The Federal Reserve's Final Board Effectiveness Guidance for Large Financial Institutions

VISUAL MEMORANDUM

March 3, 2021

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Background

Background

- On February 26, 2021, more than three years after it was proposed, the Board of Governors of the Federal Reserve System (**Federal Reserve**) released final supervisory guidance on board of directors' effectiveness (**Board Effectiveness Guidance**).
- The final Board Effectiveness Guidance is a key milestone in the Federal Reserve's multi-year review of the practices of boards of directors, particularly at the largest banking organizations.
- As then-Governor and now-Chair Jerome Powell explained in the spring of 2017, a key purpose of the Federal Reserve's review of its supervisory expectations for boards of directors was to enable boards to "focus on setting the overall strategic direction of the firm, while overseeing and holding senior management accountable" rather than being distracted "by an overly detailed checklist of supervisory process requirements."
- The finalized Board Effectiveness Guidance is generally consistent with this principle, and therefore should be welcomed by banking organizations – see slides 7 – 22 for further information.
- In addition to finalizing the Board Effectiveness Guidance, the Federal Reserve also announced the results of its review of 27 Supervision and Regulation and Consumer Affairs letters (for convenience, **SR Letters**) which contain supervisory expectations for boards – see slides 25 – 32 for our deep dive into the SR Letters.

Background

- As discussed in our previous visual memorandum, the Federal Reserve finalized a new supervisory rating system for large financial institutions (**LFIs**) in November 2018.
  - The LFI rating system includes a **Governance and Controls** component that evaluates the effectiveness of a firm's board of directors, its management of business lines, its internal risk management, its internal controls and, for U.S. G-SIBs, its recovery planning.
- The Federal Reserve believes that the Board Effectiveness Guidance builds on the principles set forth in the LFI rating system, and intends to use the Board Effectiveness Guidance in informing its assessment of the governance and controls at all firms subject to the LFI rating system.
- The Federal Reserve also proposed, in early January 2018, supervisory guidance for senior management, business line management, independent risk management (**IRM**) and internal controls (the **Management Guidance**).
  - Like the Board Effectiveness Guidance, the Management Guidance would, when finalized, inform the Federal Reserve's evaluation of an LFI's governance and controls.
  - Nothing in the Federal Reserve's release of the Board Effectiveness Guidance mentions the Management Guidance, which remains a proposal.

Applicability

Applicability

- The Board Effectiveness Guidance applies to:
  - All domestic bank holding companies (**BHCs**) and domestic savings and loan holding companies (**SLHCs**) with total consolidated assets of **$100 billion or more.**
    - The $100 billion asset threshold for application of the Board Effectiveness Guidance is a change from the 2017 proposal, but is consistent with the Economic Growth, Regulatory Relief and Consumer Protection Act (**EGRRCPA**)**,** enacted in 2018, and with the US banking agencies' later revisions to the thresholds for the application of certain enhanced prudential standards.
      - By applying to all SLHCs above the $100 billion asset threshold, the Board Effectiveness Guidance goes further than the LFI rating system, which does not apply to insurance or commercial SLHCs, regardless of size.
  - Systemically important nonbank financial companies designated by the Financial Stability Oversight Council for supervision by the Federal Reserve (currently none).
- U.S. intermediate holding companies (**IHCs**) of foreign banking organizations established pursuant to the Federal Reserve's Regulation YY are **not subject** to the Board Effectiveness Guidance.
  - When the Board Effectiveness Guidance was first proposed in 2017, the Federal Reserve stated that it anticipated proposing guidance on board effectiveness for IHCs at a later date.
  - The Federal Reserve has not yet done so, and the final Board Effectiveness Guidance is silent as to any next steps related to IHCs.

Final Board Effectiveness Guidance

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Final Board Effectiveness Guidance

OVERVIEW

Board Effectiveness

- Like the proposal, the final Board Effectiveness Guidance sets forth supervisory expectations for boards as distinct from expectations for senior management and identifies **five key attributes** of effective boards. The wording of the five key attributes is slightly revised from the proposal but is consistent with the LFI rating system.

No One-Size-Fits-All

- Consistent with the proposal, the final Board Effectiveness Guidance is a "**principles-based approach**" that "reflects the view that including standardized expectations would not take into account material differences in activities, risk profile, and complexity among large financial institutions as they relate to boards of directors."

Five Key Attributes	
1.	Set clear, aligned and consistent direction regarding firm's strategy and risk appetite
2.	Direct senior management regarding the board's information needs
3.	Oversee and hold senior management accountable
4.	Support the independence and stature of the firm's independent risk management and internal audit functions
5.	Maintain a capable board composition and governance structure

Final Board Effectiveness Guidance

INTERACTION WITH OTHER LEGAL REQUIREMENTS

- The Board Effectiveness Guidance notes in its introduction that none of its contents are believed to conflict with any other legal, regulatory or listing requirements.
- We believe that the guidance is not intended to exceed any applicable state law fiduciary duties.
  - The absence of any federal general common law (see *Erie Railroad Company v. Tompkins*, 304 US 64 (1938)) or any statutory authority on the fiduciary duties of boards means that the banking agencies do not have the power to override or change binding state law fiduciary duties.
  - In a recent change to its Director's Book, which explains the role of directors of national banks and federal savings associations, the OCC made this point clear by noting explicitly that the corporate governance expectations discussed in the Director's Book "are not intended to . . . exceed[] applicable state law requirements."
- In essence, the Board Effectiveness Guidance, like the OCC's Heightened Standards, is best viewed as allocating tasks and responsibilities to boards rather than changing any fiduciary duties.
- It is an open question whether courts will, in the future, be influenced by the supervisory expectations or the tasks assigned in their analysis of state law fiduciary duties either under the duty of care or the duty of loyalty.
  - The *Caremark* line of cases, including *Marchand* and *Clovis*, all under Delaware law, is the current focus of plaintiff's lawyers.

