STATEMENT OF

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GUIDANCE, SUPERVISORY EXPECTATIONS, AND THE RULE OF LAW:

HOW DO THE BANKING AGENCIES REGULATE AND SUPERVISE INSTITUTIONS?

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My name is Margaret E. Tahyar, known as Meg, and I have been a partner at Davis Polk & Wardwell LLP in the Financial Institutions Group for 22 years. I am one of the co-authors of the law school textbook, *Financial Regulation and Policy* (Barr, Jackson, Tahyar, 2nd Edition, Foundation Press 2018). In addition to my day job as a partner at Davis Polk, I have taught as a Lecturer on Law at Harvard Law School for each of the last 5 years, most recently co-teaching a FinTech course. I represent a large range of financial institution clients, but I am here today in my individual capacity and not on behalf of any client. The views I express are my own, and not necessarily those of Davis Polk, any client or any other organization with which I am affiliated. Many of the views expressed in this testimony have been previously published in my article *Are Banking Regulators Special?*, 6 BANKING PERSPECTIVES, or in my working paper *Legal Interpretation is Not Like Reading Poetry – How to Let Go of Ordinary Reading and Interpret the Legal Framework of the Regulatory State*, Dec. 4, 2018 Working Draft, available on the Davis Polk website.

Introduction

Many sectors of the economy are regulated. Only the banking sector is also supervised. The legal framework that governs the banking sector and the banking agencies is written and public. Whether you agree or disagree with the policy choices, the legal framework is made in full sight of all. Supervision happens behind closed doors. It relies upon secrecy and involves a system of discretionary actions by supervisory staff. This zone of secrecy is traditionally justified for the sake of financial stability and bank safety and soundness. There has long been an uneasy truce between the transparency and accountability required by the rule of law and the secrecy and discretion of supervision.

That uneasy truce has become untenable. One canary in the coal mine is the increase in leaks of confidential supervisory information. The melody that canary is singing is changed societal mores about transparency. It also matters that confidential supervision can be a shield that makes it more difficult to hold the banking supervisors accountable. The public, including the Congressional oversight committees, scholars and others, has limited information about the work of the banking supervisors. Should they be praised or criticized?[1] Nobody knows. The public debate, and academic scholarship, is critically underinformed.

As Hyman Minsky has noted, "Perfection is out of the question, but better is possible."[2] Understanding that some secrecy is necessary for bank safety and soundness and candid conversations, I recommend beginning with three changes.

First, the regulations governing confidential supervisory information need to be modernized. Their core framework was put in place during the late 1960s and only lightly updated in the mid-1990s. They no longer match the reality of the digital age. The realm of confidential supervisory information should be narrowed to the core minimum necessary to protect financial stability or individual bank safety and soundness.

Second, we should recognize that one of the after effects of the Financial Crisis has been a vast expansion in the nature of supervision and its zone of secrecy and discretion. Social and economic policy choices are being made within a shadow regulatory system. From "moral suasion" to the matters requiring attention and matters requiring immediate attention that come out of the examination process, as well as horizontal reviews, banking organizations are subject to both a public and a nonpublic web of guidance and expectations. Sensible guardrails are needed so that supervision does not make economic and social policy choices that impact credit, jobs and growth in an ad hoc manner free from oversight. We should also recognize that secret lore[3] and guidance have a troublesome placement in the legal framework since the concept of secret law in a democracy is on shaky ground.

Third, Congress and the banking agencies need to think clearly about how to create an environment where the supervisory staff are given the training, resources and tools that would permit them to do their jobs in a way that is more transparent to the world, where there is more accountability and where there is

[1] Banking supervisors are highly professional men and women acting in good faith to carry out an important mission in monitoring the banking sector for safety and soundness and compliance with the law. The pressures on the supervisory staff during and since the Financial Crisis have been enormous. I am convinced that more openness will lead to as much praise as criticism.

[2] Hyman P. Minsky, Financial Instability and APT Bank Supervision, Hyman P. Minsky Archive Paper 470, 24 (1992).

[3] I prefer the term "secret lore" to "secret law" even though many banking lawyers, myself included, will, in conversation refer to "secret law." We do well to remind ourselves that, in a democratic country, law cannot be secret. And, under the Administrative Procedure Act, it is not.

more consistency with the rule of law. As the zone of secrecy and discretion has widened, it has increasingly become delinked from the legal framework of the regulatory state. One way to increase those tools and resources, in light of the increased complexity of both the legal framework and the banking sector, is that training for the supervisory staff should be expanded to include core modules on the rule of law in a Constitutional democracy and the legal framework that governs the regulatory state.

The time has come for a rebalancing of how the banking regulators supervise banking organizations. The extensive scope of the shadow regulatory system, which operates without transparency and with limited accountability, has become untenable in the digital age. The rebalancing should be in favor of more transparency, accountability and observance of the rule of law by the banking supervisors. We need to get this balance right as we move toward a more digital world with increasing reliance on algorithms. If the norms of the rule of law, transparency and accountability are not part of supervisory culture, they will not find their way into new technology.

We should not jettison confidential supervision but we ought to reform it for the 21st Century digital era.

The need to rethink the theory of supervision and how we might go about it are inextricably linked to its history. I therefore begin in Part I by describing that history and suggesting principles for how to reform the regulators' approach to confidential supervisory information. In Part II, I set forth my view that supervisory staff have not been trained in the legal framework at a time when their jobs have grown tougher and the legal framework itself has become more complex.

I. The Need to Reform Confidential Supervisory Information

The federal banking regulators have long operated under a cultural mindset different from other independent federal agencies both in the financial sector and in the larger regulatory state.[4] History explains why the separate cultural tradition exists. This Part examines two regulatory traditions—a tradition of secrecy and discretion unique to banking supervision and a New Deal tradition of transparency in the regulatory state more broadly.

A. The Tradition of Secrecy and Discretion

In banking supervision, two regulatory traditions have lived in an uneasy truce since the New Deal. The central core and direct ancestor of federal banking supervision is the confidential bank examination, which dates back to at least the mid-19th Century.[5] Many do not realize, however, that these traditions of secrecy and discretion developed at a time when there was limited federal regulation of any sector, long before federal deposit insurance, the creation of the Federal Reserve as the lender of last resort, the New Deal administrative state of the 1930s and the Administrative Procedure Act (APA) of 1946. The lack of a solid foundation in federal law for many of the secrecy traditions of the banking regulators will surprise many who have accepted them as if they were contained in hallowed texts.

