

The role of boards of financial services firms: a new approach by the Federal Reserve

Last year Jerome Powell, now chairman of the Federal Reserve Board, gave an important speech setting out a revised role for the boards of US financial firms.¹ He explained that the current regulatory expectations muddle the roles of boards and executives. The purpose of the speech was to set out a new “framework” which would allow boards to return to their core responsibilities of overseeing management “as they devise a clear and coherent direction for the firm”, holding the executive to account and ensuring the independence and “stature” of risk management and internal audit.

To do this the Fed would move away from specific directives aimed at boards to a principles-based approach. There would be five principles. Boards should:

- “guide the development of a clear and coherent strategy for the firm”, setting the acceptable “types and levels of risk”,
- “manage its information flow and deliberations”,
- hold senior management accountable for implementing the firm’s strategy and risk appetite and maintaining the firm’s risk management and control framework”,
- ensure the “independence and stature of the risk management and internal audit functions”,
- have a “composition, governance structure” and practices appropriate to the firm’s size, complexity, risk profile etc. Boards should “engage in probing self-assessments regularly and systematically”.

The Fed has consulted on these proposed changes which are aimed at large financial services firms with consolidated assets of more than \$50 Bn.²

While these principles are sound they omit a number of important expectations of bank boards set out by the Basel Committee on Banking Supervision.³ Central to this role is leading the establishment of the “bank’s corporate culture and values”.⁴ As has been seen many times all regulation is as nought if the culture and ethics of a firm fail. In parallel, there is no mention of any requirement that the board will be open and cooperative with regulators. These omissions from the Federal Reserve’s core expectations are surprising. It may presage a divergence of US bank regulation from global standards.

¹ Jerome Powell, Remarks at the Large Bank Directors Conference, Chicago, 30th August 2017, on “The Role of Boards of Large Financial Firms”

² “Proposed Guidance on Supervisory Expectations for Boards of Directors”, Federal Register, Vol.82, No. 152, (8th August 2017), Docket No. OP-1570, 37219-37227

³ Basel Committee on Banking Supervision, Guidelines: Corporate Governance Principles for Banks, (July 2015),

⁴ Ibid, 8