



The Clearing House®

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The Role of the Board of  
Directors in Promoting Effective  
Governance and Safety and  
Soundness for Large U.S.  
Banking Organizations

May 2016





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# Report Preface

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As part of The Clearing House Association's ("TCH") ongoing efforts to promote sound corporate governance, this Report articulates views on the fundamental functions of the board of directors of a large U.S. banking organization, offers recommendations for bank regulatory authorities to consider in promulgating requirements applicable to the board, and identifies board-related regulatory requirements and certain relevant supervisory guidance.

In March 2012, TCH published *Matters to be Addressed by Board of Directors Pursuant to Statute or Regulation* (the "2012 Report"), which provided a summary of numerous requirements set forth in federal banking laws and regulations, as well as in certain agency guidance statements (including examination guidance), that apply to the board of directors of a U.S. banking organization.<sup>1</sup> This Report and the accompanying annexes update and expand upon the 2012 Report, enumerating hundreds of legislative and regulatory requirements and guidance statements that call for matters to be addressed at the board level. In addition, the Report expands upon certain concepts discussed in TCH's *Guiding Principles For Enhancing U.S. Banking Organization Corporate Governance* (2015) ("TCH Governance Principles") by setting out our views on what the core oversight responsibilities (referred to as "core board functions"<sup>2</sup>) of the board of a large U.S. banking organization should include, how the board may choose to approach those

responsibilities, and how regulatory authorities may help strengthen and support the ability of directors to function effectively with respect to their core board functions.<sup>3</sup>

Boards of directors of large U.S. banking organizations are subject to requirements promulgated by multiple authorities. For example, state corporate law, federal securities laws and regulations, and stock exchange listing standards set forth corporate governance requirements that establish responsibilities for an organization's board and senior management. These include requirements relating to financial disclosure, the auditing process, incentive compensation, conflict of interest standards, internal controls over financial reporting, and the composition of the board and its committees, among others. Separately, boards of U.S. banking organizations are also subject to requirements prescribed under federal – and for state-chartered institutions, state – banking laws, regulations and agency guidance statements. Among others, these include requirements relating to board composition, audit functions, capital and liquidity management, financial disclosure and reporting, conflicts of interest, insider activities, risk management and the oversight of specific products and activities, and review and/or approval of a number of reports made by a banking organization to its regulators.

Annexes A and B (the "Annexes") to this Report identify requirements for boards of directors of

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1 As used herein, "examination guidance" refers to published examination manuals, handbooks and guidelines for examiner reference in carrying out examination activities.

2 See pp. 10 to 13 of this Report setting out the core board functions.

3 The TCH Governance Principles can be found at <https://www.theclearinghouse.org/issues/banking-regulations/dodd-frank/corporate-governance/20150624-tch-revises-guiding-principles-on-corporate-governance>.



U.S. banking organizations that are prescribed under these U.S. federal banking laws, regulations and certain agency guidance statements, including examination guidance.<sup>4</sup> Annex A provides an extensive list of these requirements and guidance relating to board responsibilities (organized by the U.S. authority issuing the requirement and type of release), while Annex B provides a narrower list of requirements and guidance (organized by topic) that specifically call for board review and/or approval of specific items.<sup>5</sup> The specific statutes, regulations and agency guidance statements reviewed for this Report, which are identified by category in the introduction to each Annex, have been promulgated by several different authorities and issued over the course of many years. They include requirements set forth in federal banking laws, as well as requirements in regulations and certain agency guidance statements by the Board of Governors of the Federal Reserve System (“Federal Reserve Board” or “FRB”), the Office of the Comptroller of the Currency (“OCC”), the Federal Deposit Insurance Corporation (“FDIC”) and the Federal Financial Institutions Examination Council (“FFIEC”). The Annexes also include guidance statements issued by the Consumer Financial Protection Bureau (“CFPB”). Certain of these sources of guidance have been designed for use by agency examiners and generally indicate that examiners are given discretion in how to apply them. The banking

4 The Annexes can be found at <https://www.theclearinghouse.org/~media/Action%20Line/Documents/Volume%20VII/20160505%20TCH%20Role%20of%20Board%20Annex%20A.pdf>  
<https://www.theclearinghouse.org/~media/Action%20Line/Documents/Volume%20VII/20160505%20TCH%20Role%20of%20Board%20Annex%20B.pdf>

See also American Association of Bank Directors “*Bank Director Regulatory Burden Report*” (2014) (a compilation of more than 800 provisions in law, regulation and guidance imposing obligations on bank boards of directors).

5 Annex B also identifies reports that are to be provided to boards pursuant to U.S. federal banking laws or regulations.

regulators also impose requirements or guidance more informally through the supervision and examination process. In addition, the regulators are increasingly requiring direct interaction with the board through, *e.g.*, attendance at sessions with boards and board committees and meetings with individual directors.

The Annexes do not include the entire universe of legal requirements that could potentially apply or be applied to a particular organization’s board of directors. For example, they do not include requirements that may apply pursuant to federal securities laws, state laws, or stock exchange listing standards, as noted above.<sup>6</sup> Moreover, the Annexes do not include corporate matters that, in accordance with company policy, practices or charters and in the normal exercise of fiduciary duties, would be presented to the board even if not specifically required by a statute, regulation or agency guidance statement.<sup>7</sup>

6 For example, 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. In addition, Section 303A.05 of the New York Stock Exchange (“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.

Moreover, U.S. state-chartered banking organizations may be subject to various requirements under applicable state law that are not addressed in this Report or the Annexes (*e.g.*, qualifications for bank directors, and items that are required to be reviewed or approved by the board of directors).