There is another, more recent policy tradition, dating from the New Deal, which created federal securities disclosure laws and put in place a legal framework that favors transparency and accountability by administrative agencies. Both traditions must abide by the rule of law in our Constitutional democracy.

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[4] For the purposes of this testimony, the concept of a banking regulator is limited to the Federal Reserve, the OCC and the FDIC. The CFPB operates under newer, more transparent cultural norms.

[5] As Professor Conti-Brown has noted, "the Examination Report from the Comptroller of the Currency for each bank remained the same in general form from 1865 to 1953—an extraordinarily stable institutional arrangement across a long period of economic, political, legal, and financial tumult." Peter Conti-Brown, Stress Tests and the End of Bank Supervision, The Regulatory Review (Apr. 21, 2016), available at link.

The truce remained workable when banks were engaged almost exclusively in taking demand deposits and making commercial loans. But, as market competition and technological change made the banking sector more complex, the uneasy and unexamined truce was, counterintuitively, sustained by the expansion of both the tradition of secrecy and discretion and that of transparency and the rule of law. In today's complex times, we have both more secrecy and discretion and more transparency. The problem is that we have them randomly and without serious thought about how the zone of secret supervision ought to work in the 21st Century digital era.

The bank examination, where an outside person appointed by the state examines the books and records of the bank, has a long history. The 19th Century bank examiner's job was to look closely at the loans and liabilities of each individual bank and to make sure that vault cash and reserves really existed.[6] He, and in the 19th Century it was always a he, performed his task in conditions of utmost secrecy.[7] His critically important job was to assess whether the bank was safe and sound in an era when rumors could lead to deposit runs and bank panics were frequent.[8] Thus developed the tradition of the secret bank examination, the crime of spreading false rumors about a bank[9] and the view that bank supervision was best done inside a cone of confidentiality to preserve the stability of the financial system and avoid triggering a bank panic.

Central to the concept of a confidential bank examination is the need for a free flow of communication in conditions of high trust between a bank's management, its board of directors and supervisory personnel. Bank examiners and the banking sector feel strongly about the need for this candid conversation, which has contributed to the creation of a common-law bank examiners' privilege that keeps reports out of the public domain and out of the hands of the plaintiff's bar.[10] The other justification for a confidential bank examination report has been that it contains private personal information about bank customers and unvarnished views about the creditworthiness of borrowers. The free flow of information, much of it deliberately and appropriately leaning toward the negative and critical, and the protection of personal information are policy goals to be taken seriously today.

The federal banking regulators used the passage of FOIA in the mid-1960s, a statute meant to expand the scope of information available to the public, to expand their zone of confidentiality beyond the scope of the traditional bank examination. There is no federal statute that explicitly prohibits anyone other than

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[6] Simpler times exemplified in *It's a Wonderful Life* by Mr. Carter, a diligent bank examiner checking whether the Bailey Building & Loan had cash in its vault.

[7] The first woman bank examiner was Adelia M. Stewart who officially become a bank examiner in 1921, after having gone to law school at night and having worked as a "clerk-stenographer" at the OCC since 1892. In 1922, the year after she was the first woman to pass the test for national bank examiners, she was promoted to head of the examination division. *See* Office of the Comptroller of the Currency, The Changing Role of Women in the Workplace, available at link. I like to imagine that the first woman examiner understood the tight link between the legal framework and supervision.

[8] Panics took hold of the American banking sector in 1819, 1837, 1857, 1873, 1893, 1901, 1907, 1929 and 1933, as well as in 2007–2008.

[9] N.Y. Banking Law § 671 False Statements or Rumors as to Banking Institutions.

[10] The need for candid conversations in the supervisory context is hotly defended in the courts by banking regulators. By sharp contrast, banking regulators frequently take the view that the attorney-client privilege should be waived by the banks or limited in supervisory communications. So, sometimes candid conversations are encouraged and sometimes they are not.

bank examiners from disclosing the bank examination or parts of it,[11] such as CAMELS or other ratings.[12] Soon after the passage of FOIA,[13] each of the Federal Reserve, the OCC and the FDIC promulgated stern but ambiguous regulations that contain additional constraints on the sharing of confidential supervisory information. These regulations also introduced the assertion of the federal banking regulators that bank examinations and other supervisory communications are the property of the banking regulators.

The authority to treat confidential supervisory information as property is less solid than one might think, relying on a general federal statute relating to federal government property. One suspects that the general federal property law was pressed into service by the federal banking regulators because no other statutory authority was available. The result of viewing bank examinations or other supervisory communications as the property of the state is that stealing them or misusing them becomes a crime. It is solely from this source that the criminal prohibitions on banking organizations revealing bank examinations or other supervisory communications derive. With the increased scope of confidential supervisory information along with the changes in technology and societal mores, it is increasingly uncomfortable for banking entities and their personnel to have to worry about criminal liability for the "property" of the banking regulators.[14]

The banking regulators have defined this type of "property" very broadly in their regulations, the plain text of which could be read to encompass a vast amount of information. Tracking the statute, the Federal Reserve's definition of confidential supervisory information includes any document prepared by a banking organization "for the use of" the Federal Reserve.[15] The FDIC's definition is similar.[16] The Federal Reserve's definition excludes documents prepared by the banking organization "for its own business purposes and that are in its possession."[17] The FDIC does not have such an explicit exclusion. The OCC's definition of confidential supervisory information (in OCC parlance, "non-public OCC information") is broader and includes any "record" that is "obtained" by the OCC in connection with the OCC's performance of its duties, including "supervision."[18]

These regulations were put in place before a world of email, electronic files, the cloud and PowerPoint and at a time when the data and information flow was much smaller. The line between data prepared by the banking organization "for the use" of the agency or for its own "business purposes" is a troublesome one in the supervisory context today. It cannot be that, by some means of transubstantiation, every bit of data or every PowerPoint sent to the regulators becomes confidential supervisory information.[19]

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[11] There is a federal criminal statute that prohibits bank examiners from disclosing the results of an examination. *See* 18 U.S.C. § 1906. Few are aware, however, that the Comptroller may, if he is not satisfied with the response of a national bank, disclose an examination. *See* 12 U.S.C. § 481.

[12] CAMELS is used in this testimony for simplicity even though there are other ratings systems with their own acronyms.

[13] The precise words of the FOIA statute's exemption, which were originally drafted by the banking regulators, encompass matters "contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions" from disclosure.

