

**FEDERAL RESERVE BANK
OF NEW YORK**

[Circular No. 10778]
April 26, 1995]

**GUIDELINES FOR APPEALING AN ADVERSE
MATERIAL SUPERVISORY DETERMINATION**

*To All Member Banks, Bank Holding Companies, and Branches and Agencies
of Foreign Banks in the Second Federal Reserve District, and Others Concerned:*

Following is the text of a statement issued by the Board of Governors of the Federal Reserve System:

The Federal Reserve Board has issued final guidelines on an internal appeals process for institutions wishing to appeal an adverse material supervisory determination.

The guidelines are effective immediately.

The Riegle Community Development and Regulatory Improvement Act of 1994 requires the Board (as well as other Federal banking agencies) to establish an independent, intra-agency appellate process, which will be available to review material supervisory determinations made at insured depository institutions, such as an adverse examination report.

Printed on the following pages is the text of the Board's official notice in this matter. Questions concerning these guidelines may be directed to Maureen F. LeBlanc, Supervising Examiner, Domestic Bank Examinations Department (Tel. No. 212-720-6712).

WILLIAM J. McDONOUGH,
President.

FEDERAL RESERVE SYSTEM

[Docket No. R-0867]

Internal Appeals Process**AGENCY:** Board of Governors of the Federal Reserve System.**ACTION:** Final guidelines.

SUMMARY: The Board is issuing its final guidelines on an internal appeals process for institutions wishing to appeal an adverse material supervisory determination.**EFFECTIVE DATE:** March 24, 1995.**FOR FURTHER INFORMATION CONTACT:**

Gregory A. Baer, Managing Senior Counsel, Legal Division (202/452-3236); Shawn McNulty, Assistant Director, Division of Consumer and Community Affairs (202/452-3946); or Ann Marie Kohlligian, Senior Counsel/Manager, Division of Banking Supervision and Regulation (202/452-3528), Board of Governors of the Federal Reserve System. For the hearing impaired only, Telecommunication Device for the Deaf (TDD), Dorothea Thompson (202/452-3544).

SUPPLEMENTARY INFORMATION:**Background**

Section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994 (the Act), 12 U.S.C. 4806, requires the Board (as well as the other Federal banking agencies) to establish an independent, intra-agency appellate process that is available to institutions to seek review of material supervisory determinations. Section 309 specifies various requirements that the appellate process must meet.

On December 29, 1994, the Board published for public comment its proposed guidelines that would implement the intra-agency appellant

process required by section 309 of the Act. (59 FR 67297 (December 29, 1994)). In general, the proposed guidelines required that: (1) All appeals be in writing and approved by the institution's board of directors; (2) all appeals be heard and decided within specified timeframes; (3) the initial appeal be heard by a person or persons selected by the Reserve Bank (the review panel) who had not participated in, or reported to the persons who made, the material supervisory determination under review; (4) an adverse decision by the review panel be appealable to a Reserve Bank President; (5) an adverse decision by a Reserve Bank President be appealable to the Board; and (6) Reserve Banks establish safeguards to protect institutions that file appeals from examiner retaliation.

Although section 309 requires the Board to develop an internal appeals process only for state member banks, the proposed guidelines expanded the process and made it available to all institutions that are subject to Federal Reserve oversight, including bank holding companies, U.S. agencies and branches of foreign banks and Edge corporations.¹ The proposed guidelines also defined a "material supervisory determination" to include all material matters relating to the examination or inspection process, but exclude those matters, such as the imposition of a prompt corrective action directive or a cease and desist order, for which an alternative, independent right of appeal exists.

As noted in the proposed guidelines, the Board continues to believe that questions about or objections to supervisory determinations made during the course of an inspection or examination are most effectively handled through the longstanding Federal Reserve practice of resolving any problems informally during the course of the inspection or examination process.

