



INSTITUTE OF INTERNATIONAL BANKERS

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Jennifer J. Johnson
Secretary, Board of Governors of the
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Washington, D.C. 20551
regs.comments@federalreserve.gov

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, D.C. 20219
regs.comments@ooc.treas.gov

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429
comments@FDIC.gov

Re: Proposed Joint Guidance on Stress Testing for Banking Organizations with More Than \$10 Billion in Total Consolidated Assets (Board Docket No. OP-1421; OCC Docket No. 2011-0011)

Ladies and Gentlemen:

The Institute of International Bankers (“IIB”) appreciates the opportunity to comment on the above-referenced proposed joint guidance on stress testing (the “Proposed Guidance”).¹ A substantial portion of IIB member banks conduct banking operations in the United States through “Banking Organizations” that have total consolidated assets in excess of \$10 billion and therefore would be covered by the Proposed Guidance. These U.S. operations consist of FDIC-insured bank subsidiaries, U.S. bank holding company subsidiaries and federally- and state-licensed branches and agencies.

Stress testing is an integral component of effective risk management. We applaud the Agencies for undertaking to develop supervisory guidance that is consistent with the Basel

¹ 76 Fed. Reg. 35072. Capitalized terms used in this letter that are not otherwise defined in this letter have the meanings given in the Proposed Guidance.



Committee’s “Principles for Sound Stress Testing Practices and Supervision” and that builds upon the consideration of the uses and merits of stress testing in prior guidance issued by the Agencies in specific contexts, including funding and liquidity risk management, interest rate risk and commercial real estate concentration risk. In setting forth a broad, principles-based stress testing framework, the Proposed Guidance provides a useful means to strengthen Banking Organizations’ efforts in this critical area.

The IIB and its members support the principles-based approach adopted by the Agencies in the Proposed Guidance. The Proposed Guidance rightly adopts as its leading principle recognition that each Banking Organization’s stress testing framework must be adapted to the particular characteristics of its structure, activities, risks and exposures. In addition, the Proposed Guidance describes several stress testing approaches and applications while avoiding rigid prescription. We also agree that stress testing should be forward-looking and flexible and should be conducted so as to produce clear, actionable² and well supported results that facilitate informed analysis and decision-making related to a Banking Organization’s business strategies, limits, risk profile, and other aspects of risk management, all in a manner that is consistent with the organization’s risk appetite.

The Proposed Guidance does not explicitly address the stress testing requirements imposed upon certain companies by Section 165(i) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, but the Agencies have explained that they expect to implement those provisions in a manner that would be consistent with the Proposed Guidance.³ We support this approach to implementation of Section 165(i).

Regarding the \$10 billion asset threshold set forth in the Proposed Guidance, we request that the final guidance specify the basis on which the threshold is measured. We recommend that a Banking Organization’s total consolidated assets for purposes of the Proposed Guidance be determined based on the average of its four most recent consolidated reports of condition and income (in the case of banks), consolidated financial statements (in the case of bank holding companies) or reports of assets and liabilities (in the case of U.S. branches and agencies of foreign banks).

Our remaining comments are directed at aspects of the Proposed Guidance as they apply to the particular circumstances of Banking Organizations that are either direct or indirect U.S. subsidiaries of foreign banks or U.S. branches and agencies of foreign banks (collectively, “Foreign-Affiliated U.S. Banking Organizations”). As an initial matter, we note that the Proposed Guidance confirms that a Banking Organization need not incorporate into its stress

² Regarding “actionable” results, we note that the Proposed Guidance recognizes that a Banking Organization “may decide to maintain its current course based on test results; indeed, the results of highly severe stress tests need not always indicate that immediate action has to be taken” (76 Fed. Reg. at 35080).

³ See 76 Fed. Reg. at 35074.



testing all of the approaches and applications described in the Guidance, a consideration that is especially relevant (but not exclusively so) to use of enterprise-wide stress testing and reverse stress testing by U.S. branches and agencies of foreign banks.

More generally, we note that a multiplicity of practices exists among Foreign-Affiliated U.S. Banking Organizations involving varying degrees of involvement by the foreign bank itself. In some instances, such as where key risk management functions are conducted centrally, stress testing of the U.S. operations is incorporated into the foreign bank's global framework. In other instances, the local, U.S. operation lacks the IT infrastructure required to conduct full-scale stress testing on its own and instead relies on the foreign bank's systems – in effect, the stress test inputs supplied by the U.S. operation are processed through the foreign bank. Depending on the structure of a foreign bank's businesses, and the allocation of its risk management functions, there are also situations in which certain elements of the Banking Organization's stress testing (for example, with respect to credit risk) are conducted locally while others (for example, with respect to market risk) are conducted in conjunction with the foreign bank's stress testing.⁴

Further clarification regarding how the Proposed Guidance should be applied to these situations would be helpful. We believe the key point is whether the U.S. operation maintains appropriate oversight and control over the stress test, and the Agencies are able to make an adequate assessment of their performance of these responsibilities, and not whether the test is conducted through the foreign bank's systems.

