

Press Release

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Seven Point Reform Plan to Restore Trust in Business and in the Global Financial System

The Caux Round Table (CRT) today laid out a seven point reform plan to restore trust in business and the global financial system and to ensure financial system stability. The CRT, which is an international network of business and professional leaders working to promote moral capitalism, urged the G20 leaders to immediately implement these essential reforms.

“Capitalism’s so called immune system of laissez-faire market discipline has failed the test and the underlying causes of this systematic breakdown - greed and narrow self interest - must be addressed”, said Lord Dan Brennan QC, the Chairman of the Caux Round Table and past Chairman of the Bar of England and Wales.

“Business leaders, governments and regulators alike must act now if we are fully to deal with the greatest threat to capitalism and global prosperity since the Great Depression. The CRT’s seven point reform plan lays out fundamental reforms that are needed to restore trust and confidence in business and ensure financial system stability”, Lord Brennan said.

The CRT’s seven point reform plan takes responsible capitalism from the fringes of business behavior and firmly entrenches it at the heart as to how good business is done. Importantly, the proposed reforms address the key underlying causes of the crisis and the critical need to restore the soundness of financial institutions which remains of first importance for a successful market economy.

“Failures to properly assess risk and a dysfunctional and shortsighted system of incentives and remuneration have been at the heart of the problem”, said Dr Stephen Young, Global Executive Director of the CRT.

“Compensation of senior executives, traders and fund managers was, and still is in most cases, built on narrow self interests and decoupled from long-term wealth creation. Rewards rose with excessive risk taking and have been provided in ways that have largely shielded senior corporate officers and fund managers from liability for their decisions”, Dr Young said.

“Also at the core of the problem has been a failure of governance. Boards of directors were not sufficiently encased in an environment of sound risk management, responsibility, transparency and ultimate accountability. And financial regulation failed to offset the inherent dysfunctionality of the markets”, Dr Young said.

Lord Brennan noted that “despite the need for urgent action to address the underlying causes, there are inadequate reforms on the table. Business leaders and boards are largely silent, and politicians, regulators and central banks are flat out putting out the fires.”

“The CRT’s proposed reforms represent essential steps in rebuilding a market immune system of accurate pricing, risk management and valuation transparency, and ensuring ethical and responsible capitalism”, Lord Brennan said.

The Caux Round Table’s Seven Point Reform Plan to Restore Trust in Business and in the Global Financial System

1. Require board directors to consider interests beyond shareholders, which may affect the company’s success, by codifying the principle of “*enlightened shareholder value*” in company law.

Proposed reforms:

- Require corporate board directors to disclose all material risks and uncertainties to the future development, performance and sustainability of the company and its business in the annual report.
- Specifically, require corporate boards to disclose annually the material risks and impacts flowing from:
 - workplace and employee issues;
 - customer, product and service issues;
 - supply chain matters;
 - environmental risks; and
 - social and community issues and concerns.

2. Require minimum standards of corporate governance knowledge and expertise for corporate board directors.

Proposed reforms:

- Require corporate board directors to have the skills and expertise to:
 - responsibly execute their duties of trust and profit, given business is not without consequence for society;
 - oversee the full spectrum of financial, governance, social and environmental risks to the company; and
 - ensure business practices meet minimal ethical standards.

3. Require corporate boards to have a dedicated board committee responsible for risk oversight across the full spectrum of risks - financial, governance, social, environmental.

Proposed reforms:

- Require the Board Risk Committee have an independent chair and a majority of independent directors on the committee.
- Require corporate boards to commission independent assurance reports annually on the effectiveness of their company's risk management processes and to disclose the assurance report findings.

4. Regulate executive remuneration structures to ensure that they are consistent with prudent risk management, align with long-term wealth creation, and do not reward poor performance.

