May 10, 2012

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Attention: Jennifer J. Johnson, Secretary
Docket No. 1438; RIN 7100-AD-86

Re: Bank and Financial Company Risk Committee Requirements Under Dodd-Frank Section 165

To the Board of Governors:

Thank you for the opportunity to comment on proposed rules implementing Sections 165 and 166 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank). We are writing today about the proposed rules requiring a board-level risk committee for large bank and financial company boards.

About NACD

For the past 35 years, the National Association of Corporate Directors (NACD), now 12,000 members strong, has provided education and resources to directors and boards to help them improve their performance. As part of our work, by convening experienced corporate directors together with stakeholders, we have developed and issued recommended practices in a wide range of areas, including board oversight of risk as well as board and committee structure. We have conducted research, convened groups, and published reports on risk oversight and are forming a standing committee of advisors on this topic.

NACD's Response to the Dodd-Frank Risk Committee Provision

NACD has no objection to the language of the Dodd-Frank provision itself. In a March 2012 white paper prepared for our members, we noted that under Dodd-Frank, the Board of Governors of the Federal Reserve System requires certain financial institutions to establish a board-level risk committee. (The requirement applies to any publicly traded non-bank financial company supervised by the Board of Governors and to any publicly traded bank-holding company with consolidated assets of $10 billion or more.) Under the

Dodd-Frank provision, the board-level risk committee of certain financial companies and banks must:

- be responsible for the oversight of the enterprise-wide risk management practices of the company;
- include the number of independent directors the Board of Governors recommends (based on the nature of operations, size of assets, and other appropriate criteria related to the company); and
- include at least one risk-management expert with experience in "identifying, assessing and managing risk exposures of large, complex firms."

NACD's Concerns About the Proposed Rule

The proposed rule, as published in the Federal Register January 5, 2012, goes far beyond the scope of the actual provision in Dodd-Frank as described in the three bullet points above. The proposed rule would make board adaptation to this provision cumbersome and unworkable, particularly through the following requirements:

- The requirement that the risk committee include at least one member with "risk management expertise." The definition of risk management expertise is vague and lacks a comprehensive explanation of acceptable experiences and background. We believe a more robust definition is needed that provides guidance as to who would qualify as a risk management expert.

- The additional "expectation" that all risk committee members should "have experience developing and applying risk management practices and procedures, measuring and identifying risks, and monitoring and testing risk controls with respect to banking organizations (or, if applicable, nonbank financial companies)." This expectation may be challenging to implement and goes beyond the scope of the Dodd-Frank provision. Essentially, the proposal would require that not one member but all members of the board have risk management experience. An expectation of this sort may limit not only who sits on the committee but on the larger board as well.

- The requirement to fully document and maintain records of the risk committee's "risk management decisions" is particularly troublesome. At best, this provision lacks specificity; at worst, it demonstrates a general misunderstanding of the board's role in risk management and oversight. Boards of directors do not make decisions on risk management practices or procedure. Rather, the board may offer constructive criticism of management's risk plans and eventually vote to approve (or disapprove) of them. As currently written, the proposed rule blurs the line between the roles of board and management in risk management responsibilities. As such, sec. 252.126(b)(4) should be corrected to reflect the board's oversight role and rewritten as follows: "Meet with an appropriate frequency and as needed, and fully document and maintain records of its proceedings, including *matters voted upon by the independent directors of the committee*."

- The requirement to have the chief risk officer report to the risk committee and the CEO, and whose compensation must be "appropriately structured to provide for an objective assessment of the risks taken by the company." There are two issues with this provision. First, requiring the CRO to report to the risk committee crosses a line. We believe that having the CRO additionally report to the risk committee may drag directors into the day-to-day operations of the organization. Secondly, the CRO's proposed pay structure does not allow for discretion in crafting a compensation model. Compensation committees are best suited to approve decisions regarding executive pay programs and this proposal forces a rigid structure that may not be appropriate for all covered organizations.

- The prohibition on housing the board risk committee within another committee or be part of a joint committee. We are concerned that this provision may weaken the current risk oversight practices at some boards. According to the NYSE, audit committees are already required to discuss policies with respect to financial risk assessment and risk management. While this may not apply to every covered company, the proposal may lead to a duplication of work at the board level. Additionally, there may be some confusion as to which committee truly owns risk oversight. Finally, we believe the focus on risk oversight responsibilities is more important than any particular rigid structure. As explained later in this letter, putting risk responsibilities in the hands of one committee is the least effective oversight practice. A more balanced approach would be to remove the prohibition and allow organizations to assign the responsibilities of sec. 252.126(c)(1-7) where appropriate. In these instances, the board would have to disclose the rationale for its assignment and the forgoing of a risk committee.

NACD believes that a risk committee should not be alone in setting risk management policies. Instead, the full board should approve and oversee the policies developed by management. Risk management by a board risk committee—especially one that works in isolation from management and other board committees—could weaken both risk management and risk oversight.

Furthermore, the responsibility for risk oversight has changed in recent years. It has increasingly become a matter for the full board, not solely a committee. Four years ago, as we noted in the *NACD Public Company Survey* of 2008, the majority of boards (66.7 percent) placed risk oversight in the hands of the audit committee. That practice is slowly changing. In 2011, the NACD's annual Public Company Governance Survey reported that 43.5 percent of boards assigned the majority of tasks directly related to the oversight of risk with the audit committee and 38.8 percent with the full board. Only 9.8 percent of companies used a risk committee for oversight purposes.

The data show boards beginning to recognize that risk oversight is a board responsibility and each director must take part. This perception was grounded in the 2009 *Report of the NACD Blue Ribbon Commission on Risk Governance* (see enclosed). The report states:

> …as a general rule, the full board should have primary responsibility for risk oversight, with the board's standing committees supporting the board by addressing the risks inherent in their respective areas of oversight. It is rare that any one committee—such as the audit committee or a risk committee—would have the time, resources, and expertise to oversee the full range of risks facing a company. Moreover, the critical link between strategy and risk points to the need for the full board—rather than any one committee—to have responsibility for risk.

The report continues by stating, "it is important to note that any committee with the word 'risk' in its title cannot be the sole overseer of risk. Risk committees should not replace the board's active engagement in risk oversight." It is NACD's stance that active, proper, and effective risk oversight requires the full board's attention.

While we agree with the intention of improving risk oversight, we are concerned that the proposed risk committee rules cross too far over into management's role for risk management. Further, the proposed rule should make it clear that the full board remains responsible for oversight of risk. The rulemaking should bolster existing enterprise risk management programs and place more responsibility for risk oversight into the hands of the full board.

We hope that the Federal Reserve System can amend the rule on risk committees so as to allow bank boards to take responsibility for governance, rather than forcing them to conform to rules that could weaken their ability to provide effective oversight to their institutions.

Sincerely,

Ken Daly President and CEO NACD	Barbara H. Franklin Chairman NACD