Guiding Principles for Enhancing U.S. Banking Organization Corporate Governance

BANK POLICY INSTITUTE

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*BPI welcomes public comments on the exposure draft by **March 1, 2021**. Please send all comments to: gregg.rozansky@bpi.com and cheryll.merritt@bpi.com.*

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Introduction

The attached document sets out a series of corporate governance principles (including the commentary, collectively, the "Guiding Principles") that the Bank Policy Institute ("BPI") believes will be useful for U.S. banking organizations to consider in structuring the manner in which the board of directors of the consolidated bank holding company (the "BHC") carries out its oversight responsibilities. [1] These Guiding Principles were initially published by BPI's predecessor, The Clearing House Association, in June 2012 and later updated in 2015 with a view to revising them periodically to reflect changes in law, regulation and practice. In 2016, The Clearing House Association also published "The Role of the Board of Directors in Promoting Effective Governance and Safety and Soundness for Large U.S. Banking Organizations" (the "2016 Publication") to provide further guidance on the core duties of BHC boards. [2] The 2016 Publication also identified hundreds of requirements directed at boards of directors under U.S. federal banking laws, regulations and agency guidance, including examination guidance. This 2021 edition of the Guiding Principles updates the 2015 edition and incorporates concepts from the 2016 Publication. For a more complete list of updates, please refer to **Annex A.**

These Guiding Principles are structured as a set of general principles, supplemented by commentary. The commentary includes considerations that banking organizations may want to take into account to determine the manner in which they will implement these Guiding Principles, as well as references to relevant statutes, regulations, case law, supervisory guidance and other source material. The commentary also references academic and supervisory views and various recommendations on corporate governance practices and principles but, unless otherwise noted, BPI is not endorsing the position of these commentators.

Corporate governance in this context refers to the relationships among the board of directors, management, shareholders, and other stakeholders and their respective roles and responsibilities, with a focus on issues unique to banking organizations. In developing these principles, BPI considered the collective experience of the BHC governance professionals who are members of BPI.

Bank holding companies are subject to state laws on corporate governance practices. Additionally, specific to the banking industry, the standards and expectations of bank regulators are expressed in the form of regulations and supervisory guidance (issued both broadly through manuals and publications and specifically in the course of an organization's own supervisory discussions and reports). Supervisory guidance from bank regulators, in contrast to actual law, rules and regulations, is not binding, and regulators should not criticize or initiate an enforcement action against a banking organization for failure to follow such guidance. [3] When referring to regulatory pronouncements, commentary to these Guiding Principles reflects this distinction between binding laws and regulations, which set "requirements," and non-binding supervisory guidance, which provides "expectations" or "recommendations." Nonetheless, banking organizations should consider supervisory guidance carefully in light of their particular businesses and circumstances and the context in which the guidance is provided. Furthermore, although regulations and supervisory guidance about corporate governance at the bank level are not directly applicable for bank holding companies, they often can provide important guidance for the boards of bank holding

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1. These Guiding Principles are principally designed for U.S. banking organizations because non-U.S. banking organizations (including their U.S. subsidiaries and other U.S. operations) are generally subject to a different set of governing laws, regulations and relationships presenting certain unique issues and considerations not addressed in these Guiding Principles.

2. The 2016 Publication is available at https://www.theclearinghouse.org/-/media/action%20line/documents/volume%20vii/tch_report_the-role-of-the-board-of-directors-in-promoting-governance.pdf.

3. Interagency Statement Clarifying the Role of Supervisory Guidance (September 11, 2018) (affirming that supervisory guidance should not have the force of law); OCC, Federal Reserve System, FDIC, NCUA & CFPB, Role of Supervisory Guidance, 85 Fed. Reg. 70,512 (Nov. 5, 2020). BPI continues to recommend that the agencies take steps to modify existing guidance as and where necessary to avoid suggesting that guidance has the force of law. For example, a reference to guidance in the text of a rule could create ambiguity as to the legal status of any expectations articulated in such guidance. *E.g.*, 12 C.F.R. § 7.2010 ("The board of directors should refer to OCC published guidance for additional information regarding responsibilities of directors."). The OCC recently clarified that 12 C.F.R. § 7.2010 "only refers boards of directors to OCC guidance for additional information and does not suggest that guidance has the force of law." OCC, Activities and Operations of National Banks and Federal Savings Associations, 85 Fed. Reg. 83,686 (Dec. 22, 2020).

companies.

Each banking organization and its board of directors should have the ultimate flexibility in developing its own governance practices that are tailored to the banking organization's strategic objectives, plans, businesses and circumstances. These Guiding Principles are intended to help guide BHCs as they address corporate governance issues, but are not designed to be prescriptive or to set minimum requirements or best practices applicable to all banking organizations. Each banking organization must tailor its governance practices as it deems appropriate for its own situation. Within that context, any number of individual principles may, in whole or in part, be of less significance or may require adaptation with respect to a particular banking organization.

BPI believes that it is important to bear in mind that corporate governance structures and practices facilitate, rather than determine, effective corporate governance. Significant governance failures can occur, and have occurred, even in a context of well-documented and rigorous formal governance policies and structures. Although well-designed corporate governance structures are necessary, they are not sufficient—ultimately, effective corporate governance is determined by the quality, skills, expertise and judgment, individually and collectively, of the members of the board and the management of the banking organization, and the culture of objective and informed oversight, director and management integrity, ethical behavior and performance that those individuals foster. These Guiding Principles should be read and applied in accordance with this fundamental understanding. In addition, it must be recognized that the skills and experience of members of the board appropriate for an institution will vary based on considerations such as an institution's size, business model, scope of operations, risk profile, and other characteristics that may change over time.

A central tenet of good corporate governance is the distinction between the board's responsibility for *oversight* of the business and affairs of the BHC and the board's delegation to management of the responsibility for the day-to-day *operations* of the BHC. Absent extraordinary circumstances, the board should not involve itself in day-to-day operations, as this likely will reduce efficiency, impair the board's ability to perform its critical oversight role objectively, and create uncertainty as to roles and responsibilities. Indeed, excessive board involvement in the day-to-day affairs of a banking organization could compromise the board's independence and its ability to discharge its fiduciary duties, which is a hallmark of sound corporate governance. Similarly, holding directors accountable based on an after-the-fact hindsight assessment of board oversight is in tension with the principles-based approach to corporate governance and the oversight role and core oversight responsibilities of the board,[4] and is contrary to the state law principle that decisions by the board should not be second-guessed. Over the past five years, U.S. regulators have increasingly acknowledged the need for the board to return to a focus on core oversight functions and top-tier strategies (*i.e.*, to move away from devoting substantial time and effort to fulfilling granular supervisory expectations and requirements that, in practice, conflate the roles of the board and management),[5]

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4 The Model Business Corporation Act (May 2019 Revisions), Official Comment to § 8.31 ("Boards of directors and corporate managers make numerous decisions that involve the balancing of risks and benefits for the enterprise. Although some decisions turn out to have been unwise or the result of a mistake of judgment, it is not reasonable to impose liability for an informed decision made in good faith which with the benefit of hindsight turns out to be wrong or unwise. Therefore, as a general rule, a director is not exposed to personal liability for injury or damage caused by an unwise decision and conduct conforming with the standards of section 8.30 [which describes processes in oversight efforts and decision-making] will almost always be protected regardless of the end result."); *In re Citigroup Inc. Shareholder Derivative Litig*., 964 A.2d 106, 131 (Del. Ch. 2009) ("Oversight duties under Delaware law are not designed to subject directors, even expert directors, to personal liability for failure to predict the future and to properly evaluate business risk.").

5 *E.g.*, Federal Reserve System, Proposed Guidance on Supervisory Expectation for Boards of Directors, 82 Fed. Reg. 37,219 (August 9, 2017) ("Board Effectiveness Proposal"). Annex C contains a list of the Federal Reserve supervisory guidance identified in the Board Effectiveness Proposal as being considered for possible rescission or revision. BPI continues to support the Federal Reserve Board's efforts to review all existing supervisory expectations and regulatory requirements relating to boards of directors and rescind or revise those that do not relate to the board's core responsibilities or are not aligned with the Federal Reserve Board's supervisory framework. These efforts are consistent with BPI's approach of periodically revising these Guiding Principles to reflect changes in law, regulation and practice. Just as these Guiding Principles evolve, so too should guidance and regulations. We accordingly encourage the other banking agencies to review and, as appropriate, rescind or revise their guidance and regulations on corporate governance matters. In addition to addressing their guidance, BPI also recommends that the agencies review and revise their approach to allocating responsibilities to the board and management in enforcement actions. Enforcement actions often provide for a board to be inappropriately and granularly

although this acknowledgement remains to be consistently reflected in the specific language of regulatory pronouncements. BPI agrees with the regulators' approach to align supervisory expectations with core board functions and supports reflecting this alignment in examinations and supervisory practices. The revised Section 4 in this 2021 edition of the Guiding Principles incorporates concepts from the 2016 Publication and focuses on only those core functions of the board that are fundamental to the safe and sound operation of a banking organization.

The typical structure contemplated by BPI in these Guiding Principles is that of a top-tier public holding company with one or more wholly owned subsidiary banks (and typically non-bank subsidiaries). BPI generally designed these Guiding Principles to be applicable to a banking organization as a whole, but with the understanding that the interplay between the holding company and the subsidiary bank(s) will vary from organization to organization, and that an identical corporate governance approach often will not apply to both a public holding company and a wholly owned subsidiary. In particular, the governance structure of a holding company organization should reflect the critical responsibility of the board of directors of the subsidiary bank to protect the safety and soundness of the bank.

Generally speaking, it should be acceptable for entity-level risk and control functions (including at bank subsidiaries) to be part of an enterprise-wide risk management structure managed at the parent company level, and generally overseen by the parent company board. However, this is the case only to the extent that the system provides for necessary entity-level legal and safety/soundness considerations and board involvement. Although banking organizations should be allowed the flexibility to integrate and coordinate the oversight of risk management within an enterprise-wide structure, it remains critical that boards at the subsidiary level remain cognizant of entity-level considerations. Where the parent company framework is adequate for the subsidiary and the framework allows for the consideration by subsidiary boards of entity-level concerns, any mandating of duplicative structures can create administrative distraction and inefficiency, as well as confusion, and subvert enterprise-wide risk management.

The 2021 edition of the Guiding Principles has been refocused on matters that are of unique relevance for the boards of banking organizations in discharging their oversight duties (*e.g.*, the important role that boards play in overseeing banking organizations' liquidity risks, capital, recovery and resolution planning, and meeting expectations of prudential supervision). However, the bedrock principles of corporate law that apply to boards of large companies should continue to apply to boards of banking organizations. For example, the same overarching fiduciary duties should guide the boards' consideration of issues relating to strategy and emerging risks, technological transformation, cybersecurity, management of general operational risks, regulatory compliance and the safety and soundness of the banking organization.

Moreover, even in times of crisis or emergency such as the COVID-19 pandemic, boards continue to have the same overarching fiduciary duties even though discharging those duties may require increased frequency of board meetings and enhanced oversight of management's response to the crisis.[6] Boards, for example, have been taking steps as appropriate to become satisfied that management has adequately evaluated the growing challenges presented by COVID-19 for business lines of the banking organization and third party bank vendors, including adjusting controls in the context of switching from in-person to remote operations, as well as the financial impact on several sectors of the economy. In addition, where and as appropriate, boards have been asking questions of management, and receiving updates, on the banking organization's participation in, and risks relating to, emergency lending programs. At the same time, many boards have adapted and modified board practices under the circumstances of the pandemic, including implementing telephonic and/or electronic board meetings to reduce logistical constraints and health risks associated with in-person meetings.[7]

This updated exposure draft of these Guiding Principles was published for public comment on January 12, 2021.

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involved in remediation projects, which, like much existing guidance, does not appropriately reflect the distinct oversight role of a board.

[6] It is the same level of duties as described in greater detail in Section 4.

[7] *See* Section 11 (discussing board remote meetings).

BPI recognizes that governance practices are not immutable. Although the distinction between the role of the board versus that of management remains a core precept for effective governance, governance practices evolve over time in response to market and industry practice, the regulatory and supervisory environment and the collective experiences of market participants. BPI expects to continue to revisit these Guiding Principles from time to time to assess whether further changes or updates are appropriate. Readers of these Guiding Principles should bear in mind that this document speaks as of its date and should consider the impact of any subsequent developments.

These Guiding Principles were prepared under the auspices of BPI's Corporate Governance Committee with the assistance of BPI's special counsel, Sullivan & Cromwell LLP.

Guiding Principles

Note: These principles should be read together with the related commentary set forth in the next section of this document.

SECTION 1. BASIC RESPONSIBILITIES OF THE BOARD AND MANAGEMENT

a) Under law, the business and affairs of a corporation, including a banking organization, are managed under the direction of a board of directors. The duties of a board of a banking organization are consistent with those of boards of other companies.
b) The board delegates to a professional and full-time management team the day-to-day operation of the company. This positions the board to provide oversight of—and serve as an independent check on—management. Maintaining a distinction between the respective roles of the board and of management is necessary in any corporation, including banking organizations.
c) The board is responsible for providing oversight of the business and affairs of a banking organization and its management, for selecting the Chief Executive Officer (the "CEO"), and for making statutorily identified decisions. The board may discharge all its duties and responsibilities directly or through board committees to the extent permitted by law.
d) Management is responsible for the day-to-day operations of the banking organization. Boards may rely reasonably on management and employees for responsibilities delegated to them, as well as consultants and other advisors.

SECTION 2. INDEPENDENCE OF BOARD MEMBERS

a) A substantial majority of the directors of the top-tier entity within a banking organization should be independent, and only a relatively small number of directors should be members of management.
b) The board of the holding company should receive updates, as appropriate for its particular circumstances, regarding the composition of the boards of its subsidiary banks and other material subsidiaries. Directors who serve on both holding company and subsidiary bank boards should remain cognizant of the role in which they are acting at any particular time, and their responsibilities to the entity of which they are acting as a board member.

SECTION 3. COMPOSITION OF THE BOARD

a) The board of the top-tier entity within the banking organization should have the flexibility to determine its own appropriate composition, taking into consideration the size of the board, the diversity, expertise and tenure of the board members, and the capacity of board members to commit to serving on the board of a banking organization. Within any state or federal statutory requirements, the top-tier entity should have the flexibility to determine the appropriate composition of the boards of its subsidiary banks.
b) The board should be small enough to facilitate effective functioning but large enough to allow members to contribute sufficient knowledge, experience and diversity to the board's oversight role and its committees.
c) Decisions on board composition will depend on a banking organization's particular circumstances, needs and objectives, including:
    i. the nature, scope and complexity of its business, as well as its strategic objectives and/or plans;
    ii. the need to meet applicable independence and other regulatory standards;
    iii. the need to provide a range of skills commensurate with the board's oversight role and a diversity of views that can provide necessary insight into the banking organization's multiple constituencies; and
    iv. the ability to staff board committees with a sufficient number of members that meet relevant independence and qualification criteria and the needs and expertise of the committees.

SECTION 4. CORE BOARD FUNCTIONS

a) The oversight duties and responsibilities of the board of a banking organization should focus on the following five core functions:
   i. Function 1: Reviewing and approving strategic objectives and/or plans;
   ii. Function 2: Monitoring financial performance and condition;
   iii. Function 3: Overseeing talent management, including for the CEO and other senior executives;
   iv. Function 4: Overseeing the risk management and internal control frameworks, including top-tier policies and plans in fundamental areas; and
   v. Function 5: Reinforcing, demonstrating and communicating the "tone at the top" for the values and culture of the organization and overseeing enterprise-wide approaches/programs intended to promote organizational values, culture and reputation.

b) The board should perform all other oversight duties and responsibilities required by statute, regulation or regulatory orders (including oversight of executive compensation programs, liquidity and stress testing) or that the board deems appropriate from time to time.

c) For subsidiary banks, many of these responsibilities may be discharged by the board of the top-tier entity within the banking organization, depending on the structure of the organization and the judgment of the top-tier board and the subsidiary bank board as to the appropriate allocation of responsibilities (subject in any case to specific regulatory requirements at the subsidiary bank level).

SECTION 5. BOARD COMMITTEES

a) The board of the top-tier entity within a banking organization should establish board committees to assist the board in its oversight of (i) audit, (ii) nominating/corporate governance, (iii) compensation and (iv) risk management activities, as well as any other standing or temporary committees appropriate to the circumstances and businesses of the banking organization.

b) The board should have the flexibility to allocate responsibilities among board committees. The responsibilities of each standing committee should be described in a written charter or similar document. Certain matters might be within the scope of two or more committees (*e.g.*, audit and risk management), and the board may determine which committee is best suited to address a certain matter as it deems appropriate, taking into account any regulatory requirements providing that a particular matter be the responsibility of a particular committee. Periodic joint meetings may be appropriate for particular issues or topics. The relevant committees should coordinate as they or the board deem appropriate.

c) The standing committees should report regularly to the full board. The board should adopt a schedule for the reports to be delivered by each committee, recognizing that it may be appropriate for some committees to report more frequently than others.

d) The board and each committee of the board should have the authority to engage counsel and outside advisors as they deem necessary or appropriate to carry out their duties.

SECTION 6. AUDIT COMMITTEES AND BOARD OVERSIGHT OF FINANCIAL REPORTING AND AUDIT FUNCTIONS

a) The board of the top-tier entity within a banking organization should have an audit committee, composed entirely of independent directors, with the responsibility to oversee internal audit and internal controls as well as the sole authority to appoint, terminate and approve compensation for independent auditors.

b) The members of the audit committee of the top-tier entity collectively should have appropriate accounting, banking and related financial expertise and experience, including at least one member who is an audit committee financial expert under SEC rules.

c) The audit committee, or another independent committee, should review and approve the policies governing the receipt, retention and treatment of complaints regarding accounting or auditing concerns, including confidential, anonymous submissions by employees or other parties.

SECTION 7. NOMINATING/CORPORATE GOVERNANCE COMMITTEES, DIRECTOR QUALIFICATIONS AND BOARD OVERSIGHT OF DIRECTOR NOMINATION PROCESS

a) The board of the top-tier entity within a banking organization should have a committee, composed entirely of independent directors, to conduct the director nomination process and assess the qualifications and independence of director candidates. This committee should establish factors to be considered in evaluating prospective director nominees and in evaluating directors for membership on board committees, taking into account the circumstances and businesses of the banking organization, the responsibilities of the various committees, and the importance of having appropriate diversity, expertise and experience among board members.
b) The board of the top-tier entity within a banking organization should have a committee, composed entirely of independent directors, with responsibility for corporate governance, including responsibility for the board self-evaluation process and advice and assistance to the board in overseeing the entity's corporate governance structures, processes and performance.
c) The nominating and corporate governance committee functions may be joined together, may be undertaken by separate independent committees or may be apportioned to independent committees that have other functions.

SECTION 8. COMPENSATION COMMITTEES AND BOARD OVERSIGHT OF EXECUTIVE COMPENSATION

a) The board of the top-tier entity within a banking organization should have a compensation committee, composed entirely of independent directors, to review and approve the compensation of the CEO and to oversee the compensation of other senior executives and the development of compensation programs that attract and retain highly qualified executives and other employees, satisfy regulatory standards and discourage inappropriate risk taking.
b) The compensation committee should have an understanding of compensation practices in the financial services sector and should review and approve compensation practices that appropriately balance risk and reward (with input from the chief risk officer and the risk committee, as appropriate) and take into account compliance performance and ethical behavior.

SECTION 9. RISK COMMITTEES AND BOARD OVERSIGHT OF RISK MANAGEMENT

a) The board of the top-tier entity within a banking organization should have a committee to oversee its risk management systems and control procedures for identifying, assessing and managing its risk exposures, and to oversee the organization's adherence to the agreed risk profile.
b) This committee should include at least one member with substantial risk management knowledge and experience.

SECTION 10. INDEPENDENT LEADERSHIP OF THE BOARD

The board should determine its own form of independent leadership. The board may determine to have an independent director, the CEO or another non-independent director as the chairperson. If the board determines that the CEO or another non-independent director should serve as chairperson, the independent directors of the board should designate, among themselves, a lead independent director. The lead director should generally have authority to:

a) Work with the chairperson to approve the agenda and schedule for each board meeting and the information to be provided to the board (board materials and board presentations);
b) Convene and chair regular and special executive sessions of the board (*i.e.*, sessions where no member of management, including the CEO, is present); and
c) Review and report on results of board self-evaluations.

SECTION 11. AGENDA, MATERIALS, LENGTH AND FORM OF MEETINGS

a) The agenda for each board and committee meeting should list the subjects that are expected to be discussed at the meeting.

b) Although board and committee meetings generally should follow the agenda, some flexibility may be necessary or appropriate to discuss matters that, because of the time at which they arose or for other reasons, are not listed on the agenda.

c) Materials for board and committee meetings (including the agenda) should be provided to directors sufficiently in advance of meetings, and should contain sufficient detail to enable the directors to prepare appropriately. It is recognized, however, that circumstances may necessitate shortening this time period on occasion. Directors are expected to have read board and committee materials that were provided in advance.

d) Board meetings should include presentations by senior management, other employees of the company and advisors, as appropriate, covering major business, financial performance, risk and control, and legal and compliance matters. Committee meetings should include presentations tailored to the needs of the committee from time to time. Significant time should be reserved for board and committee discussions. Directors should devote sufficient time in a meeting to address all agenda subjects and such other subjects as may be brought to their attention.

e) Although board and committee meetings of banking organizations are traditionally conducted in person and in-person meetings have some advantages, boards of banking organizations should conduct meetings in the format that the board considers appropriate and effective, to the extent permitted by applicable laws and the entity's organizational documents.

SECTION 12. MINUTES OF BOARD MEETINGS

a) The minutes of meetings of the board and its committees should be kept in accordance with the applicable corporate statute under which the banking organization is organized. The board should decide on the level of detail that it believes is appropriate for the minutes, balancing the need to maintain an adequate record to satisfy legal requirements and the need to avoid chilling discussion among directors. Although minutes may prove to be useful for bank regulator examiners reviewing corporate decision making, they are not designed for that purpose.

b) It is common practice not to create detailed minutes of executive sessions of independent directors, because doing so would be antithetical to the very objective of these sessions. The subject matter of these sessions and any formal actions taken may be noted in the minutes, as appropriate.

SECTION 13. BOARD COMPENSATION

The board should adopt a compensation structure for the non-management directors, committee members and the individual directors with designated responsibilities (*e.g.*, lead director and committee chairs) so that the most qualified individuals can be attracted and retained and the interests of directors and shareholders can be aligned, as appropriate.

SECTION 14. MEETING WITH REGULATORS

The board (or, as the board deems appropriate, specified directors) should seek to engage with the principal regulator(s) of the banking organization in connection with the organization's receipt of annual examination reports and otherwise seek consultation with the regulator(s) as the board deems appropriate. Boards, directly or through specified directors, should be receptive to engagement with principal regulator(s) informally, outside the context of board meetings.

Commentary

SECTION 1. BASIC RESPONSIBILITIES OF THE BOARD AND MANAGEMENT

Principles:

a) **Under law, the business and affairs of a corporation, including a banking organization, are managed under the direction of a board of directors. The duties of a board of a banking organization are consistent with those of boards of other companies.**

b) **The board delegates to a professional and full-time management team the day-to-day operation of the company. This positions the board to provide oversight of—and serve as an independent check on—management. Maintaining a distinction between the respective roles of the board and of management is necessary in any corporation, including banking organizations.**

c) **The board is responsible for providing oversight of the business and affairs of a banking organization and its management, for selecting the Chief Executive Officer ("CEO"), and for making statutorily identified decisions. The board may discharge all its duties and responsibilities directly or through board committees to the extent permitted by law.**

d) **Management is responsible for the day-to-day operations of the banking organization. Boards may rely reasonably on management and employees for responsibilities delegated to them, as well as consultants and other advisors.**

Commentary:

The role of directors of banking organizations is established by a matrix of federal banking statutes and regulations and state statutes and common law, as well as pronouncements by bank regulators.[8] The Board of Governors of the Federal Reserve System (the "Federal Reserve Board") has recognized that "[i]n the exercise of their duties, directors [of banking organizations] are governed by federal and state banking, securities, and antitrust statutes, as well as by common law . . . ."[9]

Under general and longstanding principles of corporate law, the fundamental obligations of the board of directors of a corporation are its fiduciary duties of care and loyalty owed to the entity and its shareholders. The specific obligations imposed on directors of banking organizations by banking statutes, regulations and pronouncements are largely intended to protect the safety and soundness of banking organizations; these requirements should not be viewed as altering the directors' core duties or creating "new" fiduciary duties, but rather should be viewed as providing specific directives that inform the manner in which the directors undertake their traditional duty of care.

The directors of two corporations organized under the same corporate statute would not have different fiduciary duties depending on whether they are members of the board of a banking organization or another type of corporation. The business of the corporation and the regulatory framework within which it operates would, however, inform how directors discharge the generally applicable fiduciary duties. The manner in which directors of a highly regulated corporation, such as a banking organization, discharge their fiduciary duties may differ from

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[8] *See*, *e.g.*, 12 U.S.C. § 24 (conduct of business of national banks); 12 U.S.C. §§ 71-76 (management of affairs of national banks); 12 C.F.R. § 7.2010 ("The business and affairs of the bank shall be managed by or under the direction of the board of directors."); 8 Del. C. § 141(a) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . . ."); N.Y. Bus. Corp. § 701 ("[T]he business of a corporation shall be managed under the direction of its board of directors . . . ."); N.Y. Banking § 7001 ("The affairs of every corporation shall be managed by a board of directors . . . .").

[9] *See* Division of Banking Supervision and Regulation, Federal Reserve Board, Commercial Bank Examination Manual (1995) ("Commercial Bank Manual"), Section 5000.1, at 1 (2013).

that of directors of corporations that are not similarly regulated.[10]

Suggestions that the directors of banking organizations should have fiduciary duties to persons other than just shareholders are beyond the scope of these Guiding Principles. BPI believes, however, that these suggestions should be approached with caution because of the uncertainty and potential conflicts that such an expansion of fiduciary duties could create and the potential discouragement of qualified individuals from serving on bank boards. Similarly, the interpretation of recent statements that the purpose of a corporation is to serve a variety of constituencies is beyond the scope of these Guiding Principles.

Technological transformation is affecting all aspects of the economy, including the banking sector. For a banking organization, as for any corporation, technology transformation may affect its business and strategic objectives as well as which areas receive greater board attention. Technological transformation does not and would not, however, change the core duties of the board under general and longstanding principles of corporate law.

Exercising oversight is inherently an active and not passive role. An informed and actively engaged board is a core element of effective governance and contributes to the effective exercise of core board functions, including guiding the strategic direction of the organization and providing effective and objective oversight of management performance. Informed and active engagement in the performance of core board functions may be exhibited through several different types of actions, including by directors: (i) overseeing the development of, and approving, the banking organization's strategic objectives and/or plans; (ii) understanding, and being satisfied with, how responsibility and leadership (*e.g.*, managerial governance committees) are structured and decisions are made within the management team for key issues and, where the board considers appropriate, providing input or advice on managerial, corporate and risk governance structures; (iii) overseeing that management's initiatives have been thoroughly evaluated (including, where relevant, understanding what alternatives have been considered or offered and the underlying rationale and facts supporting the initiative); (iv) providing feedback on senior management's performance; (v) providing guidance to matters to be included on the board agenda, including the types of matters/information that should generally be brought to the attention of the board; and (vi) asking informed questions of management (*e.g.*, relating to assumptions underlying proposed initiatives).

