

Provisional translation
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Outline of Trends and Issues in Compliance Risk Management

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Financial Services Agency, the Japanese Government (JFSA)

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Overview

- In October 2018, the JFSA published **“JFSA’s Approach to Compliance Risk Management”**, a discussion paper that is in line with basic concepts presented in **“JFSA’s supervisory approaches -replacing checklists with engagement-”** released in June 2018.
- In order to respond to public comments requiring JFSA to publish actual cases and issues that would support financial institutions in enhancing their compliance risk management, we analyzed actual conditions through dialogues with relatively large banks, securities companies, insurance companies and foreign financial institutions, as well as monitoring on several financial institutions. **“Trends and Issues in Compliance Risk Management”**, released in June 2019, collects 1) trends and issues in compliance risk management at financial institutions, 2) examples of efforts based on issues indicated in “JFSA’s Approach to Compliance Risk Management”, and 3) examples that led to major compliance issues.

Emerging Trends and Issues

<p>Management & Corporate culture</p>	<ul style="list-style-type: none"> • It is not easy to instill the management’s message in all workers of all positions. However, the management should show that they are putting their corporate principles into practice through everyday conduct, in order to prompt a genuine understanding by the executives and employees, to achieve implementation in day-to-day operations, and to develop their ideal corporate culture.
<p>Internal Control</p>	<ul style="list-style-type: none"> • Middle level are expected to incorporate the management’s attitude into their everyday actions. Progress should be made with checking the degree to which their subordinates also fully incorporate the same attitude and analyzing implications to their next policy. • Amidst examples of scandals related to improper incentive systems or a dysfunctional whistleblowing system, progress should be made with analyzing how the incentive system and whistleblowing system should be designed to support compliance risk management.
<p>Governance</p>	<ul style="list-style-type: none"> • While some financial institutions are taking efforts to utilizing the opinions of not only external directors, but also of retirees, outside experts and customers, it is difficult to take proactive measures with only people outside the company. Under the leadership of the management, an environment should be maintained in which these people can fulfil their roles.

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Emerging Trends and Issues (continued)

<p>Framework for Risk Management (3LoD)</p>	<ul style="list-style-type: none"> • Only a few financial institutions have the concept of front divisions’ risk ownership fully incorporated at each workers’ level. Together with securing human resources and systems for compliance divisions as well as internal audit divisions, progress should be made to strengthen risk ownership of the front divisions under the leadership of the management.
<p>Group Companies & Overseas Offices Management</p>	<ul style="list-style-type: none"> • It may be difficult for each group company to analyze risks from the viewpoint of the degree of influence on the society and the economy as a whole. The management of the holding company and outside directors should take a leading role in considering the effect on consumer protection, market fairness and transparency, and raise awareness of the issues at each group company. • Amidst cases where response was delayed due to insufficient communication with overseas offices, financial institutions should discuss compliance risk management at a global basis.
<p>Infrastructure (Human resources & IT)</p>	<ul style="list-style-type: none"> • Facing the issue of lack of specialized human resources, financial institutions should strategically secure and assign human resources for compliance risk management. • While this may be a long-term issue, financial institutions should discuss how to utilize IT for effective and efficient compliance risk management with consideration on potential risks of IT.
<p>Risk-based Approach</p>	<ul style="list-style-type: none"> • Most financial institutions adopted the risk-based approach recently. The management should set priorities and address issues in order to prevent damage and increase corporate value. • Many financial institutions appear to have difficulty in breaking out of the thinking that simply observing existing rules set forth by laws and ordinances is sufficient. The management should take a leading role in making progress to grasp a wide range of risks with flexible imagination.

Towards Compliance Risk Management that Increases Corporate Value

Moving forward

Currently, many financial institutions are running trial-and-error processes, dealing with various issues such as the need to strengthen the business division and improve efficiency under the current business environment, the limits of human and material resources, and the need to balance incentives of executives and employees and effective compliance risk management.

While the state of progress of each financial institution varies, efforts to enhance compliance risk management have been made steadily.

On the other hand, we still see cases where executives and employees, including the management, retain the thinking that simply observing existing rules set forth by laws and ordinances is sufficient, and where some of the management may be attempting to grasp compliance risk from a broad perspective, but not being fully understood by executives and employees at each division of the head office and branch.

It is necessary for all financial institutions to continuously make further efforts to enhance compliance risk management that leads to higher corporate value, pursuing a sustainable business model alongside.

With the awareness that compliance risk management is an issue of the management, the highest priority is to break out of the thinking that simply observing existing rules set forth by laws and ordinances is sufficient. It is necessary for the management to keep this in mind and make further sincere efforts to develop a high quality corporate culture.

In order to support financial institutions in their efforts to achieve compliance risk management that leads to higher corporate value, the JFSA shall ① analyze actual conditions of a wider range of financial institutions, ② monitor financial institutions with specific issues, ③ and disclose major findings and implications.