

## GAO governance audit

The Board of Governors, the Reserve Banks and the Federal Reserve System as a whole are subject to several levels of audit and review. The GAO is one of the entities that review Federal Reserve activities. In 2010, the Dodd Frank Act required the GAO to complete a specific audit of Federal Reserve governance. The Act required the GAO to examine the following:

- The extent to which the current system of appointing Reserve Bank directors effectively represents the public without discrimination and with due consideration to the interests of agriculture, commerce, industry, services, labor and consumers as required by the Federal Reserve Act.
- Whether there are actual or potential conflicts of interest created when the Reserve Bank directors are elected by member banks.
- Whether there are any changes to the director selection process or other aspects of Reserve Bank governance that would improve how the public is represented, eliminate actual or potential conflicts of interest in bank supervision, increase the availability of information useful for the formulation and execution of monetary policy or increase the effectiveness or efficiency of Reserve Banks.

The GAO audit started after the passage of Dodd Frank and ended with the issuance of a final report on October 19, 2011. In conducting the audit, the GAO reviewed the Reserve Banks' bylaws and board of directors meeting minutes. GAO staff interviewed Reserve Bank directors and staff from both the Board of Governors and the Reserve Banks and conducted a survey of directors who served in 2010. The GAO did not limit its review to just Federal Reserve governance documents but also reviewed governance documents at comparable institutions.

## GAO audit report

The Reserve Banks and the Board of Governors were given the opportunity to respond to the GAO report. In Chairman Bernanke's response, he noted that the report: (i) recognized that the Reserve Bank directors provide a unique and valuable perspective on the economic and business environment in each local region which is factored into the development of monetary policy; (ii) confirmed that the Board and Reserve Banks have in place a number of policies and procedures to address both potential and perceived conflicts of interest associated with a governance structure that includes bankers on the Reserve Bank boards. In particular, the Board and the Reserve Banks have adopted policies and procedures that prevent directors from being involved in supervisory matters, including examinations, supervisory ratings, applications for System approval of transaction, or development and implementation of supervisory policy, and from being involved in discount window lending decisions or decisions regarding emergency lending facilities; (iii) found that there was no special treatment of firms with director representation in any discount window lending decision or decision regarding the emergency lending facilities established by the Federal Reserve during the financial crisis; and (iv) found no instance where a Reserve Bank director was involved in any supervisory matter involving an institution with which the director was affiliated.

## GAO recommendations

At the end of the report, the GAO made the four following recommendations:

1. To help enhance economic and demographic diversity and broaden perspectives among Reserve Bank directors who are elected to represent the public, consider ways to broaden the pools of potential candidates for directors, such as including officers who are below the senior executive level at their organizations.
2. To further promote transparency, clearly document the roles and responsibilities of the directors, including restrictions on their involvement in supervision and regulation activities, in the Banks' bylaws.
3. As part of the Federal Reserve System's continued focus on strengthening governance practices, develop, document, and adopt a process for requesting waivers from the Federal Reserve Board director eligibility policy and ethics policy for directors. Further, consider publicly disclosing waivers that are granted to the extent disclosure would not violate a director's personal privacy.
4. To enhance the transparency of Reserve Bank board governance, make key governance documents, such as such as board of director bylaws, committee charters and membership, and the Federal Reserve Board director eligibility policy and ethics policy, available on the Banks' websites or otherwise easily accessible to the public.

The Federal Reserve Bank of Chicago has already begun work on implementing the GAO's recommendations. Diversity has been and continues to be supported by the Bank's director-selection process. We will continue to look for ways to broaden our pool of director candidates and seek candidates who represent diverse perspectives. We will review our bylaws and make sure the roles and responsibilities of our directors are clearly spelled out including the restrictions on their involvement in supervision and regulation matters. The Board has established a process governing waiver requests by Reserve Banks to the eligibility policy and is considering adopting a process for waivers to the Guide to Conduct as well. While the Bank rarely, if ever, requests waivers, we will certainly comply with the Board's processes. To further increase transparency, our governance documents such as the bylaws and more detailed information about the board of directors and its committees are available on the Bank's public [website](#).

For more information about the GAO governance audit, please see the Federal Reserve Board's [website](#).