[14] One of the elements of the confidential supervisory information regulations that needs updating is the requirement that any "property" of the banking regulators be viewed on bank premises. This made sense in the late 1960s, but with the development of email and the cloud, it no longer does.

[15] 12 C.F.R. § 261.2(c)(1)(iii).

[16] *See* 12 C.F.R. § 309.5(g)(8).

[17] 12 C.F.R. § 261.2(c)(2).

[18] 12 C.F.R. § 4.32(b).

[19] Even if such information were not considered confidential supervisory information, other exemptions from FOIA disclosure may apply, such as the exception for trade secrets, confidential commercial or financial information and personal information.

The Federal Reserve, the FDIC and the OCC all permit sharing of confidential supervisory information within the banking organization. Under the OCC's regulation, sharing within the banking organization is permitted only "where necessary or appropriate for business purposes."[20] The OCC has not defined what would be necessary or appropriate for business purposes and criminal liability may hang on this ambiguous phrase. These ambiguities will get more intense as we enter into more technologically infused RegTech. There is a real question whether these vague standards, along with the changes in the world since the 1960s, ought to continue to contain the threat of criminal liability.

B. The Other Tradition of Transparency

The other regulatory tradition has as its central paradigm that of the disinfectant of disclosure.[21] Created in the New Deal or as an immediate reaction to it, the norms of the securities disclosure laws and the APA illustrate this cultural mode of transparency. These laws take a very different approach to the relationship between the government and the governed.

The APA is properly viewed as a "bill of rights for the new regulatory state."[22] It demands that regulations be public and subject to notice and comment, and has transparency and accountability as its central core. The APA was the end product of a decade's worth of political wrangling between New Dealers, who fought for the expansion of a discretionary administrative state, and those concerned with the rule of law and transparency. A compromise was finally reached following Truman's assumption of the Presidency, in a post-WWII environment more sensitive to authoritarian tendencies.[23] Public choice scholarship since the New Deal has widely shown that the regulators also have their own stakeholder interests.

It was not immediately clear whether or to what extent this new approach would apply to banking regulators, at least from the perspective of the supervisors accustomed to secrecy and discretion. While for many readers the New Deal and the passage of the APA may seem like long ago developments, it is important to understand that, by the time of their passage, the cultural traditions and institutional path dependency of the banking supervisors had already been set. Early versions of the bill that became the APA excluded the federal banking agencies from its scope.[24] The banking regulators might be forgiven, in the early years after the APA, for thinking that the APA only lightly applied to them. But we are now nearly 85 years since the passage of the Securities Exchange Act and 73 years since the passage of the APA. The impulse toward secrecy remains strong within the banking regulators, even as transparency and accountability have become foundational tenets of administrative law.[25]

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[20] 12 C.F.R. § 4.37(b)(2). The Federal Reserve does not have this limitation on sharing in the group. The FDIC's regulations require that there be an annual board resolution for a bank to share a report of examination with its parent, which must contain a number of archaic requirements. These requirements include that the resolution specifically name the parent holding company and state the snail mail address to which the reports are to be sent. *See* 12 C.F.R. § 309.6(b)(7)(iii)(B).

[21] As Justice Brandeis famously said just before his time on the court, "[s]unlight is said to be the best of disinfectants." Louis D. Brandeis, Other People's Money and How the Bankers Use It 93 (Frederick A. Stokes Company ed. 1914).

[22] George B. Shepherd, Fierce Compromise: The Administrative Procedure Act Emerges from New Deal Politics, 90 NW. U. L. REV. 1557, 1558 (1996).

[23] *See id.* at 1683.

[24] *See id.* at 1618.

[25] As stated by Professor Gillian Metzger, "Accountability is administrative law's central obsession, which it furthers through mechanisms for public participation, congressional oversight, centralized White House regulatory review, and judicial review. Fear of agency capture is a recurring theme, as is the concern that agencies will wield their delegated powers arbitrarily." Gillian E. Metzger, Through the Looking Glass to a Shared Reflection: The

A key question is how both of these regulatory traditions—the long-standing secrecy of banking regulators and the 20th Century paradigm of a transparent administrative state more broadly—have managed to co-exist in an uneasy truce for so long. One part of the answer is counterintuitive: as the banking sector has become more complex, *both* transparency and secrecy have expanded in scope.

For example, the scope of financial disclosure and its companion market discipline has been expanding over the last 50 years vis-à-vis banking organizations.[26] In addition to the constraints of the securities laws, Pillar 3 of Basel II, now in full implementation, also requires more disclosure. The existence of enhanced capital and liquidity requirements, subordinated debt, credit default swaps and, more recently, TLAC debt that might be bailed in, all push towards market signaling functions.

The public nature of these disclosures has become so embedded in our consciousness that many have forgotten that the requirements to disclose hundreds of pages of information, whether in periodic reports under the securities laws, Pillar 3 or the many public reports filed by banking organizations, were once new and shocking in the banking sector. Banking-sector requirements for disclosure lagged the disclosure norms in other sectors by many years. Call reports were not made public by the FDIC until 1972 and even then, it was upon request, with a fee for search costs,[27] bank stocks were not subject to periodic reporting until 1964,[28] the requirements of Guide 3 date from 1976[29] and audited bank financial statements were not required under federal law until 1991.[30] When CAMELS ratings were first created, they were not even disclosed to bank management.[31]

The formal and informal punitive actions of the banking regulators against banking organizations have also become increasingly more public. Banking regulators were not given formal enforcement powers until 1966. Before that, moral suasion and "jawboning" were the main powers of the banking supervisors, backed by the nuclear, and therefore not used, threat to revoke a charter or terminate deposit insurance. Even after the banking regulators were given the power to remove directors and officers, impose civil money penalties and enter into informal written memoranda or formal consent or cease and desist orders, the tendency was to favor informal—that is, nonpublic—board resolutions and memoranda of understanding (MOU). The long litany of very public post-Financial Crisis consent orders shows that the old custom has definitively changed to be more transparent. As a result, there is an increasing

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Evolving Relationship Between Administrative Law & Financial Regulation, 78 LAW & CONTEMP. PROBS. 129, 130 (2015).

[26] The long-standing spat between the banking regulators and the SEC on the calculation of allowances for loan losses is an example of the transparency and secrecy traditions clashing. *See* George J. Benston & Larry D. Wall, How Should Banks Account for Loan Losses?, Federal Reserve Bank of Atlanta (2005), available at link. That clash was resolved by an administrative detente in the early 2000s. Nonetheless, so-called GAAP/RAAP debates sometimes show up in the footnotes to call reports. It remains to be seen how the implementation of CECL will impact this dynamic.