Final Board Effectiveness Guidance

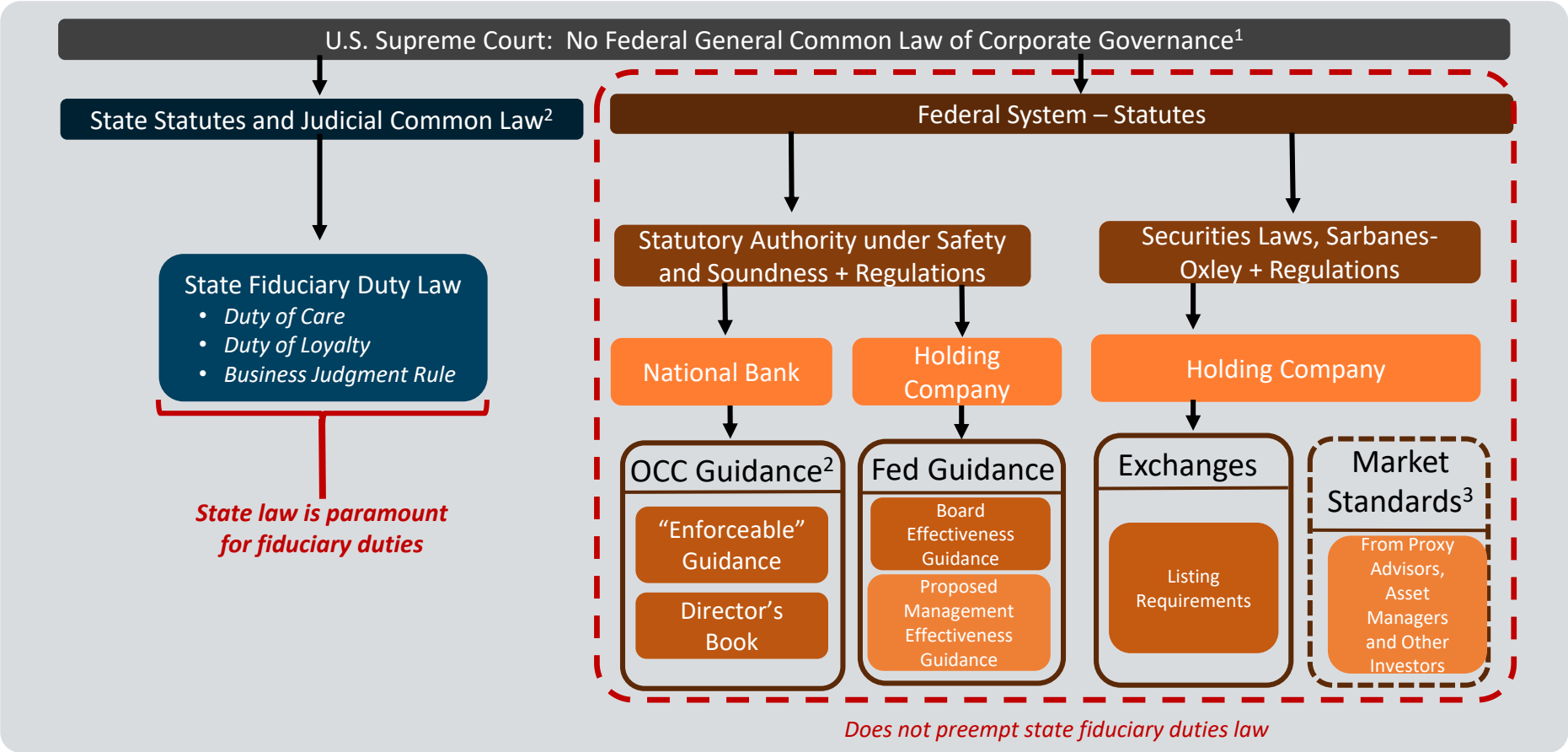
INTERACTION WITH OTHER LEGAL REQUIREMENTS

- There are different bodies of law, guidance and market standards that apply to the boards of holding companies and their subsidiary banks.
- The visual on the following slide illustrates the interaction among the various bodies of law, guidance and market standards.
- The Dodd-Frank Act, as amended by the EGRRCPA, and the Federal Reserve's Regulation YY requires BHCs or SLHCs with total consolidated assets of $50 billion or more to maintain risk committees with independent members. Similarly, audit and compensation committees are subject to certain requirements under the Sarbanes-Oxley Act and SEC regulations.
- We believe that the Board Effectiveness Guidance is consistent with listing standards to which publicly traded BHCs and SLHCs are already subject, and with corporate governance recommendations made by large asset management firms and proxy advisors.

Final Board Effectiveness Guidance

INTERACTION WITH OTHER LEGAL REQUIREMENTS

- This visual shows the interaction among the various bodies of law and guidance applicable to a public holding company with a bank subsidiary.



