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## INSTITUTE OF INTERNATIONAL BANKERS

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March 15, 2018

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Ann E. Misback  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, DC 20551

Re: Proposed Supervisory Guidance (Docket No. OP-1594)

Dear Ms. Misback:

The Institute of International Bankers (the “IIB”) appreciates the opportunity to comment on the proposed guidance issued by the Board of Governors of the Federal Reserve System (the “Board”) describing core principles for (1) effective senior management, (2) the management of business lines and (3) independent risk management and controls for large financial institutions.<sup>1</sup> The Proposal would apply to U.S.-headquartered bank holding companies with consolidated total assets of \$50 billion or more (“U.S. BHCs”) and the combined U.S. operations of foreign banking organizations (“FBOs”) that have combined U.S. assets of \$50 billion or more, which includes many of our members.

We appreciate the Board’s response to industry concerns about the need for greater clarity regarding supervisory expectations for risk management, and we are grateful for the opportunity to provide our comments, which focus on the unique challenges facing U.S. senior management and the U.S. risk management function of FBOs operating in the United States.<sup>2</sup>

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<sup>1</sup> 83 Fed. Reg. 1351 (Jan. 11, 2018) (the “Management Proposal” or the “Proposal”). Capitalized terms in this letter have the meanings ascribed in the Proposal except as otherwise noted or required by the context.

<sup>2</sup> Regarding the broader aspects of the Proposal, we generally share the views expressed in the letter submitted by The Clearing House Association L.L.C.



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### OVERVIEW

We support the core substance of the Board's proposed guidance, including the recognition of the differing roles of the board of directors and senior management and of the responsibilities of senior management for the development and implementation of an appropriate risk management framework. However, "one size does not fit all," and this is particularly true for FBOs operating in the United States. As the Board has recognized, the combined U.S. operations of FBOs operate as part of larger global organizations.

We strongly recommend that separate principles-based guidance be issued for FBOs and that FBOs be given a meaningful opportunity to comment on that guidance, taken together with the Board's guidance to be issued on board effectiveness for intermediate holding company ("IHC") subsidiaries of FBOs and its Large Financial Institution ("LFI") Rating System proposal. This letter describes our reasoning for these recommendations and makes a number of general and specific suggestions for how the guidance for FBOs could be clarified and improved.

**A. Separate "principles-based" guidance should be issued for FBOs operating in the United States that takes into account the fact that the U.S. operations of FBOs are part of larger global organizations.**

The Management Proposal is clearly designed and drafted with top-tier U.S. BHCs in mind. However, FBOs in the United States are part of larger global organizations, and strategic, personnel and resource decisions that affect the U.S. operations are more often than not made at the parent company level. This is to be expected and is consistent with the Board's expectations in terms of effective enterprise-wide risk management for U.S.-headquartered BHCs and their senior management at the parent level, as well as prudential regulation applicable to an FBO as a whole. An FBO's U.S. management nonetheless is accountable for the safe and sound operation of the FBO's U.S. businesses. If decisions made at the parent company level compromise the U.S. business' ability to operate in a safe and sound manner, U.S. senior management has a variety of options to address the situation, including, depending on the circumstances, escalating the issues to responsible management at the parent company (and as appropriate the IHC Board) and following up until they are resolved.

In select footnotes, the Board explains certain ways in which the guidance should be adapted for FBOs, taking into consideration the fact that the combined U.S. operations of an FBO are part of a larger global banking organization. In some cases, the explanations in footnotes appear meant to clarify that the guidance is limited in scope to an FBO's U.S. operations, and to provide some flexibility to take into account the structure of an FBO. However, often the explanations create questions about the intent of the guidance, and raise potential concerns that it could create unintended extraterritorial consequences for FBOs and their senior management. It is also unclear at times how the conceptual adaptation in the footnote of the wording of the proposed guidance in the main text should be carried through in practice.



