



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Responsibility Mapping

Discussion Paper

Applicable to:

1. Licensed banks
2. Licensed investment banks
3. Licensed Islamic banks
4. Licensed insurers
5. Licensed takaful operators
6. Prescribed development financial institutions
7. Financial holding companies

Issued on: 23 February 2018

BNM/RH/DP 028-6

This discussion paper sets out the Bank's thinking on clarifying the responsibilities of individuals holding leadership positions in financial institutions.

The Bank invites written feedback on this discussion paper, particularly on the specific questions raised throughout the document. Responses may include suggestions on areas to be clarified or alternatives that the Bank should consider. To facilitate an effective consultation process, the feedback should be supported with clear reasons, including accompanying evidence or illustrations where appropriate.

Responses must be submitted to the Bank by 20 April 2018 to–

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Electronic submission is encouraged. Submissions received may be made public unless confidentiality is specifically requested for the whole or part of the submission.

In the course of providing your feedback, you may direct queries to the following officers at 03-26988044:

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PART A OVERVIEW

1 Introduction

- 1.1 The Bank has introduced various reforms in recent years to strengthen corporate governance in the Malaysian financial system. This has translated into observable improvements in institutional governance arrangements and practices. With efforts to raise the bar for existing corporate governance standards substantially in place, the Bank is now sharpening its focus on the equally important, softer, aspects of governance (i.e. organisational culture and conduct). The state of culture and conduct within a financial institution is often perceived to be a reflection of the strength of its governance and is therefore critical to sustain confidence and the long term viability of the institution.
- 1.2 Leaders of financial institutions have a significant influence over organisational culture through the tone they set from the top, in their actions, decisions and attitudes. This discussion paper outlines the Bank’s thinking for a framework to sharpen the accountability of individuals in senior roles through responsibility mapping. Clarity on the roles, responsibilities and accountability will incentivise leaders to take greater ownership in fostering a sound culture and addressing misconduct risk.

2 Broad approach

- 2.1 The Bank’s approach to responsibility mapping entails three key elements:
- (a) identifying the senior roles within each financial institution;
 - (b) allocating responsibilities of the senior roles to specific individuals; and
 - (c) holding individuals in senior roles to account.

Key elements of responsibility mapping	
Identification of roles	<ul style="list-style-type: none"> • Each key business, operational and control activity must be within the responsibility of a senior role • Some senior roles will be unique to certain types of financial institutions • Most senior roles will be executive (for members of senior management), but some will be oversight roles to be held by non-executive directors
Allocation of responsibilities	<ul style="list-style-type: none"> • Each senior role must be assigned to an individual, whose responsibilities are clearly documented • In some cases, an individual may hold more than one senior role, or share the role with another individual – depending on potential conflicts of interest and competing commitments
Individual accountability	<ul style="list-style-type: none"> • Individuals in senior roles may be held accountable for regulatory contraventions occurring within their area of responsibility, and for personally failing to discharge a basic duty • Individual accountability for senior roles displaces neither the personal responsibility of subordinates nor the collective accountability of the board and of senior management

Diagram 1

PART B PROPOSED FEATURES

3 Identification of roles

- 3.1 The first element of responsibility mapping involves identifying the senior roles which will be subject to the proposed regime.

Question 1

Please describe how individual roles and responsibilities are currently allocated for directors and senior managers in your financial institution. Please include any existing documentation¹ relied on internally to clarify individual roles and responsibilities.

Guiding principles

- 3.2 The primary consideration for identifying senior roles in a financial institution is to minimise organisational **blind spots**. All key business, operational and control functions should fall clearly within the responsibility of a senior role. This is the chief end of responsibility mapping.
- 3.3 In addition, the identification of senior roles should also reflect **diversity** across different financial institutions. Certain senior roles may be uniquely necessary for particular types of licensed business (e.g. appointed actuary for an insurer or takaful operator). Likewise, each financial institution should have sufficient flexibility in determining an internal structure appropriate to the needs and nuances of its activities.
- 3.4 While most senior roles will be **executive** positions for members of senior management, some will be **oversight** roles to be held by non-executive directors.

Question 2

Do you agree with the proposed principles for identifying senior roles? Please indicate suggestions of considerations other than those identified in paragraphs 3.2 to 3.4.