Active oversight should not result in an adversarial relationship between the board and management. BPI recognizes that the board's oversight role includes what has become termed by bank regulators as "challenge" or "credible challenge" to management. We believe that challenge or credible challenge should consist primarily of informed and probing questions of management, at or outside of board meetings, rather than a formal record of disagreements with management or rejections of management recommendations. In particular, a lack of disagreement with management is not equivalent to a lack of board oversight, and we do not believe that the effectiveness of challenge or credible challenge can be evaluated based on the number of challenges recorded in the minutes or elsewhere. Ordinarily, the absence of a board's disagreement with management reflects that, prior

[10] State corporate law establishes applicable fiduciary duties and has, in some cases, been interpreted to require that the legal and regulatory framework applicable to a corporation inform the manner in which a board discharges its oversight responsibilities. For example, in 1996 the Delaware Court of Chancery found that directors' fiduciary duties include "a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists" *In re Caremark Intern. Inc. Derivative Litigation*, 698 A.2d 959, 970 (Del. Ch. 1996). In 2019, the Delaware Supreme Court confirmed that "directors must make a good faith effort to implement an oversight system and then monitor it." *Marchand* v. *Barnhill*, 212 A.3d 805, 821 (Del. 2019). The Delaware Chancery Court has described the *Marchand* decision as "underscor[ing] the importance of the board's oversight function when the company is operating in the midst of 'mission critical' regulatory compliance risk" and noted that the decision "makes clear [that] when a company operates in an environment where externally imposed regulations govern its 'mission critical' operations, the board's oversight function must be more rigorously exercised." *In re Clovis Oncology, Inc. Derivative Litig.*, 2019 WL 4850188 (Del. Ch. Oct. 1, 2019). Delaware courts noted that, compared to "a failure to monitor and prevent harms flowing from risks that confront the business in the ordinary course of its operations", the "[f]ailure to monitor compliance with positive law, including regulatory mandates . . . is more likely to give risk to oversight liability." *In re Facebook, Inc. Sec. 220 Litig.*, 2019 WL 2320842, at *14.

Banking organizations are subject to laws and regulations affecting all aspects of their operations, including their "mission critical" operations. The recent cases building on *Caremark* have made it increasingly important for directors of banking organizations to evidence their oversight of legal and regulatory compliance.

to presenting a matter or initiative to the board, management had appropriately analyzed, developed and vetted the key issues, including potentially with the leadership or membership of relevant board committees. A view that oversight requires disagreement is misguided and could jeopardize a banking organization's safety and soundness by fomenting unnecessary discord between a board and management. Similarly, BPI believes that collegiality among board members contributes to the effective oversight of a banking organization.

The formulation of strategic plans and/or objectives and day-to-day management of the organization is delegated to the organization's officers, with the board exercising oversight and relying on the management discharging its responsibilities in day-to-day operations that are appropriately delegated to it. The line between oversight and management will not always be clear, and the manner of implementation of the board's oversight will vary from institution to institution. Nevertheless, it is a well-established principle of corporate governance that the board of a corporate entity, including a banking organization, generally is responsible for supervising and overseeing the affairs of the organization, while the responsibility for the day-to-day conduct of the organization's business resides with management. Indeed, the board should not embroil itself in so many details that it interferes with management prerogatives or is limited in performing its general oversight role. Moreover, for the directors to attempt to exercise active day-to-day management or control could compromise the board's independence and create serious safety and soundness issues because the directors normally would lack the experience, expertise, time and knowledge to perform this role, and doing so could compromise the board's independence, which is a hallmark of sound corporate governance.

This crucial distinction between the oversight responsibilities of the board and the day-to-day management of banking organizations by managers and employees has been recognized by federal bank regulators. The Federal Reserve Board has stated that the board of a member bank "should delegate the day-to-day routine of conducting the bank's business to its officers and employees . . . ."[11] The Office of the Comptroller of the Currency (the "OCC") also has stated that the role of national bank directors is to oversee the bank, and that one of their most fundamental responsibilities is to select and retain competent management who are "able to direct day-to-day operations to achieve the bank's strategic goals."[12] Similarly, the Federal Deposit Insurance Corporation (the "FDIC"), in the Pocket Guide for Directors (the "FDIC Pocket Guide"), has declared that the role of an insured banking organization's board is to oversee the conduct of the institution's business.[13]

In addition to recognizing the fundamental distinction between the roles of the board and management, federal bank regulators have also sought to clarify the contours of management's day-to-day responsibilities. The OCC has expounded upon management's role in strengthening the risk management and governance practices of large national banks with a particular emphasis on the role of the CEO, "front line" unit executives, the chief risk executive, and the chief audit executive.[14] The Federal Reserve Board, in its rules promulgated under Section 165

[11] Commercial Bank Manual, Section 5000.1, at 1; *see also* Michael P. Malloy, Banking Law and Regulation, (2nd ed., 2019-5 Supplement) ("Malloy– Banking Law"), Section 4.02[D], at 1 ("As a general rule . . . it is expected that much of the function of day-to-day management will be delegated to the executive officers . . . ."); Board Effectiveness Proposal, at 37,219 (proposing to "better distinguish between the roles and responsibilities of an institution's board of directors and those of senior management").

[12] OCC, Director's Book: Role of Directors for National Banks and Federal Savings Associations (November 2020) ("OCC Director's Book"), at 28; *see also* OCC, Comptroller's Handbook, Corporate and Risk Governance (July 2019) ("OCC Handbook"), at 6 ("The board's role in the governance of a bank is clearly distinct from management's role. The board is responsible for overall direction and oversight of the bank—but is not responsible for managing the bank day-to-day.").

[13] *See also* FDIC, Supervisory Insights: A Community Bank Director's Guide to Corporate Governance: 21st Century Reflections on the FDIC Pocket Guide for Directors (revised October 2018) (April 2016) ("FDIC Supervisory Insights"), at 5 ("while directors and officers often work hand-in-hand, their formal roles within the bank are distinct and should not be intermingled. Ultimately, the board is responsible for monitoring senior management").

[14] *See* OCC, Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations and Insured Federal Branches; Integration of Regulations (September 2, 2014) (the "OCC Heightened Standards"); *see also* OCC Handbook, at 56 ("The OCC expects senior management to be responsible for developing and maintaining the risk governance framework").

of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010[15] (the "Dodd-Frank Act," and such rules, the "Federal Reserve Enhanced Standards"), which are binding on covered bank holding companies, requires the appointment of a chief risk officer with experience in identifying, assessing and managing risk exposure to oversee the risk management framework at large bank holding companies.[16] Under the Federal Reserve Enhanced Standards, the chief risk officer has an expanded role and must meet regularly with the board risk committee, members of senior management and, for large foreign banking organizations, the Federal Reserve Board.[17] The Federal Reserve Board also has issued proposed guidance which would clarify core principles of effective senior management, the management of business lines and independent risk management and controls for large financial institutions.[18] The OCC Heightened Standards, the Federal Reserve Enhanced Standards, and the Proposed Risk Management Guidance demonstrate a heightened focus on clarifying and, in some cases, expanding expectations for risk management and the roles and responsibilities of senior management, vis-à-vis the board of directors, in implementing an effective risk governance framework.

The separate roles of directors and officers have been recognized by bank regulators outside the United States as well.[19] For instance, David Walker observed in his review of corporate governance at U.K. banks that "the core separation between the roles [of the board and management] is well-entrenched if not always well-understood."[20] The Basel Committee on Banking Supervision (the "Basel Committee"), a committee consisting of senior representatives of bank supervisory authorities and the central banks of over 25 countries, adopted this precept as one of its foremost principles for sound corporate governance of banking organizations.[21] The Group of Thirty also emphasized the importance of this distinction in its April 2012 publication on the governance of financial institutions.[22] The U.K. Financial Reporting Council, which sets the U.K.'s Corporate Governance and Stewardship Codes, also has noted that "[the board's] role is to promote the long-term sustainable success of the company" and "it should seek assurance that management has taken corrective action" if "it is not satisfied that policy, practices or behaviour . . . are aligned with the company's purpose, values and strategy."[23]

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15 Pub. L. No. 111-203, 124 Stat. 1426.

16 *See* Federal Reserve Board, Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17,240 (February 18, 2014) ("Original Prudential Standards"), as amended by Federal Reserve Board, Prudential Standards for Large Bank Holding Companies, Savings and Loan Holding Companies, and Foreign Banking Organizations, 84 Fed. Reg. 59,032 (November 1, 2019) ("Revised Prudential Standards").

17 12 C.F.R. §§ 252.33 & 252.155; Revised Prudential Standards, at 59,078.

18 *See* Federal Reserve Board, Proposed Supervisory Guidance, 83 Fed. Reg. 1351 (January 11, 2018).

19 Although the importance of a clear distinction between the respective roles of the board and senior management has been recognized by international standard-setting bodies and non-U.S. bank regulators, the legal and regulatory frameworks and the roles and responsibilities of a board may differ in important ways from one jurisdiction from another. For example, in some jurisdictions, the legal and regulatory framework may place greater responsibility on a board, including, in some cases, differentiating among the responsibilities and potential liabilities of individual directors. Those jurisdictions have a fundamentally different paradigm from the U.S. framework addressed in these Guiding Principles.

20 David Walker, A Review of Corporate Governance in U.K. Banks and Other Financial Industry Entities: Final Recommendations (2009) ("Walker Review"), at 35.

21 *See* Basel Committee, Corporate Governance Principles for Banks, (July 2015) (the "Basel Principles"), at 7 ("The board has overall responsibility for the bank, including approving and overseeing management's implementation of the bank's strategic objectives, governance framework and corporate culture."); *see also* Organization for Economic Co-Operation and Development, Principles of Corporate Governance (2015) ("OECD Principles"), at 45 ("Together with guiding corporate strategy, the board is chiefly responsible for monitoring managerial performance . . . .").

22 *See* Group of Thirty, Toward Effective Governance of Financial Institutions (2012) ("G30 Report"), at 40 ("[I]t is essential that the board remain independent and allow management to execute the day-to-day activities of the organization"); *id.* at 42 ("[B]oards may make a critical mistake if they permit their time and attention to be diverted disproportionately into compliance and advisory activities at the expense of strategy, risk governance, and talent issues"); *id.* at 66 ("It is one thing to support and encourage an active and engaged board that is properly familiar with the risks being taken by the organization; it is another to drive boards to an excessive focus on detailed operational matters that are more properly the purview of management.").

23 Financial Reporting Council (the "FRC"), The UK Corporate Governance Code (July 2018) ("UK Governance Code"), at 4.

Of course, the division of responsibilities between the board and management is not restricted to banking organizations and is generally applicable to corporate entities.[24] As the ABA further explains, directors should provide leadership for the business organization through decision making and oversight.[25] In general, the board's oversight function involves (i) reviewing and approving corporate policy and strategic goals, (ii) hiring, evaluating and compensating a CEO and other senior executives, (iii) approving major expenditures, acquisitions and divestitures, (iv) evaluating the risk management structure and (v) monitoring financial performance, management performance and compliance with legal obligations and corporate policies.[26] For a further discussion of the core functions of the board's oversight responsibilities, *see* Section 4 of these Guiding Principles.

One key component of the board's oversight role is to review, discuss and approve overall strategy for the banking organization (with a strategy articulated in a form that is tailored to the banking organization's needs and practices) and to oversee the establishment of policies (including, importantly, those related to risk management) such that all significant activities of the banking organization are "covered by clearly communicated written policies that can be readily understood by all employees."[27] The board should oversee management's implementation of the banking organization's strategy and policies and delegate responsibility for day-to-day business decisions to senior executives and other employees.[28]

Although core board functions include reviewing and overseeing "top-tier" or overarching enterprise-wide policies fundamental to the banking organization's business, strategic priorities and safe-and-sound operation (for example, a banking organization's capital policy), policies that are to be approved by the board should be limited to the "significant" ones and the vast majority of policies and all procedures that address day-to-day operations should be within the sole purview of management and should not be presented to directors for their review or approval. Accordingly, boards should determine which policies the board will review and, as appropriate, approve, taking into consideration the organization's particular circumstances, as well as applicable legal and regulatory

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24 *See*, *e.g.*, *Schoonejongen* v. *Curtiss-Wright Corp.*, 143 F.3d 120, 127 (3rd Cir. 1998) ("[T]he ability to delegate is the essence of corporate management, as the law does not expect the board to fully immerse itself in the daily complexities of corporate operation."); *Grimes* v. *Donald*, 1995 WL 54441, at *8 (Del. Ch. Jan. 11, 1995), *aff'd*, 673 A.2d 1207 (Del. 1996) (noting that Delaware law expressly permits the board to "delegate managerial duties to officers of the corporation"); *Cahall* v. *Lofland*, 114 A. 224, 229 (Del. Ch. 1921), *aff'd*, 118 A. 1 (Del. Ch. 1922) ("The duties of directors are administrative, and relate to supervision, direction and control, the details of the business being delegated to inferior officers, agents and employees. This is what is meant by management."); The American Law Institute, Principles of Corporate Governance: Analysis and Recommendations, § 3.01, Cmt. a, at 80 (1994) ("[I]t is generally recognized that the board of directors is not expected to operate the business. Even under statutes providing that the business and affairs shall be 'managed' by the board of directors, it is recognized that actual operation is a function of management. The responsibility of the board is limited to overseeing such operation." (citation omitted)); Committee on Corporate Laws, American Bar Association (the "ABA") Section of Business Law, Corporate Director's Guidebook (6th ed., 2011) ("ABA Guidebook"), at 11 ("Although the board is responsible for managing and overseeing corporate affairs, it typically delegates responsibility for day-to-day operations to a team of professional [m]anagers"); OECD Principles, at 12 ("Together with guiding corporate strategy, the board is chiefly responsible for monitoring managerial performance . . . ."). The guidance in the ABA Guidebook that is referenced throughout these Guiding Principles is not tailored to banking entities specifically, but rather applies to all public companies (and, to some extent, to corporations generally). *See* ABA Guidebook, Foreword ("The Guidebook provides important information for directors of public companies, but it is also relevant to directors of all companies . . . .").

25 ABA Guidebook, at 11-12.

26 *Id.* at 13.

27 FDIC Pocket Guide; FDIC Supervisory Insights, at 14-15.

28 *See* Basel Principles, at 20 ("Under the direction and oversight of the board, senior management should carry out and manage the bank's activities in a manner consistent with the business strategy, risk appetite, remuneration and other policies approved by the board."); OCC Director's Book, at 71 ("Senior management should be responsible for developing and implementing policies, procedures, and processes that translate the board's goals, strategic objectives, and risk appetite and limits into prudent standards for the safe and sound operation of the bank."); FDIC, Statement Concerning the Responsibilities of Bank Directors and Officers (last updated April 20, 2014) ("Officers are responsible for running the day-to-day operations of the institution in compliance with applicable laws, rules, regulations and the principles of safety and soundness.").

requirements.[29]

To exercise appropriate oversight, the board should receive sufficient information from management—and, where appropriate, external sources—to assess its approach to policies and whether any changes should be made in light of developments relating to the organization or market or other external conditions. Reasonable reliance is an inherent aspect of effective delegation. In delegating to management the day-to-day business operations, the board accordingly is entitled to rely on the statements, reports, summaries or opinions presented to the board by its officers and employees, legal counsel and public accountants, whom they reasonably believe to be reliable and competent, in discharging its oversight duty.[30] Further, in evaluating their approach to policies, as well as reviewing and, where appropriate, approving policies, boards should maintain flexibility as to using summaries and reports prepared by management or external consultants, so that the degree of board attention is commensurate with the significance of the issue or policy under consideration.

BPI believes that it is appropriate to expect the board of directors to oversee the process in place for the establishment of, and adherence to, business or management-level policies, consistent with the board's oversight role, without requiring continuous approval of specific business-level policies and procedures in the ordinary course (for example, absent any "red flags" or unless it is otherwise determined that the circumstances warrant specific board attention/ approval).[31] Similarly, the requirement or expectation in various regulatory pronouncements[32] that a board "ensure" the achievement of certain outcomes is incompatible with the oversight role of the board. Although the board has the authority and the responsibility to oversee management in the operation of business (including with respect to compliance with laws and regulations), this authority does not enable the board to guarantee the desired results.

In the wake of the financial crisis of 2008, Congress and federal bank regulators have often asserted an expanded role for the boards of banking organizations. This trend is exemplified by certain provisions of the Dodd-Frank Act and accompanying regulations. For example, the Federal Reserve Enhanced Standards include requirements for

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29 There are a number of considerations that may be taken into account in determining those matters that warrant particular board attention. These may include, for example, (i) the banking organization's involvement in the relevant products or activities at issue (*e.g.*, limited in scope, volume or nature as opposed to potentially significant impact on the firm's core business, critical operations, etc.), and (ii) the risk posed by the relevant activities at issue when viewed in the context of the overall risk profile of the organization. A banking organization's board of directors should maintain flexibility in the manner it seeks to address these matters.

30 A board's ability to rely in good faith on management as well as external experts in performing its oversight duties is deeply rooted in corporate law. *E.g.*, 8 Del. C. § 141(e); N.Y. Bus. Corp. § 717; VA Code Ann. § 13.1-690. The board of a banking organization should not be treated differently and in fact the principle of reasonable reliance is reflected in banking law as well. For example, New York banking law provides that directors may, when acting in good faith, rely upon financial statements with respect to which officers in charge of the books and records or the corporation's accountant represent to be accurately or fairly presented, as well as reports required to be submitted by officers or committees to the directors in the ordinary course of business. N.Y. Banking Law § 7015(1) (McKinney).

31 Indeed, a 2011 Georgia Department of Banking and Finance report recognizes that the cumulative impact of requiring board review or approval of procedures and business-level policies may result in an overload on the board that is counterproductive. This report suggests:

> "[A] thoughtfully crafted, overarching, comprehensive, high-level set of policies and limits may be reviewed and approved at the board level while more detailed management level policies or procedures designed to align to the overarching board policies flesh-out in-depth guidance to financial institution personnel for use in day-to-day activities. Management level policies and procedures serve as a complete roadmap of standards and expectations, which when effectively and faithfully implemented, promote achievement of the board's objectives as set forth in the strategic plan in addition to compliance with risk tolerance as articulated in board policies, limits, and the statement of risk appetite . . . ."

32 *E.g.,* OCC Heightened Standards, at 12 & 108; Federal Reserve System, Division of Banking Supervision and Regulation, Supplemental Policy Statement on the Internal Audit Function and Its Outsourcing, SR Letter 13-1 (January 23, 2013); Federal Reserve System and the OCC, Guidance on Model Risk Management, SR Letter 11-7 (April 4, 2011); OCC Director's Book, at 34.

board oversight, and certain of these rules establish requirements for boards.[33] Furthermore, under the Federal Reserve Board's capital plan rule,[34] the board or a committee of the board of a bank holding company with total consolidated assets of $100 billion or more must annually approve the organization's capital plan.

Enforcement actions by bank regulators also have imposed expanded responsibilities on the boards of particular banking organizations in specific contexts. For example, consent orders entered into between federal bank regulators and numerous banking organizations regarding their mortgage servicing operations require the banking organization's board to "ensure that . . . the Bank achieves and maintains effective mortgage servicing, foreclosure, and loss mitigation activities . . . , as well as associated risk management, compliance, quality control, audit, training, staffing, and related functions."[35]

A 2015 International Monetary Fund (the "IMF") report[36] on, and review of, the U.S. bank supervisory framework found that, in many cases, U.S. bank regulatory releases do not clearly distinguish between the role and mandates imposed on bank boards and that of senior management, leading to possible confusion between the roles. For example, the IMF report noted that there were numerous examples in both regulations and in actual supervision where the standard term "board and senior management" was used in situations where traditional corporate governance principles would dictate that only one of the two be responsible for the task in question and that the respective roles of the board and senior management are fundamentally different.[37]

BPI believes that, although the exact delineation between the roles of the board and management depends on a banking organization's particular situation, any significant involvement by the board in day-to-day operations is likely to reduce the board's ability to perform its general oversight role most effectively and impede its ability to act in its fiduciary oversight capacity. Moreover, BPI recognizes that the time commitment of directors will depend on the banking organization's circumstances but cautions that, absent extenuating, temporary circumstances, requiring abnormal time commitments of directors could impede an organization's ability to attract qualified candidates for board positions. In addition, a board should be highly reluctant to take on additional roles unless the board is convinced that it has the necessary expertise and time to perform those roles appropriately and that doing so will not result in confusion as to decision-making authority. Of course, certain unusual circumstances may require an enhanced level of oversight by the board (though this does not mean that the board is acting in the role of management). For example, when a banking organization is subject to an enforcement action by the regulators, directors of the organization may be obligated to oversee in a more active manner the timely implementation of corrective actions and assess the banking organization's compliance.[38] It is critical, however, that the specific

33 *See* Sections 4 and 9 for a further discussion of these rules; *see also* OCC Heightened Standards (requiring an increased responsibility for the boards of directors of certain large national banks).

34 12 C.F.R. § 225.8.

35 OCC, Consent Orders with National Bank Mortgage Servicers (April 13, 2011, amended February 28, 2013) (collectively, the "OCC Consent Orders"), Article III, Section 2; Federal Reserve Board, Consent Orders Related to Residential Mortgage Loan Servicing and Foreclosure Processing (April 13, 2011, amended February 28, 2013) (collectively, the "Federal Reserve Consent Orders") (requiring bank holding company boards to submit written plans to strengthen their oversight of enterprise-wide risk management, internal audit, and compliance programs concerning the residential mortgage loan servicing, loss mitigation, and foreclosure activities conducted through their subsidiary banks).

36 *See* United States Financial Sector Assessment Program, Detailed Assessment of Observance of the Basel Core Principles for Effective Banking Supervision (April 2015) IMF Country Report No. 15/89.

37 The phenomenon of blurring the distinction between the role of the board and that of management continues to be reflected in numerous recent regulatory releases. For example, the October 2019 proposed Interagency Guidance on Credit Risk Review appears to expect directors to have deep knowledge and be granularly involved in establishing allowances and provisions for credit losses. Other examples of supervisory releases that do not appropriately reflect the distinct roles of the board and management include OCC Fraud Risk Management Principles (OCC Bulletin 2019-37) (July 2019) (expecting senior management and the board to "measure, monitor, and understand" fraud losses); OCC Compliance Management Systems - Version 1.0 (June 2018) (discussing responsibilities of "board and senior management" and conflating their roles); CFPB Compliance Management Review: Examination Procedures (Board and Management Module) (August 2017) (referring to "board and management oversight" and providing that the board should adopt certain compliance programs instead of reviewing and approving, as appropriate, policies developed by management).

38 *See* OCC Director's Book, at 8-10.

requirements with respect to corrective actions in this context should not be permitted to distract the board from its broader oversight functions.[39]

The board also may, as a practical matter, become more active as an organization experiences financial difficulty. For instance, directors of an insolvent Delaware corporation may determine to participate more actively in key corporate decisions to the extent necessary to protect the interest of creditors. Furthermore, under Delaware law, the actions of directors reacting to a threatened change in control may be subject to enhanced judicial scrutiny, and the level of involvement of directors in decision making should be considered in that light.[40] Moreover, when directors are deciding to sell the company for cash, they are charged with the duty to seek the best price for the shareholders.[41] In these circumstances, the board will often determine to be more closely involved in making key decisions and, in certain circumstances, to consider relying on its own legal and financial advisors in addition to management.

The foregoing situations may lead to enhanced involvement by the board on a temporary basis, but the board is nevertheless still acting in an oversight role. There may be truly exceptional circumstances where the board's role may go beyond oversight. For example, in the event of a sudden departure or incapacitation of one or more senior executives, it may be necessary and appropriate for a director selected by the board to assume a lead management role on a temporary basis pending the appointment of succeeding senior executives. This level of involvement, however, is not a normal function of the board.

Finally, the ability of a board of directors to delegate functions to a board committee is a fundamental concept of corporate law and one recognized by the U.S. federal banking authorities.[42] The Federal Reserve Board clearly recognized this foundational principle in its Proposed Guidance on Supervisory Expectations for Boards of Directors, which noted, at the very beginning of the proposed guidance, that references to "'[b]oard or 'board of directors' also refers to committees of the board of directors, as appropriate."[43] Board committees, in turn, are accountable to and routinely report to the whole board. In practice—under principles of corporate governance and subject to other applicable law (*e.g.*, banking regulations)—boards routinely delegate to a committee the authority to address board responsibilities that are properly within the scope of the committee in order to efficiently allocate responsibility among directors.[44]

BPI recognizes that the attention of the full board may be required or warranted in certain cases. For example, a board may determine that certain matters may be appropriate for full board oversight, more in-depth consideration or examination (*e.g.*, certain matters that relate to strategy and fundamental issues relating to

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39 This point was addressed by former Federal Reserve Governor Daniel Tarullo in a June 9, 2014 speech, in which he notes that it has "perhaps become a little too reflexive a reaction on the part of regulators to jump from the observation that a regulation is important to the conclusion that the board must certify compliance through its own processes," and that regulators "should probably be somewhat more selective in creating the regulatory checklist for board compliance and regular consideration." Governor Tarullo noted as an example the Federal Reserve's supervisory guidance regarding board review of "Matters Requiring Attention" ("MRAs"), noting that "[t]here are some MRAs that clearly should come to the board's attention, but the failure to discriminate among them is almost surely distracting from strategic and risk-related analyses and oversight by boards." Speech by Governor Daniel K. Tarullo at the Association of American Law Schools 2014 Midyear Meeting, Washington, D.C. (June 9, 2014); *see also* Speech by Federal Reserve Governor (now Chairman) Jerome H. Powell at the Large Bank Directors Conference, Chicago, Illinois (August 30, 2017) ("Powell Speech") (noting that many corrective actions "are at a level of granularity that is more appropriate for management to remediate, with board oversight").

40 *See Unocal Corp.* v. *Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985).

41 *See Revlon, Inc.* v. *MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986).

42 *See* Delaware General Corporation Law § 141(c); Model Business Corporation Act § 8.25(d); *see also* Original Prudential Standards, at 17,248 (discussing the delegation of certain risk management oversight responsibilities to the risk committee of the board); 12 C.F.R. § 225.8(e)(iii)(C) (requiring that the capital plan of a bank holding company subject to the capital plan rule be approved at least annually by the organization's "board of directors or a designated committee thereof").

43 Board Effectiveness Proposal, at 37,224 n.9.

44 Committee charters—as well as regulatory standards that address committee-level responsibilities—should define the respective roles of committees so as to avoid the duplication of effort.

enterprise risk management, and/ or formal approval by the full board). However, even in these cases, delegation of the initial review and analysis to an appropriate committee that can devote particularized attention to the issue (*e.g.*, in such technical areas as liquidity risk tolerances) may be an efficient allocation of responsibility. In view of the foregoing, BPI believes that it is reasonable for a banking organization to interpret the generic uses of the term "board" in agency regulations and in these Guiding Principles—unless the meaning is otherwise clear—to be either the full board or a board committee. Similarly, references to the "board" in these Guiding Principles should be interpreted as referring to either the full board or a committee of the board, unless the context suggests otherwise.[45]

SECTION 2. INDEPENDENCE OF BOARD MEMBERS

Principles:

a) **A substantial majority of the directors of the top-tier entity within a banking organization should be independent, and only a relatively small number of directors should be members of management.**
b) **The board of the holding company should receive updates, as appropriate for its particular circumstances, regarding the composition of the boards of its subsidiary banks and other material subsidiaries. Directors who serve on both holding company and subsidiary bank boards should remain cognizant of the role in which they are acting at any particular time, and their responsibilities to the entity of which they are acting as a board member.**

Commentary:

"Independence" for these purposes means that a director of a banking organization does not have other direct or indirect relationships with the organization that could impede the director's exercise of independent judgment in executing the duties of a director. Directors who are executives of the organization (*i.e.*, "management" directors) clearly are not independent, and, as discussed below, there should in practice be a limit on the number of management directors separate and apart from the limit on the number of total non-independent directors.

In addition to independence requirements and recommendations, discussed below, that apply generally to public companies, federal bank regulators encourage banks to establish and maintain the independence of the board by including an appropriate number of independent directors on their boards. For instance, the OCC Heightened Standards require certain large national banks to have at least two "independent" directors on their boards.[46] In the OCC Director's Book, the OCC stresses the importance of independent directors on national bank boards who can provide "perspective and objectivity" in overseeing bank operations and evaluating management recommendations.[47] According to the OCC Director's Book, a director generally can be deemed independent if he or she is "free of any family relationships or any material business or professional relationships (other than stock ownership and directorship itself) with the bank or its management."[48]

Regulators and commentators disagree as to whether significant stock ownership, or affiliation with a significant stockholder, should be seen as impairing a director's independence. On the one hand, the New York Stock Exchange (the "NYSE") and NASDAQ listing standards expressly state that stock ownership does not, by itself,

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45 *See* the Board Effectiveness Proposal, at 37,224, n.9.