[1] Under OCC guidelines, including 12 CFR § 7.2000, a national bank elects to follow the corporate governance of a chosen state law.
[2] OCC standards not applicable to state chartered banks.
[3] Market standards are a form of private guidance or soft law.

Final Board Effectiveness Guidance

INTERACTION WITH OTHER LEGAL REQUIREMENTS

Interaction with OCC Heightened Standards

- There is complete or substantial overlap between the members of the boards of many large BHCs or SLHCs, where the Board Effectiveness Guidance applies ($100 billion), and the members of the boards of their national bank or federal savings association subsidiaries, where the OCC's Heightened Standards apply ($50 billion).
- We believe that there is no substantive conflict between the Board Effectiveness Guidance and the OCC's Heightened Standards. As written, they focus on slightly different board tasks and responsibilities.
- Different supervisory agencies or examiners may look at the same pattern through these different lenses.

Final Board Effectiveness Guidance – Five Key Attributes
1. Set clear, aligned and consistent direction regarding firm's strategy and risk appetite
2. Direct senior management regarding the board's information needs
3. Oversee and hold senior management accountable
4. Support the independence and stature of the firm's independent risk management and internal audit functions
5. Maintain a capable board composition and governance structure

OCC's Heightened Standards for Boards of Directors
A. Require an Effective Risk Governance Framework
B. Provide Active Oversight of Management
C. Exercise Independent Judgment
D. Include Independent Directors
E. Provide Ongoing Training to All Directors
F. Annual Self-Assessments

For further details on the OCC's Heightened Standards, refer to our 2014 visual memorandum

Final Board Effectiveness Guidance

KEY CHANGES TO THE PROPOSAL

- In a notable departure from the proposed board effectiveness guidance, the final Board Effectiveness Guidance **removes the suggestion** in the proposal that a board provide the results of any **self-assessment** of its effectiveness to supervisors for the Federal Reserve to take into consideration in its evaluation.
  - The Federal Reserve noted that many commenters had observed that requiring boards to share their self-assessments with the Federal Reserve could chill the candor of such self-assessments, thus undermining their value.
  - The Federal Reserve went on to observe that, "[b]ecause examiners draw on a variety of information when assessing the effectiveness of board oversight, [it] agreed with commenters that providing the results of self-assessments was not needed."
- The policy reasons behind the choice to remove the requirement that written evaluations be shared are valid ones because the best board self-evaluations are highly candid.
- As a result, we believe that supervisory staff at the Federal Reserve should not feel empowered by the silence in the final guidance to ask to see such evaluations.
  - It is to be hoped that OCC supervisory staff will also be convinced by the Federal Reserve position on self-evaluations.

Final Board Effectiveness Guidance

KEY CHANGES TO THE PROPOSAL

- Further, the final Board Effectiveness Guidance made edits to all five key attributes to **clarify the distinction between the roles of a board of directors and of management**.
  - For example, in clarifying that an effective board should "**direct**" management to provide it with the information needed to make well-informed decisions, **rather than "actively manage"** such information flow, the final Board Effectiveness Guidance specifically **reflects a rejection of a comment** that "management should control the flow of information to the board."
    - The Fed stated that "Boards are in the best position to determine their information needs," and therefore the final Board Effectiveness Guidance "does not include specific practices that boards should adopt."
  - These clarifying changes are consistent with the types of changes made in the 2020 update to the OCC Director's Book, which reduced references to a board's duty to "ensure" an outcome, favoring actions intended to "support" or "promote" results instead.

Final Board Effectiveness Guidance

KEY CHANGES TO THE PROPOSAL

- Additional **changes** in the final Board Effectiveness Guidance include:
  - Elimination of the requirement **that the risk committee be involved in determining membership of management committees,** which would arguably have conflicted with requirements applicable to the risk committee.
  - **Multiple references to "safety and soundness and compliance with laws and regulations"** as important goals of effective oversight.
  - **Additional examples of effective board practices.**
  - An explicit reference to a director selection process that "considers **a diverse pool of potential nominees**, including women and minorities."
  - An increase in the **threshold for applicability** of the Board Effectiveness Guidance **from $50 billion to $100 billion** in total consolidated assets.
  - Clarification in the summary of comments that **board minutes need not include detailed records of individual questions and answers** provided by directors to show that the board is holding senior management accountable.
    - This clarification aligns with best board practices in board minute taking.

Final Board Effectiveness Guidance

ATTRIBUTE #1 – SET CLEAR, ALIGNED AND CONSISTENT DIRECTION REGARDING THE FIRM'S STRATEGY AND RISK APPETITE

- An effective board **oversees** the development of and approves, and periodically monitors, the firm's strategy and risk appetite, which should be **clear and aligned** and include a **long-term perspective on risks and rewards** consistent with the capacity of the firm's risk management framework.
  - Although the final Board Effectiveness Guidance for attribute 1 is generally consistent with the proposed guidance, it more clearly distinguishes the board's role in setting a firm's strategy and risk appetite from management's role by stating that an effective board ***oversees*** the development of the firm's strategy and risk appetite, rather than ***guiding*** the process.
- An **aligned strategy and risk appetite** helps a firm "maintain sufficient financial and operational strength and resilience for safety and soundness and to promote compliance with laws and regulations."
  - A firm's strategy and risk appetite are aligned when they are developed, reviewed and approved consistent with one another but do not have to be developed and approved simultaneously to be aligned.
- A **clear strategy** articulates a firm's strategic objectives for its businesses and helps establish and maintain:
  - An effective risk management structure;
  - Appropriate processes and resources for strategy implementation plans and budgets for each business line and risk management or control function;
  - An effective risk management and control function; and
  - Direction to senior management about how to determine which business opportunities to pursue consistent with the firm's risk appetite and risk management capacity.