[27] *See* 37 Fed. Reg. 28607, 28608 (Dec. 28, 1972).

[28] *See* Alfred D. Mathewson, From Confidential Supervision to Market Discipline: The Role of Disclosure in the Regulation of Commercial Banks, 11 J. OF CORP. L. 139, 141 (1986).

[29] *See id.* at 161.

[30] *See* Eugene N. White, Lessons From the History of Bank Examination and Supervision in the United States 1863-2008, *in* Financial Market Regulation in the Wake of Financial Crisis: The Historical Experience Conference 15, 34 (2009), available at link.

[31] *See* Ron Feldman, Julapa Jagtiani & Jason Schmidt, The Impact of Supervisory Disclosure on the Supervisory Process: Will Bank Supervisors Be Less Likely to Downgrade Banks? *in* Market Discipline in Banking: Theory and Evidence, edited by G. Kaufman in Research in Financial Services, Elsevier, at *3 (2003), available at link.

tendency to disclose informal and private MOUs in securities disclosure documents, with the express consent of the banking regulators, when their contents are deemed material to investors.[32]

Also on the side of transparency, the long-term trend has been toward a greater tendency to publish guidance, interpretations and FAQs, and greater disclosure of informal and formal enforcement actions against banking organizations. Many interpretive positions, even in the form of written letters, were typically kept secret well into the 1990s. It was long a given that the only way to find out the interpretive views of the Federal Reserve was to file a FOIA request and hope for the best.[33] The development of the Internet, which brings with it increased expectations of transparency, has meant that many, but not all, interpretive positions now find their way onto the banking regulators' websites. There is more in the public domain than ever before. This trend started even before the Financial Crisis and the Dodd-Frank Act, which required 390 new rulemakings by the banking agencies.[34] A prominent pre-Dodd-Frank example is that the long history of semi-public interpretations under Section 23A of the Federal Reserve Act came to an end with the promulgation of Regulation W in 2002.

Yet, all of these advances in transparency and accountability are not enough, either for the rule of law or for the norms of the digital age. The disparate elements of increased use of the Congressional Review Act, the GAO ruling that guidance can be subject to the Congressional Review Act, an increased focus on cost-benefit analysis in financial regulation and increased attention by the OMB on major guidance issued by independent agencies each, in their own way, are attempts to answer the call for more transparency and accountability.

C. The Increasing Scope of Secret Guidance and Lore

Against this recent societal backdrop of increased transparency and accountability is the opposite tradition covered by confidential supervisory information, secret guidance and secret lore. As a noted administrative law scholar has argued:

> "The banking agencies of the federal government have long maintained systems of secret evidence, secret law, and secret policy. The result has been a degree of unchecked and unstructured discretionary power that is far greater than it should be. Sound principle calls for openness, so that discretion may be checked and structured. To some extent the systems the agencies have been following violate existing legal requirements. The banking agencies can and should make procedural changes that will increase both efficiency and fairness."[35]

What may come as a surprise is that these statements were made in 1966. They remain fresh today.

Indeed, I would posit that as supervision and the banking sector have grown more complex, the amount of confidential supervisory information shielded from public view has increased vastly not only since 1966, but also at an accelerated pace after the Financial Crisis. One reason for the expansion of confidential

[32] Requirements to raise capital and restrictions on dividends are the core examples. Other MOUs remain undisclosed.

[33] As a young lawyer in the early 1990s, I was frequently given the task of crafting a FOIA request to capture a secret interpretive letter that was known by the bank regulatory bar to exist but that was not public. Letters received under FOIA were carefully tended in paper files and shared among banking lawyers. Contrast that cultural mode with that of the SEC, which began publishing no-action letters in 1970. *See* Donna M. Nagy, Judicial Reliance on Regulatory Interpretations in SEC No-Action Letters: Current Problems and a Proposed Framework, 83 CORNELL L. REV. 921, 948–49 (1998).

[34] *See* Davis Polk & Wardwell LLP, Dodd-Frank Progress Report (July 19, 2016), available at link.

[35] Kenneth Culp Davis, Administrative Procedure in the Regulation of Banking, 31 LAW & CONTEMP. PROBS. 713 (1966).

supervisory information is that the traditional bank examination has morphed into something much wider in scale and scope than its 19th and early 20th Century ancestor. A regional banking organization will have up to 50 bank examinations on different topics a year; a G-SIB will have hundreds. The annual roll-up examination now covers multiple areas, and the number of matters requiring attention or immediate attention have expanded into hundreds for some banking organizations. It is a fair question, in a time of high capital and liquidity, what these matters requiring attention are covering and at what level of materiality. It goes without saying that there is no sense of cost-benefit or proportionality. The lack of public data is disturbing.

Economic and social policy, affecting financial stability, economic growth and jobs, is being fashioned in the shadows of the confidential supervisory arena. Some of these economic and social policy choices may reflect the right tradeoffs, but, as they are made, Congress and the public have no way of knowing. Before regulators act through matters requiring attention, horizontal reviews, guidance or lore, we should ask why a particular policy choice or regulatory interpretation is being made under the rule of discretion rather than the rule of law. In an era of increased transparency and accountability, policy choices that have an impact on access to deposit services, credit allocation and investment in the banking sector—that is on jobs and growth—should be open, not secret.

Today's supervisory culture has moved far away from the core of examining the quality of a bank's loans or the amount of cash it has in its vault. It is easy to understand how the supervisory theory of the traditional bank examination translates into supervision over capital and liquidity, including stress testing. The theory of supervision for the 21st Century becomes muddled, however, once one leaves the realm of qualitative judgements around a quantitative core. How should compliance with law examinations be fashioned? What is the purpose behind supervisors' focus on the internal governance structure of management, the review of the minutes of management's discussions and forced changes in reporting lines?[36] On what basis was the ideology of the three lines of defense imposed upon almost all banking organizations?[37] The word supervision, although longstanding, appears nowhere in the legal framework governing the banking sector. The only public source is the explanations published in agency reports and on agency websites. These explanations are not helpful to understanding the theory of banking supervision beyond logical extensions of the traditional banking examination.[38] Academic scholarship on

[36] Since the Financial Crisis, the banking agencies have required that compliance in larger institutions report to risk, not legal. These decisions were taken without any public comment or discussion, and the evidentiary basis for them was not developed. In most smaller and regional banking organizations, compliance remains within legal. The collateral consequences of two competing poles of legal interpretation and judgement within the organization were not considered.