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We strongly recommend that the Proposal be revised to address FBOs separately. The text of the proposed guidance is relatively short, and it easily could be divided into separate guidance for U.S. BHCs and for FBOs. That would allow for greater clarity and avoid potential concerns about scope and expectations that arise from the wording of the footnotes, which we address further below. It would also be consistent with the way in which the Board organized and approached the implementation of enhanced prudential standards for FBOs in Regulation YY.<sup>3</sup>

A separate proposal also would allow the Board to more clearly address the roles of U.S. senior management and risk management of an FBO's U.S. branches and agencies. In the current proposal, this issue is subsumed in the discussion of adaptations for an FBO's combined U.S. operations without clear distinctions. There are parallels between (a) the roles of U.S. senior management and risk management of an FBO's IHC in relation to its parent company and (b) the roles of U.S. senior management and risk management of an FBO's branch(es) in relation to head office. There are also differences and limitations arising under home country laws and regulations, however, and these considerations should be addressed in a separate FBO proposal.

We also urge the Board to refrain from overly prescriptive guidance beyond a principles-based approach to U.S. management's responsibility for safety and soundness. "One-size does not fit all," and FBOs may reasonably vary in their approaches to achieve strong risk management depending upon their culture, their home country jurisdiction, the applicable regulatory framework and business models in the United States.

### **B. FBOs should be given a meaningful opportunity to comment on the Board's management and risk management guidance, together with the Board's proposals on board effectiveness for IHCs and the proposed LFI Rating System.**

We have addressed separately the issues for FBOs presented by the timing and sequence of the Proposal in our letter dated February 15, 2018 (attached to this letter). In short, the Management Proposal was released January 4, 2018, several months after the August 2017 publication of proposed guidance addressing supervisory expectations for boards of directors<sup>4</sup> and a proposed rating system for U.S. BHCs and IHCs.<sup>5</sup> The Board Effectiveness Proposal explicitly provided that it would not apply to IHCs, and that IHCs would be addressed through a separate future proposal. The Board then extended the deadline to comment on the Board Effectiveness Proposal and the LFI Rating Proposal until February 15, 2018 to "provide an opportunity for the public to understand the proposed division of responsibilities between the

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<sup>3</sup> 79 Fed. Reg. 17240 (Mar. 27, 2014).

<sup>4</sup> 82 Fed. Reg. 39049 (August 17, 2017) (the "Board Effectiveness Proposal").

<sup>5</sup> 82 Fed. Reg. 37219 (August 9, 2017) (the "LFI Rating Proposal") (together, the Board Effectiveness Proposal, the LFI Rating Proposal and the Management Proposal, the "Proposals").



board, senior management, and business line management[.]”<sup>6</sup> The Management Proposal describes in several places how it is meant to work in tandem with the Board Effectiveness Proposal.

For U.S. BHCs, the Proposals thus represent a cohesive whole, with elements that relate to each other and draw distinctions among the roles of boards of directors, senior management and the risk management function. FBOs, in contrast, face a number of difficulties stemming from the way the Management Proposal has been released. For FBOs with IHCs, we are not able to evaluate how the Board’s guidance for IHC boards of directors and U.S. senior management and risk management of FBOs are meant to work together, since the Board has not yet published a proposal for IHC boards of directors. In fact, the Board includes a specific question related to this issue, asking: “How could the roles and responsibilities between the board of directors set forth in the proposed board effectiveness guidance, and between the senior management, business line management, and IRM be clarified?”<sup>7</sup> This is a question that FBOs cannot meaningfully answer. For FBOs without IHCs, the various references to the role of senior management as distinct from the board of directors make no sense as there is no board of directors in that case.

As discussed in our February 15<sup>th</sup> letter (attached), the interrelationships among the Proposals as they apply to FBOs call for an integrated proposal (or integrated set of proposals) which comprehensively addresses the Board’s expectations for governance of their U.S. operations and enables more informed commentary on the ramifications. Our comments accordingly should be considered preliminary and subject to further developments.

**C. In the meantime, we have a number of specific concerns regarding the wording of the Management Proposal.**

In the “Discussion” section below, we address a number of specific concerns regarding the wording of the guidance in the Proposal, most of which flow from the two issues described above. In summary, the Board could more effectively clarify its expectations of the roles and responsibilities of an FBO’s U.S. senior management and U.S. risk management function by:

- clarifying (or, if necessary, reorienting) the scope of the Proposal to apply to U.S. management and the U.S. risk management function, and their roles in relation to the risks of the combined U.S. operations of an FBO;
- more clearly and specifically addressing the distinctions between FBOs that have and do not have an IHC; and

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<sup>6</sup> See 82 Fed. Reg. 55841, 55842 (Nov. 24, 2017) and 82 Fed. Reg. 55791 (Nov. 24, 2017) (“An additional extension of the comment period will provide an opportunity for the public to comment on the ratings framework and related supervisory expectations as a whole.”), respectively.