¹ Please use readily available material (e.g. job descriptions, organizational charts, etc.) within your financial institution, rather than documentation prepared for the purpose of this question.

Prescribed and additional senior roles

- 3.5 The Bank is considering to prescribe certain senior roles which financial institutions must establish. Each **prescribed** senior role will have a set of “generic responsibilities” attached to it. Since the exact scope of duties for a senior role may vary with differences of scale and organisation, financial institutions may also articulate “specific responsibilities” over and above those set by the Bank.
- 3.6 Financial institutions would also be free to articulate **additional** senior roles which have not been prescribed by the Bank, along with corresponding “specific responsibilities”.

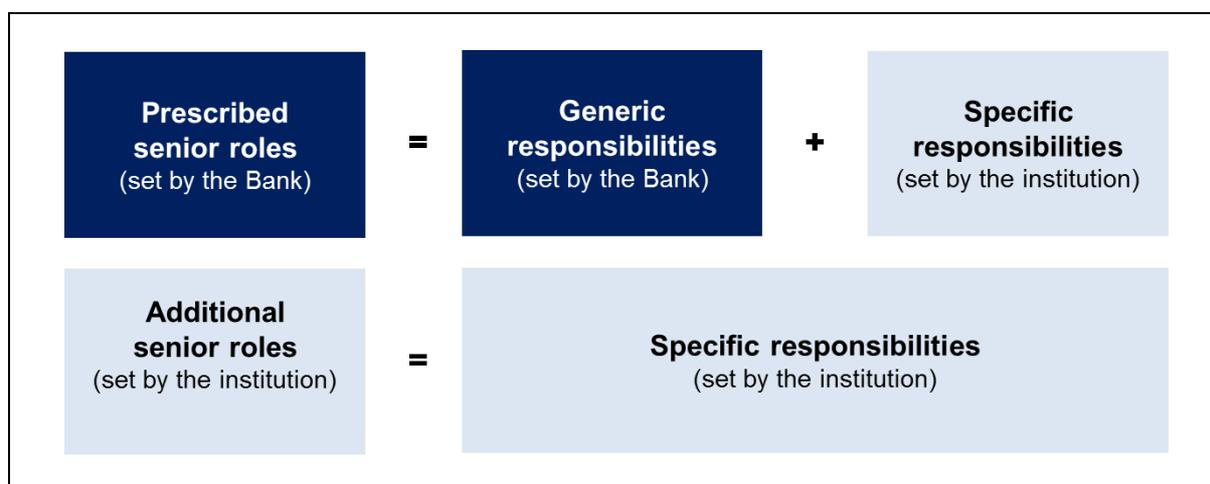


Diagram 2

- 3.7 In substance, this combination of prescribed and additional senior roles already exists under the present corporate governance framework. All financial institutions are currently required to have certain prescribed senior roles, such as board chairman, chief executive officer and chief risk officer. Various *generic responsibilities* are assigned to each of these roles, by virtue of the definition of the role as well as through standards set in policy documents. Beyond these, many financial institutions set *specific responsibilities* for individuals in senior roles, which differ from institution to institution. Financial institutions also assign additional senior roles for individuals who are considered members of senior management. This includes roles such as head of human resources, chief operating officer and head of a key business function – each of whom is internally assigned *specific responsibilities* based on the internal needs of the financial institution.
- 3.8 The responsibility mapping regime will streamline the existing expectations set by the Bank (represented by the dark blue boxes in Diagram 2). This will entail a review of the present set of prescribed senior roles and clarifying their corresponding generic responsibilities.
- 3.9 Diagram 3 summarises the prescribed senior roles already present under the existing framework, along with a non-exhaustive list of other senior roles which may be prescribed under the proposed responsibility mapping regime.