[37] The three lines of defense appears in only one place in the legal framework in guidelines issued by the OCC in 2014. *See* 12 C.F.R. pt. 30 app. D. It is otherwise not a part of the traditional bank supervision. There was no cost-benefit analysis around its adoption in the OCC's guidelines and it was imported from a position paper of The Institute of Internal Auditors. *See generally* The Institute of Internal Auditors, IIA Position Paper: The Three Lines of Defense in Effective Risk Management and Control (January 2013), available at link.

[38] The Federal Reserve describes supervision as follows: "Once the rules and regulations are established, supervision—which involves monitoring, inspecting, and examining financial institutions—seeks to ensure that an institution complies with those rules and regulations, and that it operates in a safe and sound manner." Board of Governors of the Federal Reserve System, The Federal Reserve System: Purposes & Functions, at 73 (10th ed., Oct. 2016), available at link. Until recently, however, the OCC included the promulgation of regulations in its concept of supervision. The OCC's 2017 annual report, for example, listed the power to issue regulations as one of its supervisory powers, but that was removed from the 2018 report. *Compare* Office of the Comptroller of the Currency, 2017 Annual Report, at 2, available at link, *with* Office of the Comptroller of the Currency, 2018 Annual Report, at 1, available at link. The FDIC's 2018 annual report does not explicitly distinguish between supervision and regulation under its "Supervision" section. Federal Deposit Insurance Corporation, 2018 Annual Report, at 14–20, available at link. Moreover, it contains a section titled "Supervision Policy" that groups together discussions of supervision programs, rulemaking and supervisory guidance. *Id.* at 20–26.

supervision is almost non-existent and hard to do given that what is happening is kept confidential. Congressional oversight is also made more difficult.

The bias, for important policy choices affecting economic and social conditions, should be toward the rule of law and transparency. The realm of lore or secret constraints on banking organizations should be narrowed to a core minimum of what is necessary to preserve financial stability or the safety and soundness of any one banking organization. Part of the challenge is that, a decade ago, the supervisory staff, like the rest of us, lived through the Financial Crisis and its aftermath on the economy. When the fire is raging, the firefighters appropriately use whatever tools are handy, whether it is by the stretching of legal texts or the need for tough supervisory actions. But, long after the fire, when the house has been rebuilt on a better foundation, it is time to leave behind the emergency culture of firefighting and think in terms of regular maintenance.

As those within banking organizations will know, it is only possible, because of the constraints of confidential supervisory information, to speak about those examples that have randomly become public. Those who are at banking organizations or the regulators will know that there are many additional examples. This informal nonpublic shadow system of regulation is neither transparent nor accountable.

For example, what became the leveraged lending guidelines, which are meant to guard against the next asset bubble, started in the bank examination. They were originally sent to banks as confidential letters, and banks were not permitted to disclose to their clients such letters' existence, or the reasons why banks were not making certain loans. From the perspective of the banking regulators, the leveraged lending guidelines were an advancement in transparency and disclosure. They were, after all, public and had been subject to notice and comment. From the perspective of those who have been thinking deeply about the administrative law and its march towards transparency and accountability, they did not go far enough. Similarly, there have been attempts to take legal interpretations on the Volcker Rule in the context of bank examinations.

As one more significant example of important policy being made in the shadows, the Federal Reserve's lore on what constitutes a "controlling influence" and the so-called "tear-down rules" were mostly secret for a long time. These are not "rules" at all, but a series of oral principles, not made public nor written down, but which reflect the views of some legal staff at a moment in time. In a welcome development, the Federal Reserve last week announced a move from the "Delphic and hermetic process" for ordaining control to notice and comment rulemaking.[39] In announcing the proposed rulemaking, Vice Chair for Supervision Quarles acknowledged that divining whether the Board will find control under the existing framework requires "supplication to a small handful of people who have spent a long apprenticeship in the subtle hermeneutics of Federal Reserve lore, receiving the wisdom of their elders through oral tradition in the way that gnostic secrets are transmitted from shaman to novice in the culture of some tribes of the Orinoco."[40] As the Vice Chair for Supervision implies with his colorful metaphor, the oral tradition from shaman to novice is not good governance.

Another example arises because of the ability of the Federal Reserve to impose limitations on the conduct and activities of a financial holding company. To qualify as a financial holding company, an institution and all of its insured depository institution's subsidiaries must be both "well managed" and "well capitalized." Under Section 4(m) of the Bank Holding Company Act, the Federal Reserve may impose

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[39] Board of Governors of the Federal Reserve System, Federal Reserve Board Invites Public Comment on Proposal to Simplify and Increase the Transparency of Rules for Determining Control of a Banking Organization, Press Release (Apr. 23, 2019), link (statement of Vice Chair for Supervision Quarles).
[40] Board of Governors of the Federal Reserve System, Transcript Open Board Meeting on April 23, 2019, at 2–3, available at link.

limitations on the conduct and activities of a financial holding company that fails to satisfy either condition, and the financial holding company is required to enter into a 4(m) agreement to comply with those limitations. Because the Federal Reserve treats the failure to be well managed as confidential supervisory information, the existence and scope of 4(m) limitations are confidential if based on the failure to satisfy the well managed condition. One study, which examined the securities disclosures of 60 financial holding companies (FHCs) between the years 2005 and 2017, noted that nearly all FHCs disclose that they are well capitalized but many do not disclose if they are well managed.[41]

Another example has come about due to the informal "penalty box" rules of thumb that the banking supervisors have applied to banking organizations as a result of CAMELS ratings, especially as to Management ratings, BSA/AML compliance reviews and consumer compliance reviews. Tacit principles in the evaluation of management include the fact that any compliance problem resulting in an enforcement action will result in a downgrade of the Management rating and that it is often hard for a bank to obtain a Composite rating better than "3" if it has a Management rating of "3".[42] Bank expansion is not possible as long as a consent order is pending, meaning banks of all sizes devote board and management time as well as technology resources toward even the most immaterial compliance concerns to ensure regulators are fully satisfied.[43] Appeals against adverse ratings are rare because appeals must be made to the same agency that issued the rating—part of evaluation is the readiness with which management responds to regulator criticisms, and banks are warned that "examiners have long memories."[44]

The evolution of the living wills guidance is also instructive. Resolution plans and their guidance started out as largely confidential, then morphed into a mix of confidential and public feedback—all of which applied—and finally, over the years, regulators nudged toward public guidance. The first set of public guidance was issued without advance warning or notice and comment and stated that all previous guidance, public and private continued to apply. For those working on living wills, figuring out which parts of which years' private guidance no longer applied—because it was not aligned with the public guidance—was a puzzle. More recently, and in a welcome move, the Federal Reserve and the FDIC have issued new guidance, subject to notice and comment, that makes it clear that all previous guidance has now been superseded. The point here is that banking organizations were subject to a mix of private and public expectations, many of which were not clearly aligned and all of which were perceived as binding.

