



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

WASHINGTON, D.C. 20551

DIVISION OF SUPERVISION
AND REGULATION

SR 21-19

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Revision History:

On January 9, 2026: This letter was revised to remove references to reputational risk.

**TO THE OFFICER IN CHARGE OF SUPERVISION
AT EACH FEDERAL RESERVE BANK**

SUBJECT: The Federal Reserve reminds firms of safe and sound practices for counterparty credit risk management in light of the Archegos Capital Management default

Applicability: This letter applies to institutions supervised by the Federal Reserve that have large derivatives portfolios and relationships with investment funds.

Archegos Capital Management, an investment firm heavily concentrated in a small number of U.S. and Chinese technology and media companies, defaulted on March 26, 2021, causing over \$10 billion in losses across several large banks, principally outside the United States. The Federal Reserve, along with other U.S. and foreign regulators, initiated a supervisory assessment to understand the actions that led to Archegos' failure and assess any risk-management shortcomings at supervised firms.

In light of the Archegos default, and in the context of firms' relationships with investment funds, the Federal Reserve is issuing this guidance to remind firms of the supervisory expectations in Interagency Supervisory Guidance on Counterparty Credit Risk Management, and to make firms and industry participants aware of practices that may be inconsistent with safe and sound banking practices.¹ This letter is intended primarily for use by banking organizations with large derivatives portfolios and relationships with investment funds, as well as for supervisors as they assess and examine such institutions. This letter is generally not applicable to

¹ See SR Letter 11-10, <https://www.federalreserve.gov/supervisionreg/srletters/sr1110.htm>.

community banking organizations and banking organizations with insignificant derivatives portfolios or relationships with investment funds.

The Federal Reserve is concerned with practices where, both at the inception of a fund relationship and, on an ongoing basis during periodic credit reviews, firms accept incomplete and unverified information from the fund, particularly with regard to the fund's strategy, concentrations, and relationships with other market participants. These concerns are heightened where a fund client has a history of concentrated positions and losses. More generally, these practices represent insufficient due diligence and may be inconsistent with safe and sound banking practices. Similarly, when initiating a relationship and on an ongoing basis, firms should obtain critical information regarding size, leverage, largest or most concentrated positions, and number of prime brokers with sufficient detail or frequency to determine the fund's ability to service its debt. If a client refuses to provide this information, firms should consider whether it is consistent with safe and sound practices for them to begin or maintain a relationship with the fund or whether they can use strong compensating measures, such as significantly more stringent contractual terms, to mitigate the risk.

The Federal Reserve also is reminding firms that poor communication frameworks and inadequate risk management functions, as well as fragmented systems and ineffective governance, hamper their ability to identify and address risk. Risk management and control functions should have the experience and stature to effectively control risks associated with investment funds. Further, both oversight and business groups should review contractual terms and practices relating to internal limits to assess whether they are commensurate with the risk the fund poses to the firm.

Finally, the Federal Reserve is concerned that firms may agree to margin terms inappropriate to their investment fund clients, failing to provide for adequate margin levels or sufficient risk-sensitivity. Contractual terms that prevent a firm from improving its margin position or closing out positions quickly if a fund misses margin calls, even when presented with an increasing risk profile at the fund, may be inconsistent with safe and sound practices.

In summary, consistent with the guidance in Interagency Supervisory Guidance on Counterparty Credit Risk Management,² firms should:

- Receive adequate information with appropriate frequency to understand the risks of the investment fund, including position and counterparty concentrations, and either reconsider the relationship or set sufficiently conservative terms for the relationship if the client does not meet appropriate levels of transparency
- Ensure the risk-management and governance approach applied to the investment fund is capable of identifying the fund's risk initially and monitoring it throughout the relationship, and ensure applicable areas of the firm – including the business line and the oversight function – are aware of the risk their investment fund clients pose to the firm and have tools to manage that risk; and

² See <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20211210a.htm>.

- Ensure that margin practices remain appropriate to the fund's risk profile as it evolves, avoiding inflexible and risk-insensitive margin terms or extended close-out periods with their investment fund clients

Reserve Banks are asked to distribute this letter to the supervised organizations in their districts and to appropriate supervisory staff. The Board is continuing to review firms' weaknesses identified in the above areas and may take further action. Questions may be sent via the Board's public website.³

Michael S. Gibson
Director
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Cross References:

- SR Letter 11-10, "Interagency Counterparty Credit Risk Management Guidance"

³ See <http://www.federalreserve.gov/apps/contactus/feedback.aspx>