7 Matters that may be presented to the board in accordance with company policy, practices or charters may include review of acquisitions, divestitures, and expenditures as well as settlement of certain litigation matters, which companies may as a matter of policy and good governance desire to present to the board even when not required otherwise. The thresholds for determining when these types of items would be presented may well vary by company based on size, complexity, internal corporate policies, etc.

We are hopeful that the analysis and recommendations contained in this Report regarding the delineation between the core functions of boards at large U.S. banking organizations relative to those of management, as well as the supporting Annexes, are considered thoughtfully by all banking industry stakeholders. Recognizing the critical function that boards serve, it is increasingly important that legal frameworks support the ability of boards to de-

vote their time and efforts to the highest-level organizational priorities to both fulfill their fiduciary duties and enhance banking organization safety and soundness.

This Report and the supporting Annexes were prepared under the auspices of TCH's Committee on Corporate Governance with the assistance of TCH's special counsel, Sullivan & Cromwell LLP.



# Promoting Effective Governance and Safety and Soundness for Large U.S. Banking Organizations

The oversight provided by the board of directors is fundamental to the successful and safe and sound operation of a U.S. banking organization. As noted in the TCH Governance Principles, a central tenet of effective corporate governance is the distinction between, and complementary nature of, the board's responsibility for *oversight* of the business and affairs of the banking organization, and management's responsibility for the *day-to-day* operations of the organization. This distinction is particularly critical in the context of the board of directors of a large U.S. banking organization as it navigates a confluence of fiduciary responsibilities under state law, requirements under federal banking law, as well as supervisory expectations and mandates of regulators (which typically include a number of U.S. and non-U.S. regulatory bodies for a large banking organization operating in multiple jurisdictions).<sup>8</sup> As the TCH Governance Principles note, blurring of this distinction detracts from effective governance by potentially reducing the board's ability to focus on its core oversight functions, impairing the board's ability to perform its critical oversight role objectively, and creating uncertainty as to roles and responsibilities.<sup>9</sup>

<sup>8</sup> Non-U.S. banking organizations with U.S. banking operations generally are subject to a differing set of governing laws, regulations and relationships which present certain unique issues and considerations that are not applicable to U.S. domestic institutions. For example, the U.S. operations of such foreign banking organizations ("FBOs") may be able to utilize existing governance and control structures inside and outside the U.S. to perform certain functions and satisfy U.S. (and home country, as applicable) regulatory requirements. While the scope of this Report does not specifically address the application of U.S. bank regulatory requirements for boards of directors of FBOs and their U.S. operations, the basic principles outlined herein regarding the oversight role of a board of directors and the delineation between the core functions of a board and those of management are equally applicable in this context.

<sup>9</sup> See TCH Governance Principles, Section 1(a).

A 2015 International Monetary Fund ("IMF") report<sup>10</sup> on, and review of, the U.S. bank supervisory framework describes the current framework's treatment of the role and mandates imposed on U.S. bank boards relative to that of senior management as an area of "concern". In particular, according to the IMF report – while there has been increasing and welcome attention paid to this issue very recently – in many cases, U.S. bank regulatory releases do not clearly distinguish between the two, 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 (as illustrated in the Annexes) where the standard term "board and senior management" was used in situations where good practices would dictate that only one of the two be responsible for the task in question.<sup>11</sup>

<sup>10</sup> 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.

<sup>11</sup> Certain U.S. federal bank regulatory pronouncements have, however, also acknowledged this important distinction. 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 . . ." FRB Commercial Bank Examination Manual, Section 5000.1. In *The Role of a National Bank Director: The Director's Book* (reprint September 2013) ("OCC Director's Book"), the OCC has stated that the role of national bank directors is to oversee the bank, that one of the board's most fundamental responsibilities is to select and retain competent management, and that "[e]ffective management has the ability to manage day-to-day operations to achieve the bank's performance goals." Similarly, in the *Pocket Guide for Directors* ("FDIC Pocket Guide"), the FDIC has stated that the role of a financial institution's board is to oversee the conduct of the institution's business, noting that the board of directors should select and retain competent management.

Senior U.S. regulators have recently called attention to the important board-management distinction highlighted in the IMF report as well as in the TCH Governance Principles and have also expressed concerns relating to the increasing regulatory compliance-related obligations of directors that may divert attention from core board functions. The following statements are among those recently addressing these issues:

*“There are many important regulatory requirements applicable to large financial firms. Boards must of course be aware of those requirements and must help ensure that good corporate compliance systems are in place. But 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. [Regulators] should probably be somewhat more selective in creating the regulatory checklist for board compliance and regular consideration . . . the failure to discriminate among [MRAs] is almost surely distracting from strategic and risk-related analyses and oversight by boards.”<sup>12</sup>*

**DANIEL TARULLO**

– Federal Reserve Board Governor (June 2014)

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12 Speech by Governor Daniel K. Tarullo at the Association of American Law Schools 2014 Midyear Meeting, Washington, D.C. (June 9, 2014).

*“We don’t expect directors to manage the bank, but we do expect the board to look at high level issues that relate to culture. . .”<sup>13</sup>*

**THOMAS CURRY**

– Comptroller of the Currency (June 2015)

*“The increasing workload may dilute an audit committee’s ability to focus on its core responsibilities: selecting and overseeing the independent auditors; internal controls and auditing; setting up an appropriate system for the receipt and treatment of complaints about accounting; and reporting to shareholders.”<sup>14</sup>*

**MARY JO WHITE**

– Chair of the Securities and Exchange Commission (December 2015)

TCH shares with U.S. and global regulatory authorities a common objective to promote strong and effective governance of U.S. banking organizations and believes that the development of a common understanding around core board functions will: (i) facilitate more effective execution of the board oversight function, (ii) enhance bank safety and soundness, and (iii) encourage consistent supervisory guidance that supports and strengthens the board’s ability to focus on, and take a forward-looking

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13 Remarks by Thomas J. Curry, Comptroller of the Currency, before the Prudential Bank Regulation Conference, Washington, D.C. (June 9, 2015).

