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Prohibition on Use of Reputation Risk by Regulators: Notice of Proposed Rulemaking

To

Chief Executive Officers of All National Banks, Federal Savings Associations, and Federal Branches and Agencies; Department and Division Heads; All Examining Personnel; and Other Interested Parties

Summary

The Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC) are issuing a notice of proposed rulemaking to codify the elimination of reputation risk from their supervisory programs. Among other things, the proposed rule would prohibit the agencies from criticizing or taking adverse action against an institution on the basis of reputation risk. The proposed rule would also prohibit the agencies from requiring, instructing, or encouraging an institution to close an account, to refrain from providing an account, product, or service, or to modify or terminate any product or service on the basis of a person's or entity's political, social, cultural, or religious views or beliefs, constitutionally protected speech, or solely on the basis of politically disfavored but lawful business activities perceived to present reputation risk.

Comments on all aspects of the proposed rule are due 60 days after it is published in the *Federal Register*.

Note for Community Banks

The proposed rule would apply to community banks.

Highlights

- The agencies have removed reputation risk from their supervisory frameworks and are proposing regulations to codify this change.
- The proposed rule would prohibit the agencies from criticizing, formally or informally, or taking adverse action against an institution on the basis of reputation risk.

Background and Overview of Proposal

- Banking regulators' use of the concept of reputation risk as a basis for supervisory criticisms increases subjectivity in banking supervision without adding material value from a safety and soundness perspective. The agencies have not clearly explained how banks should measure the reputation risk from different activities, business partners, or clients. Different stakeholders may have different perspectives on how activities or relationships impact an institution's reputation. In addition, focusing on reputation risk can distract institutions and the agencies from devoting resources to managing core financial risks.
- The proposed rule would define "reputation risk" as the risk, regardless of how the risk is labeled by the institution or by the agencies, that an action or activity, or combination of

actions or activities, or lack of actions or activities, of an institution could negatively impact public perception of the institution for reasons unrelated to the current or future financial condition of the institution.

- Under the proposal, the agencies would be prohibited from requiring, instructing, or encouraging an institution or its employees to refrain from contracting with or to terminate or modify a contract with a third party, including an institution-affiliated party, on the basis of reputation risk.
- Under the proposal, the agencies also could not require, instruct, or encourage an institution or its employees to refrain from doing business with or to terminate or modify a business relationship with a third party, including an institution-affiliated party, on the basis of reputation risk.
- The proposed rule would also prevent the agencies from requiring, instructing, or encouraging an institution to enter into a contract or business relationship with a third party on the basis of reputation risk.
- The proposed rule would further prohibit the agencies from requiring, instructing, or encouraging an institution or an employee of an institution to terminate a contract with, discontinue doing business with, or modify the terms under which it will do business with a person or entity on the basis

of the person's or entity's political, social, cultural, or religious views or beliefs, constitutionally protected speech, or solely on the basis of the third party's involvement in politically disfavored but lawful business activities perceived to present reputation risk.

- The proposed rule would also make conforming amendments to OCC and FDIC regulations, including part 1 and part 30 of OCC regulations, to eliminate references to reputation risk.

Further Information

Please contact Joanne Phillips, Counsel; or Collin Berger, Attorney, Chief Counsel's Office, at 202-649-5490.

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Related Link

- Prohibition on Use of Reputation Risk by Regulators (PDF)

Topic(s): CORPORATE & RISK GOVERNANCE (CARG) LAWS & REGULATIONS OCC REGULATIONS

- RISK-BASED SUPERVISION