Prescribed senior roles

<i>Type of financial institution</i>	Existing under the current framework	Potential extensions under the new framework
All	<p><u>Board</u> (oversight)</p> <ul style="list-style-type: none"> • Chairman • Chair of board risk management committee • Chair of board audit committee • Chair of board remuneration committee • Chair of board nominations committee • Non-executive director for whistleblowing <p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Chief executive officer • Chief risk officer • Chief of internal audit • Chief compliance officer • Chief financial officer 	<p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Head(s) of key business function(s) • Outsourcing • Legal
Banking (including investment banks and Islamic banks)	<p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Head of Shariah function 	<p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Capital funding and liquidity • Treasury management • Financial information and regulatory reporting • Recovery and resolution planning • Internal stress tests • Technology and infrastructure management • Corporate and business strategy
Insurance / takaful	<p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Appointed actuary • Head of Shariah function 	<p><u>Senior management</u> (executive)</p> <ul style="list-style-type: none"> • Head of actuarial function (pricing) • Chief underwriting officer • Financial information and regulatory reporting • Technology and infrastructure management • Corporate and business strategy

Diagram 3

Question 3

Among the senior roles listed for consideration in the second column, which of these are not appropriate for inclusion as prescribed senior roles? Are there any other senior roles that should be considered but is not currently stated? Please elaborate and provide specific reasons for your answers.

- 3.10 This discussion paper does not set out the generic responsibilities for each prescribed senior role. These will be consulted upon at a later stage, after the Bank has reviewed the responsibilities presently attached to existing prescribed senior roles.

Basic duties for senior managers

- 3.11 Under the existing framework, all directors are individually subject to a basic set of duties that are set out in the law². There is presently no parallel set of basic duties for senior managers. Although they are subject to generic and specific responsibilities, these are attached to their respective senior roles rather than applied to all senior managers equally.
- 3.12 The responsibility mapping regime will introduce a set of basic duties for senior managers to promote a baseline expectation for each individual in an executive senior role. These will apply equally across all types of executive senior roles, and will underpin the generic and specific responsibilities applied to each senior role.
- 3.13 The proposed basic duties are that senior managers must–
- (a) take reasonable steps to ensure that the activity for which they are responsible is managed effectively;
 - (b) take reasonable steps to ensure that the activity for which they are responsible complies with relevant legal and regulatory requirements;
 - (c) take reasonable steps to ensure that any delegation of their responsibilities is to an appropriate person and that they oversee the discharge of the delegated responsibility effectively; and
 - (d) disclose appropriately any information which the Bank would reasonably expect notice.

Group-wide senior roles

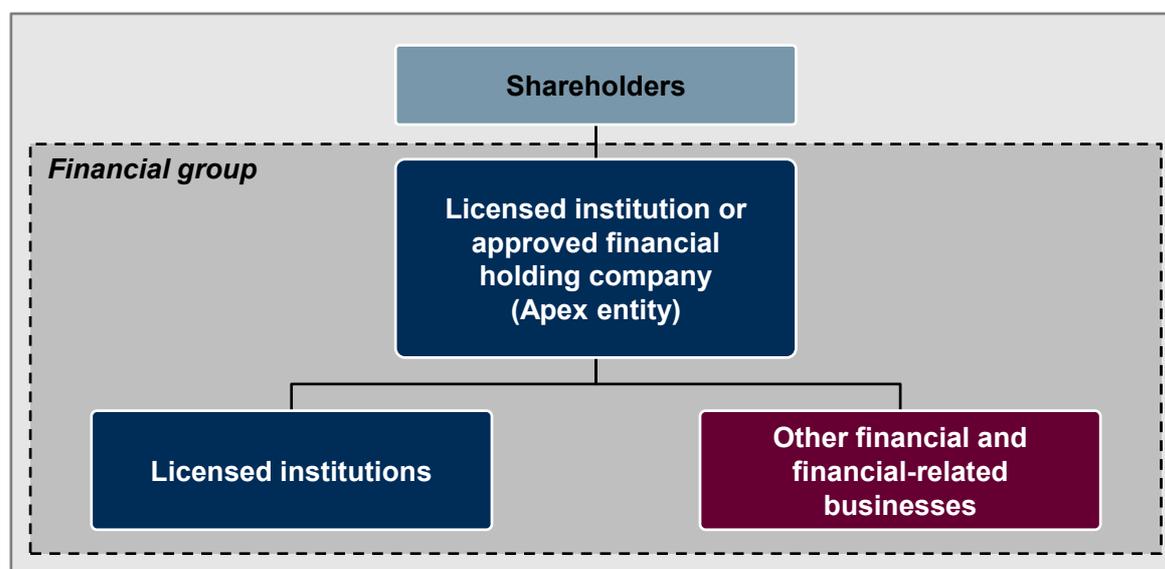
- 3.14 Proposals in this discussion paper focus on applicability at the level of each legal entity. At the same time, the Bank is exploring the appropriateness of responsibility mapping at the group level.
- 3.15 Under the existing framework, the Bank implements group-wide prudential standards through the “apex entity” of a particular group³. As such, the responsibility of establishing and operating a clear governance structure for the group rests with the apex entity⁴. However, this group-wide responsibility does not displace the legal and governance responsibilities of each subsidiary financial institution as a separate legal entity⁵.