14 Keynote Address by Chair Mary Jo White at the 2015 AICPA National Conference: “Maintaining High-Quality, Reliable Financial Reporting: A Shared and Weighty Responsibility,” Washington, D.C. (December 9, 2015).



view of, strategic risks that both the regulatory community and industry believe are most fundamental to the safety and soundness and vibrancy of U.S. banking organizations.

In furtherance of this objective, this Report offers an approach to help clarify both:

- » the delineation between the core functions of boards, from a prudential perspec-

tive, at large U.S. bank holding companies relative to those of management, and

- » how core board functions should be executed (*i.e.*, in an informed and active manner).

We also offer recommendations to help strengthen and support the ability of directors to function effectively with respect to their core functions.

## I. Core Board Functions

The focus of large U.S. banking organization boards on the core functions of strategy, oversight (including oversight of risk management and culture), and senior executive talent management are central to promotion of sound governance, high-level risk management and safety and soundness. Core board functions – which are set out below in greater detail – should be understood within the context of the following concepts:

- » The five core functions set out below can be thought of as a way to organize several of the board’s fundamental and critical responsibilities from a prudential perspective at their highest level.<sup>15</sup> Though principally focused on holding company board functions, in many respects, the core board functions also

apply at the subsidiary bank level as well. 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 (or applicable board committee, as appropriate) to devote its time and efforts to the highest-level organizational priorities.
- » Though certain aspects of the role of the board may evolve over time, the funda-

<sup>15</sup> 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, this Report does 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.

mental or “core” functions remain constant absent unusual circumstances.<sup>16</sup>

- » The core functions should be not be read or viewed as a checklist of required actions. The functions are by their very nature ongoing, dynamic and forward-looking. Moreover, there is no single approach to sound corporate governance – the processes/practices adopted by each organization should be appropriate for the organization’s 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.<sup>17</sup> For example, boards may opt to utilize 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, which determines where to vet particular matters. Accordingly, references to the “board” in the following text should be understood to refer to either the whole board or a committee thereof.

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16 As the TCH Governance Principles note, 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 certain enforcement actions 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. See TCH Governance Principles Commentary to Section 1.

17 This Report focuses on core board functions other than internal board governance. Sound internal board governance is, however, a predicate for overall board effectiveness, and a meaningful and important responsibility in its own right as discussed in the TCH Governance Principles.

- » How core functions are manifested and the circumstances to which they apply may change over time. In other words, 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 (for example, with respect to cybersecurity in recent years). Care should be taken to ensure that adequate time on the board agenda is reserved for “deep 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 strategy, 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 are not intended to serve, or be relied upon as, a summary of applicable U.S. legal standards or supervisory expectations that may apply to any particular banking organization.



## CORE BOARD FUNCTIONS FOR LARGE U.S. BANKING ORGANIZATION BOARDS

### FUNCTION 1: Reviewing and approving the strategic objectives and plans.

- a. Strategic objectives and 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;<sup>18</sup> however, in all cases these strategic objectives and plans 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 strategic plan(s) for evaluation by the board.
- b. 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, various aspects of the organization's strategic plan/objec-

<sup>18</sup> 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.

tives, and (ii) providing strategic advice to senior management.

- c. The board should monitor management's performance in formulating and implementing the organization's strategic objectives and plans.

### FUNCTION 2: Monitoring financial performance and condition.

- a. This 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 board's strategic objectives and plans. The board should obtain sufficient information from management to inform board decisions on matters such as capital actions and, where necessary, contingency/recovery plans. See TCH Governance Principles, Sections 4(a)(i), (ii) and (iii).

### FUNCTION 3: Talent management for the CEO and other senior executives.

- a. This includes selecting the CEO and evaluating the performance and compensation of the CEO and such other senior executive officers as the board deems appropriate and consistent with the organization's



values.<sup>19</sup> Talent management also includes approving a management succession plan for the CEO, and reviewing management succession plans for other senior executive officers. See TCH Governance Principles, Sections 4(a)(v), and (vi).

#### **FUNCTION 4: Overseeing the risk management and internal control frameworks, including top-tier policies and plans in fundamental areas.**

- a. Foundationally, this involves overseeing that the corporation has established appropriate risk management and control programs for identifying and dealing with the significant risks faced by the organization and overseeing how management implements those programs. This includes understanding the organization's risks and risk profile, reviewing the standards for the nature and level of risk the organization is willing to assume in light of the organization's capital and liquidity levels and reputational considerations, approving the risk appetite statement, and 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 interests of the organization. See TCH Governance Principles, Sections 4(a)(vii) and (viii).

- 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; these policies and plans may generally include top-tier capital and liquidity plans, resolution and recovery plans, a credit policy/credit risk management policy, and the overall risk governance, audit and compliance frameworks.
  - 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. (See Part III below for related concerns and recommendations around this point.)
- b. This function also includes providing oversight of the risk management, 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:

19 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).

The commentary to the TCH Governance Principles notes that "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." See TCH Governance Principles, Commentary to Section 4(a)(5).

- capital/liquidity/stress testing planning processes,
  - financial, capital and risk profile reporting and disclosures processes,
  - information security (including cyber vulnerability), outsourcing and recovery processes,
  - customer, client service and compliance standards and processes, and
  - loan underwriting and review
- c. Appropriate means should be utilized by the board to create 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).<sup>20</sup>
  - 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 the firm's policies and procedures 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, and to help determine where controls and the auditing process can be strengthened), (iii) emerging risks or future changes to the business that may materially impact the overall risk profile or changes to fundamental internal models, and (iv) effective identification, tracking and remediation of any risk-management or compliance deficiencies.

