U.S. Chamber of Commerce

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December 8, 2023

Mr. James P. Sheesley
Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions with Total Consolidated Assets of $10 Billion or More (88 FR 70391)

Dear Mr. Sheesley:

The U.S. Chamber of Commerce (Chamber) Center for Capital Markets Competitiveness (CCMC) submits these comments in response to the Federal Deposit Insurance Corporation's (FDIC) recently proposed corporate governance and risk management standards (Proposal). The Chamber has long advocated for effective corporate governance policies that strengthen investor confidence and help businesses and financial institutions compete in an increasingly competitive economy.

However, the Chamber believes that the Proposal would weaken, not strengthen, the corporate governance of banking institutions and make it more difficult for directors to perform their critical duties. The Proposal blurs the line between the responsibilities of directors and management, includes certain expectations for boards based upon vague criteria, improperly imposes new federal requirements that would preempt or conflict with existing state law, and would impose prescriptive mandates on individual board members that will distract them from focusing on the long-term performance of the institutions they oversee.

In January 2018, the Chamber submitted comments to the Federal Reserve's then-proposed guidance surrounding supervisory expectations for boards.[1] In those comments, the Chamber explained our reservations with the Federal Reserve's approach, including that the proposed guidance:

> ...is at times overly prescriptive, while at other times subjective with the potential to create open-ended standards with which it will be difficult for boards to comply. We are also concerned that the proposed guidance could lead the Federal Reserve towards defining what constitutes an "effective" board. This will lead to subjective

[1] Proposed Guidance on Supervisory Expectations for Boards of Directors (82 Fed. Reg. 37,219) [Federal Register :: Proposed Guidance on Supervisory Expectation for Boards of Directors]

determinations made in future examinations and could create regulatory conflicts as boards seek to discharge their fiduciary duty to shareholders."[2]

When the Federal Reserve issued its final guidance in 2021, it addressed many (though not all) of the concerns that the Chamber and other commenters raised during the comment period. Specifically, the Federal Reserve took steps to "further [distinguish] the roles and responsibilities of boards from those of senior management" and to "[provide] illustrative examples of effective board practices." The Federal Reserve also removed the unnecessary expectation that boards provide examiners with the results of their periodic self-assessments.[3] Further, the final guidance explicitly stated that the Federal Reserve's intent was not to "supersede or replace any applicable legal, regulatory, or listing requirements to which firms may currently be subject in the United States…"

Additionally, the Office of the Comptroller of the Currency (OCC) issued updated guidance in 2014 to heighten the risk governance of national banks.[4] Those final guidelines contained significant changes from the original OCC proposal, and the OCC acknowledged in its final guidance that its intent was not "to assign managerial responsibilities to the board of directors or its risk committee."[5]

Blurring the Lines Between Board and Management Responsibilities

Unfortunately, many aspects of the Proposal depart from existing Federal Reserve and OCC guidance and would impose new requirements on boards that place inappropriate expectations on directors and will allow examiners to second-guess decisions made by the board. For example, the Proposal contains an expectation that a board ensure a covered institution "operates…in compliance with all laws and regulations."[6] This broad requirement is likely to be interpreted by any reasonable board member of a covered institution as an obligation that boards regularly and thoroughly inspect all activities of a bank to confirm their compliance with laws and regulations.

This is not—and never has been—the proper role of boards with respect to a bank or any other institution. Board members should not be expected to behave as either a bank's lawyer or examiner, which would be a laborious process that takes the focus of a board away from its most important duties, most notably, that of oversight. Further, as FDIC Director McKernan

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[2] January 5, 2018 comment letter from U.S. Chamber, available at https://www.centerforcapitalmarkets.com/wp-content/uploads/2018/01/CCMC-Comment-Docket-No.-OP-1570.pdf?

