered and Non-Executive Director Nationwide Building Society
- Alan Smith, Senior Advisor, ESG and Climate Risk, HSBC

- Jan Tighe, Non-Executive Director, Goldman Sachs
- Tom Woods, Non-Executive Director, Bank of America

## EY

- Jan Bellens, Global Banking and Capital Markets Leader
- Nigel Moden, EMEIA Financial Services Banking and Capital Markets Leader

## Tapestry Networks

- Dennis Andrade, Partner
- Brennan Kerrigan, Senior Associate
- Tucker Nielsen, Principal

## About the Bank Governance Leadership Network (BGLN)

The BGLN addresses key issues facing complex global banks. Its primary focus is the non-executive director, but it also engages members of senior management, regulators, and other key stakeholders committed to outstanding governance and supervision in support of building strong, enduring, and trustworthy banking institutions. The BGLN is organized and led by Tapestry Networks, with the support of EY. *Summary of Themes* is produced by Tapestry Networks and aims to capture the essence of the BGLN discussion and associated research. Those who receive the *Summary of Themes* are encouraged to share it with others in their own networks. The more board members, members of senior management, advisers, and stakeholders who become engaged in this leading edge dialogue, the more value will be created for all.

## About Tapestry Networks

Tapestry Networks is a privately held professional services firm. Its mission is to advance society's ability to govern and lead across the borders of sector, geography, and constituency. To do this, Tapestry forms multistakeholder collaborations that embrace the public and private sector, as well as civil society. The participants in these initiatives are leaders drawn from key stakeholder organizations who realize the status quo is neither desirable nor sustainable and are seeking a goal that transcends their own interests and benefits everyone. Tapestry has used this approach to address critical and complex challenges in corporate governance, financial services, and healthcare.

## About EY

EY is a global leader in assurance, tax, transaction, and advisory services to the banking industry. The insights and quality services it delivers help build trust and confidence in the capital markets and in economies the world over. EY develops outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, EY plays a critical role in building a better working world for its people, for its clients, and for its communities. EY supports the BGLN as part of its continuing commitment to board effectiveness and good governance in the financial services sector.