Public Comments

The Board received 27 comments on its proposed guidelines from Federal Reserve Banks, financial institutions, trade associations, law firms and a consulting firm. While the comments were generally supportive of the proposed guidelines, most comments submitted suggested changes or raised concerns regarding the implementation of the internal appeals process. These proposed changes and concerns, which

¹ The final guidelines have been modified to state explicitly that third party EDP servicers subject to examination by the Federal Reserve may appeal any material supervisory determination.

are discussed below, relate to five areas: (1) protection from examiner retaliation; (2) independence of the review panel; (3) who should decide the final appeal at the Board; (4) the need for additional, specific timeframes; and (5) procedural issues.

(1) Protection From Examiner Retaliation

Thirteen comments raised concerns about examiner retaliation. Several comments suggested that the Ombudsman, which the Board is required to establish under section 309 of the Act, should play a role in addressing this issue, such as serving as an independent contact for institutions that believe they have been subject to some form of retaliation or ensuring that different examiners conduct examinations that commence after an appeal has been filed. Some comments suggested that greater Board involvement in the appeals process would protect institutions against retaliation, while others suggested that the guidelines include specific sanctions and disciplinary actions for examiners found to have engaged in retaliation due to an appeal.

The Board acknowledges that some institutions may perceive that availing themselves of the appeals process may result in retaliatory action by examiners. As proposed, the guidelines require the Reserve Banks to establish safeguards to protect institutions that file appeals from retaliation. While the Board believes that this provides sufficient protection and meets the requirements of section 309, the Ombudsman is available to address such concerns and may be contacted by institutions who believe they may have suffered retaliation as a result of an appeal. The role of this official and his/her procedures for addressing these concerns will be outlined in the Board's Policy Statement for the Ombudsman.

(2) Independence of Review Panel

Six comments suggested modifications to the part of the guidelines that addressed the independence of the review panel. Several stated that the appeals process cannot be independent so long as it remains an internal procedure and suggested that outside parties, such as a peer review panel or a panel appointed by the Federal Financial Institutions Examination Council, hear and decide all appeals. Another comment suggested that the review panel exclude not only persons who participated in, or who directly or indirectly report to the person(s) who participated in, the material supervisory determination

under appeal, but anyone who directly or indirectly supervises the person(s) who made such determination.

Section 309 of the Act reflects a Congressional conclusion that an intra-agency appeals process will provide institutions with an adequate means to redress adverse material supervisory determinations. The Board does not believe that it is necessary to expand the guidelines beyond what is required by the statute. Similarly, section 309 requires that the person hearing the appeal not directly or indirectly report to the person who initially made the supervisory decision under review. Consequently, the composition of the review panel has not been modified in the final guidelines.

(3) Who Decides the Final Appeal at the Board

The proposed guidelines provided for an appeal of an adverse decision by a Reserve Bank President to the appropriate Board division director, who would consult with the appropriate Governor of the Board's oversight committee for that division. Three comments suggested that it would be more suitable for a Governor to review a decision by a Reserve Bank President. The final guidelines have been modified so that an appeal of a Reserve Bank President's decision will be to the Governor who serves as chairman of the appropriate oversight committee, who will consult with that division's director.

(4) Need for Additional Timeframes

The proposed guidelines required institutions to file an appeal within 30 days of the material supervisory determination and the review panel to decide the appeal within 30 days of its receipt. The proposed guidelines also required Reserve Bank Presidents to make a decision on any matter appealed to them within 30 days of receipt. Several comments noted that the proposed guidelines did not contain timeframes for other actions, such as the time in which an appeal should be filed with a Reserve Bank President or the Board, or the time in which the Board would make a decision on an appeal.

The Board agrees with these comments on the need for additional timeframes. Consequently, the final guidelines require that an appeal to a Reserve Bank President or the Board to be filed within 30 days of receipt of an adverse decision by the review panel or the Reserve Bank President, respectively. The final guidelines also require that the Board decide any appeal within 60 days of its receipt.

(5) Procedural Issues

Several comments suggested that the Board's guidelines include some additional procedures in order to ensure that the internal appeal process works smoothly. One comment suggested that the guidelines explicitly provide that the material supervisory determination remain in effect while it is under appeal, while another comment suggested that the determination be stayed pending the completion of the appeal. The Board believes that it is appropriate for the determination to remain in effect while it is under appeal, and the final guidelines have been modified to state this explicitly. The Board does not believe that section 309 of the Act is intended to stay the Board's supervisory decisions, but rather is designed to provide institutions with a procedure by which to voice objections to supervisory determinations for which no other formal appeals procedures exist.