Final Board Effectiveness Guidance

ATTRIBUTE #1 – SET CLEAR, ALIGNED AND CONSISTENT DIRECTION REGARDING THE FIRM'S STRATEGY AND RISK APPETITE

- A **clear risk appetite**:
  - Includes sufficient detail for the chief risk officer (**CRO**) and IRM to set firm-wide risk limits; and
  - Specifies the level and types of risk that the board is willing to assume, that the board believes the firm is capable of managing, and that allows senior management to establish risk management expectations and monitor risk-taking for the full set of risks.
- An effective board also **reviews and approves significant policies, programs and plans** based on the firm's strategy, risk appetite, risk management capacity, and structure.*
  - A firm's policies, programs, and plans should be sufficiently clear regarding the allocation of responsibilities to enable the board to evaluate senior management's execution of the firm's strategic plan.
  - An effective board can review summarized forms of policies, programs and plans as long as those summaries include sufficient detail and context for the board to make an informed decision and to consider consistency with the firm's strategy, risk appetite, and risk management capacity.

According to the final Board Effectiveness Guidance, significant policies, programs and plans include, but are not limited to, the following:

- Capital plans
- Recovery and resolution plans
- Audit plans
- Enterprise-wide risk management policies
- Liquidity risk management policies
- Compliance risk management program
- Performance management and compensation programs

* In its review of SR Letters, the Federal Reserve removed certain policies, programs and plans, from the list of policies, programs and plans that necessarily warrant board review and approval. See slides 25-32 for more information on the Federal Reserve's SR Letter review.

Final Board Effectiveness Guidance

ATTRIBUTE #2 – DIRECT SENIOR MANAGEMENT REGARDING THE BOARD'S INFORMATION NEEDS

- An effective board **directs senior management** to provide directors with information that is sufficient in scope, detail, and analysis to enable the board to make sound, well-informed decisions and consider potential risks.
  - The final Board Effectiveness Guidance clarifies the role of the board as one of oversight by stating that an effective board **directs, rather than actively manages,** senior management regarding information flow.
  - Boards should direct senior management to provide information that is timely and accurate, with the appropriate level of detail and context to enable the board to make sound, well-informed decisions.
  - Boards should **evaluate the sufficiency and quality of information flows** they receive. If information flow is insufficient or of unacceptable quality, boards should direct senior management to make improvements, including by directing management to provide more information or to address board concerns regarding the **volume, structure, content or quality of the information** provided. Boards should also, when necessary, direct management to improve relevant processes and practices for the preparation of board information.
- Directors may **seek additional information** about the firm and its activities, risk profile, talent, and incentives outside routine board and committee meetings.
  - Director training is another way for directors to learn more about topics relevant to their responsibilities.
- Directors should take an active role in **setting board meeting agendas** such that the content, organization, and time allocated to each topic allows the board to discuss strategic tradeoffs and to make sound, well-informed decisions. In a change from the proposed guidance, the final Board Effectiveness Guidance highlights the role of the lead independent director or independent board or committee chairs in setting agendas.

Final Board Effectiveness Guidance

ATTRIBUTE #3 – OVERSEE AND HOLD SENIOR MANAGEMENT ACCOUNTABLE

- An effective board **oversees and holds senior management accountable** for effectively implementing the firm's strategy, consistent with its risk appetite and while maintaining the firm's risk management and control framework and system of internal controls.
  - An effective board executes this responsibility consistent with safety and soundness and in compliance with laws and regulations, including those related to consumer protection, under a range of conditions.
- An effective board should **actively engage** senior management in a variety of ways, including by allocating time in board meetings, encouraging diverse views, challenging senior management when warranted, and engaging senior management outside of board and committee meetings.
- An effective board engages in robust inquiry into, among other things:
  - Drivers, indicators, and trends related to current and emerging risks;
  - Adherence to the board-approved strategy and risk tolerance appetite by relevant lines of business; and
  - Material or persistent deficiencies in risk management or control practices, whether in policy or in practice.
- The final Board Effectiveness Guidance adds a new paragraph specifying that an effective board should **review reports of internal and external complaints**, including whistleblower reports.

Final Board Effectiveness Guidance

ATTRIBUTE #3 – OVERSEE AND HOLD SENIOR MANAGEMENT ACCOUNTABLE

- **Independent directors** should be sufficiently empowered to serve as a **check on directors who are firm executives and on senior management**.
- An effective board should **regularly oversee and evaluate** the **performance and compensation** of senior management, including overseeing, evaluating, and holding senior management accountable for the development and implementation of performance management and compensation programs.
  - A board should establish and approve clear financial and nonfinancial performance objectives that are aligned with the firm's strategy and risk tolerance for the CEO, CRO and Chief Audit Executive (**CAE**) and other members of senior management as appropriate.
- An effective board should approve and periodically reassess **succession plans** for the CEO and, depending on the size, complexity and nature of the firm, the CRO and CAE or other senior management officials.

Final Board Effectiveness Guidance

ATTRIBUTE #4 – SUPPORT THE INDEPENDENCE AND STATURE OF IRM AND INTERNAL AUDIT

- Risk and audit committees should **assess and support the independence and stature of the IRM and internal audit functions.**
- An effective board monitors the independence and stature of IRM and internal audit and **takes action if the views of either of these functions are not taken into account** when decisions are made or if these functions are **unduly influenced by business lines.**
- A **risk committee** should:
  - Communicate directly with the CRO on material risk management issues;
  - Oversee the appropriateness of IRM's budget, staffing, and systems of internal controls;
  - Coordinate with the compliance function;
  - Provide IRM with direct and unrestricted access to the risk committee; and
  - Be able to effect changes that align with the firm's strategy and risk tolerance.
- An **audit committee** should:
  - Meet directly with the CAE regarding the internal audit function;
  - Support internal audit's budget, staffing, and systems relative to the firm's size and complexity and the pace of technological and other changes; and
  - Review the status of recommendations to remediate deficiencies and supervisory findings.

Active engagement by directors on the risk committee and audit committee entails inquiring into (among other things):

- The causes and consequences of material or persistent breaches of risk appetite and risk limits;
- The timeliness of remediation of material or persistent internal audit and supervisory findings; and
- Appropriateness of the annual audit plan.

Final Board Effectiveness Guidance

ATTRIBUTE #5 – MAINTAIN A CAPABLE BOARD COMPOSITION AND GOVERNANCE STRUCTURE

- An effective board considers whether its **composition, governance structure, and practices** support the firm's safety and soundness and are appropriate for the firm's asset size, complexity, operations and risk profile, as they change over time.
- Directors should have a **diversity of skills, knowledge, experience, and perspectives.**
  - The process for identifying and selecting director nominees should consider a potential nominee's expertise, availability, integrity, and potential conflicts of interest, and should consider a diverse pool of potential nominees, including minorities and women.
- An effective board maintains a **governance structure** that is capable of overseeing and addressing issues arising from the firm's size, operations, activities, risk profile, and resolvability.
  - A board should engage third-party advisors and consultants, when appropriate, to supplement its knowledge, expertise and experience.
- Consistent with the proposal, the final Board Effectiveness Guidance notes that an effective board should evaluate its strengths and weaknesses on an ongoing basis, including the performance of the board committees, particularly the risk, audit, and other key committees.
  - As noted above, however, there is no a longer a suggestion that a board's evaluation of its performance be provided to the Federal Reserve for review.

Governance structure refers to the structure of board committees and to management-to-committee reporting lines. The final Board Effectiveness Guidance notes that management-to-committee reporting lines should support effective oversight, timely access to information, and sound decision-making.

Board Involvement in Federal Reserve Communication of Supervisory Findings

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Board Involvement in Federal Reserve Communication of Supervisory Findings

- In 2017, when proposing the Board Effectiveness Guidance, the Federal Reserve also proposed new guidance governing the communication of supervisory findings, which would have replaced the guidance currently found in SR Letter 13-13.
- SR Letter 13-13 provides that Matters Requiring Immediate Attention (**MRIAs**) and Matters Requiring Attention (**MRAs**) should generally be directed **to the board**, with the board in turn directing management to take corrective action, providing management with appropriate oversight and approving management actions as necessary.
- In 2017, the Federal Reserve proposed to instead typically **direct MRIAs and MRAs to senior management**, rather than to the board. As proposed, supervisory staff would direct MRIAs and MRAs to the board itself, or an executive-level board committee, only when either:
  - The supervisory finding relates to significant weaknesses in the board's governance structure or practices; or
  - Senior management has failed to take appropriate remedial action with respect to a supervisory finding that was originally addressed to senior management.
- SR Letter 13-13 has, for now, been retained without change.
  - In its summary of comments on the proposal, the Federal Reserve stated that its staff "continues to consider ways to improve the clarity and consistency of supervisory communications, including public feedback, related to SR Letter 13-13."

Revisions to Other Supervisory Guidance Applicable to Boards

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Revisions to Other Supervisory Guidance Applicable to Boards

- When it proposed the Board Effectiveness Guidance in 2017, the Federal Reserve noted that it was in the process of a two-phase review "of all existing supervisory expectations and regulatory requirements relating to boards of directors of bank and savings and loan holding companies of all sizes."
- In the first phase, the Federal Reserve focused on SR Letters, and in 2017 preliminarily identified 27 SR Letters for potential elimination or revision.
- On the same day it released the final Board Effectiveness Guidance, the Federal Reserve announced the completion of the first phase of its review.
- Of the 27 SR letters that it identified in 2017, the Federal Reserve has decided to **revise twelve** SR Letters, **make inactive nine** SR Letters, and **retain six** SR letters without change.
  - The following slides contain a detailed summary of the disposition of each of the 27 SR Letters identified in 2017.
- Our deep dive into the changes in the SR Letters shows a pattern of removing "ensure" in favor of "oversight" or other similar words or removing a requirement that the board, as opposed to the institution, review or approve a policy or action. In general, the clear trend is towards fewer tasks for the board and a greater understanding of the board's oversight role.
- The Federal Reserve in 2017 described the second phase of its review as "focused on requirements and supervisory expectations set forth in Board regulations or in various forms of interagency guidance" and stated that it expected to propose changes to these regulations and interagency guidance documents at a later date.
  - In last week's actions, the Federal Reserve did not provide an update on the status of this phase of its review.