<sup>7</sup> 83 Fed. Reg. at 1355.



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- including statements recognizing the roles of the FBO's global board of directors and other governance structures, the importance of flexibility to take into account the role of the combined U.S. operations as part of business lines and risk and control functions headquartered elsewhere, and consideration of deference to home country legal, regulatory and supervisory considerations that inform these matters.

In addition, we urge the Board to consider appropriate statements clarifying the meaning and intent of the Proposals as guidance and not as a checklist of examination items. Especially in light of the uncertainty regarding the intended application and effect of Board guidance in contrast to regulations, the Proposals would appear to present a prime opportunity to be clear on this subject. Adding statements that the guidance is meant to articulate basic principles, with appropriate flexibility in application, would be especially important for the combined U.S. operations of FBOs, in light of their more varied structures and the way in which those operations are incorporated into global organizations operating under home country standards and expectations

### DISCUSSION

In this section of our letter we describe a number of specific concerns with the way in which the guidance in the Proposal is worded or explained.

#### A. Applicability/Scope

For FBOs, the Proposal “would apply to an FBO’s combined U.S. operations, including branch and subsidiary operations.”<sup>8</sup> The IIB supports this delineation of the scope of application of the guidance in the Proposal.

However, the clarity of this statement is significantly undercut by later statements in the Proposal regarding how the guidance should be understood and applied. For example, after describing the Regulation YY risk committee and IHC requirements, the Proposal suggests that the Board’s “expectations for governance of the combined U.S. operations of an FBO are generally consistent with its expectations for governance of large domestic firms and, in this guidance, a reference to ‘firm’ should be taken also as a reference to the combined U.S. operations of an FBO, unless the context requires otherwise.” Apart from the general difficulty of interpretation that this approach creates (since the context frequently requires otherwise), this statement begs significant questions regarding differences among FBOs, for example between FBOs that have an IHC and ones that do not, and between FBOs whose U.S. risk committee may be a committee of its global, home country board of directors and those whose U.S. risk committee may be a U.S. or management committee. It also begs the question whether the guidance is intended to reflect explicit or implicit expectations of boards of directors or senior

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<sup>8</sup> 83 Fed. Reg. at 1356.



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management of the FBO itself in a way that would be inconsistent with the clear statement that the guidance applies to the FBO's combined U.S. operations.

Similarly, the guidance in the Proposal recognizes that the combined U.S. operations of an FBO function within a larger global organization, and accordingly, certain elements of the organization's governance framework may be located outside of the United States.<sup>9</sup> The guidance suggests that "in this event, these elements should enable effective governance and risk management by the U.S. senior management, the U.S. risk committee, and the IHC board (as applicable), and should facilitate U.S. supervisors' ability to assess the adequacy of governance and controls in the combined U.S. operations."<sup>10</sup> The first part of these statements appears to be intended to provide some flexibility in how the guidance is applied to FBOs. However, the second part risks creating an impression that the Board is establishing standards for home country governance, a concern that is amplified by later statements in the context of core principles, as described below.

To avoid confusion regarding the scope of the guidance, we urge the Board to clarify the FBO discussion in the "applicability" section of the guidance. As noted, we support the clear and simple statement that the guidance would apply to the combined U.S. operations of covered FBOs. The guidance could then recognize that the combined U.S. operations of an FBO are part of a larger global organization. The guidance could further recognize that the global organization and its governance framework operate under home country legal, regulatory and supervisory standards, and the Board will generally defer to those standards.

### **B. Core Principles of Effective Senior Management**

#### **1. Definition of Senior Management**

The Proposal would define senior management generally as "the core group of individuals directly accountable to the board of directors for the sound and prudent day-to-day management of the firm."<sup>11</sup> As this definition does not typically work for FBOs, the guidance provides that for an FBO "senior management *can* refer to individuals located inside or outside of the United States who are accountable to the IHC board, U.S. risk committee, or global board of directors with respect to the U.S. operations."<sup>12</sup> Apart from the difficulty this approach creates in interpreting the guidance (since the rest of the discussion often articulates distinctions between senior management and the board of directors in ways that not meaningfully applicable

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<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> 83 Fed. Reg. at 1356 n. 28.

