

## The Importance of Bankers on the Richmond Fed's Board

Like many organizations, the Richmond Fed has a board of directors. Actually, we have three: one for the Bank as a whole and one for each of our branch offices in Baltimore and Charlotte. Historically, the directors of those boards have come from a wide range of backgrounds, including businesses representing sectors across the economy, nonprofit groups, labor organizations, and academia. Among the directors on our Bank-wide board, almost invariably, are three chief executives of Fifth District banks. Why do we, an institution responsible for regulating banks, have bankers on our board?

This question has both a short answer and a somewhat longer answer. The short answer is that federal law dictates that six board members of every Federal Reserve Bank are elected by its member banks. Of these six, three are commonly bankers, while three must be non-bankers. These directors are known as “class A” and “class B” directors, respectively. For voting purposes, the banks in the District are classified according to their amount of capital into categories of small, medium, and large; banks in each category elect one class A director and one class B director. The other three directors, known as “class C,” are appointed by the Fed's Board of Governors. (Still another set of legal rules determines the selection of the boards of directors for our Baltimore and Charlotte branches.)

But why does the law provide for bankers potentially to make up a third of a Federal Reserve Bank's board? That's where the longer answer comes in.

Directors play two roles in the life of a Federal Reserve Bank. First, the board carries out the classic corporate governance function, overseeing the Bank's operations, budgets, and strategic direction. It manages the Bank's internal audit program. It appoints the Bank's president and first vice president, subject to the approval of the Board of Governors. For these roles, because some of our operations (particularly in the payments area) resemble the operations of private-sector banks, directors from the banking sector bring helpful and unique expertise to our board.

Second, the directors of a Federal Reserve Bank assist the Bank in its function of funneling economic information about the region into national policymaking. At the Richmond Fed, the observations of our directors, together with data from our Research Department's detailed surveys of business activity, provide us with a snapshot of the economic conditions in the diverse communities around our District. Like other Federal Reserve Bank presidents, I use this information in combination with research on important policy issues affecting the macro-economy to inform the perspectives that I bring to meetings of the Federal Open Market Committee. All of our directors — from the banking, non-banking, and nonprofit sectors —

provide valuable and complementary points of view in this regard. Yet if I were to go to a midsized city in our District and look for an individual who knows as much as possible about the area's economy, there's a good chance that person would be a banker, since bankers tend to have exposure to a diverse range of economic sectors.



How, then, do we avoid the conflicts of interest that could occur from having leaders of regulated companies on our board? Our governance structure is carefully designed to involve board members only in functions in which it is appropriate for them to be involved. Class A directors — the category that may include bankers — do not participate in the appointment of the Bank's president and first vice president, or in the appointment or compensation of any Bank officers whose primary duties involve bank supervision. No board members take part in making supervisory policy, which is determined by the Fed's Board of Governors. Nor are board members permitted to become involved in the consideration of any supervisory matters or to receive confidential information about supervisory matters. These federal laws are, of course, treated seriously by all of us — Federal Reserve Bank leaders, directors, and supervisory staff.

In my experience, the rules laid down by Congress on the composition of Federal Reserve Bank boards and their powers have benefited the public by bringing the views of longtime bankers to the boards' deliberations, while ensuring that supervisory actions such as bank examination ratings and assessments of applications are free of improper influence. And we at the Richmond Fed are mindful that the integrity of our processes — both in reputation and in reality — is essential to protecting the stability of and the public's confidence in the U.S. financial system. **RF**

A handwritten signature in black ink, appearing to read "Jeffrey M. Lacker". The signature is fluid and cursive, with a large initial "J" and "L".

JEFFREY M. LACKER  
PRESIDENT  
FEDERAL RESERVE BANK OF RICHMOND