Another comment suggested that institutions that consent to the issuance of a formal enforcement action, such as a cease and desist order, be allowed to use the internal appeals process to challenge the material supervisory determinations that led to the enforcement action. This suggestion seems inconsistent with the intent of section 309 of the Act, which is to provide an avenue for the review of material supervisory determinations and not to contest enforcement actions for which an alternative appeals mechanism exists. Therefore, the Board has not adopted this suggestion. Another comment suggested that the record be expunged of any material supervisory decisions that have been modified or overturned on appeal. The Board believes that it is appropriate to maintain all records of its supervisory actions, including those relating to a decision that is modified or overturned as a result of an internal appeal. Nonetheless, the Reserve Banks are expected to maintain complete records of any appeal, including updating all files, both hard copy and electronic, to reflect the results of all appeals.

One comment suggested that the board of directors of an institution only be required to approve the initiation of an appeal, but that management be allowed to decide on any subsequent appeals to a Reserve Bank President or the Board. Another comment noted that getting approval of the board of directors of a foreign bank would be extremely difficult in order for its U.S. agency or branch to file timely appeals. The Board continues to believe that the board of directors should be involved in

each step of the appeals process; therefore, the final guidelines still require board approval for each step in the appeals process. On the other hand, the final guidelines have been modified to allow the senior management person(s) with authority for U.S. operations of a foreign bank to approve appeals; however, he or she must approve each step of the appeal.

The Board has decided to adopt several other procedural suggestions. The final guidelines provide that any appeal filed must contain all of the facts and arguments that the institution would like to present to the review panel, the Reserve Bank President or the Board, as the case may be, and that the review panel, the Reserve Bank President or the Board may reject the appeal for lack of clarity or information. In such a case, an institution would have 30 days in which to refile a rejected appeal. Last, the final guidelines make explicit that the internal appeals process does not give the appealing institutions any discovery or other similar rights.

Guidelines for Appeals of Material Supervisory Determinations

Section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994, 12 U.S.C. 4806, requires the Board and the other Federal banking agencies to establish an independent, intra-agency process to review appeals of material supervisory determinations.

The purpose of these guidelines is to allow each Reserve Bank to administer its own appellate process, but to establish procedures under which all Reserve Banks' appellate process must operate. Doing so will ensure that each Reserve Bank's process is consistent with section 309 and that institutions will be granted the same appellant rights regardless of the Federal Reserve district in which they reside.

Procedures for Appealing a Material Supervisory Determination. Any appeal of a material supervisory determination pursuant to section 309 shall be filed and considered pursuant to the following procedures.

(1) Any appeal shall be approved by the board of directors of the institution, or in the case of a U.S. agency or branch of a foreign bank, the senior management person(s) responsible for the bank's U.S. operations, and filed in writing with the Secretary of the Reserve Bank or other appropriate Reserve Bank official within 30 calendar days of receipt of the written material supervisory determination, unless the time for filing is extended by the Reserve Bank. The Reserve Bank shall

promptly provide a copy of the appeal to the appropriate division director of the staff of the Board of Governors.

(2) Any appeal shall contain all the facts and arguments that the institution wishes to present. The appeal may be rejected for lack of clarity or information. In such case, the institution may refile the appeal within 30 calendar days of receipt of written notice of the rejection of any filing.

(3) The appeal shall be considered in the first instance by a person or persons selected by the Reserve Bank (the review panel) who—

(A) did not participate in the material supervisory determination;

(B) do not directly or indirectly report to the person who made the material supervisory determination under review; and

(C) are qualified to review the material supervisory determination.

(4) The appellant institution may appear before the review panel in order to present testimony and, with the consent of the review panel, witnesses. The review panel shall also solicit the views of the Reserve Bank staff involved in the determination under appeal, Board staff, and, where appropriate, the staff of other supervisory agencies (for example, in case of joint examinations or inspections). Nothing in this appeals process shall create any discovery or other such rights.