<sup>12</sup> Id. (emphasis added). The meaning of "can" in this sentence creates separate questions regarding whether it is meant to be permissive or expected, but these questions would be addressed if the modifications we suggest below are adopted.



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to FBOs<sup>13</sup>), this approach creates some potentially fundamental concerns about the scope and meaning of the guidance.

We endorse and appreciate the Board's intent to take a flexible approach in adapting the definition of senior management for FBOs. However, the current wording could create the impression that the Board's guidance is designed to articulate standards for the global senior management of an FBO and its relationship to the FBO's global board of directors, a subject that would clearly be the purview of home country governance standards and supervisory expectations. For our members, the combined U.S. operations will typically have a senior management team with responsibility for the day-to-day operations of the combined U.S. operations. That senior management team may have reporting lines on geographical and/or business line bases to senior management in head office or another part of the global banking organization. To avoid the implication that the guidance applies to extraterritorial activities, the Board should clarify that its expectations relate specifically to the United States rather than more generally. Consequently, we urge the Board to revise the definition of senior management for FBOs to mean the senior-most management located in the combined U.S. operations with responsibility for the day-to-day management of those combined U.S. operations.

Clarifying the definition of U.S. senior management in this way would also clarify how the definition would apply to FBOs with and without IHCs. The way the definition is currently worded in the Proposal begs a number of questions about how senior management is viewed in the context of the senior management of the IHC itself (with clearer responsibilities in relation to the board of the IHC) vs. the combined U.S. operations (including branches and agencies), with responsibilities in relation to the U.S. risk committee but not necessarily to the IHC board, depending on the governance approach adopted by the FBO. While these questions could be addressed by further discussing and clarifying that distinction, the simpler approach we have suggested above should mitigate that concern.

### 2. Effective Senior Management

The uncertainty regarding the scope of application that arises from the definition of senior management carries through to, and is compounded by, some of the phrasing of the guidance as it relates to the role of senior management in the FBO context. For example, the general statement in the text of the guidance to the effect that senior management is responsible for maintaining an effective risk management framework and manages risk within it, has an understandable meaning in the context of the combined U.S. operations of an FBO (even if it necessarily does not take into account some nuances associated with the way senior management and risk functions report into global functions). However, the Proposal adds explanations in a footnote that create significant uncertainty regarding the scope of the guidance. In footnote 31, the Proposal indicates that, for FBOs:

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<sup>13</sup> See, e.g., 83 Fed. Reg at 1357 ("Senior management is responsible for providing timely, useful, and accurate information to the board. Senior management should also be responsive to direction from the board and to the board's informational needs. Further, senior management is responsible for ... escalating issues to the board ...").



[R]egardless of whether a firm's senior management resides in the United States, senior management should fully understand the risks of U.S. operations and communicate information on the risks of combined U.S. operations to global management, so that these risks are included in the aggregate risk assessment of the global organization. Further, senior management with authority over budgeting and strategy for the combined U.S. operations should allocate appropriate resources and expertise to meet the expectations of this guidance.<sup>14</sup>

The IIB supports what we understand to be the ultimate objective of these statements, allowing the risks of the combined U.S. operations to be managed as part of the broader organization, and ensuring that the combined U.S. operations have adequate staffing and resources. However, the potential implication that the guidance could be used as a basis for assessment of the responses of global management to information communicated by U.S. senior management, or of decisions by management outside the United States per se regarding budgeting, staffing, priorities and the like, would constitute a significant extraterritorial extension and thus be problematic.

We therefore suggest that the guidance be clarified to focus on the Board's expectations of U.S. senior management with respect to the U.S. operations of the FBO. We understand that an evaluation of the effectiveness of U.S. senior management will depend on their ability to manage the business in a safe and sound manner within the context of a global organization. U.S. senior management decisions regarding strategy, budgeting and personnel will of course be guided and influenced by head office decisions. Just as the Board expects the parent companies of internationally active U.S. BHCs to implement effective enterprise-wide risk management across their global organizations, foreign banks' home country supervisors expect parent companies headquartered in their jurisdictions to do the same. An FBO's U.S. senior management remains accountable, however, for the safe and sound operation of the FBO's U.S. businesses. If decisions made at the parent company level were to compromise the ability of U.S. senior management to meet this expectation, U.S. senior management would have a variety of options to address the situation, including, depending on the circumstances, escalating the issues to senior management at the parent company (and, as appropriate, to the IHC board of directors), and following up until the issue is resolved.