The long tradition of regulation by negotiation in the applications process is another type of shadow regulatory system.[45] Conditions, sometimes not linked to the pending application, are imposed. Regulators strategically use delays and silence to encourage silent, nonpublic withdrawals of applications. Some have called this regulation by negotiation but it is more akin to regulation by threat or intimidation.[46] An illustrative example, which can be used because it is one of the few to become public, comes from applications by Citicorp, J.P. Morgan, and Bankers Trust New York Corporation in 1987 to

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[41] Ethics Metrics, Analysis of Bank Holding Company Disclosures, comments submitted May 8, 2017 to the SEC on its Industry Guide 3, Statistical Disclosure by Bank Holding Companies, 8, link.

[42] *See* Examination of the Federal Financial Regulatory System and Opportunities for Reform: Hearing Before the U.S. H. Financial Services Subcomm. on Financial Institutions and Consumer Credit, 115th Cong. 10 (2017) (statement of Greg Baer, President, The Clearing House Association), available at link.

[43] *See id.* at 11.

[44] *See id.* at 12.

[45] *See* Culp Davis, Administrative Procedure in the Regulation of Banking, *supra* note 35, at 713 (arguing the OCC practice of making decisions regarding charter applications without providing reasoned opinions or findings of fact lends itself toward arbitrariness).

[46] Daniel Schwarz & David T. Zaring, Regulation by Threat: Dodd-Frank and the Non-Bank Problem, 84 U. CHIC. L. REV. 1813, 1817 (2017).

underwrite and deal in municipal revenue bonds, mortgage related securities and commercial paper.[47] During negotiations with agency staff, each applicant "voluntarily" consented to market share limitations while protesting that they saw no need for them. When considered for review by the Federal Reserve Board of Governors, the banks admitted that they agreed to the limitations only to "expedite the applications."[48] In this instance, the market share limitations were ultimately overturned by the Second Circuit but normally such "voluntary" commitments do not come up in final orders and are unlikely to be challenged in court or known to the public.[49] As a result, the staff conducting negotiations during the application process wield an immense policymaking power.

Many have debated whether confidential supervision and its secret lore are binding upon banking organizations. The recent "guidance on guidance" from the banking regulators seeks to settle that debate by stating that guidance is not binding unless it impacts safety and soundness. In a world where the supervisor can punish the banking organization and mold its behavior through these tools, from the perspective of those who receive it, the secret guidance and lore may as well be binding. Of course, banking organizations frequently seek and are happy to receive nonpublic guidance, on a written or oral basis, from the supervisory staff. The point is not to eliminate these communications but to put more guardrails around them, as the guidance on guidance begins to do.

D. Uneasy Truce is Now Untenable—Tilt Towards Accountability and Transparency

The uneasy truce between the tradition of secrecy and the tradition of accountability has become untenable. The signal that the balance is askew is the increase in leaks of confidential supervisory information. By my count, there have been 7 leaks of confidential supervisory information that have made their way into the media since 2011, some but not all of which can be traced to regulators. In addition, in 2016 one judge released the CAMELS ratings of a bank[50] and, near the time of the Financial Crisis, two exam reports were released by the Financial Crisis Inquiry Commission. Before 2011, leaks of confidential supervisory information into the public square were virtually unknown. So far, each of these releases has been treated as a one-off situation. It is time to consider, however, whether they are a signal of the pressures felt by humans living in a digital society where there is a strong tilt towards transparency.

There is also an increase in the officially sanctioned publication of confidential supervisory information by the banking supervisors themselves. Confidential supervisory information belongs to the supervisors who can choose, when they so desire, to disclose it. Although the Comptroller has not used his power to disclose examination results to the public, that power exists. The New York Department of Financial Services in 2017 used its power to release information in the public interest to release its otherwise confidential ratings of Bank of Tokyo-Mitsubishi as part of its ongoing spat with the bank and the Comptroller over who should be the primary regulator of the bank's New York branch.[51] The decision about what is in the public interest and its timing is entirely in the hands of the supervisors.

Banking organizations, however, are silenced in the public arena when the media or Congress make statements that might otherwise be corrected but for the rebuttal being considered confidential

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[47] *See* Alfred C. Aman Jr., Bargaining for Justice: An Examination of the Use and Limits of Conditions by the Federal Reserve Board, 74 IOWA L. REV. 837, 894–95 (1989).
[48] *See id.* at 895.
[49] *See id.*
[50] *See* Memorandum Opinion and Order, *Builders Bank v. FDIC.*, No. 15-cv-06033 (N.D. Ill Apr. 25, 2016), ECF No. 26.
[51] Letter from Shirin Emami, Executive Deputy Superintendent-Banking, N.Y. State Dept. of Fin. Servs., to Marva V. Cummings, Director for District Licensing, OCC (Nov. 13, 2017), available at link.

supervisory information, even when that information has been made public by the regulatory staff. As one example of the potential chilling effect, the OCC issued a bulletin reminding banking organizations of their confidentiality responsibilities and potential criminal liability just 2 weeks before the CEOs of the nation's largest banks were scheduled to testify before the House Financial Services Committee.[52]

E. What Policy Purpose is Served by Confidential Supervision and Discretionary Actions?

The question then becomes how to improve the existing situation by narrowing the scope of confidential supervisory information. Following in the footsteps of Minsky, we should aim for better, not perfect. We are moving into an era where policy making will increasingly be driven by data analytics and evidence in a technological environment. Going forward, three key questions ought to be asked about confidential supervision. Each one of these questions would involve a new way of thinking.

1. ***Why is this topic being treated confidentially?*** Banking regulators and banking organization should begin to ask themselves why a given topic is being treated as confidential. There should be a tight link to financial stability and the need for candid conversations. There should be a serious re-examination, from first principles, of how the obligations of the securities laws and confidential supervision interact. It is fair to ask why shouldn't banks have the option to make their CAMELS ratings public. After all, since 1990, the results of CRA examinations have been made public.[53] Or, one could ask why the banking regulators don't publish examination findings and trends in matters requiring attention in anonymous aggregate but with granular detail.[54] One thing is certain, however, and that is that any reform of the confidential supervisory information regulations and culture needs to be done on a *systemic* basis that applies equally to all banking organizations. Right now, the practical reality is one where some institutions sometimes are subject to random leaks or disclosures and others are not. There is a deep unfairness in that situation.