46 A director is "independent" for these purposes if the director (i) is not an officer or employee, and has not been an officer or employee within the last three years, of the parent company or the bank, (ii) is not a member of the immediate family of a person who is, or has been within the last three years, an executive officer of the parent company or the bank and (iii) qualifies as an independent director under the listing standards of a national securities exchange, as demonstrated to the satisfaction of the OCC. *See* OCC Heightened Standards, at 76 & 127.

47 OCC Director's Book, at 15; OCC Handbook, at 7.

48 OCC Director's Book, at 15; *see also* FDIC Pocket Guide (stating that banking institutions should establish and maintain the independence of the board); FDIC Supervisory Insights, at 7 ("[f]irst and foremost, the board and individual directors should establish and maintain the board's independence"); Basel Principles, at 13 ("the board should be comprised of a sufficient number of independent directors.").

impair independence, because the key consideration is independence *from management*.[49] Similarly, the OCC carves out "stock ownership" from the factors compelling a non-independence determination.[50] In contrast, the Federal Reserve Board notes that it is important for the board of a bank to include "directors with no ownership or family-ownership interest in the bank and who are not employed by the bank."[51] Similarly, the FDIC considers stock ownership of 10% or more of any outstanding class of voting securities of a bank to be a factor that may impair director independence for purposes of the board's audit committee.[52] BPI believes that ownership of a significant stock position, or affiliation with such an owner, should not be a bar to independence of a director of a banking organization. In most cases, the interests of a shareholder and the public interests that a director is meant to protect—including the safety and soundness of the organization—will be aligned. In those circumstances where a particular shareholder may have divergent interests from the other shareholders or the organization (for example, if he or she owns a controlling interest in the organization), the other independent directors should assess whether a director who is, or is affiliated with, the shareholder can continue to exercise independent judgment. If a director cannot exercise independent judgment on a particular matter, he or she should be recused from voting on, and, if appropriate, recused from the deliberations on, the matter.

There is no "one-size-fits-all" standard for a banking organization board's composition, including the number of independent directors on the board. Various approaches may be appropriate for a given banking organization in light of its particular circumstances, and any given approach that is appropriate for one organization may not be appropriate for another. Similarly, within an organization, an approach that is appropriate for one legal entity may not be appropriate for another legal entity. For example, although the same basic independence principles apply at both the top-tier entity and subsidiary bank levels, there will ordinarily be requirements, such as stock exchange listing standards and the OCC Heightened Standards, that apply at only one level.

Independence of Holding Company Board

Bank holding companies with securities listed on national securities exchanges are subject to the director independence rules of those exchanges.[53] These rules require a company with securities listed on these exchanges to have a majority of independent directors on its board.[54] According to the NYSE, the independence rule is designed to "increase the quality of board oversight and lessen the possibility of damaging conflicts of interest."[55]

BPI believes that, as a matter of good corporate governance, a *substantial* majority (*e.*, at least two-thirds) of directors of the top-tier entity within a banking organization should be independent, with independence to be defined pursuant to applicable stock exchange standards and an independence policy adopted by the board (as described further below). Although this standard is in excess of any securities exchange or other explicit regulatory requirements, BPI believes that a board with only a slight majority of independent directors risks being dominated by the non-independent directors, particularly if they are members of management and closer to the day-to-day business of the organization.[56]

For similar reasons, BPI believes that only a relatively small number of directors should be members of management; specifically, management directors should not comprise more than 25% of the board. Although a

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49 *See* NYSE, Listed Company Manual ("NYSE Manual"), Section 303A.02(a) (commentary); NASDAQ, Listing Rules ("NASDAQ Rules"), IM-5605.

50 OCC Director's Book, at 15.

51 *See* Commercial Bank Manual, Section 5000.1, at 1.

52 *See* 12 C.F.R. Pt. 363, App. A.

53 To the extent the top-tier public company with securities listed on a national securities exchange is a bank, these rules also apply to the bank.

54 NYSE Manual, Section 303A.01; NASDAQ Rules, Section 5605(b)(1).

55 NYSE Manual, Section 303A.01.

56 *See*, *e.g.*, U.S. General Accounting Office, Report to Congressional Requesters, GAO-04-75, Securities Markets: Opportunities Exist to Enhance Investor Confidence and Improve Listing Program Oversight (2004) ("GAO Report"), at 73-74.

management presence on the board provides an indispensable connection between the board and management and the board may determine to have more than one management director in order to have consistent access to a variety of management views, having more than 25% management members on a holding company board may tend to restrict the independence of the board overall. As David Walker noted in his review of U.K. banking organizations, "the stronger the executive presence in any board . . . the greater the risk that overall board decisions come to be unduly influenced by what has been described as 'executive groupthink.'"[57] In special circumstances, the board of a particular organization may decide that, for reasons specific to the organization, this limitation on management directors is not appropriate.

The NYSE provides that a director is not "independent" unless the board of a listed company makes an affirmative determination that there is no material relationship (including commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships, among others) between the director (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company) and the listed company.[58]

The NYSE advises the board to consider "all relevant facts and circumstances" in reaching its determination as to a director's independence, including the director's personal relationships with the listed company as well as the relationships, if any, between the listed company and "persons or organizations with which the director has an affiliation."[59] BPI believes that banking organizations should adopt a formal policy, setting forth categories of relationships that generally will be deemed material or immaterial for these purposes, in order to assist the board in making independence determinations in a consistent and reasoned manner.

Although the NYSE grants discretion to the board in reaching independence determinations based on the director's relationships with the company, it also sets certain minimum standards that must be met before a director can be deemed independent. The NYSE has identified the following types of relationships as presumptively inconsistent with a director's independence:

- the director is, or was, an employee of the listed company, or an immediate family member is, or was, an executive officer, of the listed company, within the last three years;
- the director or an immediate family member received more than $120,000 per year in direct compensation from the listed company within the last three years, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service);
- the director currently is affiliated with or employed by a firm that is the internal or external auditor of the listed company, (B) the director or an immediate family member was affiliated with or employed by such firm within the last three years and personally worked on the listed company's audit within that time, (C) an immediate family member currently is affiliated with such firm or (D) an immediate family member currently is employed by such firm and personally works on the listed company's audit;
- the director or an immediate family member is, or was employed as, an executive officer of another company where any of the listed company's present executives serves or served on that company's compensation committee within the last three years; or
- the director is a current employee, or an immediate family member is a current executive officer, of another company that, within the last three years, has made payments to, or received payments from, the listed company for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of $1 million and 2% of such other company's consolidated gross revenues.[60]

For these purposes, "immediate family member" includes "a person's spouse, parents, children, siblings, mothers

[57] Walker Review, at 42; *see also* N.Y. Banking Law § 7001 (2014) (requiring that no more than one-third of the directors of a New York state chartered bank be active officers or employees of the bank).

[58] NYSE Manual, Section 303A.02(a).

[59] *Id.*

[60] NYSE Manual, Section 303A.02(b).

and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and anyone (other than domestic employees) who shares such person's home."[61] The term "executive officer" is defined by reference to the definition in Securities Exchange Act of 1934[62] (the "Exchange Act") Rule 16a-1(f), as follows:

> [A]n issuer's president, principal financial officer, principal accounting officer (or, if there is no such accounting officer, the controller), any vice president of the issuer in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy making function, or any other person who performs similar policy making functions for the issuer. Officers of the issuer's parent(s) or subsidiaries shall be deemed officers of the issuer if they perform such policy making functions for the issuer.[63]

This definition generally is consistent with that used for proxy disclosure purposes[64] and under Regulation O, 12 C.F.R. § 215.2(e). The NASDAQ has adopted similar bright-line tests for determining director independence. Specifically, the following persons are not considered independent[65]:

i. a director who is, or at any time during the past three years was, employed by the company;

ii. a director who accepted or who has a family member[66] who accepted any compensation from the company in excess of $120,000 during any period of twelve consecutive months within the last three years, other than compensation for director and committee service, certain retirement plan benefits or non-discretionary compensation;

iii. a director who is a family member of an individual who is, or at any time during the past three years was, employed by the company as an executive officer[67];

iv. a director who is (or has a family member who is) a partner in, or a controlling shareholder or an executive officer of, any organization to which the company made, or from which the company received, payments for property or services within the past three years that exceed the greater of 5% of the recipient's consolidated gross revenues for that year or $200,000 (except payments solely from investments in securities and non-discretionary charitable contribution matching payments);

v. a director who is, or has a family member who is, employed as an executive officer of another entity where at any time within the past three years any of the executive officers of the company serve on the compensation committee of such other entity; or

vi. a director who is, or has a Family Member who is, a current partner of the Company's outside auditor, or was a partner or employee of the Company's outside auditor who worked on the Company's audit at any time within the past three years.

Federal bank regulators, the SEC and the national securities exchanges also have adopted regulations requiring the

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61 *Id*.

62 15 U.S.C. § 78a *et seq*.

63 Exchange Act Rule 16a-1(f); *see also* NYSE Manual, Section 303A.02.

64 *See* Exchange Act Rule 3b-7.

65 NASDAQ Rules, Section 5605(a)(2).

66 Under the NASDAQ rules, "family member" means a person's spouse, parents, children and siblings, whether by blood, marriage or adoption or anyone residing in such person's home. *Id*.

67 Similar to the NYSE rules, "executive officer" is defined by referring to the SEC Rule 16a-1(f). NASDAQ Rules, Section 5605(a)(1).

independence of directors serving on the board's audit, risk, compensation and nominating/corporate governance committees.[68] These independence requirements are discussed in detail in Section 5 through Section 9.

Finally, the Depository Institution Management Interlocks Act[69] prohibits director and officer interlocks among depository organizations, with certain exceptions. Directors at both the holding company level and the bank level should not have other positions that could cause them to be a "management official" of another depository organization, absent an applicable exception. Similarly, banking organizations should monitor the application of antitrust provisions that may prohibit individuals from serving as directors or officers of two competing corporations.[70]

Independence and Composition of Subsidiary Bank Board

Federal bank regulators have not adopted specific independence requirements for boards of banks,[71] although, as discussed above, the regulators generally have cited the importance of independent directors, and the OCC Heightened Standards required certain large national banks to have at least two independent directors on their boards.[72] BPI believes that, with regard to the composition of the boards of subsidiary banks, banking organizations should have significant flexibility. Decisions on composition may turn on a variety of factors, and a holding company with multiple bank subsidiaries may decide that different models of board composition are appropriate for the boards of those subsidiary banks. Some appropriate models for the composition of subsidiary bank boards include the following:

i. *The board of the subsidiary bank has little or no overlap with the holding company board, and includes some independent directors*. This may be more appropriate where the bank is one of a number of businesses within the holding company structure. In this case, separate oversight at the bank level, including some independent directors, can help serve as an additional check on business or strategy decisions relating to the operation of the bank that may make sense for the holding company as a whole, but risk undermining the safety and soundness of the bank as an entity. In regard to any non-independent directors on the subsidiary bank's board, the holding company board may reasonably conclude that the subsidiary board's effectiveness will be enhanced if its composition includes management directors. Management directors are often in a strong position to oversee the bank, since they possess knowledge and expertise as to the bank's operations.
ii. *The boards of the holding company and the subsidiary bank largely or completely overlap*. This may be especially appropriate if the lead bank comprises the predominant portion of the holding company's operations, due to the high degree of alignment between the interests of the bank and the interests of the holding company. As a general matter, there is no reason why an independent director serving on the holding company board would not also be viewed as independent when serving on the bank board as

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68 *See* 12 C.F.R. § 363.5(a)(2); Federal Reserve Enhanced Standards, §§ 252.22(d) & 252.33(a)(4); Exchange Act Rule 10A-3(b)(3)(ii); NYSE Manual, Sections 303A.04, 303A.05 & 303A.06; NASDAQ Rules, Sections 5605(c)(2)(A), 5605(d)(2)(A) and 5605(e)(1)(B).

69 As implemented by Regulation L, 12 C.F.R. § 212.

70 *See* Clayton Antitrust Act of 1914, Pub. L. No. 63-212, 38 Stat. 730 § 8.

71 However, as noted in Section 6, the FDIC regulations do require that each insured depository institution with total assets of $1 billion or more have an independent audit committee. 12 C.F.R. 363.5(a)(1). The depository institution may choose to use the definition of audit committee member independence set forth in the listing standards of a national securities. Guidelines to 12 C.F.R. 363.5., 28(d). As discussed further in Section 5, the insured depositary institutions may satisfy this requirement through the audit committee at the holding company level if the insured depositary institutions of the holding company have consolidated total assets comprising 75% or more of the holding company's consolidated total assets, subject to certain other conditions.

72 *See* OCC Heightened Standards, at 76 & 127. The OCC further noted that, if the bank's independent directors are also members of the parent company's board, the OCC expects that such directors would consider the safety and soundness of the bank in decisions made by the parent company that impact the bank's risk profile. *Id*. at 76. In addition, as discussed in Sections 5 and 6 below, federal bank regulations require certain banks to have audit committees that satisfy specified independence criteria. *See* 12 C.F.R. § 363.5(a)(2).

well. Of course, directors who serve on both holding company and subsidiary bank boards should remain cognizant of the role in which they are acting at any particular time, and their responsibilities to the entity of which they are acting as a board member.[73] In general, in business as usual and other circumstances, the "source of strength" requirements of holding companies and74 the "safety and soundness" considerations for banks create alignment of interests between the holding company board and the bank board and mitigate any potential conflict of interests.

iii. *The board of the subsidiary bank emphasizes representation of local constituencies*. This model may be particularly useful for multi-bank holding companies spread over a large geographic area. In such cases, the holding company board may reasonably determine that it will oversee the entity-wide risk oversight function, while the local bank board will be in a better position to provide input helpful to fostering optimal service to the local community and, in overseeing risk management at the bank, to identify any concerns with the application of the organization's risk oversight practices to the particular bank.

Using these or other models, banking organizations should review the composition of boards of subsidiary banks based on the particular circumstances and needs of those banks and the organization as a whole. This approach also is consistent with the rules of the national securities exchanges which generally exempt "controlled companies" (*i.e.*, wholly or majority owned subsidiaries) from their independence rules.[75] BPI believes that the top-tier entity of a banking organization should have considerable flexibility regarding the structure of the boards of its subsidiary banks, and processes for evaluating and determining the appropriate structure. Depending on the circumstances of the banking organization, it may be desirable for both the top-tier entity board, as the governing body of the controlling shareholder of the subsidiary bank, and the subsidiary bank board to review periodically the subsidiary bank's board structure. The appropriate nature and frequency of these reviews will depend on each organization's particular circumstances. Relevant factors could include, among others: the degree of overlap between the holding company and subsidiary bank boards, the extent to which the organization's overall operations are conducted in the bank, the particular businesses and activities of the bank, and the number of subsidiary banks within the organization.

SECTION 3. COMPOSITION OF THE BOARD

Principles:

a) **The board of the top-tier entity within the banking organization should have the flexibility to determine its own appropriate composition, taking into consideration the size of the board, the diversity, expertise, and tenure of the board members, and the capacity of board members to commit to serving on the board of a banking organization. Within any state or federal statutory requirements, the top-tier entity should have the flexibility to determine the appropriate composition of the boards of its subsidiary banks.**

b) **The board should be small enough to facilitate effective functioning but large enough to allow members to contribute sufficient knowledge, experience and diversity to the board's oversight role and its committees.**

c) **Decisions on board composition will depend on a banking organization's particular circumstances, needs and objectives, including:**

    i. **the nature, scope and complexity of its business, as well as its strategic objectives and/or plans;**

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73 The directors of the subsidiary are obligated to manage the affairs of the subsidiary consistent with their regulatory obligations, their duties to the subsidiary as a legal entity and their duties to the parent company as a shareholder. These duties also apply in a dual-directorship context.

74 *See* Federal Reserve, Bank Holding Company Supervision Manual (2013): "The term 'source of strength' means the ability of a company that directly or indirectly owns or controls an insured depository institution to provide financial assistance to such insured depository institution in the event of financial stress to the insured depository institution."; 12 U.S.C. § 1831o-1.

75 *See* NYSE Manual, Section 303A.00 and NASDAQ Rules, Section 5615(c).

ii. **the need to meet applicable independence and other regulatory standards;**

iii. **the need to provide a range of skills commensurate with the board's oversight role and a diversity of views that can provide necessary insight into the banking organization's multiple constituencies; and**

iv. **the ability to staff board committees with a sufficient number of members that meet relevant independence and qualification criteria and the needs and expertise of the committees.**

Commentary:

There is no "one-size-fits-all" approach to determining board composition and there can be no general prescription regarding optimal board composition for all banking organizations. Each banking organization has to evaluate its own circumstances and needs in determining the appropriate board composition to meet its strategic objectives. The composition of the board of a bank holding company must, of course, comply with the general corporate laws of the state in which that company is incorporated, though these are typically not very prescriptive. Delaware law, for example, requires only a minimum of one director.[76] Holding companies with stock listed on an exchange should have a board size that enables compliance with applicable stock exchange rules, including having enough independent directors to maintain the required committees. Board composition at the subsidiary bank level is the subject of more specific regulation and guidance, though significant flexibility still exists, as discussed further below.

Maintaining an appropriate board composition is essential to the board's ability to make sound, well-informed decisions and effectively discharge its oversight responsibilities. Directors serving on the board of a banking organization should, collectively, possess diverse skills and expertise and have diverse experience and perspectives so that they can support a banking organization's development and pursuit of its strategic objectives and/or plans. Director tenure and achieving the right mix of organization-specific experience and new insight is another important consideration for composition. In recent years, for example, based on specific needs and circumstances, some financial services firms have expanded the number of directors with expertise in technology and cybersecurity to help oversee these areas in light of the growing importance and risks they pose.[77] The right mix is not necessarily static and may change as a result of a variety of factors, including changes in the organization's business, plans and strategies.

Diversity on the board has increasingly become a focus among banking organizations, regulators and other stakeholders.[78] Many banking organizations have found that deliberate efforts to expand the diversity of board members have yielded more vibrant, engaged and forward-thinking boards of directors, which has allowed the boards to better support the development and pursuit of these organizations' strategies and objectives.[79] As a banking organization considers the appropriate board composition, it should also take into account the benefits of diversity in all senses of the word, including demographic diversity, diversity of backgrounds, viewpoints and perspectives, and diversity in areas of skills, expertise and professional experience.[80] Because there is no single

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[76] 8 Del. C. § 141(b).

[77] Tucker Bailey, Soumya Banerjee, Christopher Feeney & Heather Hogsett, Bank Policy Institute, Cyberscurity: Emerging Challenges and Solutions for the Boards of Financial Services Companies (Oct., 2020) ("Cybersecurity Report"), at 5.

[78] For example, the Federal Reserve's Proposed Guidance on Supervisory Expectation for Boards of Directors notes "[a]n effective board … composed of directors with a diversity of skills, knowledge, experience, and perspectives" as one of the attributes of an effective board. Board Effectiveness Proposal, at 37,226. The OCC similarly recognizes that "[t]he ideal board is well diversified and composed of individuals with a mix of knowledge and expertise in line with the bank's size, strategy, risk profile, and complexity." OCC Director's Book, at 15. The U.K. Governance Code states that director "appointments and succession plans should be based on merit and objective criteria, and, within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths." U.K. Governance Code, at 8.

[79] As discussed further in Section 4, a nominating/corporate governance committee may determine that having a number of directors with experience outside the financial industry could provide helpful additional perspectives to the board.

[80] *See* OCC Director's Book, at 17 ("Diversity among directors is another important aspect of an effective board. The board should actively seek a diverse pool of candidates, including women and minorities, as well as candidates with diverse knowledge of risk management and internal controls."); OECD Principles, at 53 ("In order to avoid groupthink and bring a

metric for diversity, each banking organization must assess how to collect, monitor, use and disclose board-related diversity information in light of its own circumstances.

The ideal number of directors to serve on a board is the subject of considerable debate. Literature on corporate governance contains various qualitative and quantitative guidance, although there is no agreement on any specific "ideal" size. The Basel Committee, for instance, broadly recommends that a board "structure itself in terms of leadership, size and the use of committees so as to effectively carry out its oversight role and other responsibilities."[81] The ABA notes the substantial variation in the size of boards of public companies, but states that "[e]xcept perhaps for the very largest and most complex corporations, smaller boards (seven to eleven members) generally function more effectively than larger ones."[82] The ABA's position is based on the view that smaller boards can allow directors more opportunities to participate actively in board deliberation, whereas larger boards can limit such participation. Large boards use their authority to delegate significant activities to committees of the board as a way of addressing this participation issue. Delegation of specific duties to committees also allows a subset of the board to delve more deeply into particular matters on behalf of the entire board.[83]

Moreover, there is recognition that banking organizations may require somewhat larger boards than other companies. The ABA notes that financial services corporations and corporations operating complex businesses typically have larger boards (as many as 15 or more members).[84] These commentaries support the general principle that decisions on board size should be commensurate with the nature and complexity of a banking organization's business. Larger boards can also help support director diversity, in all its forms.

It is the view of BPI that the appropriate size of the board of the top-tier entity within a U.S. banking organization depends on what would be most efficient in light of that organization's circumstances and for that organization's oversight objectives. Factors that should inform appropriate board size include, among others that may be applicable depending on a banking organization's particular circumstances, the committee structure of the board, the board's workload, the time commitment of directors, the desired expertise among board members, and the need to balance having board members who can offer a diversity of views, perspectives and experiences, with maintaining an environment that can promote and preserve director engagement at meetings. For example, one circumstance that could result in a relatively large number of directors would be a merger, where substantial representation from both constituent organizations could assist in the oversight of the integration process.

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diversity of thought to board discussions, boards should also consider if they collectively possess the right mix of background and competences."); *see also* The Harvard Law School Forum on Corporate Governance, U.S. Board Diversity Trends in 2019 (June 18, 2019), available at https://corpgov.law.harvard.edu/2019/06/18/u-s-board-diversity-trends-in-2019/ (showing rapidly increasing proportion of female and minority directors on public company boards); Deloitte LLP, The Inclusion Imperative for Boards (Apr. 2, 2019), available at https://www2.deloitte.com/us/en/insights/topics/value-of-diversity-and-inclusion/redefining-board-responsibilities-to-support-organizational-inclusion.html (citing studies and interviews to explain why board diversity benefits the companies).

81 *See* Basel Principles, at 15.

82 ABA Guidebook, at 42; *see also* G30 Report, at 34 ("[T]he bigger a board gets, the more difficult it is to manage. Meetings can get out of control or become so structured that it is difficult to have effective debate. Ultimately, the right size of the board depends on those seated around the table and how they interact, but on balance, smaller boards that require a greater time commitment from their members are better than larger boards that require a more modest commitment.").

83 *See id.* at 42-43; *see also* OCC Director's Book, at 35 ("Delegation of work to a committee can enhance board effectiveness by enabling the board, through its committees, to cover a wider range of issues with greater depth of analysis."); Walker Review, at 41 ("Discussion and consultation in the course of the present [r]eview points to a widely held view that the overall effectiveness of the board, outside a quite narrow range, tends to vary inversely with its size. That view would probably tend to converge around an 'ideal' size of 10-12 members, not least on the basis that a larger board is less manageable, however talented the chairman, and that larger size inevitably inhibits the ability of individual directors to contribute.") (citation omitted); John L. Colley, Jr. *et al.*, Corporate Governance, at 37 (2003) ("Colley–Governance"), at 37 ("There is a semblance of a consensus that some number between 12 and 15 is most effective for many organizations. Many people feel that fewer than 12 directors can allow a small group to control the board, whereas more than 15 directors renders the board unwieldy.").

84 ABA Guidebook, at 42; *see also* Walker Review, at 41 (citing research by Deloitte showing U.K.-listed banks as having much bigger boards, and that the median bank board size has increased from 15 members in 2002/03 to 16 members in 2007/08, whereas the average board size across the whole of the FTSE 100 decreased from 11 to 10 members over the same period).

Whether the board size should be increased or decreased should be a subject of discussion in the board's self-evaluation process discussed in Section 7.

At the subsidiary bank level, federal banking laws provide considerable flexibility to set board size within a numerical range. For example, in prescribing the required number of board members for national banks, the National Bank Act sets a range of not less than 5 nor more than 25 members, but the OCC's regulations authorize a national bank to request to expand its board even above the 25 member limit.[85] State member banks also are subject to a 5 to 25 member range for board size.[86] Different states also may have requirements on board size at the bank level. For example, the New York State Banking Law generally requires New York state chartered banks to have no less than 5 nor more than 15 board members, but allows larger banks to choose from a wider range for board size.[87]

BPI believes that the top-tier entity of a banking organization should have considerable flexibility regarding the size of the boards of its subsidiary banks, depending on the complexity of the subsidiary banks, their roles within the larger organization and the extent to which the holding company board performs certain of the oversight functions with respect to the banks.[88]

SECTION 4. CORE BOARD FUNCTIONS

Principles:

a) **The oversight duties and responsibilities of the board of a banking organization should focus on the following five core functions:**
   i. **Function 1: Reviewing and approving strategic objectives and/or plans;**
   ii. **Function 2: Monitoring financial performance and condition;**
   iii. **Function 3: Overseeing talent management, including for the CEO and other senior executives;**
   iv. **Function 4: Overseeing the risk management and internal control frameworks, including top-tier policies and plans in fundamental areas; and**
   v. **Function 5: Reinforcing, demonstrating and communicating the "tone at the top" for the values and culture of the organization and overseeing enterprise-wide approaches/programs intended to promote organizational values, culture and reputation.**

b) **The board should perform all other oversight duties and responsibilities required by statute, regulation or regulatory orders (including oversight of executive compensation programs, liquidity and stress testing) or that the board deems appropriate from time to time.**

c) **For subsidiary banks, many of these responsibilities may be discharged by the board of the top-tier entity within the banking organization, depending on the structure of the organization and the judgment of the top-tier board and the subsidiary bank board as to the appropriate allocation of responsibilities (subject in any case to specific regulatory requirements at the subsidiary bank level).**

Commentary:

The focus of large U.S. banking organization boards on the core functions of approving strategic objectives, oversight (including oversight of risk management and culture), and senior executive talent management (including the retention of the CEO) are central to promotion of sound governance, high-level risk management and safety and soundness. Core board functions set out in this section should be understood within the context of the following concepts:

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85 12 U.S.C. § 71a; 12 C.F.R. § 7.2024(c); *see also* OCC Director's Book, at 87.

86 *See* 12 U.S.C. § 71a; Commercial Bank Manual, Section 5000.1, at 1.

87 N.Y. Banking Law § 7002 (McKinney 2019).

88 *See* Section 2 for further discussion of the composition of subsidiary boards.

- There are a number of industry-specific safety and soundness considerations and compliance obligations unique to the banking industry; however, the fundamental oversight role of the bank board and its core board functions is not industry-specific. Bank board practices and responsibilities to carry out the core board functions reflect these bank-specific considerations (e.g., the unique nature of a bank's balance sheet, highly regulated environment and technical compliance regime, detailed safety and soundness requirements including the incorporation of appropriately stressful conditions and events into planning for large institutions, etc.) several of which are described below.

- The five core functions are a way to organize several of the board's fundamental and critical responsibilities from a prudential perspective at their highest level.[89] Though principally focused on holding company board functions, in many respects, the core board functions also apply at the subsidiary bank level. More generally, the performance of core board functions at the various levels of the organization may be coordinated at the top-tier parent holding company level (taking into account the independent legal and governance responsibilities of subsidiary boards). Each function does not need to be performed by the board or a board committee of each legal entity within the organization.