(5) Any appeal shall be decided, in writing, by the review panel within 30 calendar days of the filing of an informationally complete appeal, unless the appellant and the review panel jointly agree to extend the time for decision.

(6) Any appellant institution dissatisfied with the decision of the review panel may, with the consent of its board of directors of the institution, or in the case of a U.S. agency or branch of a foreign bank, the senior management person(s) responsible for the bank's U.S. operations, appeal that decision to the Reserve Bank President by filing a written appeal with the Secretary of the Reserve Bank or other appropriate Reserve Bank official within 30 calendar days of receipt of the review panel's written decision. The appeal shall contain all facts and arguments that the institution wishes to be considered. The appeal may be rejected for lack of clarity or information. In such case, the institution may refile the appeal within 30 calendar days of receipt of written notice of the rejection. The appeal shall be decided by the Reserve Bank President, in writing, within 30 calendar days of the filing of an informationally complete appeal.

(7) Any appellant institution dissatisfied with the decision of the Reserve Bank President may, with the consent of its board of directors of the institution, or in the case of a U.S. agency or branch of a foreign bank, the senior management person(s) responsible for the bank's U.S. operations, appeal that decision to the appropriate Governor by filing a written appeal with the Secretary of the Board within 30 calendar days of receipt of the Reserve Bank President's written decision. The appeal may be rejected for lack of clarity or information. In such case, the institution may refile the appeal within 30 calendar days of receipt of written notice of the rejection. The appeal shall be decided, in writing, by the appropriate Governor, who shall consult with the director of the appropriate division of the Board of Governors, within 60 calendar days of the filing of an informationally complete appeal.

Safeguards Against Retaliation. Each Reserve Bank shall establish appropriate safeguards to protect appellants from retaliation. The Board's Ombudsman will periodically contact institutions after their appeals have been decided in order to make certain that no retaliation has occurred. In addition, institutions who believe they have suffered retaliation as the result of an appeal may contact the Board's Ombudsman.

Availability of Procedures. Each Reserve Bank shall make these guidelines and the Reserve Bank's process for selecting a review panel available to each institution in its district, any institution appealing a material supervisory determination, and any member of the public who requests them.

Eligible Institutions. Any institution about which the Federal Reserve makes a material supervisory determination is eligible for the appeal process. This includes state member banks, bank holding companies and their nonbank subsidiaries, U.S. agencies and branches of foreign banks, Edge and agreement corporations, third party EDP servicers, and other entities examined or inspected by a Reserve Bank.

Material Supervisory Determination Defined. Whether an appealed action constitutes a "material supervisory determination" eligible for the appeals process shall be decided by the person or persons hearing the appeal, and a determination that the action is not appealable under these guidelines may be further appealed to the Reserve Bank President or the appropriate oversight Governor in the same manner as any other adverse decision.

The term "material supervisory determination" includes, but is not limited to, material determinations relating to examination or inspection composite ratings, the adequacy of loan loss reserves and significant loan classifications. The term does not include any supervisory determination for which an independent right of appeal exists. Such actions include prompt corrective action directives issued pursuant to section 38 of the Federal Deposit Insurance Act, as amended (the FDI Act), actions to impose administrative enforcement actions under the FDI Act and the Bank Holding Company Act of 1956, as amended (the BHC Act), capital directives, and orders issued pursuant to applications under the BHC Act.

Effect of Appeal on Material Supervisory Determinations. A material supervisory determination shall remain in effect while under appeal and until such time it is modified or overturned through the appeals process. The appeal of a material supervisory determination does not prevent the Federal Reserve from taking any supervisory or enforcement action—formal or informal—it deems appropriate to discharge the Federal Reserve's supervisory responsibilities.

Savings Provision. Section 309 expressly provides that it shall not affect the authority of the Board or any other agency to take enforcement or supervisory action against an institution. In such cases, the rights of appeal provided for in the statutes and regulations concerning these actions shall govern.

By order of the Board of Governors of the Federal Reserve System, March 24, 1995.

Jennifer J. Johnson,

Deputy Secretary of the Board.

[FR Doc. 95-7795 Filed 3-29-95; 8:45 am]

BILLING CODE 6210-01-P