**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.**

- a. This includes overseeing senior management's establishment of an organizational culture that provides for appropriate standards and incentives for ethical and responsible behavior. This includes:
- Board oversight of the enterprise-wide compensation philosophy that appropriately balances risk and reward and takes

<sup>20</sup> See TCH Governance Principles, Commentary to Section 4 (noting that "the board and management should put procedures into place whereby significant deviations from key policies, to the extent material to the organization, are discussed with the board").



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. See TCH Governance Principles, Sections 4(a)(vii), 8(b).
  - Board oversight of any other reputational and/or conduct risk management approaches, as and where applicable.
- b. 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. See TCH Governance Principles, Section 4(a)(iv).

- c. 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.
- d. The audit committee, or another independent committee, should review and approve procedures for the receipt, retention and treatment of complaints regarding compliance issues, including confidential, anonymous submissions. The board should oversee other appropriate mechanisms to address and investigate legitimate employee concerns. See TCH Governance Principles, Section 6(c).



## II. Informed and Active Engagement: Approach to Carrying Out the Core Board Functions

As the TCH Governance Principles observe, ultimately, effective corporate governance is determined by the quality, skills, expertise and judgment, individually and collectively, of the members of the board.<sup>21</sup> Accordingly, an informed and actively engaged board is a core element of effective governance. Informed and active boards have a meaningful commitment to carrying out their core board functions, including guiding the strategic direction of the organization and providing effective and objective oversight of management's performance in carrying out its responsibilities.<sup>22</sup>

Informed and active engagement in the performance of core board functions, including what at times has been referred to as "challenges" to management, may be exhibited through several different types of actions, including by directors:

» asking informed, probing questions of

21 See TCH Governance Principles, Commentary to Section 7(a) for a discussion regarding board composition and the merits of having a board with a diversity of experiences and perspectives to draw upon in carrying out core board functions in an informed and active manner.

22 As the TCH Governance Principles note, the time commitment of directors will depend on the particular banking organization's circumstances. See TCH Governance Principles, Commentary to Section 1. The TCH Governance Principles recommend that, as a matter of sound corporate governance, a *substantial* majority (i.e., at least two-thirds) of directors of the top-tier entity within a banking organization should be independent. See TCH Governance Principles at page 15. The TCH Governance Principles also note that quality information is critical for the board or a board committee to function effectively, and for the directors to meet their duty of care. See TCH Governance Principles, Commentary to Section 12.

management (e.g., relating to assumptions underlying proposed initiatives);

- » taking steps as necessary to become satisfied 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);
- » 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;
- » defining the approach 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;<sup>23</sup>
- » reviewing and evaluating periodically board monitoring/oversight processes; and

23 According to the TCH Governance Principles, "[t]he board should, in one form or another, articulate an approach for determining what matters should be addressed at the board and committee level, so that individual board members and senior management are aware of, and operate consistently with, the board's expectations." TCH Governance Principles, Commentary to Section 12. This approach could include, for example, agreeing that the board or chair or lead director should approve or provide input on meeting agendas.

- » providing feedback on senior management’s performance.<sup>24</sup>

The 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.

As noted in the TCH Governance Principles, board effectiveness in carrying out its responsibilities is usually evidenced in ways other than by expressing disagreement with management proposals at board meetings, although directors must always feel free to express disagreement. As part of the overall reporting framework, board discussions with management may take place in several different forums outside of formal board meetings. For example, these forums may include sessions to review meeting agendas, informal board dinners with management, and company functions where board members meet with broader groups of employees. Moreover, a board that oversees an effective governance framework and maintains candid and informed communication with management

should generally expect management’s proposals to have been both thoughtfully fashioned and reviewed prior to presentation to the board and consistent with the organization’s strategic objectives and risk appetite.<sup>25</sup> Accordingly, rather than disagreements with or opposition to management, touchstones of informed and active board engagement more typically include the board’s involvement and performance in: (i) guiding the strategic direction of the organization, (ii) maintaining a sound oversight culture, (iii) communicating and demonstrating the “tone at the top”, and (iv) holding management accountable for its performance (including, in developing and implementing initiatives that are consistent with the organization’s strategic objectives and risk appetite statement, reputational concerns and regulatory expectations).<sup>26</sup> Moreover, management should provide pertinent information to the board that is clear, accurate, and timely and responsive to inquiries made by directors. This means material information distilled in a format meaningful and useful to directors.

24 The TCH Governance Principles point out that “[t]he 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 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.” TCH Governance Principles, Commentary to Section 4.

25 In carrying out informed and active oversight, the board of directors may find it useful to regularly meet with, and/or receive information from: management, risk officers, internal auditors, outside advisers and consultants, and bank examiners. See OCC Guidelines, at III.B; TCH Governance Principles, Sections 4, 10 and 15.

26 Holding management accountable for its performance is an inherent aspect of the core board functions. The board may specifically address and consider management’s performance with respect to each of the core functions, as well as overall, and reflect such accountability through the talent management process. See *also* Recommendation 1 and Note 40 below.



### III. Report Findings and Recommendations to Support and Strengthen the Ability of Directors to Focus and Actively Engage on Core Board Functions

TCH believes that prudential regulatory requirements that prescribe responsibilities for a large U.S. banking organization’s board – including those set forth in examination guidance addressing board governance – should, in general, reflect the performance of the core board functions identified above. That this does not always appear to be the case is a principal factor underlying the concerns described above that substantial board resources and attention may be devoted to matters that would be better suited for attention by senior management, or a management committee. As discussed above, board resources should be principally devoted to the board’s core functions, *e.g.*, engaging in broader strategic issues or oversight functions, taking discretionary “deep dives” in areas that may benefit from additional board attention, and/or attending to matters that banking and other regulators themselves believe are most important to safety and soundness and governance.