- Board focus on matters and issues elevates their importance and underscores their prioritization for the organization. Accordingly, the core board functions should be managed and carried out so as to facilitate the ability of the board to devote its time and efforts to the highest-level organizational priorities. Because organizational priorities change on an ongoing basis, the degree of a board's time and attention devoted to any given matter is not static, and the appropriate degree of board involvement and engagement varies over time. For example, an issue would ordinarily be more of a board focus when it is new or evolving.

- Though certain aspects of the role of the board may evolve over time, the fundamental, or "core," functions remain constant absent unusual circumstances.[90]

- The core functions are not a checklist of required actions, and the core functions and the examples in this commentary are not intended to be prescriptive. The core functions are by their very nature ongoing, dynamic and forward-looking. Moreover, there is no single approach to sound corporate governance—the processes and practices adopted by each organization should be appropriate for the organization's strategic objectives, business model and culture and should be oriented to adapt based on lessons learned.

- The precise structures through which a particular board determines to carry out core functions will appropriately differ. For example, boards may opt to use board committees, such as the audit or risk committees, in different ways or for different purposes, although in all cases these committees are accountable to, and routinely report to, the full board.

- The issues that the board will need to confront may change, but, as noted above, the board's fundamental role and core functions generally do not. Therefore, in exercising core responsibilities, effective boards recognize the need to adapt to new circumstances. For example, the core function of the board to oversee the risk management and internal control frameworks (Core Board Function 4) must be able to address evolving risks in a dynamic environment (*e.g.*, with respect to cybersecurity in recent years). Care should be taken to ensure that adequate time on the board agenda is reserved for "deep

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[89] Supervision of bank board governance from a prudential perspective generally focuses on sound governance, oversight of internal controls and risk management, and compliance with applicable legal requirements. Though critically important, these Guiding Principles do not describe in any detail corporate matters performed in accordance with company policy, practices or charters that in the normal exercise of fiduciary duties would be presented to the board even if not specifically required by statute or regulation.

[90] As noted in Section 1, some unusual circumstances may require an enhanced level of oversight by the board (though this does not mean that the board is acting in the role of management). For example, when a banking organization is subject to an enforcement action, directors may be obligated to oversee in a more active manner the timely implementation of corrective actions and assess the banking organization's compliance.

dives" as new priority issues may arise and warrant the board's focus. These may differ by organization.

- The core functions overlap to a certain degree, work together and reinforce one another. For example, there should be linkages among strategic objectives, talent management for senior executives, oversight of risk management and risk appetite—including, for example, well-conceived processes for board review of major firm decisions integrating strategy, risk-appetite setting, reputational risk and capital planning considerations.

- The core functions are intended to be conceptual in nature and a particular banking organization may be subject to specific U.S. legal standards or supervisory expectations beyond these core functions.

- Consistent with the board's oversight role, which is distinct from the role of management, where matters fall within the purview of the board, the board should "oversee," "promote" and "approve" the matters, rather than "establish" or "set" them. Similarly, supervisory expectations that provide for the board to "ensure" that outcomes or actions are achieved are inconsistent with these principles-based core functions and are incompatible with the role of the board.

In this section, as elsewhere, these Guiding Principles address the role of the board generally, both at the holding company level and at the bank level. As discussed in Section 2 with respect to director independence, the interaction between the holding company board and the bank board will vary significantly from organization to organization, and thus the specific level at which oversight of a particular area occurs also will vary. The responsibilities of the holding company board relate to the banking organization as a whole, and thus cover the operations of the subsidiary banks and other subsidiaries. Although the OCC confirms that "the strategic objectives, corporate values, and corporate governance principles of the affiliated bank should align with the holding company," the OCC emphasizes that "the primary duty of a subsidiary bank's board is to ensure the bank operates in a safe and sound manner."[91] In addition, the OCC Heightened Standards maintain that the subsidiary bank's risk governance framework should "ensure that . . . the safety and soundness of the [bank] is not jeopardized by decisions made by the parent company's board of directors and management."[92]

BPI believes that, subject to specific regulatory requirements at the bank level, a banking organization should generally have flexibility in coordinating oversight responsibilities between the bank board and the holding company board. For example, it may be desirable for the holding company board to focus on higher level issues of strategy and policy applicable across the organization, with compliance-related oversight pertinent to the bank principally to be overseen by the bank board. However, any allocation of responsibilities to the holding company board must be consistent with the discharge by the subsidiary bank board of its critical responsibility to protect the safety and soundness of the bank. The commentary to the OCC Heightened Standards suggests that, for covered banking institutions, this includes taking steps as appropriate so that assets and businesses are not placed on the books of, or attributed to, the bank without proper due diligence.[93]

In overseeing management performance, and more generally, carrying out effective oversight of bank operations, risk management and compliance, the board should bring an appropriate level of engagement to the performance of its duties. For example, if, in the course of its oversight of the company, the board becomes aware of material deficiencies or opportunities for enhancements in management's operation of the business, in reporting or compliance systems, in risk management or otherwise, then the board should discuss with management an appropriate plan of action, which may include ongoing monitoring of progress and follow-up reports by management, all as applicable under the circumstances. The board and management share an interest in the successful implementation of an agreed plan and a board should, in the normal course, encourage and provide positive feedback on steps likely to lead to that outcome. If the board determines that management's

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91 OCC Director's Book, at 34; *see also Trenwick America Litigation Trust* v. *Ernst & Young, LLP*, 906 A.2d 168, 201 (Del. Ch. 2006) (holding that, absent specific legal obligations, directors of wholly owned subsidiaries can follow and support the business judgment and strategies of the parent).

92 OCC Heightened Standards, at 12 & 108.

93 *Id.* at 12-13.

implementation of an agreed plan is not adequate, the board should look to management for corrective measures. Management effectiveness in planning and implementation may well be taken into account for purposes of the board's ultimate decision as to whether the current management team is the most qualified for its role, as discussed further below under Core Function 3.

As Chairman (then Governor) Jerome H. Powell of the Federal Reserve Board noted, overwhelmingly granular expectations for banking boards "have fostered a 'check-the-box' approach by boards," and instead boards should spend less time on such routine matters and more on core board responsibilities.[94] The Federal Reserve Board's Board Effectiveness Proposal reflects this principle and identifies and describes five attributes of effective boards of directors of large banking institutions. According to the Federal Reserve Board, these include: (i) setting clear, aligned, and consistent direction, (ii) actively managing information flow and discussions, (iii) holding senior management accountable, (iv) supporting the independence and stature of independent risk management and internal audit and (v) maintaining a capable board composition and governance structure. For the largest U.S. bank holding companies, the Board Effectiveness Proposal states that Federal Reserve Board supervisors would use these attributes to inform their evaluation of a firm's governance and controls as part of the Large Financial Institution (LFI) rating system for large financial institutions. As noted above, the core board functions set out below are a way to organize several of the board's fundamental and critical responsibilities. The Federal Reserve Board's Board Effectiveness Proposal's attributes represents a different but similar organizational approach. Annex B to these Guiding Principles maps the attributes identified in the Board Effectiveness Proposal to the core board functions in this section.

Core Function 1: Reviewing and Approving a Banking Organization's Strategic Objectives and/or Plans

The board of a banking organization should review, discuss and approve the banking organization's overall strategic objectives on a regular schedule, as it deems appropriate. The board's role in approving the overall strategic objectives and/or plans of the banking organization, as formulated by management, reflects the distinction between the roles of the board and management and the fact that the board is ultimately responsible for the affairs of the organization.[95] According to the Federal Reserve Board, the director's role is to provide a clear set of overall objectives within which senior executives can administer the bank's day-to-day operations.[96]

Strategic objectives and/or plans provide consistent direction to senior executives for the management of the organization's affairs, including with respect to short- and long-term objectives for various business lines, material acquisitions and divestitures, and the introduction of material new business lines. The form in which a company's strategic objectives are expressed and documented will vary for each organization, as will the nature of the board's review and approval of those objectives[97]; however, in all cases these strategic objectives should be consistent with the board-approved risk appetite and should be reviewed and approved by the board on a regular basis. Generally, management, led by the CEO, will develop the organization's strategies for evaluation by the board.

The board's role in guiding the strategic direction of the banking organization may frequently include: (i) board oversight of top-tier policies and operating plans that assist in further defining and/or management's execution of

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94 Powell Speech, supra note 39.

95 *See*, *e.g.*, 12 U.S.C. §§ 71-76 (describing management of the affairs of national banks); 12 C.F.R. § 7.2010 ("The business and affairs of the bank shall be managed by or under the direction of the board of directors."); 8 Del. C. § 141 ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . . ."); *see also* discussion *supra* in Section 1.

96 *See* Commercial Bank Manual, Section 5000.1, at 2; *see also Grimes* v. *Donald*, 673 A.2d 1207, 1214 (Del. 1996) (discussing the board's duty to make informed decisions regarding matters at the "heart of the management of the corporation"); *Abercrombie* v. *Davies*, 123 A.2d 893, 899 (Del. Ch. 1956) (same); ABA Guidebook, at 11 (describing the board's responsibility for approving corporate policy and strategic goals); OCC Heightened Standards at 56-58 (describing an expectation that covered institutions have a three-year strategic plan).

97 For example, it may be possible for an organization to appropriately determine that IT, though critical, principally supports business objectives, and therefore, should not for that organization be part of a separate strategic plan or objectives statement. In either case, of course, a system of checks and balances should be in place to safeguard a robust IT infrastructure for the organization.

various aspects of the organization's strategic plan/objectives, and (ii) providing strategic advice to senior management. The board should oversee management's performance in formulating and implementing the organization's strategic objectives and oversee key business policies established by management.

For some companies, the strategy may take the form of a clearly defined strategy document reflecting proposed steps, time lines and quantified targets and objectives. In many cases, however, particularly for complex organizations, the board's engagement with the banking organization's strategic objectives will take place in the context of broad discussions by the board and management as to short- and long-term objectives for various business lines, the outlook for regulatory and compliance functions, management succession planning, challenges to be met or other similar matters. Other banking organizations may choose to review and approve their strategies through the budget approval process. Regardless of the manner in which the company's strategic objectives are documented or presented, they should provide the board and management with a framework for overseeing ongoing progress as to their implementation. Depending on the form of documentation and presentation of the company's strategic objectives to the board, the board's approval of those objectives may take the form of a formal vote concerning a defined strategy document, a consensus discussion or any other method permitting use of the strategic objectives as a framework consistent with the foregoing.

Core Function 2: Monitoring Financial Performance and Condition

The core function of monitoring financial performance and condition includes reviewing financial performance, financial forecasts, capital adequacy and liquidity, and external factors that can impact the organization on a regular basis in a manner consistent with the banking organization's strategic objectives and/or plans. The board should obtain sufficient information from management to inform board decisions on matters such as capital actions and, where necessary, contingency and recovery plans.

Core Function 3: Overseeing Talent Management, including the CEO and Other Senior Executives

One of the board's most important duties is to select, retain and evaluate executive officers who are qualified to operate the organization in an effective and sound manner. The board of directors should select the CEO and evaluate the performance and compensation of the CEO and such other senior executive officers as the board deems appropriate and consistent with the organization's strategy and oversight goals.[98] The Federal Reserve Board recommends that the board should hire and retain officers who "meet reasonable standards of honesty, competency, executive ability and efficiency."[99] The OCC expects that the board should actively manage the selection process of a CEO and that the selection criteria should include "appropriate competence, experience, and integrity to carry out his or her responsibilities."[100] The OCC further expects that the board consider adopting a formal performance appraisal process to oversee management's performance because such a process "ensures that the board discharges its responsibilities to supervise management."[101] For certain large national banks, the OCC Heightened Standards require that the bank board hire the CEO and hire or approve the hiring of the chief risk and chief audit executives.[102] Absent an express statutory or regulatory requirement, however, boards should use their judgment in determining which of the CEO's direct reports and other personnel should be approved by express board action. The board should also have flexibility to determine whether this is appropriately done at the bank level or the holding company level. Of course, the board should be very familiar with individuals appointed to senior positions, and even if the board does not formally act, it should be satisfied with those appointments and take them into account in evaluating the CEO.

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[98] Formal board approval of the appointments of certain other officers may be required or be a standard under applicable law or guidelines (see, *e.g.*, 12 C.F.R. Part 30, Appendix D – OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches).

[99] Commercial Bank Manual, Section 5000.1, at 2.

[100] OCC Director's Book, at 29.

[101] *Id*. at 24.

[102] OCC Heightened Standards, at 65-67 & 125.

As discussed in more detail in Section 8, the board or the compensation committee also is responsible for reviewing and approving the banking organization's compensation for its senior executives and, more generally, the compensation program for other employees in light of the organization's performance. These compensation practices should be appropriately balanced such that they do not jeopardize the bank's safety and soundness. In addition, the Dodd-Frank Act imposes additional oversight responsibilities on the boards of certain large banking organizations with respect to their compensation policies. These provisions and the rules proposed by federal bank regulators to implement them are discussed in Section 8.

Generally speaking, the background and level of expertise for senior executives will vary from organization to organization, and should be assessed by the board in its discretion, based on the needs of the organization and the qualifications of the best candidates. Banking regulations are rarely prescriptive with respect to the specific qualifications of executives. One exception appears in the Federal Reserve Enhanced Standards,[103] which require that bank holding companies with total consolidated assets of $50 billion or more appoint a chief risk officer with "experience in identifying, assessing, and managing exposures of large, complex financial firms." Absent this specific regulatory mandate, a board or the designated board committee could very well conclude that a chief risk officer with background in a non-financial firm (for example, a technology firm) might be in the best position to address the evolving risks that the organization faces and manage the risk management processes that identify and address those risks.

Talent management also includes approving an appropriate management succession plan for the CEO and reviewing or approving management succession plans for other senior executives,[104] addressing both emergency succession plans and long-term plans. Regulators expect to see management succession plans in place that are reviewed at least annually, as well as when other circumstances dictate further review or revisiting of the plan.[105] Within the constraints of regulatory requirements,[106] the board should use its judgment in determining the executive positions, other than the CEO, that should be covered by succession planning, depending on the particular needs of the organization.

Core Function 4: Overseeing the Risk Management and Internal Control Frameworks, including Top-Tier Policies and Plans in Fundamental Areas

Foundationally, this function involves overseeing that the banking organization has established appropriate risk management and control programs for identifying and addressing the significant risks faced by the organization, including being apprised of emerging risks that the organization may face in the future, and overseeing how management implements those programs. This includes (i) understanding the organization's risks and risk profile, (ii) reviewing the standards for the nature and level of risk the organization is willing to assume in light of the organization's business and strategic objectives, capital and liquidity levels, risk management capabilities and reputational considerations, (iii) approving the risk appetite statement, and (iv) reviewing and/or approving "top-tier" or overarching enterprise-wide risk policies and plans in areas that the board determines are fundamental to the strategic objectives of the organization. In approving the risk appetite statement, the board of directors should understand the aggregate level and types of risk the entity is willing to assume in order to achieve its strategic objectives, while complying with regulatory requirements. The OCC Heightened Standards require that the board or its risk committee review and approve the bank's appetite statement at least annually or more frequently, as necessary.[107] The Board Effectiveness Proposal views a board's inquiry into material or persistent breaches of risk

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103 *See* Revised Prudential Standards; 12 C.F.R. § 252.33(b).

104 *See* Basel Principles, at 12; ABA Guidebook, at 13; U.K. Governance Code, at 8-9; OCC Handbook, at 20 (noting that the board is responsible for approving management succession plans, while the CEO is responsible for management succession planning.).

105 *See* OCC Director's Book, at 30-31.

106 *See* OCC Heightened Standards, at 125 (the board or a board committee of a large national bank should review and approve a written talent management program that provides for development, recruitment and succession planning regarding the CEO and the chief risk and audit executives, their direct reports and other potential successors).

107 OCC Heightened Standards, at 120-122.

appetite as an important attribute of an actively engaged board.[108]

As recommended by the FDIC Pocket Guide, a banking organization should have policies that address, at a minimum, loans (including loan review procedures), investments, asset-liability/funds management, profit planning and budget, capital planning, internal controls, compliance, audit program, conflicts of interest and code of conduct. The particular top-tier policies and plans that merit board review and/or approval will depend on the nature, size and complexity of the organization's activities. Risk policies that do not fundamentally contribute to defining and/or managing the organization's primary risk tolerances do not ordinarily warrant board attention or action unless the subject matter itself may be so essential to the safe-and-sound operation of the particular banking organization that such attention/action is considered necessary. Similarly, management should establish and be responsible for a banking organization's procedures relating to day-to-day operations, and those procedures should not ordinarily be presented to the board for review and/or approval.

The board's risk oversight function also includes providing oversight of the compliance and internal audit functions, as well as the effectiveness of the organization's internal controls, through ongoing reporting to the board and the provision of feedback by the board to management. This encompasses oversight of key internal controls that relate to core business lines and critical operations and/or other fundamental processes such as: (i) capital/liquidity/stress testing planning processes; (ii) financial, capital and risk profile reporting and disclosures processes; (iii) information security (including cyber vulnerability), outsourcing and recovery processes; (iv) customer, client service and compliance standards and processes, and (v) loan underwriting and review.

Appropriate means should be utilized by the board to promote an oversight culture consistent with sound risk management, including by providing clear expectations and direction to senior management and the control functions relating to implementation of programs. Designations of authority/responsibility by the board to management should generally convey expectations relating to ongoing (*e.g.*, periodic updates) and special reporting to the board (*e.g.*, to report any significant deviations/"red-flags" from the board-approved risk-appetite or policies).

Because banking organizations are subject to an extensive regulatory scheme, regulatory compliance is one of the board's primary oversight responsibilities. The board of a banking organization has the ultimate responsibility for overseeing management's establishment and implementation or operation of a system designed to promote compliance with applicable laws and regulations.[109] To that end, the board should supervise management's creation of clear policies that govern and guide the day-to-day operations of the organization to comply with applicable laws and regulations, including internal and external audit processes[110] and disclosure controls and procedures, and the board should review these policies from time to time in light of changing legal requirements. Additionally, to promote compliance with applicable rules and regulations, the board and management should develop an understanding as to the nature of the information and matters, including, as appropriate, regulatory discussions, that should come to the attention of the board. The FDIC Pocket Guide recommends that the board adopt "a mechanism for independent third party review and testing" of compliance with policies and procedures of the banking organization and applicable laws and regulations, as well as the accuracy of information provided by

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108 Board Effectiveness Proposal, at 37,225-26.

109 The organization's compliance oversight structure should include, as applicable, compliance with the Volcker Rule, which was originally finalized by federal regulators in December 2013 (subject to phase-in periods) and modified in 2019 and 2020. The Volcker Rule restricts banking organizations from engaging in proprietary trading and from investing in and sponsoring private equity and hedge funds, and also prohibits covered transactions between a banking organization or its affiliates, on the one hand, and "covered funds" that the banking organization sponsors, organizes and offers or advises, on the other hand. *See* OCC, Federal Reserve Board, FDIC, SEC, Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5,536 (January 31, 2014).

110 *See* Federal Reserve Board, Supplemental Policy Statement on the Internal Audit Function and its Outsourcing, SR 13-1 ("SR 13-1"), at 7 (January 23, 2013) (describing the responsibilities of the board of directors and audit committee with respect to oversight of internal audit and internal audit outsourcing arrangements). The board may determine that one or more other committees be involved in overseeing compliance-related matters, subject to applicable legal or regulatory requirements.

management,[111] suggesting that such independent review may be "accomplished by an internal auditor reporting directly to the board, or by an examining committee of the board itself."[112]

U.S. banking regulators have set requirements for active board oversight of risk management. The OCC Heightened Standards impose substantial risk management-related and other responsibilities on the boards of directors of certain large national banks. Among other things, the OCC Heightened Standards require the boards of directors to "actively" oversee the banks' risk-taking activities,[113] including a duty to question and, as necessary, challenge management decisions that could cause the bank's risk profile to exceed its risk appetite or jeopardize the safety and soundness of the bank.[114] The OCC Heightened Standards also require boards of directors to approve a formal, written risk governance framework that includes three distinct functions—front line units, independent risk management and internal audit—and to approve any significant changes to the risk governance framework.[115] Boards have oversight responsibilities in regard to these three distinct functions as well as to the risk governance framework. For example, under the OCC Heightened Standards, the chief risk executive, who is responsible for the independent risk management function, must be provided unrestricted access to the board in order to bring to the attention of the board identified risks and issues.[116] Similarly, the OCC Heightened Standards require that the chief audit executive, who is responsible for the internal audit function, communicate to the board identified issues in regard to the risk governance framework, and accordingly, this officer is granted unfettered access to the board's audit committee.[117] In regard to the risk governance framework, the OCC Heightened Standards provide that the board is responsible for reviewing and approving a written talent management program for key employees.[118] The board also should review the maintenance of sufficient capital levels in light of the organization's risk profile as Congress and bank regulators have increasingly emphasized the importance of capital planning in the aftermath of the financial crisis of 2008.[119]

Additionally, as discussed in Section 9, the Federal Reserve Enhanced Standards include a wide range of measures

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111 *See also* FDIC Supervisory Insights, at 15-16; OCC Heightened Standards, at 39 (noting that front-line units, independent risk management and internal audit would find it "useful" to engage the services of external experts).

112 *See also* OCC Director's Book, at 65 ("An internal audit program provides assurance to the board and senior management not only on the quality of the bank's internal controls but also on the effectiveness of risk management, financial reporting, [management information systems], and governance practices.").

113 OCC Heightened Standards, at 73-74 & 126. The OCC clarified that the board of directors may rely on risk assessments and reports prepared by independent risk management and internal audit to meet its responsibilities to provide active oversight. *Id*.

114 *Id*. at 75. The OCC Heightened Standards define a bank's risk appetite as the aggregate level and types of risk the board and management are willing to assume in order to achieve the bank's strategic objectives and business plan, consistent with regulatory requirements. *Id*. at 114. The OCC Heightened Standards further clarify that a bank's risk appetite statement should include both qualitative components, including a description of a safe and sound risk culture, and quantitative limits that include, as appropriate, a bank's stress testing processes. *Id*. at 122.

115 *Id*. at 114 & 126. The board of directors or the board's risk committee would also be required to review and approve the bank's risk appetite statement that serves as the basis of the risk governance framework at least annually or more frequently, as necessary, and to review and approve a three-year strategic plan developed under the direction of the CEO that includes a comprehensive risk assessment. *Id*. at 120-122.

116 *Id.* at 31.

117 *Id.* at 35.

118 *Id*. at 68.

119 *See* Dodd-Frank Act, § 171(b)(2); *see, e.g.*, Revised Prudential Standards; OCC, Department of Treasury, Federal Reserve Board, Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Risk-weighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule and Market Risk Capital Rule, 78 Fed. Reg. 62,018 (October 11, 2013); Federal Reserve Board, Division of Banking Supervision and Regulation, Federal Reserve Supervisory Assessment of Capital Planning and Positions for LISCC Firms and Large and Complex Firms, SR Letter 15-18 (Dec. 18, 2015); Federal Reserve Board, Division of Banking Supervision and Regulation, Federal Reserve Supervisory Assessment of Capital Planning and Positions for Large and Noncomplex Firms, SR Letter 15-19 (Dec. 18, 2015); Federal Reserve Board, Consolidated Supervision Framework for Large Financial Institutions, SR 12-17 ("SR 12-17") (December 17, 2012).

addressing capital, liquidity, stress testing and risk management, and impose a number of specific duties on the board of directors. As discussed in Section 5, the board of directors also is required to review information provided by senior management to determine whether the company is operating within its established liquidity risk tolerance, and to approve and periodically review the liquidity risk management strategies, policies and procedures established by senior management.[120]

In addition, the risk committee or a designated subcommittee of the risk committee is required to review and approve the company's contingency funding plan at least annually and whenever the company materially revises the plan.[121] Finally, the rules require these bank holding companies to have a review function, which is independent of management functions, to evaluate the company's liquidity risk management.[122]

Under the Federal Reserve Board's capital plan rule,[123] the board of a bank holding company with total consolidated assets of $100 billion or more must annually approve the organization's capital plan. Although the capital plan rule provides that the board exercise an oversight role by approving a capital plan, certain regulatory expectations have conflated the role of the board and that of management in capital planning and contemplated that boards review information that is frequently overly granular and technical and, ultimately, inappropriate for board attention. For example, SR Letter 15-18 of the Federal Reserve Board states that the "board should direct senior management to provide information about the firm's estimation approaches, model overlays and assessments of model performance."[124] In connection with capital planning, as elsewhere, BPI believes that boards should provide oversight at a higher conceptual level; granular, prescriptive requirements and expectations on the board do not promote effective governance.

The Federal Reserve Board has also set expectations for robust recovery planning of bank holding companies,[125] aimed at "ensuring the ongoing resiliency of a firm's consolidated operations as well as its core business lines, critical operations, banking offices, and other material entities."[126] To this end, each large banking organization is expected to implement mechanisms to identify and plan for actions to remediate potential financial or operational weaknesses, as well as to integrate recovery planning into corporate governance structures and board oversight.[127]

Resolution planning is distinct from both capital planning and recovery planning. Resolution plans, or "living wills," have emerged as an area of supervisory and regulatory focus in the aftermath of the 2008 global financial crisis. Section 165(d) of the Dodd-Frank Act and the implementing regulations require large bank holding companies to develop, maintain and periodically report to the regulators on their plans for "rapid and orderly resolution in the event of material financial distress or failure" under the U.S. Bankruptcy Code in a way that would not pose systemic risk to the financial system.[128] Pursuant to these regulations, the boards of these large bank holding

120 *Id.* § 252.34(a)(2).

121 *Id.* § 252.34(b).

122 Revised Prudential Standards, at 59,104.

123 12 C.F.R. § 225.8.

124 SR 15-18; SR 15-19.

125 SR 12-17; Federal Reserve Board, Division of Banking Supervision and Regulation, Consolidated Recovery Planning for Certain Large Domestic Bank Holding Companies, SR Letter 14-8 (September 25, 2014) (providing additional guidance to eight domestic bank holding companies that may pose elevated risk to U.S. financial stability).

126 SR 12-17; SR Letter 14-8 ("The primary goal of such recovery planning is to develop a menu of options that would enable a firm to respond to a wide range of internal and external stresses and maintain the confidence of market participants without extraordinary governmental support.").

127 SR 12-17.

128 *See* FDIC and Federal Reserve Board, Resolution Plans Required, 84 Fed. Reg. 59,194 (November 1, 2019) ("Resolution Plan Requirements"); FDIC, Resolution Plans Required for Insured Depository Institutions with $50 billion or More in Total Assets (September 10, 2011) ("Interim Resolution Plan Rule") (requiring resolution plans for large depository institutions with total consolidated assets of $50 billion or more); FDIC, Resolution Plans Required for Insured Depository Institutions with $50 billion or More in Total Assets (Advanced Notice of Proposed Rulemaking), 84 Fed. Reg. 16,620 (April 22, 2019) (proposing

companies and depository institutions are required to approve an initial resolution plan and subsequent periodic resolution plans and such approvals should be duly noted in the minutes of meeting of the board of directors.[129]

In general, reports to the board should be timely, clear and accurate and designed to aid informed board oversight and decision making. Sufficient information should be provided to the board to enable it to effectively oversee: (i) the stature and independence of internal control units, (ii) the overall performance of the risk management framework (including, for example, reports by audit on whether the process is functioning in accordance with supervisory expectations and, for example, reports by risk management/compliance/other control functions on whether the firm is operating in conformity with the board-approved risk appetite statement and regulatory expectations), (iii) emerging risks or future changes to the business that may materially impact the overall risk profile or changes to fundamental risk management practices, including modelling practices, and (iv) effective identification, tracking and remediation of any risk-management or compliance deficiencies.