Proposed reforms:

- Require corporate board directors to make annual disclosures (and at the time of the appointment of any CEO) detailing:
 - conflicts of interest and other risks embedded in both short-term and long-term executive performance incentives, including how the Board proposes to manage such risks; and
 - the degree to which the remuneration structure aligns executive interests with those of shareholders, including during times of company stress and underperformance.
- Require all equity linked remuneration to be in the form of common equity escrowed for a minimum period of five years, regardless of continued employment.
- Prohibit Board members and key executives from borrowing or hedging against the common equity they hold in the company, unless there is full and timely disclosure of all such borrowing or hedging.
- Cap termination payments at one year's remuneration unless there is prior shareholder approval of a higher amount.

5. Implement stronger and globally co-ordinated financial and banking regulatory reforms to prevent systemic risk build-up or market manipulation.

Proposed reforms:

- Harmonise regulation and co-operation of financial supervisors / regulators across the G20, including cross-border supervision of globally significant financial entities, to enhance financial system stability and close opportunities for regulatory arbitrage.
- Broaden regulatory coverage to all financial entities and transactional activities that pose material systemic risk to financial stability.

- Strengthen capital adequacy of all systemically important financial institutions in line with their underlying risk profiles.
- Weed out or strictly regulate market products, behaviours and activities that are not consistent with the principles of market stability, long term value creation, and a fully informed market.

6. Regulate all financial markets instruments and investment activities that materially impact on financial system stability and on superannuation and pension system viability.

Proposed reforms:

- Broaden regulatory coverage to all financial entities, products and transactional activities that pose material risks to financial stability or to superannuation and pension fund viability.
- Enable regulators to intervene in and control excessive speculation and risk accumulation in all systemically important financial markets and instruments.
 - Market participants, including derivative and hedge funds, required to disclose trading and other information necessary to adequately access market and systemic risk.
- Establish fully regulated exchanges for credit derivatives and other systemically important instruments.
- Require registration and ensure regulatory oversight of credit ratings agencies whose ratings materially impact on financial and investment markets.
 - Review the practice of paid ratings and consider possible reform to ensure independence of ratings.

7. Reform and adequately resource the IMF and other multilateral institutions to ensure they are effective forces for economic and social justice globally.

Proposed reforms:

- Ensure the IMF and other international financial institutions and multilateral development banks are resourced to assist emerging and developing economies in dealing with the flow-on from the global financial crisis.
- Broaden Financial Stability Forum membership to all G20 members and strengthen its role including via the development of an early warning system for threats to global financial stability.
- Strengthen measures to oppose and prevent trade protectionism while renewing initiatives within the World Trade Organization towards a global free trade agreement.

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About the Caux Round Table

The Caux Round Table (CRT) is an international network of business and professional leaders working to promote a moral capitalism since 1986. The CRT advocates implementation of the CRT *Principles for Responsible Business* through which capitalism can flourish and sustainable and socially responsible prosperity can become the foundation for a fair, free and transparent global society.

Uniquely, the Caux Round Table (CRT) *Principles for Responsible Business* provide strategic ethical guidance which, had it been followed, would have kept those institutions that have triggered the Global Financial Crisis more faithful to their obligations of stewardship, good governance and stakeholder risk management.

The CRT *Principles for Responsible Business* go to the heart of constructive and ethical behaviors that enhance risk assessment and stakeholder management, boosting bottom-line valuations of business success and sustaining responsible long-term wealth creation for society.

The CRT *Principles for Responsible Business* can be accessed at <http://www.cauxroundtable.org>

The Principle of *Enlightened Shareholder Value*

The Principle of *Enlightened Shareholder Value* imposes obligation on directors to achieve the success of the company for the benefit of the shareholders by taking proper account of all the relevant considerations for that purpose including:

- a proper balanced view of the short and long term;
- the need to sustain effective ongoing relationships with employees, customers, suppliers and others;
- the need to maintain the company's reputation; and
- the need to consider the impact of the company's operations on the community and the environment.