Reserve Bank Governance Over Shared Activities

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Annual Meeting
Reserve Bank Audit Committee Chairs
Conference of General Auditors
January 11, 2005

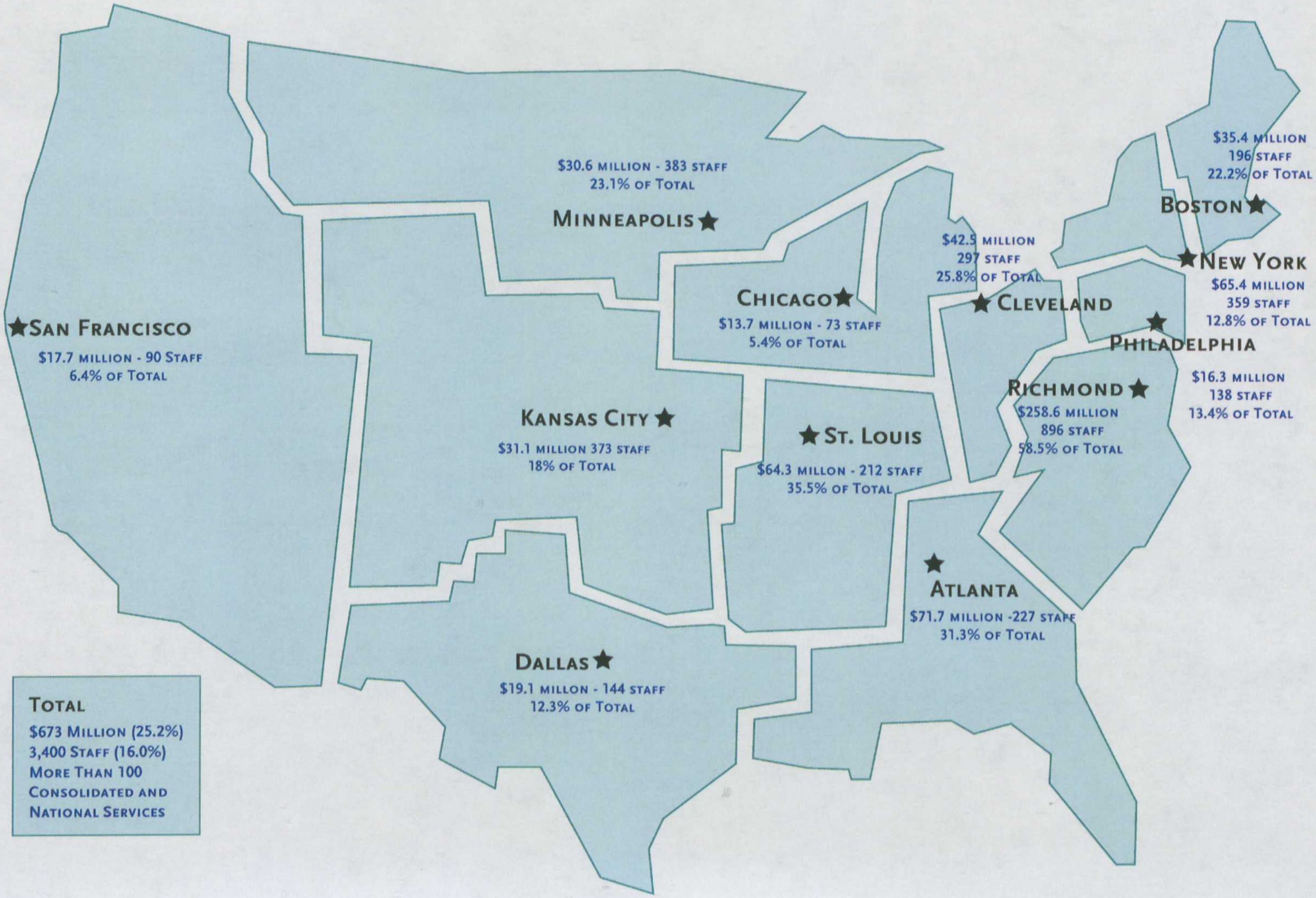
Agenda

- Background
- Governance Model
- Governance Responsibilities
- Governance Processes
- Role of Reserve Bank Audit Committees
- Questions