² Section 57 of the Financial Services Act 2013 (FSA), section 66 of the Islamic Financial Services Act 2013 (IFSA) and section 5A of the Development Financial Institutions Act 2002 (DFIA).

³ *Approach to Regulating and Supervising Financial Groups* (May 2014)

⁴ Paragraph 20, *Corporate Governance* (August 2016)

⁵ Paragraph 21, *Corporate Governance* (August 2016)

Diagram 4 (from *Financial Groups* paper)**Question 4**

Please describe the existing governance structure across the legal entities in your group. Please indicate—

- (a) any group-wide senior roles in place (e.g. group chief risk officer, group head of human resources), along with a description of their corresponding responsibilities;
- (b) the distinction, if any, between group-wide roles and responsibilities and those focused on a particular legal entity; and
- (c) whether (and if so, how) your group allocates accountability for the responsibilities set out in paragraph 20.2 of the *Corporate Governance* policy document (e.g. through specific committees or senior roles).

3.16 If the responsibility mapping regime is applied to groups, each apex entity will be required to identify group-wide senior roles which bear responsibility for significant activities cutting across the legal entities in the group. These group-wide senior roles—

- (a) may be prescribed by the Bank, or internally established as “additional senior roles” by each apex entity as it deems appropriate; and
- (b) will be distinct from the entity-specific senior roles identified within each financial institution (e.g. group chief risk officer is a separate senior role compared to chief risk officer in one of the licensed persons within the group).

4 Allocation of responsibilities

- 4.1 Once the senior roles have been identified for a financial institution, the corresponding responsibilities must be clearly allocated to specific individuals. This entails–
- (a) naming the relevant director or senior manager for each senior role; and
 - (b) articulating, on top of the generic responsibilities, the specific responsibilities attached to each individual in a senior role.
- 4.2 The allocation of responsibilities must be based on how authority is distributed in reality rather than formal designations alone. As such, an individual may be considered a senior manager even if they are not formally employed by a financial institution – for instance, in cases where the individual is an officer of an affiliate but also makes decisions for the financial institution that are characteristic of a person in a senior role.
- 4.3 Generally, each senior role would be assigned to one individual. This is to promote clarity in identifying the person with the authority and responsibility of the affairs attached to that senior role. However, there will also be instances where the Bank may accept arrangements for an individual to hold more than one senior role (“double hatting”) or for two individuals to share a single senior role (“joint responsibility”). These exceptions will only be permitted where they are in accordance with the considerations outlined in paragraphs 4.4 to 4.8 below.

Double hatting (multiple senior roles)

- 4.4 An individual may only be assigned to more than one senior role at a time if the combination of roles does not–
- (a) give rise to unacceptable conflicts of interest; or
 - (b) result in an unreasonable workload for the individual, given the nature, size and complexity of the operations.
- 4.5 The Bank will clarify the types of potential conflicts that are “unacceptable” under paragraph 4.4(a). For instance, double-hatting should not be allowed for control function senior roles, in order to protect the independence and effectiveness of such functions. The need for such safeguards are explained in paragraphs 4.11 and 4.12 below. Similarly, double-hatting between group-wide and institution-specific senior roles may also be prohibited in certain circumstances. For example, the existing framework does not allow chief executive officers to double-hat executive positions across the group unless the Bank otherwise approves⁶.
- 4.6 Arrangements for an individual to be assigned more than one senior role are less likely to result in an “unreasonable workload” under paragraph 4.4(b) where the financial institution is small and less complex. Certain senior roles are also more likely to demand full-time attention – in general, an individual in

⁶ Section 55(3) FSA 2013 and section 64(3) IFSA 2013.

a senior role that is already prescribed under the existing framework⁷ should not hold any other senior roles.

Question 5

- (a) Describe the existing arrangements for double-hatting of senior roles in your financial institution, along with any specific concerns you may have on these proposals.
- (b) Please indicate and justify the combinations of senior roles that should be considered acceptable or unacceptable.