#### A. REPORT FINDINGS

The U.S. federal banking agencies have promulgated various regulations and guidance documents governing the composition and activities of the boards of directors and management, such as requirements relating to areas including audit functions, capital, liquidity, res-

olution and recovery planning, financial disclosure, conflicts of interest, and insider activities. These regulations and guidance documents frequently require or prohibit certain actions by the board of directors. The Annexes to this Report list, organize and summarize hundreds of such requirements directed at boards of directors – at the bank holding company and/or subsidiary bank levels – under U.S. federal banking laws, regulations and agency interpretive guidance statements, including examination guidance.<sup>27</sup>

Although certain regulatory requirements helpfully serve to direct board focus on fundamental safety and soundness issues, a number also extend beyond core board functions, requiring or potentially setting an expectation of board involvement (in some cases, on a recurring basis) that could divert attention from the board’s core functions (*e.g.*, from strategic and business-related oversight and analyses).

27 As the Annexes note, whether a requirement or component of examination guidance applies to a particular institution depends upon several different factors, including the institution’s charter type, and, in some cases, size. Moreover, in certain cases, it may not readily be apparent whether or not a particular requirement or component of examination guidance applies. Indeed, in practice, a substantial amount of time may be devoted to determining applicable requirements or guidance. For example, examination guidance is not generally intended to set definitive requirements for every institution or segment of the industry and examination guidance documents generally indicate that examiners are given some discretion in how to apply them. Nonetheless, examiners may apply components of examination guidance as if they are definitive requirements.



The types of requirements or guidance that present particular issues or concerns in this regard – whether on a stand-alone or collective basis, and whether at the holding company or subsidiary bank levels – generally fall into one or more of the following categories:<sup>28</sup>

- » Requirements or guidance that do not clearly specify whether a board responsibility may be satisfied by a committee of the board (*i.e.*, rather than only by the entire board).<sup>29</sup>
- » Requirements or guidance that do not clearly distinguish between the role of the

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28 TCH acknowledges the need to apply various components of examination guidance on the basis of the particular facts and circumstances applicable to the banking organization at issue. A two-way dialogue between a banking organization and its supervisors on the ways in which the organization's particular governance structure/approach suits its own unique circumstances can often serve as a productive means to inform an examiner's approach in this regard. See Part III.B, Recommendation 1 below for additional detail in this regard.

Although not binding as a matter of law, organizations may institute a "conservative approach" and follow many of the board-related standards set out in examination handbooks and manuals in order to mitigate the perceived or actual risks that not doing so could result in an examiner taking the view that the organization has not complied with a supervisory expectation.

29 By way of illustration, FRB guidance (FRB, Federal Reserve Supervisory Assessment of Capital Planning and Positions for LISC Firms and Large and Complex Firms, SR letter 15-18 (December 18, 2015)) provides that the board of directors must annually review and approve the banking institution's capital plan (without specifying whether the responsibility may be satisfied by a committee of the board). In contrast, the FRB's regulation known as the "capital plan rule" (which is cited in SR letter 15-18) specifically provides that a committee of the board may perform that particular function in question ("The bank holding company's board of directors or a designated committee thereof must at least annually and prior to submission of the capital plan . . . approve the bank holding company's capital plan."). FRB, Section 225.8 of Regulation Y (12 C.F.R. § 225.8) (the "Capital Plan Rule").

See Part III.B, Recommendation 2 below for a discussion of related concerns and recommendations (in particular, that there be general recognition that boards may utilize board committees to address board responsibilities where a regulatory pronouncement generically uses the term "board").

board and the role of management that may lead to uncertainty or confusion as to responsibilities and roles.<sup>30</sup>

- » Requirements or guidance that state or suggest that boards should "implement", "establish" or "develop" (or use similar words), as opposed to, *e.g.*, provide "oversight" of, policies or processes that are fundamentally the role of management.<sup>31</sup>
- » Requirements or guidance that broadly state or suggest that boards should review and approve all or virtually all firm policies (which could number in the hundreds), without seeking to distinguish fundamental or top-tier policies that more generally warrant specific board action from others.<sup>32</sup>
- » Requirements or guidance that state or suggest that boards should "periodically" review

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30 By way of illustration, FRB guidance prescribes that the "board of directors and senior management of a financial institution should determine whether proposed limitations [of contractual liability in service provider contracts] are reasonable when compared to the risks to the institution if a service provider fails to perform." FRB, Guidance on Managing Outsourcing Risk, SR 13-19 (December 5, 2013).

31 By way of illustration, federal banking agency guidance documents prescribe that boards **develop** a succession policy for key executives (as opposed to just the CEO) (OCC Director's Book, at 22 - 23) or **establish** standards for the review and approval of certain types of loans (Interagency Guidelines for Real Estate Lending Policies, at 12 C.F.R. Part 208, Appendix C; 12 C.F.R. Part 34, Appendix A to Subpart D; and 12 C.F.R. Part 365, Appendix A to Subpart A) and **formulate** policies and procedures for a bank purchasing commemorative coins (OCC, BC-58(Rev), Sup. 1 - Sale of Commemorative Coins (December 28, 1983)).

32 By way of illustration, certain regulatory pronouncements include a blanket statement to the effect that the board should "approve policies that set operational standards and risk limits". See the Large Bank Supervision booklet of the Comptroller's Handbook (2015).