Revisions to Other Supervisory Guidance Applicable to Boards – Revised Letters

Letter	Disposition	Comments
SR 13-19 Guidance on Managing Outsourcing Risk	Revised	Revised to provide that, while senior management should establish policies governing the use of service providers, there is no longer an explicit requirement for the board to approve each such policy. In addition, a few references have been changed to no longer state that the "board of directors and senior management should…" but to instead state that "financial institutions should…"
SR 11-15 Disposal of Problem Assets through Exchanges	Revised	Revised to provide that, while the firm should have risk tolerance and risk mitigation policies, there is no longer an explicit requirement for the board to itself establish those policies. In addition, the Federal Reserve made edits to acknowledge that discussions concerning asset exchanges may take place at the management, rather than board, level.
SR 11-14 Supervisory Expectations for Risk Management of Agricultural Credit Risk	Revised	Revised to remove the explicit reference to a banking organization's analysis of market conditions being provided to senior management and the board.
SR 08-8 Compliance Risk Management Programs and Oversight at Large Banking Organizations with Complex Compliance Profiles	Revised	A number of potentially important revisions, including, among others: • Rather than the board and senior management working together to establish a compliance risk management program, senior management is responsible for establishing and implementing the program, under the board's oversight. • There is no longer an explicit statement that the board sets the compliance culture, establishes policies and ensures adherence to those policies. Instead, both the board and senior management should encourage ethical conduct through the firm's culture. • Several deletions of sentences saying the board "should ensure" a given result. • The board is no longer assumed to be the one assigning primary responsibility for various aspects of the compliance program.
SR 00-9 Supervisory Guidance on Equity Investment and Merchant Banking Activities	Revised	Revised to modify a previous reference to the responsibility of "senior management and the board of directors" to ensure risks do not adversely affect safety and soundness so that the sentence now refers only to senior management.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

Revisions to Other Supervisory Guidance Applicable to Boards – Revised Letters

Letter	Disposition	Comments
SR 99-7 Supervisory Guidance Regarding the Investment of Fiduciary Assets in Mutual Funds and Potential Conflicts of Interest	Revised	Revised to remove a requirement that policies be reviewed and approved by the board or a board committee.
SR 98-25 Sound Credit Risk Management and the Use of Internal Credit Risk Ratings at Large Banking Organizations	Revised	Revised to remove all references to boards so that now the only references are to management or to the banking organization as whole.
SR 98-9 Assessment of Information Technology in the Risk-Focused Frameworks for the Supervision of Community Banks and Large Complex Banking Organizations	Revised	Revised to clarify that it is the board's role to oversee, rather than to manage. In addition, a requirement that the board adequately identify, measure, monitor and control significant IT risks has been deleted. This is now an explicit responsibility only for senior management.
SR 97-3 Conversion of Common Trust Funds to Mutual Funds	Revised	Revised to delete all references to boards, including the deletion of a requirement that directors authorize or ratify management's decision to convert or transfer common trust funds to mutual funds.
SR 96-10 Risk-Focused Fiduciary Examinations	Revised	A number of revisions, including to remove guidance that a board should: • approve overall fiduciary business strategies and policies • "ensure" that management is appropriately managing risks • review the effectiveness of internal audit and other control review activities on a regular basis. In addition, rather than stating that the board and senior management should establish policies and procedures, the guidance now provides that the "institution" should do so.
SR 95-51 Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies	Revised	Revised to clarify that a board's role is not to "ensure." Instead, a board oversees and holds senior management accountable, including by staying informed. In addition, a board now must only review and approve "significant" risk exposure limits and no longer necessarily needs to itself tailor risk management policies and procedures. Rather, the board should set clear, aligned and consistent direction regarding strategy and risk appetite. Consistent with the Board Effectiveness Guidance, a board no longer needs to merely "review" the effectiveness of internal audit but instead should "engage in robust inquiry" related to effectiveness of internal audit.
SR 94-53 Investment Adviser Activities	Revised	Revised to delete a requirement that that all major policies and procedures related to investment advisory activities be periodically reviewed and approved by the board.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

Revisions to Other Supervisory Guidance Applicable to Boards – Letters Retained Without Change

Letter	Disposition	Comments
SR 16-17 – Supervisory Expectations for Risk Management of Reserve-Based Energy Lending Risk	Retained without change	Directs that a banking organization's reserve-based energy lending be subject to risk limits consistent with the risk appetite set by the board.
SR 14-8 – Consolidated Recovery Planning for Certain Large Domestic Bank Holdings Companies	Retained without change	Provides that boards should oversee the recovery planning process by focusing their oversight on the firm's ability to effectively identify and implement recovery options and by overseeing management's remediation of weaknesses identified in the firm's processes.
SR 13-13 – Supervisory Considerations for the Communication of Supervisory Findings	Retained without change	For now, retained without change, notwithstanding the Federal Reserve's 2017 proposal to revise its practices related to the communication of MRIAs and MRAs. Refer to slide 24.
SR 12-17 – Consolidated Supervision for Large Institutions	Retained without change	Still includes supervisory expectations around corporate governance that a firm's board of directors should "ensure" certain results. These are: • "Ensure that the firm's senior management has the expertise and level of involvement required to manage the firm's core business lines, critical operations, banking offices, and other material entities." • "Ensure the organization's internal audit, corporate compliance, and risk management and internal control functions are effective and independent, with demonstrated influence over business-line decision making that is not marginalized by a focus on short-term revenue generation over longer-term sustainability." • "Ensure that management information systems (MIS) support the responsibilities of the board of directors to oversee the firm's core business lines, critical operations, and other core areas of supervisory focus." This wording is flatly inconsistent with the Board Effectiveness Guidance and other SR Letters revised by the Federal Reserve, which generally move away from this formulation, as has the OCC in the most recent revision to its Director's Book. For convenience, the full corporate governance section of SR 12-17 is attached to this memo at Appendix A.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