Joint responsibility (one senior role)

- 4.7 In the exceptional case that a senior role is shared by two individuals, they will be held jointly and severally accountable for their area of responsibility. This means that each individual will be fully responsible for the entire senior role, notwithstanding the fact that they may employ a division of focus in practice. A senior role should not be shared by more than two individuals.
- 4.8 A senior role should not be shared between two individuals where one of them is subordinate to the other. In such a case, only the more senior individual should be assigned to the senior role. Likewise, a senior role should not be linked to an individual who is subordinate to another senior officer over the relevant affairs.

Question 6

Please indicate if the proposed joint responsibility approach will require changes to existing arrangements in your financial institution. Please explain any specific concerns on these proposals, along with constructive suggestions for the Bank to consider.

Collective decision-making

- 4.9 Collective decision-making is a common feature in financial institutions. Key decisions are often made by designated committees. The existing corporate governance framework recognises this, and imposes *collective accountability* for both the board and senior management. This promotes cooperation, alignment, and creates a sense of collegial responsibility within the board and senior management respectively. At the same time, the existing framework also assigns *individual accountability* through the definitions and corresponding responsibilities of prescribed senior roles (e.g. board chairman, chief executive officer, chief risk officer).
- 4.10 Responsibility mapping does not entail a departure from this complementary coexistence of individual and collective accountability. Rather, it seeks to give

⁷ The existing prescribed senior roles are listed in Diagram 3 on page 4.

effect to the existing legal and regulatory requirements by providing greater clarity on the implementation. While senior management should be collectively responsible for decisions taken together, this does not dilute the individual responsibility of each senior manager over their specific contribution to the decision-making process. It also should not absolve them of the affairs within their areas of responsibility.

Question 7

Please explain the extent to which your financial institution applies the concept of collective accountability for the board and senior management respectively. Please elaborate on–

- (a) any existing arrangements to distinguish collective accountability from individual accountability within the financial institution; and
- (b) whether your financial institution has experienced any constraints or problems in applying collective accountability in the past, and if so, the reasons for and resolution to these challenges.

Independence of senior roles in control functions

- 4.11 Control functions have the responsibility independent from business lines to provide objective assessment, reporting and assurance on the effectiveness of a financial institution's policies and processes, and its compliance with legal and regulatory obligations. This includes the risk management function, the compliance function and the internal audit function.
- 4.12 Given the unique role of the control functions, it is crucial that the senior roles bearing responsibility over them are vested with sufficient stature, authority and independence to effectively discharge their duties. Under the existing corporate governance framework, the board plays an important task in safeguarding these senior roles from inappropriate influence by business line considerations and the rest of senior management. The Bank intends to streamline and generally raise the expectations in this regard, including requirements on–
- (a) direct access to the board;
 - (b) board approval for appointments, removals and resignations;
 - (c) board involvement in performance assessment, and board approval for remuneration packages; and
 - (d) board oversight for fit and proper assessments.

Question 8

- (a) To what extent does your financial institution's board already provide the safeguards set out in paragraph 4.12?
- (b) Please indicate any concerns or additional suggestions about the safeguards proposed in paragraph 4.12.

5 Individual accountability

5.1 The main occasions for individuals in senior roles to be held accountable are illustrated in Diagram 5 below and explained in the subsequent paragraphs.