Background

- Every District involved in shared activities
- Impact ranges from 6% to nearly 60% of costs
- Effect is two-way
  - Districts perform services for others
  - Districts receive services

Current Consolidation Realities



Total

$673 Million (25.2%)
3,400 Staff (16.0%)
More Than 100
Consolidated and
National Services

Background

- What is the role of Presidents, directors in this process? How are decisions made? What management and governance models apply?
- Check Infrastructure Decisions in 2002/03
- Strategic Direction Project of the Conference of Presidents
  - Completed in 2004
  - Governance a key focus

Governance Model

- Reserve Banks are separate legal entities, but must work together
- Board of Governors provides oversight; Reserve Bank boards of directors have fiduciary duty
- Presidents are CEO's; by law and through delegation from their boards they can make vast majority of decisions related to Reserve Bank operations
- They can choose to make decisions regarding shared activities through the Conference of Presidents and its Committee structure; they have done so since at least 1936

Governance Model

- Exception: Decisions related to strategic direction or material matters must have explicit board of directors involvement and agreement
  - Strategic and material not explicitly defined; will vary
  - Boards can authorize President to vote, or can require him/her to come back for approval
  - "Opt-out" is possible, but not desirable; "Opt in" is best
  - All parties – Presidents, boards, Board of Governors - must work together
- Clear, timely communication is critical
  - From System entities to the Conference of Presidents when major matters being considered
  - Among Presidents
  - Between Presidents and their boards

Governance Responsibilities

- Presidents
  - Ensure boards are up-to-date on major System initiatives
  - Communicate early and often
  - Bring board concerns about any major matters to the Conference of Presidents
  - Reflect a duty of loyalty to the Bank while ensuring the public interest is served
  - Evaluate both what the Bank does for others and what others do for the Bank and discuss with board of directors as necessary

Governance Responsibilities

- Boards of Directors
  - Understand their responsibilities for strategic and material decisions
  - With the President, define "strategic" and "material" for the Bank
  - Receive and discuss communications from the President and from the Conference of Presidents about strategic and material items
  - Work with President to develop Bank's position on particular material and strategic matters, reflecting the Bank's own concerns and the public interest
  - Receive and discuss reports on services provided and received by the Bank
  - Work with the President and Bank management to resolve service or operational problems

Governance Processes

- Service Agreements
  - Will define both governance of and annual operational targets for shared activities
  - Will include provisions for timely communication of significant risk and control issues, as well as the annual assertion on the adequacy of financial reporting goals
  - Currently in draft form for the Wholesale Product Office, and in development for Retail, Cash and other offices as well as FRIT
- COP Guidelines
  - Will define decision-making process, i.e. what is a quorum, etc.
  - In draft form; will be discussed at COP meeting February 15-16

Governance Processes

- COP Communication
  - Board chairs will now receive COP agendas, statements of action, minutes
  - Have already received 2005 draft COP Objectives
  - More routine communication may be necessary
- Governance Review by Conference of Chairmen
  - Conference of Chairmen reviewed and accepted governance document in December 2004
  - Process is scheduled for discussion by the Chairmen in June; changes if any would be discussed in December

Role of the Audit Committee

- Audit Committees typically have close oversight of Bank operations
  - Internal audit reports
  - External auditor interaction
  - Whistle-blower procedures
- Governance processes will introduce formal service agreements

Role of the Audit Committee

- Should Audit Committees oversee performance under these agreements?
  - Primary oversight will be done by Bank management
  - There is overlap with existing Audit Committee work
  - Might be overload for the Audit Committee; involving another Committee or the full board could be useful
  - In the end, the President and the board should decide
    - Audit Committee role
    - New Committee; some examples here
    - Role of full board