See Part III.B, Recommendation 1 below for a discussion of recommendations around this point.

and/or approve policies and procedures relating to a particular compliance or business-level activity that do not warrant regular board consideration or validation through its own processes—or to approve the appointment of officers below the most senior levels.<sup>33</sup>

- » Requirements or guidance that require boards to “ensure” specific outcomes (e.g., management qualifications and effectiveness).<sup>34</sup> TCH believes that the word

33 In certain cases, agency guidance on specific products or activities acknowledges that the nature of the banking organization’s relevant policies may depend on the nature of the activity at issue and the extent to which the banking organization participates in it. However, even when the applicable requirement includes such an acknowledgement, it may nevertheless indicate that the relevant policies should be approved by the board of directors, or it may provide other prescriptive guidelines for the board. Moreover, guidelines for examiners in terms of the details of what these policies should include can be considerable and very technical in nature. See, e.g., the Asset-Based Lending booklet of the Comptroller’s Handbook.

By way of illustration, this category includes: (i) examination guidance documents that suggest examiners may expect bank boards to periodically review policies for specific categories of loans (e.g., agricultural loans) without a distinction made based on whether the specific type of loan represents a significant or insignificant part of the bank’s total loan portfolio (FRB Commercial Bank Examination Manual, Section 2140.1), and (ii) a regulation that a bank board have the responsibility to designate a security officer to develop and administer a security program for each banking office. (12 C.F.R. §§ 21.2, 326.2, 208.61(b)).

See Part III.B, Recommendation 1 below for a discussion of recommendations around this point.

34 By way of illustration, federal banking agency guidance documents state that the board must ensure that a third party to which the bank outsources collective investment fund management functions performs its functions in a safe and sound manner and in compliance with applicable laws and policy guidance (OCC, Risk Management Elements: Collective Investment Funds and Outsourced Arrangements, Bulletin 2011-11 (March 29, 2011)); the board and management should ensure that covenants related to supervisory actions or thresholds are not included in securitization documents (OCC, FDIC, FRB, and Office of Thrift Supervision, Interagency Advisory on the Unsafe and Unsound Use of Covenants Tied to Supervisory Actions in Securitization Documents (May 23, 2002)); and that the board must ensure that the information provided by management in IT reports is accurate, timely, and sufficiently detailed (OCC Director’s Book, at 39).

“ensure” should not, in general, be used without any further guidance, limitation or definition as to the meaning or scope of the term in the applicable context, because it suggests that the board can always guarantee various results. To the extent used, the word should be defined in accordance with realistic expectations, as the regulators from time-to-time do in enforcement orders.

It warrants specific mention that the Annexes, though detailed, do not cover many board requirements and supervisory expectations that apply, or could potentially be applied to, a particular board of a U.S. banking organization (whether at the top-tier holding company level (for public companies) or at the subsidiary bank level), making concerns that board resources may be devoted to matters that would be better suited for attention by management, even more pronounced. For example:

- » Certain items in the Annexes may appear as annual, semi-annual or quarterly requirements, when in practice the supervisory expectations may be for much more frequent involvement from the board or a board committee (e.g., in the context of capital planning and stress testing).
- » As noted previously, comprehensive corporate governance rules that establish the responsibility of a banking organization’s board of directors arise from state corporate and banking laws and related guidance as well as federal laws and regulations for public companies and exchange listing standards that are not included in the Annexes (relating to, *inter*



alia, financial disclosure, the auditing process, incentive compensation, ethical conduct, conflict of interest standards, internal controls over financial reporting, board composition and independence, and board committees).

- » Other supervisory handbooks not included within the scope of the Annexes (for example, the Federal Reserve Board Consumer Compliance Handbook and Federal Reserve Board Trading and Capital Markets Activities Manual) set out additional expectations for boards of directors.
- » Enforcement actions by bank regulators, as well as other supervisory communications, have imposed significant additional responsibilities on the boards of banking organizations.<sup>35</sup> For example, it is common for examiners to find multiple “matters requiring attention” (“MRAs”) during a regular exam, regardless of the organization’s size, and applicable guidance frequently requires boards to review every MRA, and authorize and/or adopt actions on behalf of the bank, including signing-off on the remediation plan and related changes to policies, processes, procedures, and controls. In practice, a substantial amount of board attention often is devoted to fulfilling requirements of MRAs.<sup>36</sup>

<sup>35</sup> Consent orders vary in the scope of requirements imposed on the board; for example, certain recent orders with banks have included requirements for boards to take intensive oversight responsibility for remediation, including completion of evaluations and assessments with respect to various operations, development and implementation of processes, and submissions of detailed written plans and progress reports to regulators.

<sup>36</sup> See FRB Supervisory Considerations for the Communication of Supervisory Findings, SR 13-13 (June 17, 2013); OCC Matters Requiring Attention, Bulletin 2014-52 (October 30, 2014).

## B. REPORT RECOMMENDATIONS

In view of the issues addressed above, and to strengthen and support the ability of directors to function effectively with respect to the core board functions, TCH offers the following recommendations:

### RECOMMENDATION 1: Regulatory Pronouncements Should Reflect the Performance of the Core Board Functions.

TCH believes that bank regulatory requirements and guidance should reflect, embrace and emphasize the performance of the core board functions set out above. TCH encourages regulators to specifically recognize the authority and utility of the board designating – whether formally or informally – senior management and/or management committees to address matters that do not warrant particular board time and attention.<sup>37</sup> Such statements should be made in future regulations and guidance and during the course of examinations or other agency discussions with banking organization officials, as and where necessary.