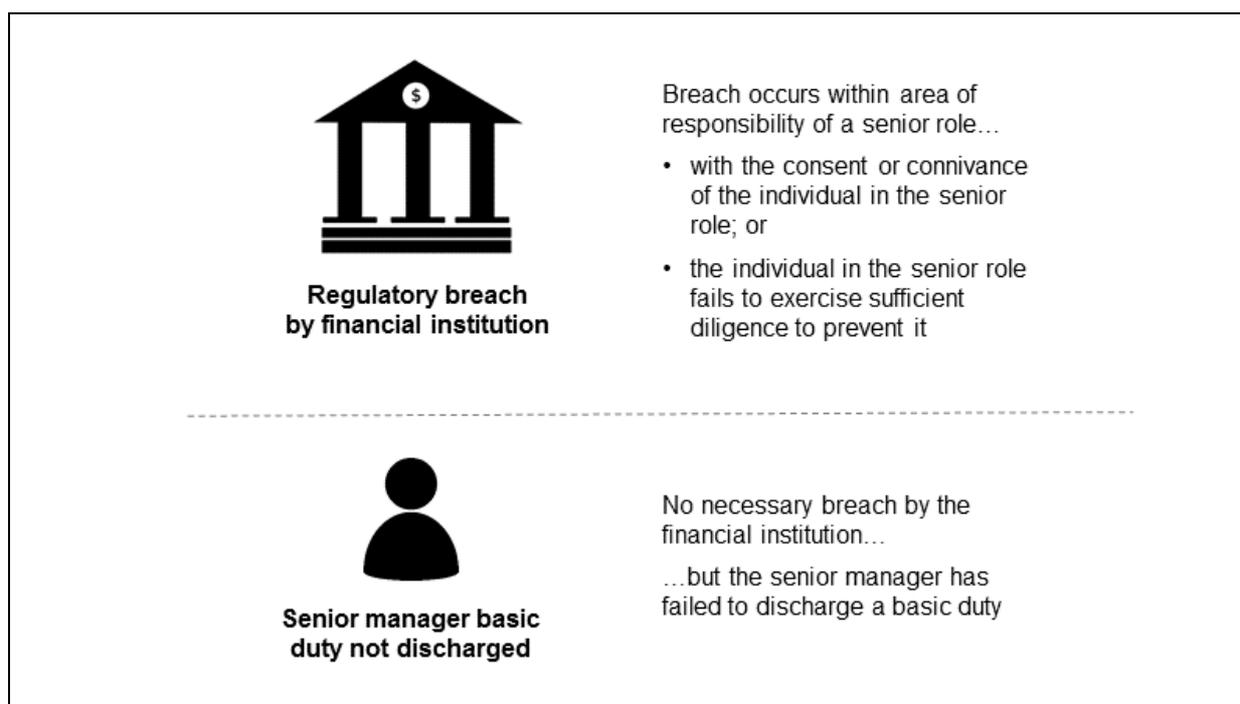


Diagram 5

Regulatory breach by the financial institution

5.2 An individual in a senior role may be held accountable where—

- the financial institution breaches a regulatory requirement;
- the breach occurs within the his area of responsibility; and
- the individual consents to or is in connivance with the breach in question, or fails to exercise such diligence to prevent the breach as he had ought to, having regard to the nature of his function in that capacity and to the circumstances.

Senior manager basic duty not discharged

5.3 A senior manager may be held accountable where he has failed to discharge any of the basic duties enumerated in paragraph 3.13.

Enforcement approach

5.4 The primary aim of individual accountability is to secure appropriate behaviour in the first place, rather than punitively respond to occurrences of misconduct.

- 5.5 The Bank prefers that its enforcement powers will not have to be employed, and is committed to implementing individual accountability in a manner that is fair and reasonable. In designing the proposals, care will be taken to avoid pushing individuals into overly-cautious behaviour, or away from the Malaysian financial sector altogether.
- 5.6 As explained in paragraph 4.10, this emphasis on individual accountability will not substitute collective accountability. Where appropriate, the Bank will also hold the board or senior management responsible. Likewise, the accountability of individuals in senior roles does not take away the personal responsibility of their subordinates. A subordinate will be held to account for their own misconduct, and an individual in a senior role will not be held accountable for misconduct by a rogue subordinate which could not have reasonably been averted.
- 5.7 Depending on the facts of each case, administrative action may entail an order to take remedial steps, a reprimand, a requirement to make a public statement in relation to the breach, a monetary penalty – or a combination of these. The appropriate action will be determined in accordance with the Bank’s individual enforcement framework.

Question 9

Please explain any specific concerns on the main occasions for senior role individual accountability, along with constructive suggestions for the Bank to consider.

PART C TIMELINE

6 Key dates

- 6.1 Responses to this discussion paper must be submitted to the Bank by 20 April 2018. These responses will be used for the development of more specific policy proposals on responsibility mapping. The Bank intends to consult the industry and finalise these specific proposals by the end of 2018, with a view for full implementation in 2019.

Question 10

- (a) Please explain the operational measures that your financial institution will need to undertake to implement the proposals outlined in this paper, along with an estimate of the time required.
- (b) Please indicate any concerns for your financial institution on working with the proposed timeline.