### **C. Core Principles of Effective Business Line Management**

Our concerns with the business line management section of the Proposal are similar to our concerns with the senior management section. In general, the way the Proposal articulates the substance of the Board's expectations of business line management, including the expectation that business line management has an appropriate role in risk management, would appear applicable to the combined U.S. operations of FBOs and is generally understandable. Questions arise, however, from the way in which the Proposal delineates business line management in the context of FBOs and in the way the Proposal words some of the expectations.

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<sup>14</sup> 83 Fed. Reg. at 1357 n. 31.



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For example, the Proposal helpfully clarifies that, in the case of a business line of an FBO that is part of a larger business conducted outside of the United States, “expectations apply only to the portion of that business conducted in the United States.”<sup>15</sup> This would appear consistent with the general scope of the Proposal, which is limited to the combined U.S. operations of the FBO.<sup>16</sup>

However, in a footnote, the Proposal suggests that business line management of the combined U.S. operations “should ensure that business line risks are captured comprehensively with consideration given to risks outside the United States that may affect the FBO’s combined U.S. operations. Moreover, business line management should provide sufficient information to global management and escalate issues, as appropriate, to enable an understanding of the risks from the combined U.S. operations.” On the one hand, these statements could be understood as reflecting ordinary course risk evaluation and escalation practices. On the other hand, they also could be understood as implying, perhaps indirectly, standards for evaluating and managing risks outside the United States or implicit standards for how global management should respond to escalated issues. Further, they could be viewed as assigning U.S. senior management a degree of responsibility for global operations as, in many instances, global operations could affect U.S. operations, even if they do not meaningfully relate to activities within the United States.

We therefore suggest that these statements be clarified to make clear that the ultimate management of non-U.S. risks, and responses to escalated issues, is a role for non-U.S. management and not the subject of the guidance in the Proposal.

### **D. Core Principles of Independent Risk Management (“IRM”) and Controls**

In general, the substance of the discussion in the Proposal regarding the independent risk management function and control functions is helpful, informative and understandable in the FBO context. However, there are elements of the guidance in the Proposal that, as in the case of the other sections, raise questions about the intended scope and operation of the guidance as applied to FBOs. For example, while footnotes in the guidance clarify to a certain extent the way that references to the CRO and the risk committee should be interpreted (*i.e.*, as references to the U.S. CRO and the U.S. risk committee required by Regulation YY), the remainder of the discussion in this part of the guidance contains references to the CRO’s responsibilities in relation to the board of directors in a way which obscures its scope in the FBO context. We assume that these references should similarly be understood as references to the way in which the U.S. CRO relates to the U.S. risk committee, but this should be clarified.

Similarly, references to the Board’s expectations of the Chief Audit Executive (“CAE”) are unclear in the context of the combined U.S. operations of FBOs. The Proposal

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<sup>15</sup> 83 Fed. Reg. at 1358.

<sup>16</sup> See above and 83 Fed. Reg. at 1356.



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notes that, other than the expectations of the CRO and the CAE, the Proposal would give covered institutions significant flexibility in designing the structure of their risk management framework and governance and internal controls. For FBOs, the CRO expectations are relatively clear, but the CAE expectations are not. The Proposal notes that “[f]or an FBO, the internal audit function for the combined U.S. operations should have independent oversight of those.”<sup>17</sup> We assume that this captures the core of the Board’s guidance in this area for FBOs.

The Board’s expectations for the CAE do not address its application to FBOs, and we therefore assume that there would not be an expectation that FBOs would have a board of directors-appointed CAE for their combined U.S. operations (as opposed to U.S. BHCs, which appear to be the main focus of this part of the guidance). Indeed, if the Board’s expectations were otherwise, it would appear to be in conflict with existing Board guidance, including Supervisory Letters 03-5 and 13-1, and we assume that the conflict or departure would have been highlighted and explained in the Proposal. The general provision in the Proposal’s guidance on internal audit suggests that those Supervisory Letters are not meant to be superseded by the Proposal.<sup>18</sup> Supervisory Letters 03-5 and 13-1 are clear in their articulation of standards for the internal audit function of FBOs, and we suggest that the Board clarify the Proposal to make clear that they remain the operative expectations for FBOs.

