



Financial Services Commission  
www.fsc.go.kr

## Press Release

---

January 11, 2010

### PROGRESS ON IMPROVING BANKS' CORPORATE GOVERNANCE

The global financial crisis has shed light on the importance of corporate governance in financial institutions. In particular, banks have been the major beneficiaries of government relief programs\* such as government guarantee for bank deposits and foreign debts. However, as the OECD and the BCBS noted, banks' board of directors often neglected their social responsibility by failing in risk management, pursuing short-term profits, and paying out excessive compensation.

\*Since September 2008, 24 countries including Korea have adopted government guarantee programs to protect the financial system.

Against this backdrop, improving corporate governance in financial institutions, particularly in the banking sector, is being actively discussed at the global level. Direct financial regulations may bring about side effects by undermining financial intermediation and adding burden to financial consumers. In contrast, improving corporate governance minimizes the side effects and restores the public trust in financial institutions to ensure that the financial sector can support the real economy and prevent the recurrence of crisis.

#### An overview of global discussions

##### 1. OECD

The OECD reports, *The Corporate Governance Lessons from the Financial Crisis* (Feb. 2009) and *The Corporate Governance and the Financial Crisis: Key Findings and Main Messages* (June 2009), assert that corporate governance in financial institutions should be improved, citing that the boards of directors, particularly outside directors, involve problems such as the pursuit of short-term oriented profit, the payment of excessive compensation, and the failure of risk management, and also citing that the current system does not give shareholders enough power to hold the management in check. To address these weaknesses, the OECD is working with the FSB to publish a set of recommendations on improving corporate governance, *Strategic Response to the Financial Crisis*.

##### 2. U.K.

Since *the Turner Review* pointed out the need to improve corporate governance, Sir David Walker has led an independent review of corporate governance in the UK banking industry



Financial Services Commission  
[www.fsc.go.kr](http://www.fsc.go.kr)

and released *the Walker Review*.

*The Walker Review* makes following recommendations:

- (1) Outside directors should commit minimum 30-36 days per year to working in board committees and take more responsibility in terms of risk management and remuneration.
- (2) The chairman of the board and the chairman of the remuneration committee should serve only a single term.
- (3) An appropriately intensive induction and continuing business awareness program should be provided for the chairman to ensure that he or she is kept well informed of significant new developments in the business.
- (4) Shareholders, in particular institutional investors, should be more actively engaged in board activities.

The UK government plans to establish these recommendations on the “comply or explain basis” as best practices in the banking sector. They also plan to revise related laws so that the FSA can directly engage in interview process to evaluate and approve outside directors.

#### Overview of the progress in Korea

During the 10 years since the system of outside directors was first adopted in Korea after the 1998 financial crisis, it has been consistently pointed out that outside directors lack independence so that the system of checks and balances cannot work as intended against the management.

On the other hand, some argue that outside directors have too much influence over the process of appointment, reappointment, compensation, and evaluation of outside directors, which leads to the “clubby board” problem.

To tackle these problems, in early 2009 the Korean government created the “Task Force for Improved Corporate Governance regarding Outside Directors.” The task force consists of scholars and front-line staff from the Korea Institute of Finance (KIF), the Financial Services Commissions (FSC), the Financial Supervisory Services (FSS).

To secure an objective perspective, the task force (1) conducted in-depth interviews and survey of former and present outside directors and (2) studied best practices of international organizations, the US, the UK, Germany, and France and (3) identified policy agenda.

The agenda involves strengthening outside directors’ responsibility and expertise, securing the independence of outside directors, and eliminating the side effects arising from the current system of outside directors such as conflicts of interest and clubby boards. Public hearings have been held to gather various opinions from the academia, the banking industry, the media, and civic groups.



Financial Services Commission  
[www.fsc.go.kr](http://www.fsc.go.kr)

Banks are encouraged to adopt best practices on the “comply or explain” basis. To prevent conflicts of interest and demand stricter qualifications for outside directors, the government revised related laws including *the Enforcement Decree of the Financial Holding Companies Act*.

- According to the revision of *Enforcement Decree of the Financial Holding Companies Act* released on November 3<sup>rd</sup>, the provisions of the decree governing financial holding companies to prevent conflict of interest should be in conformity with those of the decree governing banks.
- The original enforcement decree prohibits those who work in companies which engage in major transaction with the financial holding company, where conflicts of interest may arise, from being appointed as outside directors of the company. The revision extends the scope of companies subject to conflict of interest to include affiliates.
- The original enforcement decree prohibits the individuals from being appointed as outside directors of the financial holding companies, to whom the financial holding company outsources services such as legal or accounting services. The revision extends the scope of outsourced services subject to conflicts of interest to include computing, property management, and research and survey services.

Banking institutions and the Korea Federation of Banks created a task force to work on setting out best practices in the banking sector. The “Task Force for Best Practices in the Banking Sector” consists of 12 members: 9 from the banking sector (including 1 from the Korea Federation of Banks, 1 from the Korea Institute of Finance, 4 from banks, 2 from bank holding companies), 3 from financial authorities (one from the FSC, two from the FSS).

The global financial crisis reaffirmed that banks should take social responsibility as an essential part of a country’s financial system and should have sound corporate governance.

The Korean government will complete the ongoing process to improve the system of outside directors as soon as possible and make continued effort to establish best practices in the banking sector. The government will encourage banks to enforce best practices by taking into account the compliance with best practices when assessing banks’ CAMELS ratings.

For further inquiries:

Lee, J. Ernst  
Foreign Press Spokesperson  
Foreign Press & Relations Office  
Financial Services Commission  
Tel: +82-2-2156-9582  
Fax: +82-2-2156-9589  
E-mail: [happyhero@korea.kr](mailto:happyhero@korea.kr)