Revisions to Other Supervisory Guidance Applicable to Boards – Letters Retained Without Change

Letter	Disposition	Comments
SR 09-4 – Applying Supervisory Guidance and Regulations on the Payment of Dividends, Stock Redemptions and Stock Purchases at BHCs	Retained without change	Includes factors boards should consider when deciding whether, and in what amounts, to pay dividends or repurchase stock.
SR 08-9 – Consolidated Supervision of Bank Holding Companies and the Combined US Operations of Foreign Banking Organizations	Retained without change	Describes the Federal Reserve's risk-based approach to supervision and instructs supervisory staff on how to approach supervision. The attachments to this SR letter include a number of supervisory expectations for boards of banking organizations of different types and sizes. Like SR 12-17, SR 08-9 uses the word "ensure" where use of that word is flatly inconsistent with the Board Effectiveness Guidance and other SR Letters revised by the Federal Reserve, which move away from this formulation, as has the OCC in the most recent revision to its Director's Book. For convenience, this guidance in SR 08-09 is attached to this memo at Appendix B.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

Revisions to Other Supervisory Guidance Applicable to Boards – Letters Made Inactive

Letter	Disposition	Comments
SR 01-13 Supervisory Guidance Relating to a Change to Permissible Securities Activities of State Member Banks	Made inactive	As relevant to boards, this letter said that "[s]enior management and the board of directors should establish credit quality and position risk guidelines, including concentration risk." This letter is now outdated, and state member banks should refer to the Commercial Bank Examination Manual for information on securities activities. The Federal Reserve intends to update the Commercial Bank Examination manual to make it consistent with the Board Effectiveness Guidance and SR Letter 16-11.
SR 01-8 Supervisory Guidance on Complex Wholesale Borrowings	Made inactive	As relevant to boards, this letter said that supervisors should determine "whether the asset/liability management committee or board of directors, as appropriate, is fully informed of the risks and ramifications of complex wholesale borrowing agreements prior to engaging in the transactions as well as on an ongoing basis." This letter is now outdated, and banking organizations should refer to the Trading and Capital Markets Activities Manual sections on Liquidity Risk and Interest-Rate Risk Management; SR Letter 10-6, "Interagency Policy Statement on Funding and Liquidity Risk Management," and Regulation YY, as relevant.
SR 98-18 Lending Standards for Commercial Loans	Made inactive	As relevant to boards, this letter said that "bank directors and senior managers have the obligation to monitor lending practices and to ensure that their policies are enforced and that lending practices more generally remain within the overall ability of the institution to manage." The Federal Reserve described this letter as outdated, but did not cite to specific other guidance to which banking organizations should refer.
SR 97-25 Risk-Focused Framework for the Supervision of Community Banks	Made inactive	This letter included as an attachment a 52-page document explaining the risk-focused supervisory process for community banks, including various supervisory expectations for boards. This letter is now outdated. Community banks should refer to the Commercial Bank Examination Manual for information on the supervisory framework applicable to their activities and their boards.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

The Federal Reserve made these letters inactive because each "supervisory letter, in its entirety, was no longer relevant to the Federal Reserve's current supervision because it contained guidance that was **outdated, unnecessary, or redundant**."

Revisions to Other Supervisory Guidance Applicable to Boards – Letters Made Inactive

Letter	Disposition	Comments
SR 97-24 Risk-Focused Framework for Supervision of Large Complex Institutions	Made inactive	This letter included as an attachment a 155-page document explaining the risk-focused supervisory process for large complex institutions, including various supervisory expectations for boards. This letter is now outdated. Banking organizations should refer to the Bank Holding Company Supervision Manual for information on the supervisory framework applicable to their activities and their boards.
SR 97-21 Risk Management and Capital Adequacy of Exposures Arising from Secondary Market Credit Activities	Made inactive	As relevant to boards, this letter stated that boards "should approve all significant polices relating to the management of risk arising from secondary market credit activities and should ensure that the risk exposures are fully incorporated in board reports and risk management reviews." This letter is now outdated. Banking organizations should refer to the Bank Holding Company Supervision Manual for applicable guidance related to secondary market credit activities. The Federal Reserve intends to update the Bank Holding Company Supervision Manual to be consistent with the Board Effectiveness Guidance and SR Letter 16-11.
SR 93-69 Examining Risk Management and Internal Controls for Trading Activities of Banking Organizations	Made inactive	As relevant to boards, the letter stated that boards "should approve all significant policies relating to the management of risks throughout the institution," including those related to trading activities. In addition, a board should "be informed regularly of the risk exposure of the institution … regularly re-evaluate significant risk management policies and procedures … [and] conduct and encourage discussions between its members and senior management, as well as between senior management and others in the institution, regarding the institution's risk management process and risk exposure." The Federal Reserve described this letter as outdated, but did not cite to specific other guidance to which banking organizations should refer.
SR 90-22 Policy Statement on the Use of "Points" in Settling Foreign Exchange Contracts	Made inactive	A relevant to boards, policies and procedures relating to disputed brokered FX contracts were required to be "approved by senior management and reviewed by the board of directors." The Federal Reserve described this letter as outdated, but did not cite to specific other guidance to which banking organizations should refer.
SR 90-16 Implementation of Examination Guidelines for the Review of Asset Securitization Activities	Made inactive	As relevant to boards, major policies and procedures related to asset securitization activities were required to be "reviewed periodically and approved" by the board. The Federal Reserve described this letter as outdated, but did not cite to specific other guidance to which banking organizations should refer.