### CONCLUSION

The IIB appreciates the Board’s efforts to consolidate and clarify existing supervisory expectations regarding the roles of senior management, business line management and risk management. The Board’s effort to align complementary sources of guidance for U.S. BHCs is a welcome development, and we encourage the Board to undertake a similar initiative for FBOs.

We respectfully submit, however, that the current state of the Proposals as applied to FBOs falls well short of what the Board has published for U.S. BHCs. Numerous interpretive questions have arisen due to the way in which the Board has published the Proposals for FBOs, and specific questions and concerns arise from the way in which the Board has explained the application of the Management Proposal to FBOs.

As we have previously recommended, the Board should develop a Management Proposal to reflect the unique circumstances of FBOs’ U.S. operations. This can most usefully be accomplished through a separate proposal tailored to FBOs, rather than through suggestions in footnotes about how the U.S. BHC proposal could be adapted. Just as the Board developed a comprehensive rulemaking for FBOs as part of Regulation YY, the Board should address its supervisory expectations for FBOs in a comprehensive and coherent way through FBO-specific guidance.

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<sup>17</sup> 83 Fed. Reg. at 1359.

<sup>18</sup> 83 Fed. Reg. at 1362.



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We appreciate your consideration of our comments. Please contact the undersigned if we can be of further assistance.

Sincerely,

A handwritten signature in black ink that reads "Sarah A. Miller". The signature is fluid and cursive, with the first name being the most prominent.

Sarah A. Miller  
Chief Executive Officer



**INSTITUTE OF INTERNATIONAL BANKERS**

**ATTACHMENT TO THE MARCH 15, 2018 IIB LETTER ON  
THE MANAGEMENT GUIDANCE PROPOSAL  
(Docket No. OP – 1594)**

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February 15, 2018

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Ann E. Misback  
Secretary  
Michael S. Gibson  
Director, Division of Banking Supervision and Regulation  
Mark E. Van Der Weide  
General Counsel  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, D.C. 20551

Re: Request for an Adjustment to the Timing and Method for Proposing and Adopting Guidance on Supervisory Expectations for Boards of Directors, a Large Financial Institution Rating System and Effective Senior Management and Risk Management

Dear Ms. Misback and Messrs. Gibson and Van Der Weide:

We are writing with a pressing concern regarding the way in which the Board has issued for comment its recent proposals (1) providing guidance on the Board's supervisory expectations for effective boards of directors (the "Board Effectiveness Proposal" and such guidance the "BE Guidance"),<sup>1</sup> (2) introducing a proposed new ratings system for large financial institutions, or "LFIs" (the "LFI Rating Proposal"),<sup>2</sup> and (3) proposing guidance describing core principles of effective senior management, the management of business lines, and independent risk management and controls for LFIs<sup>3</sup> (the "Management Proposal" and, together with the Board Effectiveness Proposal and the LFI Ratings Proposal, the "Proposals").

In short, the Board has provided a workable sequence and timing to review and comment comprehensively on the Proposals together as they apply to U.S.-headquartered bank holding companies ("U.S. BHCs"), but the same opportunity has not been provided with respect

<sup>1</sup> 82 Fed. Reg. 37219 (Aug. 9, 2017).

<sup>2</sup> 82 Fed. Reg. 39049 (Aug. 17, 2017).

<sup>3</sup> 83 Fed. Reg. 1351 (Jan. 11, 2018).



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to the FBO-related aspects of the Proposals. We recommend below adjustments to the process to address this concern.

As the Board has recognized, the development of guidance for effective boards of directors, senior management, business line management, and independent risk management and controls for FBOs involves complexities not present for U.S. BHCs. These complexities chiefly stem from the fact that the U.S. operations of FBOs are part of global banking organizations, which themselves are subject to supervision and regulation by home country authorities on a consolidated basis, as well as home country corporate governance and other legal requirements. These considerations, coupled with the need to consider carefully and address directly and clearly the potential extraterritorial reach of the Board's oversight, call for a deliberate approach that gives FBOs meaningful opportunities to comment.