Core Function 5: Reinforcing, Demonstrating and Communicating the "Tone at the Top" for the Values and Culture of the Organization and Overseeing Enterprise-wide Approaches/Programs Intended to Promote Organizational Values, Culture and Reputation

In order for the board to encourage responsible, professional and ethical behavior throughout the organization, the board should promote a culture of ethical behavior within the organization through overseeing senior management's establishment of an organizational culture that provides for appropriate standards and incentives for ethical and responsible behavior, including:

- Board oversight of the enterprise-wide culture of compliance that respects the spirit of the law, as well as the technical rules, and setting "a tone at the top" emphasizing the importance of compliance at every level[130];
- Board oversight of the enterprise-wide compensation philosophy that appropriately balances risk and reward and takes into account compliance performance and ethical and responsible behavior;
- Board oversight of the development of performance/talent management and training programs that attract and retain highly qualified executives and other employees/agents who exhibit desired qualities, behaviors and skills; and
- Board oversight of any other reputational and/or conduct risk management approaches, as and where applicable.

This function also includes setting the "tone at the top" by overseeing the development and implementation of a code (or codes) of conduct that is applicable to directors and employees and that addresses treatment of code breaches or lapses in behavior. The board should itself demonstrate the values articulated in the code of conduct (and/or similar documents articulating institutional values) of the organization, and hold management and other personnel accountable for abiding by these values and communicating them throughout the organization and to other stakeholders as deemed appropriate.

The board should take steps as necessary to be satisfied that the organization's strategy and risk profile support desired behaviors, brand and reputational strategy, and align with the organization's control environment.

revising Interim Resolution Plan Rule to extend submission cycle and tailor requirements to the size of each covered insured depository institution).

129 *See* Resolution Plan Requirements, at 59,222; Interim Resolution Plan Rule, at 53.

130 *See, e.g.,* Federal Reserve Board, Compliance Risk Management Programs and Oversight at Large Banking Organizations with Complex Compliance Profiles, SR 08-8 (October 16, 2008) (noting that the board of directors has responsibility for promoting a culture that encourages ethical conduct and compliance with applicable rules and standards); *see also* SR 12-17.

SECTION 5. BOARD COMMITTEES

Principles:

- **a) The board of the top-tier entity within a banking organization should establish board committees to assist the board in its oversight of (i) audit, (ii) nominating/corporate governance, (iii) compensation and (iv) risk management activities, as well as any other standing or temporary committees appropriate to the circumstances and businesses of the banking organization.**
- **b) The board should have the flexibility to allocate responsibilities among board committees. The responsibilities of each standing committee should be described in a written charter or similar document. Certain matters might be within the scope of two or more committees (*e.g.*, audit and risk management), and the board may determine which committee is best suited to address a certain matter as it deems appropriate, taking into account any regulatory requirements providing that a particular matter be the responsibility of a particular committee. Periodic joint meetings may be appropriate for particular issues or topics. The relevant committees should coordinate as they or the board deems appropriate.**
- **c) The standing committees should report regularly to the full board. The board should adopt a schedule for the reports to be delivered by each committee, recognizing that it may be appropriate for some committees to report more frequently than others.**
- **d) The board and each committee of the board should have the authority to engage counsel and outside advisors as they deem necessary or appropriate to carry out their duties.**

Commentary:

Committee Structure

The board of a banking organization should have an organizational structure that enables it to oversee the affairs of the organization in a sound manner. As emphasized elsewhere in these Guiding Principles, unless otherwise required by law or regulation, a committee of the board should have the same authority to take actions with respect to matters appropriately delegated to it as the full board.[131] The OCC advises that an "appropriate governance and committee structure depends on the bank's needs" and that delegation to committees "allows the directors to better focus their time and attention on areas or subject matters on which they can lend their specific expertise or experience."[132] Similarly, the Federal Reserve Board notes that many boards "elect to delegate some of their workload to committees" and that the "extent and nature of the bank's activities and the relative expertise of each board member play key roles in the board's determination of which committees to establish, who sits on them, and how much authority they have."[133] Accordingly, the board should create board committees and delegate responsibilities to its committees in a manner that is tailored to the particular circumstances and businesses of the organization. The review of a board's committee structure may be done by the board itself or by a committee charged with oversight of corporate governance as described in Section 7.

As discussed in Section 1, a board should be able to discharge any and all of its duties and responsibilities through its committees unless the board determines a particular matter warrants the attention of the full board or a matter is required to be addressed by the full board under applicable law, regulation or listing requirements. Increasingly, agency guidance and regulations appropriately provide that where board-level attention is warranted, a board committee, rather than the full board, may (or, in certain cases, is required to) conduct the relevant review or provide the required approval.[134]

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131 *See* supra note 45 and accompanying text.

132 OCC Director's Book, at 35.

133 Commercial Bank Manual, Section 5000.1, at 4.

134 For example, the Risk Management of Financial Derivatives booklet of the Comptroller's Handbook notes that "[g]iven the extent and nature of demands placed on the board, committees may be created to handle matters requiring detailed review

However, many regulations and other agency pronouncements do not recognize the important ability of a board to discharge its duties and responsibilities, instead providing for the full board (and not one of its committees) to conduct a review or provide an approval. These references to the full boards at times lead to uncertainty relating to applicable regulatory requirements and supervisory expectations, as well as inappropriate constraints on the ability of boards to delegate matters to committees. For example, the Federal Reserve Enhanced Standards[135] require the full board of a U.S. bank holding company with total consolidated assets of $100 billion or more to (i) approve the acceptable level of liquidity and risk tolerance at least annually; (ii) receive and review at least semi-annually information provided by senior management to determine whether the bank holding company is operating in accordance with its established risk tolerance; and (iii) approve and periodically review the liquidity risk management strategies, policies and procedures established by senior management. As a practical matter this review could, appropriately, be undertaken by the risk committee of the board and then, depending on the organization's circumstances, approved by the risk committee or recommended to the full board for its approval.

Although there is no single "ideal" committee structure that is applicable to all banking organizations, the board of the top-tier entity within a banking organization normally will have at least the committees discussed in the following sections (audit, nominating/corporate governance, compensation and risk management). The banking organization should be able to combine these functions into fewer committees or separate them into additional committees, as the board deems appropriate, if the focus and integrity of the committees are not compromised and the members meet all relevant independence and qualification criteria.

Mandates of board committees may be subject to multiple sources of authority, including federal banking laws and regulations, federal securities laws and regulations, and stock exchange listing standards. To illustrate, the Federal Reserve Enhanced Standards require bank holding companies with total consolidated assets of $50 billion or more to establish a standalone risk committee, as discussed further in Section 9. Section 301 of the Sarbanes Oxley Act of 2002 requires public companies to have an audit committee of the board, composed entirely of independent directors, that is directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by that company for the purpose of preparing or issuing an audit report or related work. Moreover, Section 303A.05 of the NYSE Listed Company Manual requires NYSE-listed companies to have a compensation committee of the board, composed entirely of independent directors, that must review and approve goals and objectives relevant to CEO compensation, and evaluate the CEO's performance in light of those goals and objectives, among other things.[136] When structuring committees, the board should be mindful of the multiple sources of authority that may apply to the organization.

Subject to applicable laws and regulations (as discussed in detail in Sections 6 to 9) that prescribe mandates for certain committees and the securities exchange rules that apply to public companies, to the extent the board determines that certain matters are to be addressed by a board committee, the board should have the flexibility to determine which board committee would be most appropriate. The responsibilities of separate board committees will in many cases overlap. For example, management succession and director compensation may be appropriate for consideration by both the nominating/corporate governance committee and the compensation committee, and the audit and risk committees may both meet periodically with management and internal and external auditors to review the adequacy of the organization's controls. Such overlapping responsibility may be unavoidable and also is not necessarily detrimental. As one potential approach, boards may determine that having overlapping membership among committees and, in appropriate cases, joint meetings of separate committees, can allow directors to operate efficiently and with a common knowledge base, and facilitate the board's broad oversight of the organization. Joint membership and joint meetings may be a particularly helpful approach for companies with a standalone risk committee, as discussed further in Section 9. Although some committee responsibilities will

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or in-depth consideration, with each committee reporting to the board. Accordingly, the words board and committee are used synonymously throughout this document." See also 12 C.F.R. § 225.8 (the "Capital Plan Rule"); Board Effectiveness Proposal, at 37,225-26 (contemplating that the board discharges its independent risk management and internal audit functions through committees).

135 12 C.F.R. § 252.34(a).

136 *See also* NYSE Manual, Sections 303A.04, 303A.06; NASDAQ Rules, Sections 5605(c)(2)(A), 5605(d)(2)(A) and 5605(e)(1)(B).

inevitably overlap, it is important that the board periodically review the governance structure of its committees to evaluate whether the allocation of duties among its committees is appropriate given the business, strategic priorities, and circumstances of the banking organization so that both duplication and siloing among the committees can be avoided.

Banking organizations also may deem it appropriate to have some or all these committees at the subsidiary bank level depending on the size and complexity of such subsidiary bank's operations.[137] Pursuant to regulations adopted by the FDIC under the Federal Deposit Insurance Corporation Improvement Act of 1991 (the "FDICIA"), banking organizations with total assets of $500 million or more are required to establish an audit committee.[138] This requirement, however, may be satisfied by an audit committee at the holding company level with respect to subsidiary banks that have consolidated total assets comprising 75% or more of the holding company's consolidated total assets, subject to certain conditions.[139] The OCC also suggests that an audit committee may be unnecessary at the bank level if there already is a similar committee at the holding company level.[140] More generally, the OCC observes that the "appropriate governance and committee structure depends on the bank's needs," which depends in part on the "complexity and risk profile of the bank's products and services" and "skills and expertise of committee members."[141]

Many corporations, including many banking organizations, have an executive committee that is empowered to act on the board's behalf (*e.g.*, between regular board meetings). The OCC states that the executive committee should review all major bank functions but cautions that the committee should not "have the authority to exercise all of the board's powers" such as "the right to execute extraordinary contracts such as mergers and acquisitions."[142] Similarly, the general corporate law in most states allows boards to grant executive committees broad powers, other than certain specified actions such as amending the bylaws of the corporation or submitting matters to shareholders for approval.[143] BPI believes that the authority and constituency of an executive committee should be determined by the board, based on the structure of the particular organization, including how frequently the board is called upon to act between regular board meetings. The board may consider whether its use of the executive committee should be limited in any respect beyond that legally required so as not to impinge on the role of the full board and the perspective and diversity of opinion that the board will bring to bear on an issue.

Each standing committee should have a written charter that outlines "the committee's responsibilities, member qualifications, authorities, independence, and board reporting."[144] Committee charters also can help clarify, and avoid excessive overlap between, the roles of the various committees.[145]

The board of a banking organization also may find it desirable to create additional standing or temporary committees based on the size and complexity of the organization and the needs and circumstances it faces from time to time. As the Federal Reserve Board has observed, "[D]epending on the nature and complexity of the bank's business, the board may establish other committees to monitor such areas as trust, branching, new facilities

137 Following the events of the 2008 financial crisis, there has been a greater focus on the governance of legal entities within a group structure. *See* Basel Principles, at 22 ("In a group structure, the board of the parent company has the overall responsibility for the group and for ensuring the establishment and operation of a clear governance framework appropriate to the structure, business and risks of the group and its entities.").

138 12 C.F.R. § 363.5.

139 *See* 12 C.F.R. Pt. 363, App. A.

140 Comptroller's Handbook, "Internal and External Audits," (Version 1.1, July 2019), at 10.

141 *Id*. at 29.

142 *Id*. at 30.

143 *See*, *e.g.*, 8 Del. C. § 141(c)(2); N.Y. Banking Law § 7012(1).

144 OCC Director's Book, at 35; *see also* NYSE Manual, Sections 303A.07(b), 303A.05(b) and 303A.04(b) (requiring the audit, compensation and nominating/corporate governance committees of public companies to have written charters specifying the duties of those committees pursuant to the rules of the national securities exchanges); ABA Guidebook, at 63.

145 *See* OCC Director's Book, at 35 ("The board should clearly understand and define the responsibilities of each committee.")

construction, personnel/human resources, electronic data processing, and consumer compliance."[146] For instance, banking organizations may consider establishing a loan committee in order to obtain the benefits of Section 13(e) of the Federal Deposit Insurance Act (the "FDIA"), which provides that a contract may not be enforced against the FDIC, whether acting as a receiver or as liquidator, unless (among other things) it was approved by "the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee."[147] There has also recently been a trend toward creating standalone technology and/or conduct (or ethics) committees, reflecting areas that have recently been receiving heightened board attention and boards' determination that the establishment of those standalone committees will facilitate their oversight. Again, boards have the flexibility to determine where particular matters—such as consideration of risk exposures and risk events—should be considered, and accordingly, a board has flexibility to decide whether such committees are desirable or appropriate in light of the particular circumstances for a given board and banking organization.

The board and each committee of the board should have the authority to retain their own legal counsel and professional advisors when they determine direct advice from their own advisors is desirable.[148] This authority necessarily should be supported by appropriate funding by the banking organization in order to compensate counsel and advisors to the board or its committees and to pay other administrative expenses.[149] In particular, advisors can serve as valuable resources when the board or committee is considering complex or specialized issues that require expert knowledge.[150] In certain circumstances, particularly with regard to sensitive matters such as reviewing and approving compensation packages for senior executives or discussing an external auditor's concerns regarding the organization's control procedures, the board or a committee may wish to engage counsel and/or advisors that do not advise the banking organization on these matters or that have little or no relationship with the organization in any other respect. The determination of the appropriate degree of independence is a function of all the relevant facts and circumstances.[151]

The Relationship between the Board and its Committees

State corporate law generally allows board committees to perform most board functions,[152] and references in these Guiding Principles to actions to be taken by the "board" generally include actions taken through board committees. Nevertheless, the delegation of responsibilities and functions to standing or temporary committees

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146 Commercial Bank Manual, Section 5000.1, at 5; *see also* OCC Director's Book, at 35 (noting that the appropriate committee structure for a bank depends on the "complexity and risk profile of the bank's products and services" as well as the "skills and expertise of committee members.").

147 12 U.S.C. § 1823(e)(1)(C); *see also* OCC Director's Book, at 96 (discussing establishment and role of a credit committee).

148 *See* ABA Guidebook, at 48-50.

149 The Sarbanes-Oxley Act and the rules promulgated by the SEC pursuant thereto grant the audit committee of a public company the authority to engage counsel and other advisors and require the company to pay for these advisors. *See* Sarbanes-Oxley Act, § 301, Exchange Act Rule 10A-3(b)(4) & (5); *see also* NYSE Manual, Section 303A.07(b)(iii) and NASDAQ Rules, Section 5605(c)(3). Securities exchange listing standards provide similar authority for the compensation and nominating / corporate governance committees. *See* NYSE Manual, Sections 303A.04 and 303A.05; NASDAQ Rules, Section 5605(d).

150 Directors of banking organizations, like those of other corporate entities, are entitled to rely in good faith on reports, opinions, information and statements (including financial statements and other financial data) prepared by outside experts, such as legal counsel and public accountants, whom the directors reasonably believe to be reliable and competent. *See*, *e.g.*, 8 Del. C. § 141(e); *Graham* v. *Allis-Chalmers Mfg. Co.*, 188 A.2d 125, 130 (Del. 1963); *Prince* v. *Bensinger*, 244 A.2d 89, 94 (Del. Ch. 1968).

151 *See* NYSE Manual, Section 303A.05(c) and NASDAQ Rules, Section 5605(d)(2)(A) (requiring the compensation committee to consider certain independence criteria prior to hiring a compensation adviser, except for a compensation adviser that merely consults on broad-based plans or provides non-customized or issuer-specified information). These requirements are discussed further in Section 8.

152 *See*, *e.g.*, 8 Del. C. § 141(c)(2) (stating that, subject to certain exceptions, a board committee "may exercise all the powers and authority of the board of directors in the management of the business and affairs of the corporation"); N.Y. Banking Law § 7012(2).

does not relieve the full board of general oversight responsibility over those functions.[153] Moreover, the ABA states that, "[i]n accord with [the board's] obligation to provide oversight," the board committees should adopt proper procedures providing a regular flow of reports and other information to the board such that all directors are kept "abreast of each committee's activities and significant decisions."[154] In this regard, the board committees may find it desirable to conduct their own evaluations of the format and timeliness of information brought to the attention of the committee and the timeliness, scope and format of the reports subsequently provided to the board. Both standing and temporary committees should keep the board informed of their activities through reports at board meetings. These reports should summarize all significant decisions and actions taken at the committee meetings.

SECTION 6. AUDIT COMMITTEES AND BOARD OVERSIGHT OF FINANCIAL REPORTING AND AUDIT FUNCTIONS

Principles:

a) **The board of the top-tier entity within a banking organization should have an audit committee, composed entirely of independent directors, with the responsibility to oversee internal audit and internal controls as well as the sole authority to appoint, terminate and approve compensation for independent auditors.**

b) **The members of the audit committee of the top-tier entity collectively should have appropriate accounting, banking and related financial expertise and experience, including at least one member who is an audit committee financial expert under SEC rules.**

c) **The audit committee, or another independent committee, should review and approve the policies governing the receipt, retention and treatment of complaints regarding accounting or auditing concerns, including confidential, anonymous submissions by employees or other parties.**

Commentary:

Responsibilities of the Audit Committee

In general, large banking organizations in the United States are required to create an audit committee and to prescribe specific qualifications for members of the audit committee.[155] As noted in Section 5, the duties of a banking organization's audit committee are subject to multiple sources of authority, including banking laws and regulations, securities laws and regulations, and state corporate law. Broadly stated, the audit committee has general oversight responsibility for a banking organization's financial reporting process, internal controls, internal audit (including any outsourcing of internal audit functions)[156] and compliance policies and procedures, as well as responsibility for hiring and communicating with the banking organization's external auditors.[157]

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153 *See* Walker Review, at 90 (noting that the creation of a committee does not replace ultimate responsibility and accountability of the whole board for such committee's function).

154 ABA Guidebook, at 61; *see also id*. at 64 ("Board committees should regularly inform the board of their activities. Generally, standing committees should provide reports at regularly scheduled full board meetings and circulate to all directors committee agendas, minutes, and written reports . . . ."); OCC Director's Book, at 35 (committee charters should address reporting to the full board and provide for annual performance evaluations of the committee).

155 *E.g.*, 12 C.F.R. § 363.5. The importance of an independent, qualified and engaged audit committee as a governance matter has been widely recognized. In the wake of several prominent accounting scandals, Congress passed the Sarbanes-Oxley Act, which, among other things, directed the SEC and the national securities exchanges to require public companies to create an audit committee and to prescribe specific qualifications for members of the audit committee. *See* Sarbanes-Oxley Act, § 301. Federal bank regulators adopted similar regulations following the promulgations of these rules and regulations by the SEC and the national securities exchanges.

156 *See* SR 13-1, at 7 (describing the responsibilities of the board of directors and audit committee with respect to oversight of internal audit and internal audit outsourcing arrangements).

157 *See* Commercial Bank Manual, Section 5000.1, at 4-5 (noting that the audit committee typically "monitors compliance with bank policies and procedures, and reviews internal and external audit reports and bank examination reports"); OCC Director's Book, at 96 (listing main responsibilities of audit committees); ABA Guidebook, at 65 (noting that the audit committee "is

As part of the board's compliance oversight function, the audit committee (or another independent committee) should review and approve a process for the treatment of "whistleblower" claims or other reports by employees or other parties regarding accounting or auditing concerns.[158] Management, in turn, is responsible for developing, reviewing, approving, and implementing policies relating to complaints received in the ordinary course of business (such as employee and consumer complaints). Bank regulators have recommended the use of a confidential reporting system through which the employees can raise "concerns about illegal activities, violations, and nonadherence to bank policies."[159] The structure of such reporting systems, including the specific role of the board or audit committee, and the reliance on management for administrative support, will vary based on each organization's particular structure and the type of report.

The holding company should determine whether the subsidiary bank board should have its own audit committee (as well as other committees), subject to relevant regulatory requirements. Such determination should receive the concurrence of the subsidiary bank board. As noted in Section 5 above, the requirement for banking organizations with total assets of $500 million or more to establish an audit committee may be satisfied by an audit committee at the holding company level. Regardless of whether the subsidiary bank has its own audit committee, the bank board should be composed of individuals who collectively have the financial knowledge necessary to perform their oversight responsibilities effectively.

In addition to the foregoing responsibilities, the audit committees are expected to discharge the duties that generally apply to audit committees of public company boards. The Sarbanes-Oxley Act and accompanying regulations impose specific responsibilities on the audit committees of public companies, including the following: (i) selecting and engaging the external auditor and annually deciding whether to retain the external auditor, and reviewing and approving annually the external auditor's fee arrangement, (ii) overseeing the organization's procedures for issuing quarterly and annual earnings press releases and for providing financial information and earnings guidance to analysts, the financial press and rating agencies, and (iii) determining whether to recommend to the board that the audited annual financial statements of the organization be included in its annual report on Form 10-K.[160]

Composition of the Audit Committee

After the passage of the Sarbanes-Oxley Act, the SEC, the national securities exchanges and federal bank regulators adopted regulations requiring all public (and certain large private) banking organizations to create an audit committee of the board composed entirely of independent directors with certain prescribed qualifications.[161] For example, SEC Rule 10A-3 generally requires that, to be considered independent for purposes of serving on the audit committee, a director may not (other than in his or her capacity as a member on the committee or the board): (i) accept directly or indirectly any consulting, advisory, or other compensatory fee from the company or any subsidiary of the company (except for certain retirement plan payment for prior service with the company not

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critical to the corporate governance structure" and "has general oversight responsibility for the company's financial reporting process and internal controls"). *See also* Basel Committee on Banking Supervision, the Internal Audit Function in Banks (June 2012), Annex 2—Responsibilities of a bank's audit committee, at 21; NYSE Manual, Section 303A.07 (commentary) (noting the audit committee's responsibility to oversee a listed company's internal audit function).

158 Under SEC rules, the audit committees of public companies must establish procedures for the receipt, retention and treatment of complaints regarding accounting or auditing matters and for the confidential, anonymous submission by employees of accounting or auditing concerns. *See* Exchange Act Rule 10A-3(b)(3). On May 25, 2011, pursuant to the directive of Section 922(a) of the Dodd-Frank Act, the SEC adopted final rules implementing a whistleblower program designed to encourage tips of potential federal securities law violations to the SEC. The program reinforces the need for boards to continually review and improve their internal reporting and compliance systems. *See* 17 C.F.R. § 240.21.

159 OCC Director's Book, at 64; *see also* Basel Principles, at 10 (suggesting that banking organizations should establish a policy setting forth adequate procedures for employees to communicate confidentially material and bona fide concerns or observations of any illegal, unethical or questionable practices, and that the board should determine how and by whom such legitimate concerns shall be investigated and addressed).

160 *See* 12 C.F.R. § 363.5; Exchange Act Rule 10A-3; NYSE Manual, Section 303A.06; NASDAQ Rules, Section 5605(c).

161 *See* Sarbanes-Oxley Act, § 301; 12 C.F.R. § 363.5; 12 C.F.R. Pt. 363, App. A.

otherwise prohibited by national securities exchange rules) or (ii) be an affiliated person of the company or its subsidiary.[162] Both the NYSE and NASDAQ refer to this SEC rule in their respective listing requirements.[163]

The audit committee of banking organizations with assets greater than $3 billion must "include members with banking or related financial management expertise."[164] Furthermore, pursuant to Item 407(d)(5) of Regulation S-K, a public banking organization is required to disclose whether an "audit committee financial expert" serves on the audit committee. The term "audit committee financial expert" is defined as a person who has:

i. an understanding of generally accepted accounting principles and financial statements;

ii. the ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;

iii. experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that generally are comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant's financial statements, or experience actively supervising one or more persons engaged in such activities;

iv. an understanding of internal control over financial reporting; and

v. an understanding of audit committee functions.[165]

BPI believes that the board of the top-tier entity within a banking organization should have at least one member of the audit committee designated as an audit committee financial expert under SEC rules. Although nothing in the SEC rules or banking regulations absolutely requires a board to have an audit committee financial expert and there are arguments that an otherwise qualified board with access to outside financial expertise may function just as effectively, BPI believes that having such an expert on the audit committee enhances the committee's capability to address the complex issues it will face and is consistent with regulatory and market expectations.

SECTION 7. NOMINATING/CORPORATE GOVERNANCE COMMITTEES, DIRECTOR QUALIFICATIONS AND BOARD OVERSIGHT OF DIRECTOR NOMINATION PROCESS

Principles:

a) **The board of the top-tier entity within a banking organization should have a committee, composed entirely of independent directors, to conduct the director nomination process and assess the qualifications and independence of director candidates. This committee should establish factors to be considered in evaluating prospective director nominees and in evaluating directors for membership on board committees, taking into account the circumstances and businesses of the banking organization, the responsibilities of the various committees, and the importance of having appropriate diversity, expertise and experience among board members.**

b) **The board of the top-tier entity within a banking organization should have a committee, composed entirely of independent directors, with responsibility for corporate governance, including responsibility for the board self-evaluation process and advice and, if determined to be appropriate to a banking organization's particular circumstances, assistance to the board in overseeing the entity's corporate**

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162 Exchange Act Rule 10A-3.

163 NYSE Manual, Section 303A.06; NASDAQ Rules, Section 5605(c)(2).

164 12 C.F.R. § 363.5(b); *see also* Comptroller's Handbook, "Internal and External Audits," at 9 ("The audit committee of any bank with more than $3 billion in total assets . . . must include members with banking or related financial management expertise."). Similarly, pursuant to rules adopted by the national securities exchanges, members of the audit committee of a public company generally must be "financially literate" and at least one member of the audit committee must have "accounting or related financial management expertise" (as such terms are interpreted by the board in its business judgment). *See* NYSE Manual, Section 303A.07 (commentary).

165 Regulation S-K, Item 407(d)(5)(ii).

governance structures, processes and performance.

c) **The nominating and corporate governance committee functions may be joined together, may be undertaken by separate independent committees or may be apportioned to independent committees that have other functions.**

Commentary:

Pursuant to the rules of the national securities exchanges, public companies generally are required to have a nominating committee composed entirely of independent directors.[166] According to the OCC, the nominating committee's responsibilities generally include "recommending nominees for election to the board" and "reviewing and approving a management succession policy and plan for senior management positions."[167] The nominating committee may also consider re-nominations of existing directors. The NYSE listing standards contemplate that this committee also will oversee corporate governance matters, though they indicated that it is acceptable for an organization to have separate committees discharging these functions, so long as each committee is composed of independent directors.[168]

Because the holding company controls the voting securities of the subsidiary bank and establishes the corporate governance practices for the whole organization, it is customary, and BPI believes it is appropriate, for there to be no separate nominating/corporate governance committee at the wholly owned subsidiary bank level irrespective of the degree or absence of overlap between the holding company and subsidiary boards.

Qualifications of Directors

Federal and state banking statutes prescribe certain citizenship and residency requirements for directors of banks but not bank holding companies. For instance, directors of national banks must generally be U.S. citizens, and a majority of the directors must have resided in the state, territory, or district in which the bank is located, or within 100 miles of that location, for at least one year immediately prior to election to the board and during their continuance in office (though the OCC may, in its discretion, waive the residency requirement and, in the case of not more than a minority of the total number of directors, the citizenship requirement).[169] Besides complying with these basic requirements, all banking organizations should strive to have directors with qualifications and experience to exercise sound judgment and oversee the affairs of the organization. The duty of director nomination is critical because the ultimate determinant of effective corporate governance consists of the quality, skills and expertise of the individuals who comprise the board and the management of the banking organization.

Ordinarily, the nominating/corporate governance committee of the board should establish, or recommend to the board, the parameters for qualifications of directors. Typically, these do not consist of objective qualifications or disqualifications but rather lists of factors that the committee should use to assess candidates,[170] including age and tenure, diversity, expertise, experience, and time commitment and other directorships, as discussed further in Section 3 and this section. Bank regulators have set out general considerations regarding the qualifications of directors of banking organizations. For instance, the OCC expects the qualifications of directors of national banks

166 NYSE Manual, Section 303A.04; NASDAQ Rules, Section 5605(e)(1)(B).

167 OCC Director's Book, at 101; *see also* ABA Guidebook, at 97 (noting that the nominating and governance committee is "responsible for recruiting and maintaining board members").