2. ***Who or what is being protected by the confidentiality?*** Sometimes confidentiality shields the supervisors' actions from the public scrutiny. How is it that the confidential "penalty box" constraints on a banking organization's activities can exist for years?[55] Do CAMELS ratings really judge individual institutions or do they follow the trends of the business cycle? On what basis are matters requiring attention and matters requiring immediate attention issued and what patterns exist in them? Some of these examples are areas where the supervisor fears that its actions would be controversial to the public and so a confidential route is chosen, or sometimes the confidential route is traveled just because it is familiar and is done without much forethought. If confidentiality is chosen to protect the regulator from public scrutiny, it is not appropriate. If, however, it is chosen for financial stability, then it is appropriate.

3. ***Why is this policy choice or regulatory interpretation being made under the confidential rule of discretion rather than the rule of law?*** Why did the leveraged lending guidelines start as confidential letters? What is one to make, for example, of Henry Paulson admitting that he privately threatened to remove the management and board of Bank of America if it did not complete a merger with Merrill Lynch? He has since stated "[b]y referring to the Federal Reserve's supervisory powers, I intended to

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[52] *See* OCC, Bulletin 2019-15: Statement on Confidentiality (Mar. 25, 2019), available at link; United States House Committee on Financial Services, Hearing: Holding Megabanks Accountable: A Review of Global Systemically Important Banks 10 years after the Financial Crisis (Apr. 10, 2019), available at link.
[53] *See* FFIEC Interagency CRA Rating File Specifications, Community Reinvestment Act, FFIEC, link (last visited Apr. 22, 2018).
[54] The Federal Reserve's recent Supervision and Regulation Report is an excellent start. Board of Governors of the Federal Reserve System, Supervision and Regulation Report (Nov. 2018), available at link.
[55] Transcript of Q&A with Federal Reserve's Randal Quarles, WSJ (Nov. 7, 2017), available at link (statement by Greg Baer) [hereinafter Quarles Transcript].

deliver a strong message."[56] This message was not disclosed at the time. The penalty box, and many nonpublic examples involve similar threats of confidential supervisory actions.[57] The increasing number of banks requesting to strengthen their ability to appeal examination results reflects the sense that confidential supervision can look like a weapon when it is shrouded in secrecy.[58] On what basis can new standards be imposed upon banking organizations through horizontal reviews by supervisors that are not made transparent to the organizations or the public?

We have recently seen helpful steps in the right direction toward transparency and accountability. Vice Chair for Supervision Quarles has stated that increases in transparency and a re-think of supervision are high on his agenda, noting that "one of the reasons for transparency . . . is just a basic view of the right relationship between the government and the governed . . . I do think we can be much more transparent about the regulatory process generally."[59] Chairman McWilliams has also focused on increased transparency with her Trust through Transparency initiative at the FDIC.

II. Training of Supervisory Staff in the Legal Framework of the Regulatory State

Congress and the banking agencies need to think clearly about how to create an environment where the supervisory staff are given the training, resources and tools that would permit them to do their jobs in a way that is more transparent to the world, more accountable and more consistent with the rule of law.[60] Given that the legal framework governing the banking sector has become much more complex, the work of the examination staff has become more legally infused and yet the supervisory culture has become increasingly unmoored from the legal framework itself.[61] The rise in compliance with law examinations, the focus on risk and board governance and the increasing use of matters requiring attention and matters requiring immediate attention for violations of law mean that the examination staff are increasingly making judgments that are legally infused, either involving legal judgments or involving a mixture of facts and law.

At the same time, the legal departments and legal staff of the federal banking agencies remain quite slim, especially as compared to other major agencies.[62] It is fair to ask whether there is a deep enough pool of lawyers at the agencies for the agency lawyers to be able to guide the supervisory staff on the more complex legal framework and to deal with all of the increased legally-infused work that is occurring.[63] It

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[56] Martin Kady II, Paulson Admits to Threatening Lewis, Politico (July 17, 2009), link.
[57] Quarles Transcript, *supra* note 55 (statement by Greg Baer).
[58] Julia Anderson Hill, When Bank Examiners Get It Wrong: Financial Institution Appeals of Material Supervisory Determinations, 92 WASH. U. L. REV. 1101, 1165–69 (2015).
[59] Quarles Transcript, *supra* note 55 (statement by Vice Chair for Supervision Randal Quarles).
[60] One important resource, beyond the scope of this testimony, is equipping the supervisors with more advanced technology, known as RegTech or SupTech. *See* Jo Ann Barefoot, Regulation Innovation: Using Digital Technology to Protect and Benefit Financial Consumers, Harvard Kennedy School Mossavar-Rahmani Center for Business and Government Working Paper Series No. 110, at 10–11 (Mar. 2019), available at link.
[61] Of course, major elements of bank supervision are related to credit, interest rate, liquidity and other market driven elements rather than the legal framework.
[62] *See* Rory Van Loo, *Regulatory Monitors: Policing Firms in the Compliance Era*, 119 COLUMBIA LAW REVIEW 369, 436–40 (2019)
[63] The banking agencies have long been understood to be monitor- or examiner-dominated in their personnel. Based on research by an academic, some of which is estimated, the Federal Reserve is 95% monitor staff, the OCC is 93% monitor staff and the FDIC is 86% monitor staff. *See id.* at 438-39. The higher proportion of lawyers at the FDIC is likely linked to its work as the deposit insurer and bank failures. Just a comparison of the number of lawyers to the number of examination staff at each of the agencies tells us that deep training on the law, legal interpretation and the legal framework has not been possible. A memo published by two former Federal Reserve staffers has pointed out that training on the legal framework has been delegated to the regional Federal Reserve Banks. Richard K. Kim, Patricia A. Robinson and Amanda K. Allexon, *Financial Institutions Developments: Revamping the Regulatory*

is also fair to ask whether the budget, resources and stature of the agency legal departments is sufficient for the increased legal complexity and the coming digital transformation. A study should be done on whether increases in the legal staff have kept pace with increases in supervisory staff and increases in legally infused work by the supervisory staff.[64]

Examples that I have seen in my practice, as well as examples that have been relayed to me, lead me to believe that the current generation of examination and supervisory staff, who are people of goodwill trying to do a complex job under difficult circumstances, have not had in-depth training in the legal framework. Some examiners were confused about the fact that the First Amendment protects lobbying activity by banking organizations, and attempting to stop such activity or subject it to an examination is unconstitutional.[65] There is confusion about the fact that the Constitution and statutes are higher level authorities than a regulation, guidance or handbook. Some supervisory staff mistakenly believe that guidance can override a statute. Some supervisory staff are confused about what is part of the legal framework and what is not. Some supervisory staff mistakenly believe that guidance is not governed by the statutes or regulations and that they can pick and choose among the applicable guidance or law. Some supervisory staff seek to exclude in-house lawyers from meetings or tasks.