Last August, the Board published for comment the Board Effectiveness Proposal, which, it stated, would not apply to IHCs established pursuant to Regulation YY. Instead, the Board stated that it "anticipates proposing guidance on board effectiveness for IHCs at a later date"<sup>4</sup> and specifically requested comments on how the BE Guidance proposed for U.S. BHCs should be adapted to apply to IHC boards of directors. The IIB appreciates this measured approach, which will enable the Board the opportunity to develop guidance that appropriately and with due deliberation takes into account both the distinctive status of IHCs, vis-à-vis U.S. BHCs, as *intermediate* holding company subsidiaries of parent banks headquartered outside the United States and the particular governance challenges presented by vesting IHC boards with responsibility for their FBO's combined U.S. operations, which include U.S. branches that are not part of the IHC.

Today, the IIB submitted a letter addressing the IHC aspects of the Board Effectiveness Proposal (the "BE Guidance Letter"), and we look forward to commenting on a future proposal that is tailored specifically to the circumstances of IHCs. However, until that future guidance is proposed for comment, the IIB necessarily is unable to assess the Board Effectiveness component in relation to the LFI Rating Proposal and the Management Proposal.

In conjunction with issuance of the Board Effectiveness Proposal last August, the Board published the LFI Rating Proposal. In that Proposal, the Board indicated that the new LFI Rating System would apply to IHCs, but the Proposal left considerable uncertainty regarding how the Governance and Controls component of the new rating system would apply inasmuch as the Board at that time had not issued any guidance regarding how the two aspects of that component – Board Effectiveness and the management of core business lines and independent risk management and controls – would apply to IHCs. Today, the IIB submitted comments on the LFI Rating Proposal.

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<sup>4</sup> 82 Fed. Reg. at 37219, note 1.



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Last month, however, the Board published for comment the Management Proposal, which, in contrast to the Board Effectiveness Proposal, applies to FBOs' combined U.S. operations (including their U.S. IHCs, as applicable). Yet the Management Proposal provides only limited explanation of how the proposed guidance would apply to FBOs and raises significant questions regarding what the Board intends. For example, the Management Proposal does not address how the Board's expectations of IHC boards of directors would relate to the expectations of senior management and an independent risk management function, since the Board has not yet published a Board Effectiveness proposal for IHCs. The IIB is consulting with its members on the Management Proposal and will submit comments on the Proposal.

The Board's most recent extension of the comment periods for the Board Effectiveness and LFI Rating Proposals has provided approximately 45 days to consider the relationships among those two proposals and the Management Proposal before the deadline for submitting comments on the first two. The review of the Proposals as they apply to U.S. BHCs is based on fully-developed proposals designed specifically with the business models of these firms in mind. In contrast, as discussed above, the LFI Rating and Management Proposals do not comprehensively address how they apply to the specific circumstances of FBOs' U.S. operations, and the applicability of the BE Guidance to IHCs remains to be determined. We would respectfully submit that this process has not provided a sufficient opportunity to comment on the FBO-related aspects of the Proposals.

There is a straightforward way to address these concerns. The Board should, at a minimum:

- extend the comment period for the Management Proposal to end sixty days after the publication of a Board Effectiveness Proposal for IHCs.

However, we believe a more comprehensive response is called for to enable submission of meaningful comments on how all three Proposals should be adapted for FBOs, and thereby promote the Board's comprehensive assessment of the Proposals. In this context, the Board should:

- issue a Board Effectiveness Proposal for IHCs;
- issue a new Management Proposal for FBOs that specifically and comprehensively addresses the Board's expectations for FBOs in these areas, and allow comment on the governance component of the LFI Rating System in light of the FBO-specific proposals,<sup>5</sup> and

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<sup>5</sup> Ideally, the Board would issue a single proposal that covered all topics together as they relate to FBOs, but if the timing issues are addressed in the way we suggest then separate proposals would be workable.



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- finalize all three proposals as applicable to FBOs together, with a single effective date.

Under this approach, and as we explain further in our BE Guidance Letter, once the LFI Rating Proposal is adopted in final form, the existing LFI supervision framework would remain in place for IHCs with respect to the governance component thereunder until the BE Guidance and Management Proposals, appropriately adapted for FBOs, are finalized.

The IIB looks forward to working with Board staff in the development of practical approaches to these issues that accomplish the Board's supervisory objectives. We would welcome the opportunity to meet with you and your colleagues to discuss our concerns. In the meantime, please contact the undersigned if we can be of further assistance.

Sincerely,

A handwritten signature in black ink, appearing to read 'Sarah A. Miller', written in a cursive style.

Sarah A. Miller  
Chief Executive Officer