By way of illustration, three of the specific contexts in which this general approach may be applied in practice are described below:

### BOARD INVOLVEMENT IN THE REVIEW AND APPROVAL OF POLICIES/PROCEDURES AND RELATED MATTERS.

Although core board functions include review and/or approval of certain policies fundamental to the safe-and-sound

<sup>37</sup> As discussed elsewhere in this Report, such designations should ordinarily be accompanied by periodic reporting to the board or its committees, appropriate review at the board level, review/testing by control functions, and escalation of “red flags” that require board attention, as appropriate under the circumstances.

operation of the organization (e.g., the capital plan), for most large U.S. banking organizations the vast majority of policies and procedures that govern day-to-day operations of businesses should not fall within that category. Accordingly (subject to applicable law and/or fundamental safety-and-soundness considerations), agencies and examiners should encourage directors to determine which policies and issues warrant board level approval and attention in view of the individual organization's circumstances.<sup>38</sup>

A 2011 Georgia Department of Banking and Finance report recognizes that the cumulative impact of requiring board review or approval of these individual matters may result in an overload on the board that is counterproductive and suggests the following approach:

*"... 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*

38 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 bank'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 be permitted flexibility in the manner it seeks to address these matters.

*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. . ."*<sup>39</sup>

As reflected in the TCH Governance Principles, TCH 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 in the ordinary course (for example, absent any "red flags" or unless it is otherwise determined that the circumstances warrant specific board attention/approval). Moreover, in its oversight role, the board should receive sufficient information from applicable management or management committees – and external sources where appropriate – to assess whether current approaches and policies continue to be appropriate over time in light of changes in the market or other conditions.<sup>40</sup>

**BOARD INVOLVEMENT IN OVERSIGHT OF KEY PLANNING PROCESSES AND BOARD REVIEW OF REPORTS AND RELATED INFORMATION.** As noted previously (see Part I, Core Board Function 4

39 Georgia Department of Banking and Finance, *The Control Environment: Effective Systems of Internal Controls* (Oct. 2011).

40 See also TCH Governance Principles, Commentary to Section 4 ("In overseeing management's performance, the board should review and monitor key business policies and procedures for conformance with the overall strategic objectives approved by the board and with the general legal, regulatory and business environment in which the organization operates.")



above), core board functions include oversight of fundamental risk management and compliance planning processes (e.g., capital/liquidity planning/stress testing, financial, capital and risk profile reporting and disclosure processes, information security, outsourcing and recovery processes, and compliance standards and processes). As a general matter, oversight for such fundamental processes principally involves: (i) (in many cases) approval of the top-tier policy/plan (as described in detail above in Part I, Core Board Function 4 and Part III, Recommendation 1), and (ii) oversight of bank planning actions, processes and activities via active and informed engagement/discussions with senior management, receipt of pertinent information and related actions (such as those outlined in Part I, Core Board Function 4 and Part II).<sup>41</sup>

Effective oversight of bank planning actions, processes and activities requires the board's receipt and review of reports and information on key conclusions, recommendations and significant issues (including, any material process weaknesses). As noted above, senior management should highlight for the board material or significant problem areas related to fundamental risk-management processes. Moreover, as also described above, designations of authority/responsibility by the board to management should generally convey expectations relating to ongoing and special reporting to the board. Absent special considerations, however, agencies are encouraged to clarify and/or adopt the position that, as a general matter, *materiality standards* (i.e., from a board reporting perspective) should

be applicable to any risk, audit or comparable reports or related information required to be presented to the board under agency regulations or guidance. For example, mandatory board review of reports identifying any process issues or weaknesses (i.e., irrespective of the significance of the identified issues/weaknesses) could unnecessarily divert board attention from its critical core functions. Accordingly, the board, in consultation with management, should determine the type of information (e.g., items relating to a process weakness or otherwise) that is sufficiently meaningful to warrant review by the board in its oversight of key planning processes and operations.<sup>42</sup> A banking organization's approach in this regard may be implemented through internal risk management and governance processes.

As boards often receive separate briefings on topics that overlap with or relate to key risk-management processes (e.g., briefings on the quarterly financial performance of the institution and its significant business lines) agencies are encouraged to consider whether mandatory (or recommended) board briefings or reports included in agency guidance or regulations may be redundant of other reports and, if so, clarify that it should be unnecessary to present the same information to the board multiple times in order to satisfy various regulatory requirements. For example, requiring the same information to be provided as part of a quarterly capital planning/risk-management

41 See, e.g., SR letter 15-18 (setting out expectations for board oversight of the capital planning process).

42 As discussed above in Part II, the TCH Governance Principles note, "The board should, in one form or another, articulate an approach for determining what matters should be addressed at the board and committee level, so that individual board members and senior management are aware of, and operate consistently with, the board's expectations". See TCH Governance Principles, Commentary to Section 12.

report as during a financial performance report would seem to have little marginal benefit in terms risk management.

Moreover, in its oversight role, the board should, as noted above, receive sufficient information from applicable management or management committees or other sources to assess whether current approaches, including mitigating steps to address process weaknesses, are appropriate in the board's view. In general, however, it should not be necessary – and, indeed, may be counterproductive – for the board to perform management-like responsibilities (*e.g.*, such as formally “approving,” or developing, planning activities, strategies or mitigating steps to address planning process weaknesses, or carrying out other risk-management and planning-related activities undertaken in the ordinary course of business) in order to provide effective oversight of the planning/risk-management process.

**BOARD INVOLVEMENT IN OVERSEEING THE REMEDIATION OF MRAs.** In the context of board involvement in overseeing the remediation of MRAs, as noted above, Federal Reserve Board Governor Tarullo noted in a 2014 speech referred to above, that “there 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.” TCH believes that it is critical that compliance with the specific requirements of MRA-related obligations should not be permitted to distract the board from its broader functions.