Certain aspects of stress testing are most effective when centralized, and where that centralization occurs outside the United States (most typically, at a foreign bank's head office) we believe the Agencies should assess the U.S.-related aspects of such stress testing based first on their assessment of the adequacy of the stress testing framework in place at the head office. Thus, where the Agencies are satisfied with the oversight of such stress testing by the appropriate home country supervisory authority, there should be no need to require replication of the stress test in the United States. It is appropriate in these cases for management of the affected U.S. Banking Organization to report to the relevant Agency the results of the centralized stress test that relate to its operations, but the U.S. Banking Organization need not in that situation conduct any separate stress testing itself, which would be only needlessly duplicative. This approach is especially well-suited to capital stress testing exercises, where a key consideration is the ability of the foreign bank to provide capital support to its subsidiaries, including those in the United States.⁵ We recommend that these considerations be reflected in the final guidance.

⁴ In those instances in which the foreign bank itself is involved in the U.S. stress testing process, the parameters of the scenario(s) and other inputs for the stress tests are supplied by the U.S. operation. As discussed below, in some instances a Foreign-Affiliated U.S. Banking Organization may also incorporate into its stress testing scenarios and other inputs prescribed by the foreign bank or by the foreign bank's home country supervisory authority.

⁵ The Proposed Guidance confirms that the portions of the guidance related to capital stress testing do not apply to U.S. branches and agencies of foreign banking organizations. We appreciate the Agencies' inclusion of this point directly in the Proposed Guidance.



We agree that strong governance and controls are essential to an effective stress testing framework. That said, guidance on these matters should take into account the important differences between Foreign-Affiliated U.S. Banking Organizations that are separately incorporated U.S. legal entities and those that are U.S. branches and agencies. These differences are especially relevant to allocating responsibilities between a foreign bank's board of directors (or other supervisory body) and senior management responsible for the U.S. branch or agency.

As an office of a foreign bank, a U.S. branch/agency operates within the stress testing framework established, approved and overseen by the foreign bank's board of directors in the home country. As a matter of effective governance, there is no reason for the board of directors in the home country to be involved in the implementation of those policies at the branch/agency level in the United States. For example, the board of directors need not be involved in the annual review and approval of the U.S. branch's or agency's written policies or the review of its individual stress test results. Rather, senior management responsible for the U.S. branch or agency is in a much better position to undertake and discharge these responsibilities, acting within the parameters established by the foreign bank's board of directors.

It is certainly important that senior management responsible for the U.S. branch/agency report up and through to the board of directors any significant deficiencies, weaknesses or other findings identified through stress testing conducted by the U.S. branch or agency, and include any recommendations regarding actions that should be taken to address those findings. In turn, it is the responsibility of the board of directors to incorporate those findings and recommendations into its consideration of the bank's overall stress testing framework and to make such revisions and initiate such actions as it deems appropriate. Where those decisions relate to or otherwise will have a material impact on the U.S. branch or agency, senior management responsible for the U.S. branch or agency oversees their implementation at the U.S. branch or agency.

We request the Agencies to clarify their expectations regarding governance arrangements surrounding stress testing by a U.S. branch/agency and recommend that the foregoing considerations be reflected in the final guidance.

As a concluding matter, we note that stress testing undertaken by Foreign-Affiliated U.S. Banking Organizations in accordance with the Proposed Guidance may be influenced by considerations relating to the foreign bank itself. For example, by virtue of its operating as part of the larger global group, a foreign bank may require its U.S. Banking Organization to incorporate into its stress testing scenarios and other inputs prescribed by the foreign bank, or the U.S. Banking Organization itself may seek to design its stress testing to include scenarios and other inputs related to the foreign bank or its home country. Stress testing requirements and standards prescribed by the foreign bank's home country supervisory authority may also be relevant to the conduct of a Foreign-Affiliated U.S. Banking Organization's stress tests. These considerations are all consistent with the principles underlying the Proposed Guidance but are



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peculiar to the circumstances of Foreign-Affiliated U.S. Banking Organizations and should be reflected in the final guidance as well.

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We appreciate the Agencies' consideration of our comments. Please contact the undersigned if we can provide any additional information or assistance.

Very truly yours,

A handwritten signature in black ink, appearing to read "Richard Coffman", written over a horizontal line.

Richard Coffman
General Counsel