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BEHIND CLOSED DOORS: THE USE OF 4(M) AGREEMENTS TO EFFECT FEDERAL RESERVE POLICY

In this article, the authors discuss the Federal Reserve's role in supervision and enforcement, give a brief history of financial holding company activities, and describe the post-crisis regulatory response. They then highlight the use by the Federal Reserve of confidential section 4(m) agreements as a "shadow" policy tool to reign in activities it deems to be risky. They close by noting a recent speech by Vice-Chair Quarles proposing specific reforms to increase transparency of the bank supervisory process.

By Douglas Landy and James Kong *

In the years following the 2008 financial crisis, U.S. bank holding companies ("BHCs") and financial holding companies ("FHCs") have adjusted to a new normal: a cornucopia of new regulations, a renewed emphasis on oversight and supervision by prudential regulators, and a string of headline-grabbing enforcement actions. However, the breadth of the prudential regulators' supervisory and enforcement powers, as well as the confidential nature of bank supervision, mean that public enforcement actions are often only the last, and most visible, measure in a regulator's toolbox. Much of a regulator's supervisory and enforcement activity occurs behind the scenes, whether in the form of orally communicated concerns, examination reports, confidential interpretive letters, or informal enforcement actions (such as "Matters Requiring Attention" or "MRA" letters), to name a few.

In this article, we highlight one of the most impactful supervisory tools that the Board of Governors of the Federal Reserve System has wielded in recent years – agreements made under section 4(m) of the Bank Holding Company Act of 1956, (the "BHC Act").[1] These agreements (commonly known as "4(m) agreements"), are considered "confidential supervisory information" ("CSI") and may not be publicly disclosed by the subject institution.[2] At the same time, however,

[1] The BHC Act is found at 12 U.S.C. § 1841 *et seq*. Section 4(m) of the BHC Act is found at 12 U.S.C. § 1843(m).

[2] 12 C.F.R. § 261.22. In general, CSI is broadly defined and encompasses, with respect to a prudential regulator, information that is prepared by, on behalf of, or for the use of that regulator. CSI with respect to any regulator is the property of that regulator, and may only be disclosed in accordance with applicable laws and regulation. In July 2019, the Federal Reserve issued a proposed rule that would make a number of changes to the regulations governing CSI. Among the proposed changes include those that would allow financial institutions to more freely share CSI with its affiliates, other supervisory authorities, and auditors and outside legal counsel. *See* Board of Governors of the Federal Reserve System, *Rules Regarding Availability of Information*, 84 Fed. Reg. 27296 (June 17, 2019).
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