As reflected in the TCH Governance Principles, TCH believes that it is appropriate to expect the

board of directors to oversee the process in place, and monitor the progress of the remediation of MRAs as well as other regulatory findings and actions (*e.g.*, through receipt of reports from management, internal audit and/or examiners). Unless fundamental safety and soundness or other special considerations are at issue, however, regulators are encouraged to clarify and/or adopt the position that, as a general matter, it should not be necessary for the board to perform management-like responsibilities in connection with an MRA. These may include, for example, approval of remediation plans, changes to the organization’s policies, processes, procedures, and controls and/or sign off on remediation progress reports. TCH recognizes that boards may, as a practical matter, become more active in some or all of these areas to the extent supervisory findings are escalated to formal actions or the progress in resolving identified deficiencies does not meet board or examiner expectations.

**RECOMMENDATION 2: General Recognition by the Agencies that Boards May Utilize Board Committees to Address Board Responsibilities Where a Regulatory Pronouncement Generically Uses the Term “Board.”**

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.<sup>43</sup> Board committees, in turn, are

<sup>43</sup> See Delaware General Corporation Law § 141(c); Model Business Corporation Act § 8.25(d). See also Federal Reserve Board, Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17,240, 17,248 (Mar. 27, 2014) (discussing the delegation of certain risk management oversight responsibilities to the risk committee of the board).



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.<sup>44</sup>

Increasingly, agency guidance statements and regulations helpfully explicitly clarify 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 approval.<sup>45</sup> However, many agency issuances do not contain such statements, at times leading to uncertainty relating to applicable regulatory expectations.

TCH 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 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 atten-

tion to the issue (e.g., in such technical areas as liquidity risk tolerances) may be an efficient allocation of responsibility.<sup>46</sup>

In view of the foregoing, TCH recommends that the agencies take steps as appropriate (which may include, e.g., highlighting the point during examiner training, clarifying existing guidance, and future agency issuances) to clarify that when a regulatory pronouncement generically uses the term “board” – unless the meaning is otherwise clear – it should be reasonable for a banking organization to adopt an interpretation of the pronouncement to mean either the full board or a board committee. At a minimum, clarification in this regard would recognize the appropriateness of committee level consideration and vetting of issues even in cases where the full board ultimately carries out the formal “approval.” For example, 12 C.F.R. § 252.34(a) requires the full board of a U.S. bank holding company with total consolidated assets of \$50 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 recommended to the full board for its approval.

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.

45 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 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 the Capital Plan Rule.

46 As discussed elsewhere in this Report, matters that do not warrant particular board time should be appropriately carried out by management (not by a board committee).

### **RECOMMENDATION 3: The Agencies Should Conduct Periodic Reviews of the Board Requirements and Standards They Promulgate.**

In order to support and strengthen the ability of large U.S. banking organization boards to focus on their core functions, TCH recommends that U.S. banking agencies conduct periodic reviews of the board requirements included in their regulations and guidance statements, including in examination guidance, to assess whether the requirements and standards in effect at any given time reflect or meaningfully contribute to the performance of those core responsibilities.<sup>47</sup>

A comprehensive assessment of board requirements included in the entirety of an agency's regulations and guidance statements may help reveal the full extent of those requirements and aid the agency's determination of whether they continue to retain their relevance and reflect the core board functions.

Board requirements that may have been prescribed in response to a particular concern may no longer be relevant once experience with a particular area has mitigated its risk; experience has shown that detailed prescriptions that seem apposite for an issue at a point in time may lose their relevance with changing circumstances. Such a review should also help to curtail statutory requirements for board actions that are outmoded or unnecessary.

<sup>47</sup> Such reviews would appear to be particularly useful in view of the fact that the current Economic Growth and Regulatory Paperwork Reduction Act ("EGRPRA") review of existing regulations does not cover agency guidance. Accordingly, there do not appear to be opportunities for commentators to provide formal feedback on such guidance as part of the EGRPRA process.

As part of such a periodic review, a U.S. banking agency should consider how best to take into account relevant regulations and/or guidance issued by other U.S. authorities (e.g., the Securities and Exchange Commission, the CFPB and other U.S. federal banking agencies) to promote a consistent understanding of expectations.

Finally, as part of such a review, agencies should consider whether more recently issued requirements or guidance are clear in terms of whether previous regulations/guidance addressing the same or similar board responsibilities have been replaced or suspended.

### **RECOMMENDATION 4: The Agencies, Directors and the Industry Should Participate in a Continuing Dialogue to Advance Their Common Interest in Promotion of Effective Board Governance at Large U.S. Banking Organizations.**

As discussed above, TCH believes that banking organizations and their regulators can advance the development of banking organization governance by emphasizing areas of appropriate focus for boards and management in ways that provide the most effective governance. Continued dialogue with the industry around the issues addressed in this Report – including how each of the banking and supervisory communities can best strengthen and support the ability of directors of large U.S. banking organizations to effectively perform their core board functions – should be an effective means to promote and help achieve this end.



## **ABOUT THE CLEARING HOUSE**

The Clearing House is a banking association and payments company that is owned by the largest commercial banks and dates back to 1853. The Clearing House Payments Company L.L.C. owns and operates core payments system infrastructure in the United States and is currently working to modernize that infrastructure by building a new, ubiquitous, real-time payment system. The Payments Company is the only private-sector ACH and wire operator in the United States, clearing and settling nearly \$2 trillion in U.S. dollar payments each day, representing half of all commercial ACH and wire volume. Its affiliate, The Clearing House Association L.L.C., is a nonpartisan organization that engages in research, analysis, advocacy and litigation focused on financial regulation that supports a safe, sound and competitive banking system.

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