168 For convenience, we refer in these Guiding Principles to a "nominating/corporate governance committee" because most organizations combine these functions. If these functions are performed by separate committees, the committees should coordinate as appropriate. *See* NYSE Manual, Section 303A.04.

169 12 U.S.C. § 72; *see also* N.Y. Banking Law § 7001(2)(a) ("At least one-half of the directors of a bank or trust company, stock form savings bank, or stock form savings and loan association must be citizens of the United States at the time of their election and during their continuance in office.").

170 *See* OCC Director's Book, at 101 (describing the role of the nominating/corporate governance committee in recommending nominees for election as directors); NYSE Manual, Section 303A.04 (stating that the nominating/corporate governance committee must have the responsibility to "identify individuals qualified to become board members, consistent with criteria approved by the board").

to include:

- basic knowledge of the banking industry, the financial regulatory system and the laws and regulations that govern the operation of the institution;
- willingness to put the interests of the bank ahead of personal interests;
- willingness to avoid conflicts of interest;
- knowledge of the communities served by the bank;
- background, knowledge and experience in business or another discipline to facilitate oversight of the bank; and
- willingness and ability to commit the time necessary to prepare for and regularly attend board and committee meetings.[171]

Similarly, the Basel Committee recommends that boards of banking organizations be "comprised of individuals with a balance of skills, diversity and expertise, who collectively possess the necessary qualifications commensurate with the size, complexity and risk profile of the bank."[172] The Basel Committee adds that the board of a banking organization should include directors who collectively have "a range of knowledge and experience" in areas such as "financial and capital markets, financial analysis, financial stability, strategic planning, risk management, compensation, regulation, corporate governance and management skills."[173] The nominating/corporate governance committee should take into account factors such as the ones recommended by bank regulators and also establish parameters for qualifications based on the particular circumstances and businesses of the banking organization. As noted by the ABA, "there is no one-size-fits-all approach to director searches."[174]

The parameters established by the nominating/corporate governance committee should address the independence concerns discussed in Section 2 and also help the board develop an appropriate level of diversity.

The nominating/corporate governance committee should focus on the strengths and weaknesses of the organization, its board and board committees, and its strategic objectives and/or plans, and establish parameters that will attract director candidates who can provide needed additional talent and experience that will advance the governance and development of the organization.[175] When considering director candidates, the nominating/ corporate governance committee also should consider the candidate's compatibility with the organization's corporate culture and strategic objectives, as well as any criteria applicable to board committee membership, such as identifying a director who qualifies as an "audit committee financial expert" for the audit committee and a director with risk management expertise for the risk committee.[176] The nominating/corporate governance committee should consider whether a candidate for director nomination or re-nomination can commit the necessary time to satisfy director responsibilities; in this regard, the committee or the board may wish to consider adopting policies requiring directors to inform the company of a change in principal occupation or business association or of intentions to serve on a board or in an executive position of another company.[177] An increase in a director's time commitments outside the banking organization should not automatically or reflexively be viewed as a negative factor, as serving on multiple boards may also bring more experience and broader perspectives, which

171 OCC Director's Book, at 15-16.

172 Basel Principles, at 13.

173 *Id*.

174 ABA Guidebook, at 99.

175 *Id*.

176 *Id*. at 98-99.

177 *See* OCC Director's Book, at 16-17; Basel Principles, at 13.

may further the director's ability to contribute to board decision-making.

The evaluation of a banking organization's director retirement policy also is generally under the purview of the nominating/corporate governance committee.[178] Some banking organizations provide that directors may not be re-nominated upon reaching a specific age (*e.g.*, 72 or 75), which may or may not be subject to waiver by the board or a committee. Banking organizations should determine, based on their own circumstances, whether a retirement age policy is appropriate and how any such policy is implemented. Any such policy, however, should not unduly limit the ability of the board to recruit or retain directors with the experience and attributes that the board desires as part of the overall mix of directors. Many boards that have set retirement ages have, from time to time in appropriate circumstances, determined that it was justifiable to waive the requirement or increase the retirement age in light of a desire to maintain the right mix of skill sets and experience on the board.

BPI does not believe that a banking organization should have term limits for individual directors—that is, limits on overall duration of service for individual directors—or specific requirements for average director tenure. The nominating/corporate governance committee should have the flexibility to determine whether a particular director is continuing to contribute to the strength and diversity of the board or whether the board would benefit from the introduction of new directors in place of existing directors.[179] As the ABA has further noted, a "well-functioning nominating committee should be able to decline to nominate incumbents for reelection as individual situations dictate."[180] Nominating/corporate governance committees should actively consider, in assessing director nominations and re-nominations, whether the board has the right mix of company-specific experience and new insight to function most effectively, and whether changes in the organization's strategies, business, risk environment, technology or otherwise have created a need for a partial change in board constituency.

In addition, the nominating/corporate governance committee should be the "conduit for communication regarding shareholder recommendations for director nominees."[181] Although not required by the SEC rules, many public companies have implemented proxy access bylaw provisions enabling shareholders holding a specified percentage of shares to nominate director candidates using the company's proxy statement (subject to restrictions adopted by each company). The nominating/corporate governance committee will, in many cases, play a key role in formulating a public company's response to proxy access proposals and the evaluation of any nominees put forth under any proxy access bylaws that may be put in place at the company.

Director Education and Training

Typically, the nominating/corporate governance committee also is charged with the responsibility of overseeing the creation of director education and training programs.[182] As recommended by the Basel Committee, directors should be and remain qualified, including through training, for their positions.[183] Accordingly, directors should commit adequate time and effort to continuing training and education programs in order to stay abreast of the environment in which their banking organization operates, general industry trends and any statutory and regulatory developments pertinent to their organization. The FDIC Pocket Guide notes that such programs are particularly important in light of the fast-changing regulatory environment in which banking organizations operate and suggests that the board consider creating formal director education seminars.[184] These programs need not be

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178 *See* ABA Guidebook, at 105.

179 *See* Organisation for Economic Co-operation and Development, Corporate Governance Factbook (2019), at 119 (noting that a minority of jurisdictions deem the tenure of a public company director to impact independence).

180 *Id*. at 100.

181 *See* ABA Guidebook, at 101 & 104.

182 *See* ABA Guidebook, at 104.

183 Basel Principles, at 14; *see also* NYSE Manual, Section 303A.09 (requiring U.S. listed companies to address director education and training programs in their company governance guidelines).

184 *See also* OCC Director's Book, at 21 (noting that directors should stay informed of industry trends and regulatory developments, particularly those regarding their bank); Basel Principles, at 14 (noting that directors should have access to programs of tailored initial and ongoing education on relevant issues and that directors should delegate sufficient time,

conducted exclusively or even principally by third parties; presentations to the board by members of management and other employees of the organization on important business, regulatory, compliance or other matters can be an excellent mechanism for director training because these presentations can focus on the specific institution and its issues (as opposed to more general education programs). For example, a number of firms are offering directors annual training on cyber risks facing the firm and the broader industry and some offer optional deep-dives on the subject in advance of quarterly board meetings.[185]

Federal bank regulators expect boards of banking organizations to receive regular training in order to maintain an effective compliance program. Some of these supervisory expectations prescribe granular training topics that blur the line between the oversight role of the board and the role of management in having responsibility for the day-to-day operations of a banking organization. For example, the Consumer Financial Protection Bureau's (the "CFPB") examination manual expects that the board understand the "entity's responsibilities and the commensurate resource requirements" and that the board be knowledgeable about specific consumer protection laws[186]; the OCC expects that the board of the bank holding company receive anti-money laundering training.[187] Although BPI agrees that directors should consider the need for updated, refocused and/or expanded director education and training to remain appropriately knowledgeable about key matters and developments for purposes of carrying out their oversight responsibilities, boards should have the flexibility to determine the nature, frequency, focus and scope of training programs and materials, consistent with the oversight role of the board.

Training programs oriented to bank directors offered by bank regulators, trade organizations, or other parties can be an efficient and effective way for directors of banking organizations to keep up with recent developments relevant to their oversight role.

Qualifications of Members of Board Committees

In addition to setting the qualifications for directors, the nominating/corporate governance committee also should establish the qualification standards for the various committees of the board in light of the duties and functions of such committees. In doing so, the nominating/corporate governance committee should seek to develop parameters for qualifications of committee members that comply with the requirements prescribed by statute, regulation and regulators for the particular committee (in particular, the audit and risk committees).

Board Evaluations and Oversight of Corporate Governance

In addition to the nominating/corporate governance committee's traditional role of recommending candidates for directors, this committee increasingly has been charged with the task of developing corporate governance policies

budget and other resources for this purpose); OCC Heightened Standards, at 127 (requiring the boards of directors of certain large national banks to establish formal, ongoing training programs for all directors that include trainings on complex products and significant risks).

185 The Cybersecurity Report, supra note 77.

186 In examinations, CFPB will review the schedule, record of completion, and materials for recent compliance training of board members, including samples of training materials related to fair lending, new or changed regulatory requirements, etc. *See* CFPB Supervision and Examination Manual (updated August, 2019), CMR 8-9, ECOA 8 (including as an evaluation item whether board of directors receives fair lending training).

187 OCC Director's Book, at 21. A recently proposed interagency policy statement by the OCC and other federal banking regulators on the allowances for credit losses ("ACLs") has set expectations for the board to be involved in granular aspects of the ACL-determination process, requiring, for example, that the board "review[] and approv[e] the institution's written loss estimation policies" and any revisions thereto at least annually, "review[] management's assessment of the loan review system and management's conclusion and support for whether the system is sound and appropriate," and "review[] management's assessments of and justifications for the estimated amounts reported each period for the ACLs and the [provisions for credit losses]." Interagency Policy Statement on Allowances for Credit Losses, 84 Fed. Reg. 55,510, 55,520 (Proposed October 17, 2019).

and practices for the banking organization.[188] Because director selection is so central to an organization's corporate governance, it is common for the committee that is tasked with nominating directors also to be tasked with responsibility for board evaluations and oversight of the entity's corporate governance generally, including responding to shareholder proposals under Exchange Act Rule 14a-8 and discussing with management any general changes or trends in governance procedures. As noted above, if these functions are performed by separate independent committees, the committees should coordinate as appropriate.

The nominating/corporate governance committee should develop a system for "formal and rigorous evaluation" of the performance of the board and its committees.[189] These performance evaluations, which might or might not utilize third-party consultants or facilitators, should be designed to assess the effectiveness of the board and its committees in performing their oversight functions. As the Basel Committee explains, an assessment of the board's effectiveness "aims to determine the extent to which the board…demonstrate[s] effective behaviour[] that contribute[s] to good governance."[190] Such an assessment could include, for example, consideration of how successfully the board communicates and demonstrates the "tone at the top" and the ethical and cultural values of the bank, the opportunity for candid and informed communication among directors, how effectively the board interacts with management, the extent to which the board understands and takes into consideration the organization's strategic goals and business objectives and the extent to which the board has access to appropriate information that allows it to exercise its responsibilities. Information flow to the board, which includes consideration of the timeliness with which the board receives material information, and the pertinence and understandability of such information, is an important element of corporate governance effectiveness. Ultimately, the particular circumstances of the board and the organization should inform the focus, form and content of board evaluations. BPI believes, however, that the number of follow-up items coming out of a self-assessment is not an indicator of board effectiveness and that the effectiveness of a board cannot be measured by that or any similar quantitative metric.

The board and the audit, compensation and nominating/corporate governance committees of public companies generally conduct annual performance evaluations, which in some cases are required pursuant to the rules of the national securities exchanges.[191] Any board evaluation process should be appropriately organized, conducted and documented to avoid creating a misleading, and potentially harmful, record. For example, the use of written questionnaires, if not properly managed, may create a record that does not accurately reflect the overall views of a director and could be taken out of context. As an alternative, boards and committees may want to structure the evaluation as an open discussion with individual directors of issues relating to board or committee performance, which ultimately is summarized in a brief report. Interviews also are becoming an increasingly popular method of board and committee evaluation. Although not required, some boards also have begun to incorporate individual director evaluations.

Self-assessment practices appropriately vary among banking organizations, may vary from year to year and may involve a combination of evaluation methods, as the assessments are intended to serve as a tool for individual boards themselves and not for supervisory purposes.[192] Although regulators may ask and discuss with the board

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188 *See* OCC Director's Book, at 101 ("At many banks, the corporate governance/nominating committee duties involve . . . overseeing the bank's corporate governance practices…."); ABA Guidebook, at 102 & 104-05 (noting the committee's expanded role in addressing corporate governance principles and practices).

189 Walker Review, at 16.

190 Basel Principles, at 39.

191 *See* NYSE Manual, Section 303A; *see also* OCC Heightened Standards, at 128 (the boards of directors of certain large national banks should perform annual self-assessments that include evaluations of their effectiveness in meeting the standards in the OCC Heightened Standards).

192 Different approaches are typically taken by banks to foster an appropriate level of candor and self-reflection. For example, some organizations may solicit feedback in written form, and others may provide a discussion guide or questionnaires to facilitate one-on-one discussion and feedback with a chair or lead director. Some may provide a high-level summary of results in board materials, and others may have the chair or lead director lead a discussion among board members in executive session to discuss the results. It is critical that the self-assessment process remain flexible so that the process itself, areas of focus and the like can change over time depending upon the relevant facts and circumstances.

whether boards have conducted self-assessments and/or found them helpful, regulators should not be involved in the self-assessment process, because the involvement could create a chilling effect and potentially reduce this process to an auditable compliance procedure. Requiring, or expecting (even if only implicitly), a board's self-assessment to take a particular form or cover a prescribed set of issues or to be used for supervisory evaluations would be contrary to the core objectives of a self-assessment (*i.e.*, a candid assessment of how the board sees itself and areas for potential improvement), and may create another "check-the-box" requirement for boards.[193] In particular, BPI believes that requiring or expecting self-assessment results to be provided to supervisors could have a chilling effect on the responses of directors (*i.e.*, board members may not be as open and frank as they might otherwise be), particularly if self-assessment results would be used as a basis for supervisors' evaluation of the board's effectiveness or could otherwise be taken out of context or end up in the public domain. BPI also believes that such requirements or expectations could inhibit the particular forms of self-assessment currently employed by firms and lead to a "one-size-fits-all" approach based on the minimum expected level.

SECTION 8. COMPENSATION COMMITTEES AND BOARD OVERSIGHT OF EXECUTIVE COMPENSATION

Principles:

a) **The board of the top-tier entity within a banking organization should have a compensation committee, composed entirely of independent directors, to review and approve the compensation of the CEO and to oversee the compensation of other senior executives and the development of compensation programs that attract and retain highly qualified executives and other employees, satisfy regulatory standards and discourage inappropriate risk taking.**

b) **The compensation committee should have an understanding of compensation practices in the financial services sector and should review and approve compensation practices that appropriately balance risk and reward (with input from the chief risk officer and the risk committee, as appropriate) and take into account compliance performance and ethical behavior.**

Commentary:

The compensation committee of the board typically is responsible for determining the compensation of the CEO and for reviewing (or making recommendations to the board with respect to) the compensation of other senior executives of the banking organization. The compensation committee may also oversee the compensation and benefit programs for all the employees of the organization. Public companies generally are required to have a compensation committee composed entirely of independent directors pursuant to rules adopted by the national securities exchanges.[194]

In the aftermath of the financial crisis of 2008, the compensation policies of banking organizations became a subject of increased focus among regulators and commentators.[195] In June 2010, U.S. federal bank regulators issued the Guidance on Sound Incentive Compensation Policies[196] (the "Joint Guidance on Compensation"), which outlines principles aimed at ensuring that incentive compensation policies of banking organizations do not undermine their safety and soundness by encouraging employees to take imprudent risks and stresses the role of the board in overseeing the development and implementation of, and compliance with, these principles.[197] Broadly speaking, the Joint Guidance on Compensation provides that incentive compensation arrangements at banking organizations should (i) provide employees with incentives that appropriately balance risk and reward, (ii) establish

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193 *See, e.g.,* Board Effectiveness Proposal, at 37,224 (boards may voluntarily provide self-assessment results to the Federal Reserve Board).

194 *See* NYSE Manual, Section 303A.05; NASDAQ Rules, Section 5605(d)(2)(A).

195 Even prior to the financial crisis, regulatory restrictions on excessive compensation arrangements had been in place, including through the FDIA's provisions prohibiting as an unsafe or unsound practice any compensatory arrangement that would provide excessive compensation or that could lead to material financial loss to the bank. *See* 12 U.S.C. § 1831p-1(c).

196 75 Fed. Reg. 36,396 (June 25, 2010).

197 *See* Joint Guidance on Compensation, at 36,396.

and comply with effective controls and risk management practices, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board.[198] Specifically, the Joint Guidance on Compensation provides that a banking organization's board should review and approve key elements of the organization's incentive compensation system, receive and review periodic evaluations of the organization's compensation system and directly approve the incentive compensation arrangements for senior executives.[199] The Joint Guidance on Compensation also provides that the board should "have, or have access to, a level of expertise and experience in risk management and compensation practices in the financial services sector that is appropriate for the nature, scope and complexity of the organization's activities."[200]

Section 956 of the Dodd-Frank Act ("Section 956") imposes additional oversight responsibilities with respect to compensation policies on the compensation committees and boards of banking organizations that have consolidated assets of $1 billion or more. Rules to implement Section 956 were most recently proposed in 2016 but have not yet been finalized.[201] The proposed rules would prescribe granular requirements that covered financial institutions must incorporate into their compensation programs and essentially mandate a standardized, industry-wide compensation structure. BPI is of the view that financial institutions should be allowed sufficient flexibility to design a diversity of incentive compensation practices and structures that appropriately balance risk and reward and tailored to each institution's circumstances and needs; an "one-size-fits-all" approach would be counterproductive in practice and contradict the directive of Section 956, which authorizes the regulators to only *prohibit* compensation practices that are excessive or that could lead to material financial loss.

Consistent with Section 952 of the Dodd-Frank Act and SEC Rule 10C-1,[202] both the NYSE and NASDAQ have adopted rules to subject compensation committee members to enhanced independence standards. Specifically, in determining whether a director is "independent" for purposes of participation in the compensation committee, the board must consider, in addition to the general independence standards, "all factors specifically relevant to determining whether a director has a relationship to the listed company which is material to that director's ability to be independent from management in connection with the duties of a compensation committee member," including (i) the source of compensation of the director, including any consulting, advisory or other compensatory fee paid by the listed company to such director and (ii) whether the director is affiliated with the listed company or any of its subsidiaries or their affiliates.[203] The NYSE and NASDAQ rules also provide that the compensation committee may, in its sole discretion, retain a compensation adviser, and require that the compensation committee consider certain independence criteria prior to hiring the adviser.[204] Under the SEC rules, listed companies also are required to disclose retention of compensation consultants and conflicts with compensation consultants.[205] However, there is no requirement that the compensation committee retain compensation consultants, and each banking organization's compensation committee should determine whether and when a

198 *See id*. at 36,398. *See also* OCC Heightened Standards, at 215 & 126 (certain large national banks are required to establish a compensation and performance management program that, among other things, prohibits "incentive-based payment arrangements, or any feature of any such arrangement, that encourages inappropriate risks by providing excessive compensation or that could lead to material financial loss"). *See also* SR 12-17 (addressing expectations for large financial institutions relating to incentives and compensation arrangements).

199 *See* Joint Guidance on Compensation, at 36,412.

200 *Id*. at 36,402. *See also* Walker Review, at 118-19 (noting that risk adjustment in remuneration structure is essential to counterbalance any executive disposition to increase risk as the means of increasing short-term returns, and suggesting that the remuneration committee should seek advice from the risk committee on specific risk adjustments to be applied to performance objectives set in the context of incentive packages).

201 *See* Incentive-Based Compensation Arrangements, 81 Fed. Reg. 37,670 (Proposed June 10, 2016).

202 *See* 17 C.F.R. § 240.10C-1.

203 NYSE Manual, Sections 303A.05(a) & 303A.02(a)(ii); NASDAQ Rules, Section 5605(d)(3).

204 NYSE Manual, Section 303A.05(c); NASDAQ Rules, Section 5605(d)(2)(A). The compensation committee is not required to assess independence in the case of a compensation adviser that merely consults on broad-based plans or provides non-customized or issuer- specified information. *Id*.

205 *See* Item 407(e)(3)(iii) & (iv) of Regulation S-K.

consultant is appropriate for its own organization.

Bank regulatory guidance places particular emphasis on the relationship between compensation and risk taking. As the Basel Committee recommends, the compensation in banking organizations "should be in line with the business and risk strategy, objectives, values and long-term interests of the bank."[206] Regulators also are increasingly focusing on the process of determining compensation for staff engaged in financial and risk control (including audit, risk management and compliance). For instance, the Financial Stability Board (the "FSB") advises that staff engaged in financial and risk control should be compensated in a manner that is independent of the business areas they oversee.[207] In particular, the FSB Principles indicate that risk control employees play an important role in preserving the integrity of the financial and risk management, and hence their compensation should not be influenced by personnel in front line business areas.[208] In addition, the compensation of risk control employees should not be so affected by short-term performance measures such that their independence could be compromised.[209] More informally, U.S. regulators are emphasizing that absolute and relative compensation of staff in these areas should be sufficient to attract and retain qualified personnel. The Federal Reserve Enhanced Standards require that the compensation of the chief risk officer (of bank holding companies with total consolidated assets of $50 billion or more) be appropriately structured to provide for an objective assessment of the risks taken by the bank holding company.[210]

The compensation committee of the top-tier entity within a banking organization should have access to financial, legal and risk management experts, which may be internal or external as the committees may determine, to enable them to monitor and implement the developing regulatory requirements in this area. The interaction between the boards of the holding company and the bank in making compensation decisions (including whether the bank itself should have a compensation committee and what role the bank board should have in the overall compensation process in order to protect the safety and soundness of the bank) will, subject to any applicable statutory or regulatory requirements,[211] depend on the overall structure of the banking organization and will likely vary from organization to organization.

As discussed above, a compensation committee would typically oversee a banking organization's compensation and benefit programs for all the employees of the organization. In connection with that oversight, this committee may consider the organization's "human capital" resources, as appropriate, and how the organization monitors, develops, and deploys those resources, including in connection with talent management. Like technological transformation, environmental impact, and sustainability initiatives, human capital resource management is among the topics that have received increasing attention in the recent years in light of developments at banking organizations and in the wider environment.

SECTION 9. RISK COMMITTEES AND BOARD OVERSIGHT OF RISK MANAGEMENT

Principles:

a) **The board of the top-tier entity within a banking organization should have a committee to oversee its risk management systems and control procedures for identifying, assessing and managing its risk exposures, and to oversee the organization's adherence to the agreed risk profile.**

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206 Basel Principles, at 34; *see also* OCC Director's Book, at 100 and Joint Guidance on Compensation, at 36,398.

207 *See* FSB, Principles for Sound Compensation Practices (April 2, 2009) ("FSB Principles"), at 7.

208 *Id*.

209 *Id*.

210 *See* Revised Prudential Standards, at 59,103; 12 C.F.R. § 252.33(b)(3)(i). *See* Section 4 for a further discussion of the chief risk officer requirement under the Federal Reserve Enhanced Standards.

211 *See*, *e.g.*, OCC Heightened Standards, at 113 & 114 (the boards of directors or board committees of certain large national banks are required to approve the annual compensation and salary adjustment of the chief risk and chief audit executive).

b) This committee should include at least one member with substantial risk management knowledge and experience.

Commentary:

In recent years, bank regulators have increasingly emphasized the importance of risk management within banking organizations and the role of the board in that process. For instance, the Basel Committee states, "[r]isks should be identified, monitored and controlled on an ongoing bank-wide and individual entity basis…[and the] sophistication of the bank's risk management and internal control infrastructure should keep pace with changes to the bank's risk profile, to the external risk landscape and in industry practice."[212] Some commentators caution, however, that the creation and role of a risk committee should not "take the place of the ultimate responsibility and accountability of the whole board for the governance of risk."[213]

The Dodd-Frank Act imposed additional risk management responsibilities on the board of directors. The Federal Reserve Enhanced Standards require bank holding companies with total consolidated assets of $50 billion or more to establish a standalone risk committee that approves and periodically reviews the enterprise-wide risk management policies and oversees the company's enterprise-wide risk management framework.[214] The risk committee for bank holding companies with total consolidated assets of $100 billion or more also is subject to certain liquidity risk management requirements.[215] The Federal Reserve Enhanced Standards require the risk committee to be chaired by an independent director,[216] and the Federal Reserve Board encourages companies to include additional independent directors on the committee.[217] The Federal Reserve Enhanced Standards do not, however, require that the committee be composed solely of independent directors, and some banking organizations may determine that it is appropriate to include in the committee a management director with the risk management expertise.

The risk committee is required to include at least one member with "experience in identifying, assessing, and managing risk exposures of large, complex financial firms"[218] (similar to the definition for purpose of the chief risk officer as described in Section 4). For organizations not covered by this specific regulatory mandate, the board might conclude that experience with a suitably complex non-financial firm provides an appropriate level of risk management expertise for purposes of the risk committee's functions. In addition, the Federal Reserve Board has expressed its expectation that all members of the committee generally should have an understanding of risk management principles and practices relevant to the company.[219]

As a general governance matter, BPI believes that, subject to any relevant regulatory constraints, it should be acceptable, and the board may determine that it is preferable, for the audit and risk functions to be combined into a single committee if the focus and effectiveness of the committee are not undermined and the members meet all relevant independence and qualification criteria. Similarly, the board may determine that elements of risk oversight relating to particular areas, such as technology, compliance, reputation, compensation, corporate responsibility, financing or credit exposures, among others, are best housed within committees that focus on these areas, so long as the overall board structure provides for appropriate enterprise-wide risk oversight. For example, while risk and audit committees are the primary committees with oversight of cybersecurity risks, some firms are

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212 Basel Principles, at 27.

213 Walker Review, at 90.

214 *See* Revised Prudential Standards, at 59,102; 12 C.F.R. § 252.33(a).

215 Revised Prudential Standards, at 59,103-04; 12 C.F.R. § 252.34.

216 Revised Prudential Standards, at 59,103; 12 C.F.R. § 252.33(a)(4).

217 Federal Reserve Board, Proposed Enhanced Prudential Standards and Early Remediation Requirements for Covered Companies, 77 Fed. Reg. 594, 623 (January 5, 2012).

218 Revised Prudential Standards, at 59,103; 12 C.F.R. § 252.33(a)(4).

219 Original Prudential Standards, at 17,249.

establishing a technology committee to provide greater focus and help integrate oversight of cyber risk and resilience with discussions around strategic technology investment and innovation.[220] A board may also determine, depending on the committee structure and the organization's particular circumstances, that the same committee or different committees are best suited to oversee and address processes and controls designed to identify and manage risks, on the one hand, and specific risk incidents, on the other.

The board has a distinct role from that of management in liquidity risk management. Although the board is responsible for reviewing and approving top-tier liquidity policies, management is responsible for the day-to-day implementation of the specific policies and stress testing. The board should also retain the flexibility to delegate any liquidity risk management responsibility to its risk committee. In this regard, rather than a full-board review, BPI believes that the board may appropriately delegate review and approval responsibilities for the liquidity-related matters set forth in Regulation YY to the risk committee.[221]

Because the Federal Reserve Enhanced Standards will not permit bank holding companies with total consolidated assets of $50 billion or more to combine their risk committees with any other committees, these large bank holding companies should arrange appropriate coordination among board committees, possibly including joint members or periodic joint meetings as appropriate, so that the company's financial reporting, internal control, risk management and other relevant areas are considered together. The Federal Reserve Board specifically noted in the preamble to the 2014 Federal Reserve Enhanced Standards adopting release that it is acceptable for a risk committee to have members that are on other board committees, and that other board committees may be involved in establishing the banking organization's risk management framework.[222] In fact, NYSE rules require the audit committee of a listed company to maintain some oversight over the company's risk management.[223]

In addition to the Dodd-Frank Act requirements, regulations promulgated by the SEC contain a number of disclosure requirements that address risk and thus require a public company, including a public banking organization, to evaluate and describe its risk structure. A public company must disclose in its annual proxy statement its policies and practices of compensating its employees and management as they relate to the risk profile of the organization if the risks arising from these compensation policies are reasonably likely to have a material adverse effect on the organization.[224] Public companies also are required to disclose the extent of the board's role in risk oversight.[225] Thus, in light of the interrelation between compensation policy and risk management, the risk and compensation committees should appropriately coordinate efforts so that the compensation programs satisfy regulatory standards and do not encourage inappropriate risk taking.[226]

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220 Cybersecurity Report, supra note 77, at 6.