I believe that the training of supervisory staff for compliance with law is heavily weighted towards the technical elements of individual banking regulations and guidance in areas of subject matter expertise. The training has been overfocused on compliance with the technical aspects on a regulation-by-regulation basis and has underweighted fundamental principles such as the rule of law in a Constitutional democracy and the legal framework that governs the regulatory state. The training has also not focused on basic grounding statutes such as the APA or the Congressional Review Act.[66] The supervisory staff are also not trained in major case law that affects their work. There is a large difference in what the supervisory staff believe to be their authority under safety and soundness and the case law that defines the term.

There is no need for three years of law school to understand these critical concepts. We also need not be purists worrying about the unauthorized practice of law. Instead, it should be possible, especially in light of the quality of the credentialed examination staff and the base of the past training, to add more of the following elements to the training of supervisory staff so that they are better able, in light of the shortage of lawyers at the agencies, to handle legally infused judgments:[67]

Examination Process, Wachtell, Lipton, Rosen & Katz (Nov. 26, 2018). That fact alone brings into question the consistency of the training.

[64] In the private sector it is well understood that increases in the budget, resources and staffing of the in-house legal department have not kept pace with the rise of risk management and the separation of compliance from the legal function. *See* Thomas C. Baxter, Jr., The Rise of Risk Management in Financial Institutions and a Potential Unintended Consequence—The Diminution of the Legal Function, American Bar Association Business Law Today (Apr. 2, 2019), link.

[65] *See* Semi-Annual Testimony on the Federal Reserve's Supervision and Regulation of the Financial System, 115 Cong. 86 (2018) (Statement of Randal K. Quarles, Vice Chairman for Supervision).

[66] It is safe to say that none of the banking regulators, and certainly not the banking bar, noticed or were aware of the passage of the Congressional Review Act in 1996. In hindsight, the GAO ruling that the leveraged lending guidelines are a "rule" under the APA is completely obvious. *See* 5 U.S.C. § 551(4) (defining "rule"). Thinking of guidance as requiring a stop at OMB or notice to Congress has thrown a wrench into the traditional cultural mode.

[67] I began my life in the law by taking, as is common in the Midwest, a six week paralegal certification. I can attest that if a 22 year old from a small town in Michigan could grasp the basics of these concepts in a paralegal certification course, then the much more highly educated and mature supervisory staff should be able to with ease.

- the principle of the separation of powers and how the delegation of authority by Congress to agencies is based solely on written statutory authority with their being no such thing as "inherent authority";[68]
- fundamental principles of due process, including the distinction between prospective and retroactive application of rules, regulations and other standards;
- the legal hierarchy among the Constitution, statutes, regulations and guidance, including the distinction between binding law and nonbinding written public guidance;
- the statutes, regulations, other laws and guidance that are binding on the supervisory staff;
- the key major cases that impact the work of supervisory staff;
- why reading the legal framework involves cannons of construction and deference, so that it is not like ordinary reading;[69] and
- why adhering to the rule of law and fundamental principles of due process is fundamental in a representative democracy and binding upon agency staff.

The lack of training about the legal framework, the principles of how legal texts must be interpreted, the binding nature of court decisions and the regulatory state has real world consequences. One real world consequence is the creation of matters requiring attention and matters requiring immediate attention, with all that implies, based on misunderstandings of the legal framework. Another consequence is the historical failure to keep track of appeals from examinations[70] or not being sensitive to the fact that some examination judgments or matters requiring attention are legally infused.[71] One clue that there is not enough sensitivity to the role of the rule of law is that risk governance guidance on the role of risk and compliance did not mention in-house legal departments at banking organizations.[72] Another clue is the three lines of defense ideology, developed post-Financial Crisis, which was drafted and adopted by the auditing profession without consideration of the role of the rule of law or the in-house legal function.[73]

Increased training in the hierarchy of the legal framework, why legal interpretation is not like normal reading and a wider understanding of the separation of powers and the regulatory state would, I believe, also have positive knock-on effects in the private sector. Many in the growing professions of risk management and compliance had their initial training in the banking agencies. They take their confusion about the legal framework, the role of guidance and the limits of secret lore with them to the private sector.

Conclusion

Change is hard but, the longstanding uneasy truce is now untenable. I suspect that both banking organizations and supervisors might be made a little uncomfortable by what I am saying here today. If,

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[68] The safety and soundness statute, 12 U.S.C. § 1831p-1, is broad and delegates discretion to the banking agencies. It is not, however, unlimited and does not create "inherent authority."

[69] *See* Margaret E. Tahyar, Legal Interpretation is Not Like Reading Poetry – How to Let Go of Ordinary Reading and Interpret the Legal Framework of the Regulatory State, at *9–11 (Dec. 4, 2018 Working Draft), available at link.

[70] *See* Hill, *supra* note 58, at 1115–60 (describing appeals process at OCC, Federal Reserve, FDIC and NCUA, and noting data issues).

[71] *See* Davis Polk & Wardwell LLP, Comment Letter on Proposed Amendments to Guidelines on an Internal Appeals Process for Institutions Wishing to Appeal an Adverse Material Supervisory Determination, Docket No. OP-1597, at 4–5 (Apr. 30, 2018), available at link.

[72] *See* Davis Polk & Wardwell LLP, Comment Letter on the Proposed Guidance on Supervisory Expectation for Boards of Directors, Docket No. OP-1570, at 9–11 (Feb. 15, 2018), available at link ("The Management Proposal is similarly silent on the importance of a firm having a sufficiently robust legal department with appropriate resources, budget and independence and a general counsel with sufficient stature and authority, instead addressing only risk management, internal audit and compliance functions.").

[73] *See generally* The Institute of Internal Auditors, *supra* note 37.

however, the changes I recommend are made, and if both supervisors and banking organizations are a little bit uncomfortable, the balance is moving in the right direction.