Some of these SR Letters apply only to certain banking organizations (e.g., US G-SIBs). Some letters may have a corresponding Consumer Affairs number, but for simplicity we have only listed the SR number.

The Federal Reserve made these letters inactive because each "supervisory letter, in its entirety, was no longer relevant to the Federal Reserve's current supervision because it contained guidance that was **outdated, unnecessary, or redundant**."

Appendix A: Corporate Governance Section of SR Letter 12-17

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Appendix A: Corporate Governance Section of SR Letter 12-17

In order for a firm to be sustainable under a broad range of economic, operational, legal or other stresses, its board of directors (or equivalent for the U.S. operations of FBOs) should provide effective corporate governance with the support of senior management. The board is expected to establish and maintain the firm's culture, incentives, structure, and processes that promote its compliance with laws, regulations, and supervisory guidance. **Each firm's board of directors and committees**, with support from senior management, **should**:

a. Maintain a clearly articulated corporate strategy and institutional risk appetite. The board should set direction and oversight for revenue and profit generation, risk management and control functions, and other areas essential to sustaining the consolidated organization.
b. ***Ensure*** that the firm's senior management has the expertise and level of involvement required to manage the firm's core business lines, critical operations, banking offices, and other material entities.[9] These areas should receive sufficient operational support to remain in a safe and sound condition under a broad range of stressed conditions.
c. Maintain a corporate culture that emphasizes the importance of compliance with laws and regulations and consumer protection, as well as the avoidance of conflicts of interest and the management of reputational and legal risks.
d. ***Ensure*** the organization's internal audit, corporate compliance, and risk management and internal control functions are effective and independent, with demonstrated influence over business-line decision making that is not marginalized by a focus on short-term revenue generation over longer-term sustainability.[10]
e. Assign senior managers with the responsibility for ensuring that investments across business lines and operations align with corporate strategies, and that compensation arrangements and other incentives are consistent with the corporate culture and institutional risk appetite.[11]
f. ***Ensure*** that management information systems (MIS) support the responsibilities of the board of directors to oversee the firm's core business lines, critical operations, and other core areas of supervisory focus." (Emphasis added.)

[9] "Material entities" are subsidiaries or foreign offices of the firm that are significant to the activities of a core business line or critical operation.
[10] See SR letter 08-8/CA letter 08-11, "Compliance Risk Management Programs and Oversight at Large Banking Organizations with Complex Compliance Profiles."
[11] Refer to "Guidance on Sound Incentive Compensation Policies" (*75 Federal Register* 36395, June 25, 2010).

Appendix B: Guidance from SR Letter 08-09

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Appendix B: Guidance from SR Letter 08-09*

Objectives: One of the primary areas of focus for consolidated supervision of large complex BHCs is the adequacy of governance provided by the board and senior management. The culture, expectations, and incentives established by the highest levels of corporate leadership set the tone for the entire organization, and are essential determinants of whether a banking organization is capable of maintaining fully effective risk management and internal control processes.

The board and its committees should have an ongoing understanding of key inherent risks, associated trends, primary control functions, and senior management capabilities. **Primary expectations for the board and its committees include**:

a. Selecting competent senior managers, ***ensuring*** that they have the proper incentives to operate the organization in a safe and sound manner, and regularly evaluating senior managers' performance;
b. Establishing, communicating, and monitoring (for example, by reviewing comprehensive MIS reports produced by senior management) institutional risk tolerances and a corporate culture that emphasizes the importance of compliance with the law and ethical business practices;
c. Approving significant strategies and policies;
d. Demonstrating leadership, expertise, and effectiveness;
e. **Ensuring** the organization has an effective and independent internal audit function; Ensuring the organization has appropriate policies governing the segregation of duties and avoiding conflicts of interest; and
f. **Ensuring** that public disclosures (i) are consistent with how the board and senior management assess and manage the risks of the organization, (ii) balance quantitative and qualitative information with clear discussions about risk management processes, and (iii) reflect evolving disclosure practices for peer organizations." (Emphasis added.)

*SR 08-09 includes separate attachments laying out supervisory expectations for large complex BHCs, regional BHCs and the combined U.S. operations of FBOs, respectively. The supervisory expectations in SR 08-09 related to corporate governance are substantially the same for large complex BHCs and regional BHCs, and those expectations are reflected above.

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