[3] Overview of Comments and Revisions to Proposed Guidance on Supervisory Expectations for Boards of Directors. https://www.federalreserve.gov/supervisionreg/srletters/SR2103aCommentSummaryPublication.pdf

[4] OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches, Integration of Regulations. (79 Fed. Reg 54518) https://www.govinfo.gov/content/pkg/FR-2014-09-11/pdf/2014-21224.pdf

[5] 79 Fed. Reg. 54,526

[6] 88 Fed. Reg. 70,404

explained in his dissent to the Proposal, “the responsibility of the board should be to ensure that the company has in place a *framework* to ensure compliance with law.”[7]

The Proposal also establishes the expectation that boards provide “active” oversight of management, although presumably the term “active” is something that will ultimately be defined through future examinations and enforcement actions rather than by a bright-line test. The Proposal explains that boards should “question, challenge, and when necessary, oppose”[8] recommendations or decisions made by management. Again, such expectations run the risk that directors will find themselves obligated to engage in day-to-day managerial decisions. The Proposal contains little color about what, for example, it may mean for a board to “question” or “challenge” certain decisions by management. As such, directors may feel pressured to go beyond what is reasonable in questioning/challenging/opposing management so as to not run afoul of the Proposal’s expectations.

Potential Conflicts with Existing Law

The primary corporate governance laws and regulations that apply to businesses stem from a combination of state law and, for public companies, rules administered by the Securities and Exchange Commission (SEC). In this context, the role of the FDIC, Federal Reserve, and OCC in the corporate governance of banking organizations is secondary to that of state law and the SEC. It is critical that any requirements or expectations imposed by the FDIC, or any banking regulator do not conflict with existing law or regulation.

While the Proposal ostensibly acknowledges the “myriad federal and state laws applicable to [a] covered institution” and its board, it proposes even more new requirements that create the real potential for conflicts with existing law—in particular, state laws that govern the duties of a covered institution’s board. For example, the Proposal embraces a malleable definition of what constitutes a “stakeholder” of a covered institution while requiring the board to consider the interests of “all” stakeholders.

One stakeholder that the Proposal lists—and which boards would be required to consider the interest of—is “the public.” It would be exceedingly difficult, if not impossible, for a board to establish effective policies that ensure it considers the interests of such a loosely defined and broad class. While the Chamber shares the FDIC’s goals of promoting a safe and sound banking system, what cannot be lost in the discussion is that the covered institutions implicated by the Proposal are for-profit entities that are already accountable to shareholders. They should not be viewed as public utilities that have some kind of amorphous obligation to any one person or organization that may fall within the definition of “the public” but otherwise have no connection whatsoever to the financial institution.

Furthermore, under organic laws governing corporations, directors have a fiduciary duty towards preserving shareholder assets, the assets of a corporation and performing oversight

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[7] Statement by Jonathan McKernan, Director, FDIC Board of Directors, on the Proposed Guidelines Establishing Standards for Corporate Governance and Risk Management (October 3, 2023) Available at https://www.fdic.gov/news/speeches/2023/spoct0323c.html#_ftn6

[8] 88 Fed. Reg. 70,405

of management. To inject public interests or other amorphous concepts creates conflict with the existing legal obligations and duties of a board member.

More fundamentally, a mandate to consider the interest of other constituencies on par with shareholders is a clear conflict with the longstanding laws of many states. As Director McKernan explained: “Under some states’ laws, a board may consider non-shareholder constituencies only if there are benefits that accrue to the shareholders. Other states more broadly permit boards to consider non-shareholder constituencies, but only a few states actually require consideration of other stakeholders.”[9] Imposing these ill-defined and novel obligations on boards would create new risks to the shareholders of banks, many of whom own interests in these institutions indirectly through pension or other retirement plans.

The Proposal also advances a novel definition of independence that restricts the ability of financial institutions to have common independent directors on the bank and holding company boards. “Independence” historically has been defined as the independent director having no material personal or other ties to the bank and bank holding company. It has not been interpreted as requiring separate membership at the bank and the holding company boards, and many U.S. institutions have common directors on the bank and holding company boards to support efficient oversight and effective enterprise risk management. The Proposal’s definition conflicts with the independence standards adopted by the OCC, Federal Reserve, SEC and listing exchanges. We urge the FDIC to drop these restrictive independence requirements.