221 Regulation YY requires that the full board of directors: (i) approve the acceptable level of liquidity risk that the bank holding company may assume in connection with its operating strategies at least annually, taking into account the bank holding company's capital structure, risk profile, complexity, activities, and size, (ii) receive and review at least semi-annually information provided by senior management to determine whether the bank holding company is operating in accordance with its established liquidity risk tolerance and (iii) approve and periodically review the liquidity risk management strategies, policies and procedures established by senior management. 12 C.F.R. § 252.34(a).

222 *See* Original Prudential Standards, at 17,250. The preamble to the original Federal Reserve Enhanced Standards also states that the rule does not prevent a parent company's risk committee from serving as the risk committee for one or more of its subsidiaries as long as the requirements of the rule are otherwise satisfied. The board may determine that the risk committee maintain oversight relating to any or all particular categories of risk (in addition to or as part of its enterprise-wide risk management responsibilities), subject to any relevant legal constraints.

223 *See* NYSE Manual, Section 303A.07(b)(iii)(D).

224 *See* Item 402(s) of Regulation S-K.

225 *See* Item 407(h) of Regulation S-K. In the context of cybersecurity risks, the SEC stated that, to the extent cybersecurity risks are material to a company's business, the disclosure of a board's risk oversight function should include the "nature of the board's role in overseeing the management of cybersecurity risk." In addition, the SEC expects companies to include a discussion on how the board engages with management on cybersecurity issues in the disclosure. Commission Statement and Guidance on Public Company Cybersecurity Disclosures, Securities Act Release No. 33-10459, 17-18 (February, 2018).

226 *See* Basel Principles, at 17-18 (suggesting that the compensation committee work closely with the risk committee to evaluate incentives arising from compensation); *see also* 12 C.F.R. § 252.33(a) (requiring the risk committee to oversee the operation

SECTION 10. INDEPENDENT LEADERSHIP OF THE BOARD

Principles:

The board should determine its own form of independent leadership. The board may determine to have an independent director, the CEO or another non-independent director as the chairperson. If the board determines that the CEO or another non-independent director should serve as chairperson, the independent directors of the board should designate, among themselves, a lead independent director. The lead director should generally have authority to:

- **a) Work with the chairperson to approve the agenda and schedule for each board meeting and the information to be provided to the board (board materials and board presentations);**
- **b) Convene and chair regular and special executive sessions of the board (*i.e.*, sessions where no member of management, including the CEO, is present); and**
- **c) Review and report on results of board self-evaluations.**

Commentary:

The chairperson of the board plays a crucial role in the functioning of the board. The chairperson provides leadership to the board and aids the board in functioning effectively and meeting its obligations and responsibilities.[227] As the Basel Committee further explains, "[t]he chair should ensure that board decisions are taken on a sound and well informed basis. The chair should encourage and promote critical discussion and ensure that dissenting views can be freely expressed and discussed within the decision-making process."[228]

In the United States, it is common for the CEO of a corporate entity also to serve as the chairperson.[229] The ABA notes, however, that in a growing number of public companies, the two functions are separated.[230] It has been suggested that separation helps to establish appropriate "checks and balances" between the board and management.[231] On the other hand, many organizations have determined that separation can cause inefficiencies, and even friction, between the board and management, and that there are significant benefits to having the CEO, who is closest to the day-to-day operations and risk environment, initially formulating the board agenda, with appropriate independent director input and feedback. While it is somewhat more common in certain non-U.S. jurisdictions to have an independent chairperson, most jurisdictions still allow companies to decide for themselves whether to have an independent chairperson, recognizing that there is no universal "right answer" to such question.[232] Board leadership structures have evolved over time, and it is the view of BPI that the board should have the flexibility to determine its leadership structure and that it would be a mistake for overly prescriptive regulation to impede this process of evolution by limiting flexibility (*e.g.*, by requiring the separation of the CEO and the chairperson and/or the independence of the chairperson).

The board of a banking organization should determine whether its CEO should be the chairperson of the board

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of an enterprise-wide risk management framework, including integration of risk management and control objectives in management goals and the company's compensation structure).

227 *See* Basel Principles, at 15.

228 *Id.*

229 *See* ABA Guidebook, at 46 ("For many public companies in the United States, the CEO of the corporation also serves as chair of the board."); NACD key Agreed Principles, at 8 (noting that "some form of independent leadership is required, either in the form of an independent chairman or a designated lead or presiding director").

230 ABA Guidebook, at 46.

231 Basel Principles, at 13.

232 *See* Organisation for Economic Co-operation and Development, Corporate Governance Factbook (2019), at 118 (noting that 30% of jurisdictions require separation of chairperson and CEO roles at public companies, and an additional 40% encourage it).

based on its unique circumstances and needs. For example, the board of one banking organization may determine that its CEO should serve as the chair because of his or her leadership abilities and other qualifications. Conversely, the board of another banking organization may select an independent director to serve as the chair because of his or her knowledge, experience and reputation. Thus, banking organizations may choose to separate or combine the positions of CEO and chairperson for a variety of reasons, and there can be no single prescription that serves all banking organizations.[233] A public company is required to disclose in its annual proxy statement the reasons why it has chosen the same or different people to serve in the positions of chairperson and CEO. Furthermore, if the same person serves as both CEO and chairperson, the company must disclose whether it has a lead independent director and what specific roles the lead director plays in the leadership of the board.[234]

BPI recognizes that some banking organizations have adopted a governance structure that separates the role of the CEO from the role of the chair, with the chairperson being an independent director. Under this structure, the chairperson should have the authority to preside at all meetings of the stockholders of the banking organization and of the board and to exercise further powers as may be conferred upon him or her by the board or as may be provided by law.

If the board determines that it is advisable to combine the positions of CEO and chairperson, or to otherwise appoint a non-independent director as the chairperson, then, as a matter of good corporate governance, BPI believes that, absent a compelling reason to the contrary, the independent directors of the board should designate, among themselves, a lead independent director.[235] The lead director should work with the CEO to approve the agenda and schedule for each board meeting and to review the types of information to be distributed to the board and its committees for their consideration.[236] He or she also may be called upon by the board or by senior management to meet with shareholders or shareholder groups that wish to convey concerns to the board. If these meetings are held, the full board should be promptly informed of those communications.[237] The lead director should be available to serve as the board's liaison to the CEO and facilitate communication between them.[238]

The lead director will ordinarily be charged with the duty to chair executive sessions of the board. Executive sessions are meetings attended solely by independent directors and are designed to allow for open discussion of management without the presence of management directors.[239] In the United States, listed companies are required to hold executive sessions of independent directors on a regularly scheduled basis.[240] The use of executive sessions by the board is advisable, as executive sessions can provide a forum for independent directors to bring up ideas or raise issues that they may otherwise be reluctant to raise in front of the non-independent directors and to share candid views about management's performance and board operations.[241]

In the United States, the same fiduciary duties apply to all directors. Although different directors may have different roles on the board (such as serving as the chairperson, the lead director, or a committee chair), or different areas of expertise, a director would not be subject to heightened or different duties on the basis of his or

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233 *See* ABA Guidebook, at 46 (noting that there is no one-size-fits-all prescription and that the board should thus decide what works best for its organization).

234 *See* Regulation S-K, Item 407(h).

235 *See* ABA Guidebook, at 46 (noting that, when a non-independent director or the CEO serves as the chairperson, the independent directors often designate, among themselves, a director to act as a lead director).

236 *Id.*

237 *Id.*

238 *Id.*

239 Under the NYSE rules, the executive sessions also may include non-independent directors who are not members of management, so long as the independent directors meet at least annually in executive session with no non-independent directors present. NYSE Manual, Section 303A.03.

240 *See*, *e.g.*, NYSE Manual, Section 303A.03 and NASDAQ Rules, Section 5605(b)(2).

241 *See* ABA Guidebook, at 50.

her role or expertise.

SECTION 11. AGENDA, MATERIALS AND LENGTH OF MEETINGS

Principles:

a) **The agenda for each board and committee meeting should list the subjects that are expected to be discussed at the meeting.**

b) **Although board and committee meetings generally should follow the agenda, some flexibility may be necessary or appropriate to discuss matters that, because of the time at which they arose or for other reasons, are not listed on the agenda.**

c) **Materials for board and committee meetings (including the agenda) should be provided to directors sufficiently in advance of meetings, and should contain sufficient detail to enable the directors to prepare appropriately. It is recognized, however, that circumstances may necessitate shortening this time period on occasion. Directors are expected to have read board and committee materials that were provided in advance.**

d) **Board meetings should include presentations by senior management, other employees of the company and advisors, as appropriate, covering major business, financial performance, risk and control, and legal and compliance matters. Committee meetings should include presentations tailored to the needs of the committee from time to time. Significant time should be reserved for board and committee discussions. Directors should devote sufficient time in a meeting to address all agenda subjects and such other subjects as may be brought to their attention.**

e) **Although board and committee meetings of banking organizations are traditionally conducted in person and in-person meetings have some advantages, boards of banking organizations should conduct meetings in the format that the board considers appropriate and effective, to the extent permitted by applicable laws and the entity's organizational documents.**

Commentary:

There is no "one-size-fits-all" methodology for determining what information boards should receive and how the boards should consider it. A board's approach to, and level of engagement on, particular issues and proposals will vary depending upon a number of considerations such as the criticality of the matter at issue and the comprehensiveness of prior reviews and analysis.

The agenda for each board or committee meeting generally dictates what the directors will discuss at the meeting and should therefore list each subject that is to be considered at the meeting. The duty of setting the agenda for board meetings typically is delegated to the CEO and the chairperson (or the lead director, if the chairperson is not independent), with the chairperson having the primary responsibility and coordinating with the other as appropriate.[242] In general, the agenda should be designed to address the significant issues and transactions of the organization, and generally should not include other, less important subjects, as this may distract the board from devoting time to the important matters.[243] Therefore, in formulating the agenda, the chairperson should consider whether a particular issue or transaction is important enough to merit board action or attention. In addition, any individual director who desires to participate in setting meeting agendas should be permitted to provide input on the agenda through a board or committee chair, a lead director or otherwise.[244] In this regard, banking organizations may consider establishing a formal system for gathering feedback and views regarding potential agenda subjects from individual directors. For example, a banking organization may decide to have the lead director or the independent chairperson convey information from other directors.

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242 *See* ABA Guidebook, at 47.

243 *See* Martin Lowy, Corporate Governance for Public Company Directors (2003), at 78.

244 *See* ABA Guidebook, at 47.

Although the agenda normally controls the flow and the content of the meeting, the board nonetheless can address matters not on the agenda if circumstances so warrant. For example, it may be necessary or appropriate for the board to discuss a matter that may have a significant impact on the banking organization even though it arises only after the agenda for the meeting already has been established and is, therefore, absent from the agenda.

Furthermore, the organization should consider preparing an annual schedule that includes matters requiring recurring and focused attention, such as periodic review of the banking organization's financial and operational plans, risk management, evaluation of the performance of the management and board, legal and compliance matters and the adequacy and appropriateness of corporate systems and controls.[245] Subject to applicable regulatory requirements, the board should have flexibility in determining the issues addressed at meetings and the items that will require board review or approval. The board should, in one form or another, articulate an approach for determining which matters should be addressed at the board level, so that individual board members and senior management are aware of, and operate consistently with, the board's expectations.

Materials for Meetings

Comprehensive and quality information is critical for the board to function effectively, and for the directors to meet their duty of care. As the ABA notes, the quality of the information made available to directors will significantly affect their ability to perform their roles effectively.[246] Accordingly, materials for a board meeting should contain material and accurate information regarding all the subjects on the agenda but should not be so voluminous that they detract from effective discussion and deliberation during meetings. Thus, meeting materials often consist of written reports or summaries.[247] As mentioned in these Guiding Principles, directors are entitled to rely in good faith on summary reports, opinions, information and statements prepared by the organization's officers and employees, legal counsel and public accountants whom they reasonably believe to be reliable and competent.[248]

Meeting materials should be furnished to the directors sufficiently in advance of the meeting to allow time for careful study and thoughtful reflection, and to give directors a basis to challenge management's assumptions and recommendations, as appropriate.[249] It is recognized, however, that some circumstances may necessitate the preparation and distribution of materials to directors at short notice. Furthermore, it may be necessary and appropriate for certain sensitive information to be presented orally at a board or committee meeting, rather than being included in the materials.

When faced with a claim of a breach of duty of care by a director, courts frequently look to the adequacy of information provided to the director and the length of time the director was permitted to review such

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245 *See id.* at 47-48.

246 *Id.* at 48.

247 For example, in certain cases, such as with respect to voluminous capital plans and resolution plans, a board may determine that review of a sufficiently detailed summary or excerpts (including key assumptions and results), with access to supporting documentation, is sufficient to support board approval. *See* supra note 30 and accompanying text; *see* also OCC Handbook ("For example, instead of being inundated with technical detail, the board might request that all pre-meeting reading materials include one- to two-page executive summaries, as well as questions the directors should be prepared to address at meetings.").

248 *See*, *e.g.*, *Graham* v. *Allis-Chalmers Mfg. Co.*, 188 A.2d 125, 130 (Del. 1963); *Prince* v. *Bensinger*, 244 A.2d 89, 94 (Del. Ch. 1968).

We believe that agency pronouncements addressing board governance should reflect this important principle. *See, e.g.*, OCC Bulletin 2020-10 (March 2020) (indicating that a bank's board may use executive summaries of contracts in its review and may delegate actual approval of contracts with third parties that involve critical activities to a board committee or senior management); *see also* the OCC Heightened Standards (the board may provide active oversight by relying on "risk assessments and reports prepared by independent risk management and internal audit").

249 *See* ABA Guidebook, at 48; *see also* OCC Director's Book, at 40 (suggesting that the directors should receive the meeting materials early enough to review the information carefully before the meeting).

information.[250] Consequently, it is important, especially in the case of significant corporate transactions, other significant decisions or significant oversight issues, to provide directors with materials a sufficient amount of time in advance of the meeting. Directors in turn should review meeting materials carefully before the meeting to make certain that they are able to participate meaningfully and actively in the deliberative process.[251]

Additionally, directors should provide guidance and direction on how board materials are prepared and how information is conveyed to directors.

Regular attendance and active participation at board and committee meetings is a fundamental expectation that a banking organization will have of its directors. Consistent with the SEC disclosure requirements in Item 407(b) of Regulation S-K, BPI believes that each director of a banking organization should attend at least 75% of the meetings of the board and any applicable committees in any given year and should strive to attend all of them.

Presentations by Management

Some commentators maintain that the asymmetry in the amount of information available to management directors and non-management directors is one of the biggest barriers to conducting effective board meetings.[252] To correct this asymmetry, the board should consider inviting senior executive officers and other relevant employees on a regular basis to present information regarding key aspects of the organization's business, recent changes in regulations and such other matters as the board deems appropriate, and should determine whether management or employee presentations should be to the full board or particular committees. A live presentation often can be more engaging than written summaries and reports and also enables directors to ask questions and have a more meaningful discussion with the organization's management. At the discretion of the chairperson (or lead director, if the chairperson is not independent), a presentation may be made in executive session. In determining whether a subject should be presented in executive session, the chairperson or lead director should consider whether to consult with legal counsel and other outside experts as appropriate. In general, effective oversight requires that the board engage in communication with management regarding key aspects of the organization throughout the year.

Length of Board Meetings

There is no prescribed length for board or committee meetings. On the one hand, meetings that are too brief can prevent the board or committee from effectively fulfilling its oversight responsibility and may adversely impact the banking organization's strategies and performance. On the other hand, prolonged meetings can lead directors to lose track of the important issues at hand and can detract from a meaningful consideration of crucial matters. As a practical matter, the length of meetings will tend to correlate with the quantity and significance of the subjects on the agenda. Nonetheless, directors should devote sufficient time to address each subject on the agenda fully and satisfactorily and also consider other subjects that may be brought to their attention.

Format of Board Meetings

Although board and committee meetings of banking organizations are traditionally conducted in person and in-person meetings have some advantages, boards of banking organizations should conduct meetings in the format that the board considers appropriate and effective, to the extent permitted by applicable laws and the entity's organizational documents. Remote communications tools provide boards with more flexibility in planning and holding board and committee meetings, could permit greater director participation and may reduce the costs, logistical constraints, and other burdens associated with conducting in-person meetings. In response to the COVID-

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[250] *See*, *e.g.*, *Smith* v. *Van Gorkom*, 488 A.2d 858, 872-75 (Del. 1985) (citing the failure of the directors to obtain adequate information prior to taking action as a breach of their duty of care); *Brehm* v. *Eisner*, 746 A.2d 244, 264 n.66 (Del. 2000) (noting that a lack of due care by the directors may be evidenced by showing the use of a "grossly negligent process" that includes the failure to consider all material facts reasonably available).

[251] *See* ABA Guidebook, at 20.

[252] *See*, *e.g.*, Colley–Governance, at 83.

19 pandemic and the practice of limiting in-person meetings, the OCC codified its prior interpretation that board meetings of national banks may be conducted telephonically or electronically.[253]

In addition to complying with regulatory requirements regarding data security, banking organizations should also be cognizant of industry best practices and developments in this area.

SECTION 12. MINUTES OF BOARD MEETINGS

Principles:

a) The minutes of meetings of the board and its committees should be kept in accordance with the applicable corporate statute under which the banking organization is organized. The board should decide on the level of detail that it believes is appropriate for the minutes, balancing the need to maintain an adequate record to satisfy legal requirements and the need to avoid chilling discussion among directors. Although minutes may prove to be useful for bank regulator examiners reviewing corporate decision making, they are not designed for that purpose.

b) It is common practice not to create detailed minutes of executive sessions of independent directors, because doing so would be antithetical to the very objective of these sessions. The subject matter of these sessions and any formal actions taken may be noted in the minutes, as appropriate.

Commentary:

Minutes

Boards of banking organizations generally are required by state corporate statutes to keep minutes of their proceedings.[254] Minutes of meetings of the board constitute an important part of a corporation's books and records. Among other matters, minutes serve as the most fundamental record of the board's actions and serve as an important corporate record of the discharge by directors of their fiduciary and other duties.

It is generally recognized that there is variation among corporate entities with respect to the level of detail presented in minutes. There is no single, correct approach to recording minutes, and the board should decide upon an approach based on its circumstances and needs. Nonetheless, BPI believes that both extremes should be avoided. The minutes should not be a verbatim transcript of the meeting and, in particular, should not attribute specific views to particular directors in a way that could chill discussion. But the minutes should cover, at a minimum, a description of significant subjects discussed, the nature of the discussions, decisions reached and any dissenting votes or abstentions. The minutes should also reflect the board's oversight role, distinct from the role of management, and, as appropriate in applicable circumstances, that oversight inherently entails delegation. Bank regulators have set the expectation that board minutes should constitute an accurate, adequate record of actions taken and should document the board's review of regular subjects (including review of the entity's financial condition and earnings, loan activity, investment portfolio, policies and procedures and audit and examination reports) as well as any other significant subjects discussed at a particular meeting.[255]

The Federal Reserve Board further advises that, at a minimum, the minutes should "record the attendance or absence of each director at each meeting, detail the establishment and composition of any committees, and note the abstention of any director from any vote."[256]

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[253] OCC, Activities and Operations of National Banks and Federal Savings Associations, 85 Fed. Reg. 83,686 (Dec. 22, 2020); *See also* 12 U.S.C. § 24; OCC Interpretive Letter No. 860 (Apr. 5, 1999).

[254] *See*, *e.g.*, 8 Del. C. § 142(a) (requiring corporations to appoint an officer to record the proceedings of the meetings of the board); *see also* N.Y. Bus. Corp. § 624(a) (requiring corporations to keep minutes of the proceedings of its shareholders, board and executive committee, if any).

[255] *See* Commercial Bank Manual, Section 5000.1, at 4.

[256] *Id*.

In terms of procedures, minutes should be drafted by an authorized officer of the banking organization and circulated to the directors promptly following the meeting. If possible, the minutes should be presented for approval at the next regular meeting of the board or committee. Draft minutes should be included in the package of materials distributed prior to the meeting at which approval of the minutes will be sought. Although directors may wish to take personal notes to assist the discussion process, to identify immediate follow-up subjects and to support their review of the minutes, they should not retain any meeting notes after reviewing and approving the formal minutes of that meeting unless otherwise required by law.[257] Once minutes have been approved by the board or a committee, they should not be altered without being resubmitted for approval.

Minutes invariably are reviewed as part of regulatory examinations and often are required to be produced in connection with litigation and governmental investigations and as part of the annual audit of a corporation's financial statements.[258] In addition, minutes also must be available for inspection by the directors and, in certain cases, shareholders may be entitled to demand access to them.[259] Accordingly, banking organizations should implement appropriate processes to address the presence of, and be prudent about including, confidential supervisory information in board minutes and, to the extent board minutes are required to be produced to a third party, to protect the disclosure of it.

Although board minutes reflect board discussions, they are not intended to serve as a transcript of proceedings or as lists of information provided to the board (or of information that a regulatory agency believes should be provided to a board). The board should decide on the level of detail that it believes is appropriate for the minutes, balancing the need to maintain an adequate record to satisfy legal requirements and the need to avoid chilling discussion among directors. A banking organization may determine that its minute-taking practices would be enhanced by referring in the minutes to relevant materials provided to directors in connection with board meetings, instead of including detailed descriptions in the minutes themselves, particularly when regulatory requirements mandate the inclusion of certain specific items in board minutes.[260] BPI believes that banking organizations should have flexibility to determine the level of detail in the minutes and the extent to which the minutes refer to meeting materials, so long as it is clear from the records what was discussed and what decisions were reached.

BPI also believes that regulatory expectation that certain information and details be included in board minutes can be overly prescriptive and deviate from sound and long-standing governance practices; moreover, preparing granular minutes may create various risks for banking organizations[261] and could divert directors' attention from important, high-level items on the agenda. The decision-making process at the board level should be an interactive one, with presentations, questions and discussion. BPI believes that it would be inimical to a board's effectiveness, through a chilling effect on discussions at board meetings, if the minutes basically transcribed all questions and points of view expressed during the meeting. A regulator could obtain a broader understanding of board challenge that occurs during or outside of board meetings by addressing the topic during the director interactions with regulators described in Section 14, as long as there is sufficient evidence that the subject matters were addressed by directors, without revealing the details of conversations and the identities of the directors raising issues or asking questions.

As discussed above, as a matter of good corporate governance, directors should meet in regularly scheduled

257 *See* ABA Guidebook, at 53 (noting that directors have no obligation to take notes).

258 *See*, *e.g.*, Commercial Bank Manual, Section 5000.3, at 2-3 (noting that examiners should obtain minutes of the meetings of the board during an examination).

259 *See*, *e.g.*, 8 Del. C. § 220(b).

260 For example, Part 9 of the OCC's regulations requires that the results of any annual audits conducted of the institution's fiduciary activities (including significant actions taken as a result of the audit) in the minutes of the board of directors. 12 C.F.R. §9.9(a). Institutions that adopt a continuous audit system must include the results of discrete audits in board minutes at least once each year. 12 C.F.R. §9.9(b).

261 *E.g.*, *Tiger* v. *Boast Apparel, Inc.*, 214 A.3d 933 (Del. 2019) (rejecting a presumption of confidentiality for books and records produced to stockholders of a corporation pursuant to section 220 of the Delaware General Corporation Law).

executive sessions at which directors can freely discuss issues among themselves. Requiring detailed minutes of executive sessions would be antithetical to the very objective of such sessions. It is therefore a common practice not to create detailed minutes of executive sessions; the ABA notes that "simple minutes that set forth the attendees at the executive sessions and generally list the topics discussed and recommended actions will normally suffice."[262]

SECTION 13. BOARD COMPENSATION

Principles:

The board should adopt a compensation structure for the non-management directors, committee members and the individual directors with designated responsibilities (*e.g.*, lead director and committee chairs) so that the most qualified individuals can be attracted and retained and the interests of directors and shareholders can be aligned, as appropriate.

Commentary:

The board of a banking organization should determine the compensation of the directors and committee members based on an assessment of the compensation policies of peer organizations (*i.e.*, other banking organizations of similar size with similar businesses and operations), an analysis of any special factors that are unique to the organization and the qualifications and expertise of the individual directors. Due to the inherent conflict of interest in the board setting its own compensation, the board should use external benchmarks, such as comparisons to peer organizations and independent compensation consultants, as appropriate.[263]

Typically, the nominating/corporate governance committee or compensation committee of the board is charged with evaluating the form and amount of director compensation, subject in some cases to approval by the full board. In evaluating director compensation, the committee should consider the factors mentioned above as well as the time commitment and responsibility of the lead director, individual committee members and chairs. For instance, the chair of the audit, risk or other key committees and other members of those committees are charged with significant and time-consuming responsibilities, and, therefore, the level of compensation for directors who serve in those positions typically is higher.[264] In general, the time commitment for directors of banking organizations is different from (and greater than) that for directors in other industries, and the particular time commitments for directors of banking organizations should factor into compensation determinations and peer benchmarking analyses.

The committee tasked with evaluating board compensation also should have flexibility in determining the form of director compensation. The committee may decide to set director compensation in the form of annual retainers or attendance fees for meetings and make payments in stock, cash, stock options or restricted stock grants. In determining the form of payment, the committee should consider the benefit of aligning the interests of the directors with the long-term interests of the banking organization.[265] As the ABA notes, compensation in the form of stock options and restricted stock grants can "strengthen the directors' interest in the overall success of the corporation and better align their personal interests with those of shareholders."[266] In addition, the board of banking organizations may consider requiring directors to purchase a minimum amount of stock in the open market or to accept at least a designated portion of their compensation in stock grants rather than cash. Other companies may require directors to maintain a minimum level of stock ownership, which can be satisfied by

262 *See* ABA Guidebook, at 51.

263 *See*, *e.g.*, ABA Guidebook, at 106 (noting that boards should make sure they have "considered the information necessary to reach a fair decision" regarding director compensation, including "data on peer companies and an analysis of any factors relating to their particular circumstance, such as the complexity of the company and the expected time commitment").

264 *See id*. (noting that higher compensation for the chair and members of the audit committee is common).

265 *Id*. at 106-07.

266 *Id*.

receiving stock grants as compensation. Ordinarily, management directors do not receive compensation for serving on the board.

The increasing complexities of the banking industry and a demanding regulatory environment have significantly increased the responsibilities placed on directors of banking organizations. These increased complexities and responsibilities are likely to lead to upward adjustments in compensation for directors. The board should seek to adopt a compensation structure that is fair and competitive with those of peer organizations so that it can attract and retain the most qualified individuals.

The expanded obligations imposed on boards and the accompanying increase in time commitment, as well as enhanced independence and qualification standards, have presented challenges for banking organizations seeking to recruit new directors. These difficulties would be greatly exacerbated if directors were subject to a risk of personal liability in the absence of bad faith or disloyal conduct. In order to attract qualified directors, banking organizations typically provide directors with an appropriate level of protection against personal liability through indemnification provisions in the organization's governing documents, indemnification agreements and/or directors and officers ("D&O") insurance. State corporate law generally empowers a corporation to indemnify a director who is a party or is threatened to be a party to any action, suit or proceeding if that individual director acted in good faith and with a reasonable belief that the director's conduct was in (or not opposed to) the best interests of the corporation. Moreover, corporations generally may provide insurance protection for their directors.[267] However, federal banking regulations limit the indemnification and the insurance coverage that an insured depository institution and its holding company can provide to a so-called "institution-affiliated party" ("IAPs") (including directors) in certain circumstances.[268] Notably, the FDIC regulations prohibit indemnifying IAPs for certain civil money penalties and purchasing insurance that would cover such indemnification payment.[269] Such restrictions, which apply to any banking group with an FDIC-insured depository institution, may discourage qualified candidates from serving on the board of a bank or bank holding company. BPI believes that providing directors with liability protection in the form of indemnification and standard D&O insurance contracts, to the extent permitted by law and regulation, will generally be necessary to attract qualified directors and encourage these directors to undertake their responsibilities diligently without undue fear of personal liability.[270] At the same time, we believe that there is no compelling public interest served by subjecting bank directors to greater risk of personal liability than directors of other corporations who are not subject to Part 359. Having the most qualified and dedicated directors serve on the boards of our leading financial institutions greatly contributes to a safe, sound and efficient banking system. Accordingly, absent a conflicting compelling public interest, agency rulemaking and policy should encourage, not discourage (*e.g*., as does Part 359), persons with qualification and dedication (and other critical attributes described in the Guiding Principles) from serving as directors on the board of banking organizations.[271]

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267 *See*, *e.g.*, 8 Del. C. § 145.

268 *See* 12 C.F.R. § 359.3 ("Part 359").

269 12 U.S.C. § 1828(k) authorizes the FDIC to prohibit or limit, by regulation or order, any indemnification payment to an institution-affiliated party. The FDIC further clarified that the purchase of indemnification insurance is impermissible even if the covered IAP were to reimburse the insurance premium. FDIC, FIL-47-2013, Director and Officer Liability Insurance Policies, Exclusions, and Indemnification for Civil Money Penalties (October 10, 2013). *See also* Statement Regarding Insurance Policies for Directors and Officers, SR 19-12 (July 23, 2019). In addition to the prohibition on indemnifying IAPs for civil money penalties, Part 359 also imposes limitations on payment or indemnification of defense costs.

270 To this end, BPI also believes that prospective directors should be permitted to review materials containing confidential supervisory information relating to the banking organizations in the decisionmaking process. This would allow prospective directors to make a more informed assessment of the anticipated time commitments of serving on the board.

271 Winning an administrative action filed by a federal banking agency is often difficult for a director, in part because the statutory authority for taking such actions is interpreted by the banking agencies to be broad and largely discretionary. For example, in the administrative action against Patrick Adams in 2014, the OCC concluded that its broad interpretation of the phrase "unsafe or unsound banking practices" should prevail even though the alleged unsafe or unsound practice might not or would not be injurious to the bank. In a recent final rule, the OCC declined to expound upon how the OCC would evaluate the "safety and soundness of indemnification payments to IAPs," noting that such determinations would be made "on a case-by-case basis based on the facts and circumstances of a particular case." OCC, Activities and Operations of National Banks

The past decade has seen a broad wave of changes in corporate governance for public companies, resulting from a combination of increased pressure from shareholder groups, evolving market practices, and regulation. The resulting changes have included the elimination of classified boards and the introduction of majority voting for directors at many companies, as well as the introduction of an advisory vote on executive compensation at public companies.[272] Although recent trends have generally favored these and other shareholder empowerment provisions and have encouraged greater engagement with shareholders, BPI believes that banking organizations should retain the flexibility to adopt the corporate governance structures and practices that the board believes are best suited to the organization. One consideration that distinguishes banking organizations from other public companies is the importance of market perceptions and the ways in which changing market sentiment can affect the organization.

Shareholder engagement is of increasing importance to public companies generally, including publicly held banking organizations. The board, and in particular the independent directors, should remain apprised of the organization's shareholder engagement strategy and implementation. The board's involvement in shareholder engagement can include overseeing the assessment of and response to director nominations and other shareholder proposals (as discussed further in Section 7 with respect to the role of the corporate governance/nominating committee) and having appropriate board or committee members, such as the lead independent director or the chairperson, meet with shareholders or shareholder groups that wish to convey concerns to the board (as discussed in Section 10).

SECTION 14. MEETING WITH REGULATORS

Principles:

The board (or, as the board deems appropriate, specified directors) should seek to engage with the principal regulator(s) of the banking organization in connection with the organization's receipt of annual examination reports and otherwise seek consultation with the regulator(s) as the board deems appropriate. Boards, directly or through specified directors, should be receptive to engagement with principal regulator(s) informally, outside the context of board meetings.

Commentary:

Directors of banking organizations are held accountable by their principal regulators who supervise the organization through on-site examinations and periodic monitoring.[273] Open and honest communication with a banking organization's principal regulators at the federal and state level is a critical component of a board's oversight responsibilities and helps the banking organization in conducting its operations in compliance with laws, regulations and safe and sound banking principles.[274] Important issues pertaining to the board's oversight of a banking organization should be addressed in directors' communications with examiners, and those communications, together with the other materials, such as board minutes, that examiners may review, should provide a basis for examiners to evaluate the effectiveness of the board.[275] BPI believes that, absent extraordinary circumstances, examiners should not need to attend board meetings in order to assess the effectiveness of a board

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and Federal Savings Associations, 85 Fed. Reg. 83,686 (Dec. 22, 2020). Notably, the OCC stated that national banks and federal savings associations have the ability to appeal the OCC's invalidation of an indemnification payment or agreement pursuant to the OCC's appeal process. *Id*.

272 *See* Dodd-Frank Act, § 951. Pursuant to Section 951 of the Dodd- Frank Act, issuers are required to conduct non-binding shareholder advisory votes on (i) executive compensation agreements (a "say-on-pay" vote) at least once every three years, (ii) whether a "say-on-pay" vote should be held annually, biennially or triennially (the "frequency vote") and (iii) certain golden parachute compensation arrangements of the company's named executive officers.

273 *See* OCC Director's Book, at 1; Commercial Bank Manual, Section 5030.1, at 1.

274 *See* Group of Thirty, A New Paradigm: Financial Institution Boards and Supervisors (October 2013) ("G30 New Paradigm") (recognizing the mutual benefits of a robust and continuous interaction between the bank boards and the supervisors, and calling for "a long-term commitment to building and sustaining closer, trust-based relations founded on open communication" from the bank boards and the supervisors).

275 *See* Section 7 (discussing board evaluations and oversight of corporate governance).

or for any other purpose. Discussion focused on the board's core functions, together with agenda items discussed at board meetings that are made available to supervisors, provides an appropriate basis to evaluate board effectiveness.

The Federal Reserve Board states that it generally is preferable for regulators to meet with the full board, but that meetings with key board committees also may be sufficient.[276] In some instances, conducting these meetings in executive sessions (*i.e.*, with only independent directors) may support a more candid discussion regarding sensitive issues at the banking organization. The OCC has acknowledged that outside directors may choose to meet with the OCC without management present.[277]

At a minimum, BPI believes the board or, as the board deems appropriate, specified directors, should seek to meet with the principal regulator(s) of the banking organization during each examination cycle in connection with the receipt of annual or similar roll-up examination reports. Depending on the issues involved, and in consultation with regulators, the board should consider whether all or part of these meetings should be without management present, and whether regulators should meet separately with any particular director, such as the lead independent director or a committee chair.

In many cases, it will be beneficial to time these meetings so that the discussion can involve the outcome of bank examinations; board members are encouraged, and in certain circumstances required, to meet with federal and state bank examiners during, or at the conclusion of, the examination process for a bank holding company or subsidiary bank. As the Federal Reserve Bank of Kansas City has observed, attending exit meetings with regulators after the examination process provides an advance look at any strengths or weaknesses identified by the examiners.[278] For banking organizations that are subject to continuous supervision, the annual meeting with regulators should serve this purpose. In addition, the Federal Reserve Board requires directors of a member bank to meet with the examiners if the bank's condition appears to be deteriorating or has shown little improvement since a prior examination.[279]

Although periodic examiner meetings with the board (or specified directors) can be mutually beneficial, supervisors' attendance at board or board committee meetings (other than during any portion of such meetings designated for presentations by, or discussions with, supervisors) is not appropriate. Examiner attendance at board meetings could have a chilling effect on discussions among board members and between management and board members.[280] Rather, BPI believes that communication is most effective when boards (directly or indirectly through specified directors) engage with the principal regulators outside board meetings. The appropriate format and frequency of supervisor engagement is ultimately dependent on the circumstances of the banking organization, and boards should have the flexibility, in consultation with supervisors, to guide the way in which these interactions take place.[281]

The OCC has recognized the benefits of an environment in which bank examiners and board members openly and

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276 Commercial Bank Manual, Section 5030.1, at 2.

277 *See* OCC Director's Book, at 8.

278 *See* Division of Supervision and Risk Management, Federal Reserve Bank of Kansas City, Basics for Bank Directors (March 2016) ("Basics for Bank Directors"), at 11.

279 *See* Commercial Bank Manual, Section 5030.1, at 3; Federal Reserve Board, Examination Frequency and Communicating with Directors, SR 85-28 (October 7, 1985), as amended by SR 95-19 (March 30, 1995).

280 Traditionally, attendance of regulators and supervisors at board meetings has, in the normal course, been reserved for special sessions focused on specific, identified issues. The presence of regulators or supervisors, even as observers, at regular board meetings raises a concern as to whether it will chill vigorous conversations among directors. *See* G30 New Paradigm, at 23 (noting that the regular presence of supervisors as observers at board meetings risks changing the behavior of the board and blurring the lines of accountability).

281 Informal engagement could take a variety of forms, including forum discussion with groups of directors, written and face-to-face communication, ad hoc consultation, and other informal channels.

honestly communicate.[282] Bank examiners often have experience with a broad range of banking activities and can provide independent, objective advice and information to the board on safe and sound banking principles, the organization's management, compliance with applicable laws and regulations, weaknesses and potential areas of improvement.[283]

Directors should pay close attention to, and carefully review, any material written communications from the banking regulators and discuss with management issues of concern raised in those communications. As part of their oversight responsibilities, directors also should evaluate whether management treats compliance issues and supervisory findings seriously and consider an appropriate plan of action as applicable under the circumstances.[284] The FDIC Pocket Guide states that board members should personally review reports of examinations and other correspondence from a banking organization's supervisors, including careful review of any findings and recommendations, should track progress in addressing problems and should discuss issues of concern with examiners. For banking organizations that receive a large number of examination reports, a board may conclude that it is more appropriate for the board or a board committee to receive summaries that identify findings and recommendations and track progress. The Federal Reserve Board has also proposed to change the process of presenting Matters Requiring Attention ("MRAs") and Matters Requiring Immediate Attention ("MRIAs") to the board, and instead would clarify that examiners and supervisory staff should direct most MRIAs and MRAs to senior management, and board attention would be required only when the board needs to address its corporate governance responsibilities or when senior management fails to take appropriate remedial action.[285]

In certain circumstances, bank regulators also may choose to take formal or informal enforcement actions to correct specific problems identified at a bank. These actions typically specify what the banking organization "needs to do to correct identified problems, such as improving lending practices, raising capital, instituting proper policies and procedures, or correcting specific violations of law."[286] These enforcement actions may include specific requirements as to the board's role in remediating or monitoring the issue. Even absent specific requirements, the board of a banking organization should be fully briefed on these enforcement actions and should carefully review the identified problems and discuss issues of concern and the progress of remediation actions with the regulators and management.

It is important to recognize that the reviews by bank examiners do not diminish the board's responsibilities to oversee the management and affairs of the banking organization. Directors are independently responsible for obtaining information from management as to the condition of the organization and should not rely on the examiners as their principal source of information to identify or correct problems. Instead, the board should look to its senior management, its auditors and other outside experts to identify any problems and should work with these parties to correct these problems.[287] Relatedly, because appropriate governance structures and practices will necessarily vary from one banking organization to another, use of regulatory horizontal reviews as a tool to mandate "best practices" will not be successful and should be limited.

The board should not necessarily limit its contact with principal regulators only to the examination process. The frequency with which the board should interact with the principal regulator(s) will of course depend on the

282 *See* OCC Director's Book, at 8.

283 *Id*. *See also* G30 New Paradigm, at 28-29 (noting that supervisors have "unique and valuable insights at the intersection of financial stability, financial institutions, and regulatory implementation," such as a range of governance practices at the marketplace, which would greatly benefit the institutions).

284 *Id*; *see also* Section 4 (discussing monitoring management performance to carry out effective oversight).

285 Board Effectiveness Proposal, at 37,222-23. Currently, an organization's appeal of any MRA, MRIA, or other material supervisory determination is required to be approved by the board.

286 *Id*. at 75.

287 *See id*. at 6.

circumstances at the banking organization.[288] As noted above, although regulators may attend board meetings for presenting the examination reports, such attendance is not intended for the purpose of evaluating the board, and regular attendance by supervisors could have a chilling effect on board discussions.

The board should be receptive to requests from regulators for communication and engagement and the board or designated directors are encouraged to indicate to the banking organization's primary regulators a willingness to engage, as necessary and appropriate. The board may deem it appropriate to consult with the local examination team or other contacts at the relevant regulators in order to discuss agendas for these meetings. Coordination between the board (or specified directors) and the local examination team (or other contacts) in advance of meetings with the primary regulators may enhance communication and mutual understanding, provide for consistent expectations of the goals of these meetings and improve efficiency for both the board and regulators.

[288] *See* G30 New Paradigm, at 23 & 35 (proposing that bank boards and supervisors should devote time and efforts to their interactions and meet regularly, and that the bank boards should be proactive in engaging supervisors in formal discussion about board effectiveness).

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Annex A – Overview of 2021 Updates

- The 2021 update focuses on aspects of governance that are unique to banking organizations, as compared to those that are generally applicable, and incorporates various legal and regulatory developments and expands on certain topics, including the following:
- Bank regulatory and supervisory developments since 2015, including the Federal Reserve Board's 2017 board effectiveness proposal;
- The nature of active board oversight and the appropriate ways for a board to provide "credible challenge" to management (Introduction);
- Greater emphasis on the impossibility of a "one-size-fits-all" approach to governance and the importance of flexibility in governance practices to accommodate each banking organization's unique circumstances (Introduction; all sections of the Guiding Principles);
- The importance of the distinction between roles of boards and management, the roles of boards and management in relation to policies and procedures, and the inherent relationship between delegation and oversight (Introduction; Sections 1 and 4);
- Duties and practices of the boards in emergency situations, such as the COVID-19 pandemic (Introduction, Section 11);
- The ability of board committees to fulfill the responsibilities of a board (Sections 1 and 5);
- The interplay between traditional state law fiduciary duties (including emerging subject matters such as cybersecurity and technology that impact the exercise of fiduciary duties) and the obligations imposed on boards by banking statutes, regulations and pronouncements (Section 1);
- Board composition, including how consideration of factors such as board size and diversity, expertise and tenure of board members factor into composition decisions (Sections 3 and 7);
- Core board functions, including approving the organization's strategic objectives, overseeing financial conditions and performance, talent management and succession planning, overseeing risk management and internal control and promoting organizational culture and values (Section 4);
- The importance of flexibility for boards to determine how responsibilities should be allocated among board committees and techniques to address allocation decisions, including the use of joint committees, joint meetings or overlapping memberships in areas that are within the purview of multiple committees (Section 5);
- Recognition that banking organizations have differing practices with respect to the role of lead independent directors (Section 10);
- The ability of boards to review and rely on materials prepared by management or consultants and to determine how board meetings should be conducted effectively (Section 11);
- Practices and approaches to promote engagement and open, frank discussions during meetings and avoid a chilling effect on discussions (Sections 12 and 14); and
- Accessibility to and engagement with examiners (Section 14).

Annex B – Relationship of Core Board Functions to Board Key Attributes in the Board Effectiveness Proposal

This Annex B maps the key attributes of an effective board identified in the Federal Reserve's Board Effectiveness Proposal (the "Key Attributes") to the core functions of a board set forth in the 2021 edition of the Guiding Principles (the "Core Functions"). The Key Attributes and the Core Functions each organize the critical and fundamental responsibilities of a banking organization's board of directors.[289]

The following five sections track the five Key Attributes, and note how concepts included therein are organized in the Core Functions. It is important to keep in mind that the scope and purpose of the Board Effectiveness Proposal and the Guiding Principles differ, and that the Key Attributes and Core Functions do not correspond one-to-one. This mapping is intended instead as a comparison of the two different descriptions of a board's essential responsibilities. Some Key Attributes map more closely to other Guiding Principles. In those cases, this mapping addresses the relationship between those Key Attributes and Guiding Principles as well.

At a high level, the overarching themes of the five Key Attributes correlate to the Core Functions. The Key Attributes, however, do not have a direct analogue to Core Function 2, "Monitoring Financial Performance and Condition".

Board Effectiveness Proposal: Key Attributes	2021 BPI Guiding Principles: BPI Core Functions
Attribute 1: Set Clear, Aligned, and Consistent Direction ▶ Guide the development of and approve firm's strategy ▶ Set the types and levels of risks the firm is willing to take ▶ Consider the capacity of the firm's risk management framework when approving strategy and risk tolerance ▶ Assess whether significant policies/plans/programs are consistent with strategy, risk tolerance and risk management capacity	Core Function 1: Reviewing and Approving the Strategic Objectives ▶ Review, discuss and approve the banking organization's overall strategic objectives ▶ Guide the strategic direction of the banking organization through board oversight of top-tier policies and operating policies and providing strategic advice to senior management Core Function 4: Overseeing the Risk Management and Internal Control Frameworks, Including Top-tier Policies and Plans in Fundamental Areas ▶ Understand the organization's risks and risk profile, review the standards for the nature and level of risk the organization is willing to assume, approve the risk appetite statement, and review top-tier enterprise-wide risk policies/plans

289 As described in the Guiding Principles, we believe that the Core Functions are appropriate components of a clear description of core board functions. Our viewpoints relating to the Key Attributes are described in a comment letter available at: https://bpi.com/wp-content/uploads/2018/07/20180215_tch_aabd_-sifma-comment_letter_on_board_effectiveness-proposal.pdf.

Board Effectiveness Proposal: Key Attributes	2021 BPI Guiding Principles: BPI Core Functions
	Core Function 5: Reinforcing, Demonstrating and Communicating the "Tone at the Top" for the Values and Culture of the Organization and Overseeing Enterprise-wide Approaches/Programs Intended to Promote Organizational Values, Culture and Reputation ▶ Set the "tone at the top" by overseeing management's establishment of an organization culture that provides appropriate standards and incentives for ethical and responsible behavior
Attribute 2: Actively Manage Information Flow and Board Decisions ▶ Actively manage information flow to the board and board deliberations ▶ Direct senior management to provide information that is timely and accurate with appropriate detail and context ▶ Establish practices and processes to evaluate information flows and engage senior management on improvements ▶ Seek information about the firm and its activities, risk profile, talent and incentives outside routine meetings ▶ Take an active role in setting board meeting agendas	Core Function 2: Reviewing Financial Performance and Condition ▶ Review financial performance, financial forecasts, capital adequacy and liquidity, and external factors that can impact the organization on a regular basis in a manner consistent with the banking organization's strategic objectives ▶ Obtain sufficient information from management to inform decisions on matters such as capital actions and, where necessary, contingency and recovery plans. Core Function 4: Overseeing the Risk Management and Internal Control Frameworks, Including Top-tier Policies and Plans in Fundamental Areas ▶ Oversee compliance and internal audit functions through ongoing reporting to the board ▶ Convey expectations relating to ongoing and special reporting to the board ▶ Develop an understanding with management about the nature of information and matters that should come to the attention of the board Section 1: Basic Responsibilities of the Board and Management ▶ Provide guidance on matters to be included on board agendas, including the types of matters/information that should generally be brought to the attention of the board

Board Effectiveness Proposal: Key Attributes	2021 BPI Guiding Principles: BPI Core Functions
	► Ask informed, probing questions of management, at or outside of board meetings Section 11: Agenda, Materials and Length of Meetings ► Articulate an approach for determining which matters should be addressed at the board level ► Provide guidance on how board materials are prepared and how information is conveyed to directors ► Regularly attend and actively participate at board and committee meetings ► Consider inviting senior executives to present information regarding key aspects of the business
Attribute 3: Hold Senior Management Accountable ► Hold senior management accountable for implementing the firm’s strategy and risk tolerance and maintaining the firm’s risk management and control framework ► Evaluate the performance and compensation of senior management ► Actively engage senior management ► Engage in robust and active inquiry into current and emerging risks, adherence to strategy and risk tolerance, material/persistent deficiencies in risk management and development/implementation of performance management and compensation programs ► Empower independent directors to serve as a check on senior management ► Establish and approve clear financial and nonfinancial performance objectives for CEO, CRO, CAO and, as appropriate, other members of senior management ► Approve and reassess succession plans for the CEO, and, as needed, the CRO and CAE	Core Function 1: Reviewing and Approving the Strategic Objectives ► Oversee management’s performance in formulating and implementing the organization’s strategic objectives ► Oversee key business policies established by management Core Function 3: Overseeing Talent Management, Including the CEO and Other Senior Executives ► Evaluate the performance and compensation of the CEO and other senior executives as appropriate and consistent with the organization’s strategy and oversight goals ► Review and approve senior executive compensation in light of the organization’s performance ► Approve an appropriate management succession plan for the CEO and review or approve management succession plans for other senior executives, as appropriate Core Function 4: Overseeing the Risk Management and Internal Control Frameworks, Including Top-tier Policies and Plans in Fundamental Areas

Board Effectiveness Proposal: Key Attributes	2021 BPI Guiding Principles: BPI Core Functions
	▶ Oversee how management implements risk management and control programs ▶ Provide oversight of the effectiveness of the organization's internal controls
▶ Attribute 4: Support the Independence and Stature of Independent Risk Management and Internal Audit ▶ Support, through the audit and risk committees, the stature and independence of the firm's independent risk management function by: communicating directly with CRO on material risk management issues; reviewing risk management's budget, staffing and systems; providing risk management unrestricted access to the risk committee; and directing inclusion of independent risk management representatives on senior management-level committees ▶ Support the stature and independence of internal audit by: meeting with the CAE regarding the internal audit function, organizational concerns and industry concerns; supporting internal audit's budget, staffing and system; and reviewing the status of actions recommended by internal and external auditors ▶ Engage in robust and active inquiry into, among other things, material or persistent breaches of risk appetite and risk limits, timely remediation of material or persistent internal audit and supervisory findings, and the appropriateness of the annual audit plan. ▶ Have the capability to identify specific instances or decisions where the independence and stature (or lack thereof) of the independent risk management and internal audit have materially impacted business deliberations, decisions, practices or the firm's strategy	Core Function 4: Overseeing the Risk Management and Internal Control Frameworks, Including Top-tier Policies and Plans in Fundamental Areas ▶ Oversee that the organization has established appropriate risk management and control programs for identifying and addressing the significant risks faced by the organization, including being apprised of emerging risks ▶ Provide clear expectations and direction to senior management and the control functions relating to implementation of programs ▶ Oversee management's establishment and implementation of systems designed to promote compliance with applicable laws and regulations ▶ Supervise management's creation of clear policies that govern the day-to-day operations, including internal and external audit processes and disclosure controls and procedures ▶ Obtain sufficient information to effectively oversee the stature and independence of the internal control units, the performance of the risk management framework, emerging risks and risk-management or compliance deficiencies
Attribute 5: Maintain a Capable Board Composition and Governance Structure	Section 3: Composition of the Board ▶ Determine board composition, considering the size of the board, the

Board Effectiveness Proposal: Key Attributes	2021 BPI Guiding Principles: BPI Core Functions
▶ Have a board composition, governance structure and established practices that align with the firm's size, complexity, scope of operations, risk profile and other changes that occur over time ▶ Select directors with a diversity of skills, knowledge, experience and perspectives ▶ Establish a process for identifying and selecting director nominees that considers the potential nominee's experience, availability, integrity and potential conflicts of interest ▶ Establish a governance structure capable of overseeing and addressing issues arising from the firm's asset size, scope of operations, activities, risk profile and resolvability ▶ Have the capacity to engage third-party advisors and consultants, when appropriate ▶ Assess board strengths and weaknesses, and adapt board structure and practices to address identified weaknesses or deficiencies and as the firm's size, scope of operations, risk profile and other characteristics change over time	diversity, expertise, and tenure of the board members, and the capacity of board members to commit to serving on the board of a banking organization ▶ Consider the nature, scope and complexity of the business, strategic objectives and/or plans of the banking organization, and the need for directors to provide a diversity of views and a range of skills commensurate with the board's oversight role Section 5: Board Committees ▶ Establish board committees to assist the board with its oversight role, in particular regarding audit, nominating/corporate governance, compensation and risk management matters ▶ Have the authority to engage counsel and outside advisors as deemed necessary or appropriate Section 7: Nominating/Corporate Governance Committees, Director Qualifications and Board Oversight of Director Nomination Process ▶ The nominating/corporate governance committee should consider the circumstances of the banking organization and the importance of appropriate diversity, expertise and experience among board members in evaluating prospective director nominees and in evaluating directors for membership on board committees ▶ This committee should have responsibility for the board self-evaluation process, and assist in oversight of the banking organization's corporate governance structure, processes and performance Section 10: Independent Leadership of the Board ▶ Determine the appropriate form of independent leadership ▶ Lead director should review and report on results of board self-evaluations

Annex C – Federal Reserve Supervisory Expectations for Boards of Directors Identified by the Federal Reserve for Potential Elimination or Revision[287]

- SR 16-17: Supervisory Expectations for Risk Management of Reserve-Based Energy Lending Risk
- SR 14-8: Consolidated Recovery Planning for Certain Large Domestic Bank Holding Companies
- SR 13-19/CA 13-21: Guidance on Managing Outsourcing Risk
- SR 13-13/CA 13-10: Supervisory Considerations for the Communication of Supervisory Findings
- SR 12-17/CA 12-14: Consolidated Supervision Framework for Large Institutions
- SR 11-14: Supervisory Expectations for Risk Management of Agricultural Credit Risk
- SR 09-4: Applying Supervisory Guidance and Regulations on the Payment of Dividends, Stock Redemptions, and Stock Purchases at BHCs
- SR 08-9/CA 08-12: Consolidated Supervision of Bank Holding Companies and the Combined U.S. Operations of Foreign Banking Organization
- SR 08-8/CA 08-11: Compliance Risk Management Programs and Oversight at Large Banking Organizations with Complex Compliance Profiles
- SR 01-13: Supervisory guidance relating to a change to permissible securities activities of state member banks
- SR 01-8: Supervisory Guidance on Complex Wholesale Borrowings
- SR 00-9: Supervisory Guidance on Equity Investment and Merchant Banking Activities
- SR 99-7: Supervisory Guidance Regarding the Investment of Fiduciary Assets in Mutual Funds and Potential Conflicts of Interest
- SR 98-25: Sound Credit Risk Management and the Use of Internal Credit Risk Ratings at Large Banking Organizations
- SR 98-18: Lending Standards for Commercial Loans
- SR 98-9: Assessment of Information Technology in the Risk-Focused Frameworks for the Supervision of Community Banks and Large Complex Banking Organizations
- SR 97-25: Risk-Focused Framework for the Supervision of Community Banks
- SR 97-24: Risk-Focused Framework for Supervision of Large Complex Institutions
- SR 97-21: Risk Management and Capital Adequacy of Exposures Arising from Secondary Market Credit Activities
- SR 97-3: Conversion of Common Trust Funds to Mutual Funds
- SR 96-10: Risk-Focused Fiduciary Examinations
- SR 95-51: Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies
- SR 94-53: Investment Adviser Activities

- SR 93-69: Examining Risk Management and Internal Controls for Trading Activities of Banking Organizations
- SR 90-22: Policy Statement on the Use of “Points” in settling foreign exchange contracts
- SR 90-16: Implementation of Examination Guidelines for the Review of Asset Securitization Activities
- SR 11-14: Supervisory Expectations for Risk Management of Agricultural Credit Risk
- SR 09-4: Applying Supervisory Guidance and Regulations on the Payment of Dividends, Stock Redemptions, and Stock Purchases at BHCs
- SR 08-9/CA 08-12: Consolidated Supervision of Bank Holding Companies and the Combined U.S. Operations of Foreign Banking Organization
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