<u>Additional Concerns</u>

As noted previously, the Proposal is replete with several vague requirements that will lead boards to constantly query whether or not they are in compliance with the FDIC’s expectations. For example, the Proposal says that a board should set an “appropriate tone” for the institution and that the “tone at the top is integral to promoting a culture and environment of responsible and ethical behavior that discourages imprudent risk-taking in pursuit of profit.”[10] While these may be appropriate goals for an institution’s leadership to consider on their own, attempting to regulate compliance with such aspirations is a much more difficult endeavor.

What is meant by “appropriate tone” and how would the FDIC assess an institution’s “tone at the top”? What individuals on the board would be expected to establish an institution’s “tone”? From the FDIC’s standpoint, is the proper “tone” of an institution only correlated with safety and soundness measures, or are there other objectives—for example consistent profitability and customer satisfaction—that should be incorporated into an institution’s “tone”? The Proposal leaves these questions curiously unanswered.

The hyper-focus on risk management processes overseen by the board may also perversely distract FDIC examiners from greater risks lurking below a particular institution or the broader banking sector at large. This is not just a theoretical concern: The Federal Reserve Inspector

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[9] *Supra* note 7.
[10] 88 Fed. Reg. 70,395

General report regarding the failure of Silicon Valley Bank (SVB) found that prior to SVB's collapse, Federal Reserve supervisors "tend[ed] to take a forward-looking approach and [focus] on risk management and associated processes more than financial results."[11] The IG report also discovered that supervisors were "highlighting risk management deficiencies when more serious problems were emerging and [supervisors] missed the deficiencies in the bank's financial condition."[12]

The Proposal also would impose a prescriptive approach to development of an institution's risk management framework by placing restrictions on the ability of a bank to adopt and implement all or part of the parent's risk management program unless the risk profiles of the bank and parent company are "substantially similar," whatever that means, and requiring that the bank have separate governance and risk management practices if certain conditions are not met. Similar to the point made above with respect to independence, institutions are seeking to create effective and efficient enterprise-wide risk management policies and frameworks. Boards need sufficient flexibility to harmonize bank and holding company-level risk management controls in a manner that is most effective and efficient taking into account the institution's size, business model, complexity and risk profile. We urge the FDIC to not impose a one-size-fits-all model of governance and risk management.

If adopted as currently drafted, the Proposal would result in banks and their boards going through an endless stream of check-the-box exercises and constantly updating policies based upon the FDIC's evolving views of risk management. By the same token, examiners will spend a substantial amount of their time poring through the particulars of a bank's policies, which will take their attention away from more pressing risks facing the bank. In other words, the Proposal has the potential to create more risk at both individual banks and within the banking system, which is entirely at odds with its purpose.

<u>Conclusion</u>

CCMC appreciates the opportunity to submit our views on this Proposal from the FDIC. However, as described throughout this letter, we are concerned that, if adopted, the Proposal would do more harm than good and fail to promote sound risk management practices at banking institutions. The Proposal is at times vague and at other times overly prescriptive in terms of expectations for banks, and its requirements will not improve the bank examination process or make it more likely that examiners will uncover and address the most critical risks to banks. Furthermore, the Proposal may impede the ability of Boards to fulfill their existing fiduciary responsibilities.

We therefore urge the FDIC to either withdraw the Proposal in its entirety or to substantially revise the Proposal so that it reaffirms the duties of boards in line with existing legal

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[11] Material Loss Review of Silicon Valley Bank. Board of Governors of the Federal Reserve System Inspector General. (September 25, 2023) Available at https://oig.federalreserve.gov/reports/board-material-loss-review-silicon-valley-bank-sep2023.pdf?utm_source=substack&utm_medium=email

[12] *Id.*

obligations and regulatory expectations, including alignment with the existing OCC and Federal Reserve guidance applicable to other financial institutions.

Sincerely,

Tom Quaadman
Executive Vice President
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce