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November 5, 2003

Office of the Comptroller of the Currency
Docket No.03-14
Public Information Room, Mail Stop 1-5
250 E Street, SW
Washington, DC 20219

Ms. Jennifer J. Johnson
Docket No R-1154
Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Robert E. Feldman
Attention: Comments
Executive Secretary, Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Regulations Comments
Docket 2003-27
Chief Counsel's Office, Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

RE: The Operational Risk Issues in the U.S. Implementation of New Basel Capital Accord

Dear Ladies and Gentlemen:

In June 2003, the Risk Management Association formed a Working Group for its members and the attendees of the Operational Risk Management Discussion Group to examine and contribute to the development of bank regulations that deal with operational risk. This Group, the Risk Management Association Working Group on Operational Risk Regulation, commented in July on the Third Consultative Document of the New Basel Capital Accord. Now it is submitting to you a more detailed review of the two subsequent regulatory documents issued for comment in the Federal Register on August 4th – the

Advanced Notice of Proposed Rulemaking and the associated Draft Supervisory Guidance.

The names of the contributing Working Group members are listed in Attachment 1.

We appreciate greatly the work undertaken by the US regulatory agencies to move reform of the 1988 Accord forward and hope that the comments in this response will be of assistance.

We also appreciate the opportunity to comment on the ANPR and the Draft Supervisory Guidance and look forward to continuing to working with you to more closely align regulatory capital requirements with underlying risk. If you have any questions about this comment, we would be happy to discuss it at your convenience.

Very Best Regards



Timothy Elliott
Vice President, Operational Risk Management
Comerica
Chairman, RMA Working Group on Operational Risk Regulation



Charles Taylor
Director, Operational Risk
The Risk Management Association (“RMA”)
Member, RMA Working Group on Operational Risk Regulation

Attachment 1

The Risk Management Association
Working Group on Operational Risk Regulation
Members

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Richard Campbell	Senior Vice President, Operational Risk Methodology and Capital Allocation	Wachovia
Tim Elliott	Vice President, Operational Risk Management	Comerica
Robert W. Jones	Director, Operational Risk	FleetBoston
Kristine Keusch	Vice President, Operational Risk Specialist	Comerica
Roland K. Ojeda	Senior Vice President, Operational Risk	BankWest Corporation
Patrick O'Neill	Head of Operational Risk, Americas	BNP Paribas
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Tara Heuse Skinner	Vice President, Corporate Strategy	Synovus
James Stoker	Vice President, Operational Risk Analytics	Suntrust Banks
Charles Taylor	Director, Operational Risk	The RMA
Sandeep Vishnu	Partner	Malvern Partners

RMA Working Group on Operational Risk Regulation
Comment Letter on the ANPR and DSG on Operational Risk Regulatory Capital

I. Introduction

In June 2003, the RMA¹ formed the RMA Working Group on Operational Risk Regulation (the Working Group) for its members and the attendees of the Operational Risk Management Discussion Group² to examine and contribute to the development of bank regulations that deal with operational risk. As its first task, the Working Group commented to the Basel Committee on Bank Supervision and to the U.S. Bank Regulatory Agencies (the Agencies) on the treatment of the Advanced Measurement Approach (AMA) in the Third Consultative Document (CP3) of the New Basel Capital Accord (the Accord).³

Now, the Working Group is pleased to submit this letter on the related Advanced Notice of Proposed Rulemaking (ANPR) and Draft Supervisory Guidance (DSG)⁴ in response to the request for comment from the Agencies.

¹ The RMA – the Risk Management Association -- is a member-driven professional association whose sole purpose is to advance the use of sound risk principles in the financial services industry.

The RMA also sponsors and supports two other Groups that are commenting on the ANPR: The Basel Securities Lending Sub-Committee, which is focusing on securities lending issues and credit mitigation and the RMA Capital Working Group, which is focusing on all other aspects of the credit risk capital charge under the A-IRB Approach.

² The Operational Risk Management Discussion Group is an informal group of US banking industry professionals formed in the 2002 to work together to strengthen the effectiveness of operational risk management through the exchange of ideas, approaches, and techniques in the financial services industry.

³ The RMA Working Group on Operational Risk Regulation consists of senior operational risk management professionals working at banking organizations throughout the United States. The names of individuals who have participated in the Working Group and agree with the letter's content are shown in Attachment 1. Their institutions are listed for identification purposes. This Working Group does not necessarily speak for RMA's institutional membership, which is diverse and includes institutions with different views on regulatory matters. Individual banking organizations whose staff have participated in the Group may be responding separately to CP3 and may hold opinions regarding the ANPR and DSG that differ from those expressed in this paper.

⁴ The ANPR and DSG were published in the Federal Register, Volume 68, No. 149 on August 4th, 2003. Subsequent footnotes that refer to sources use page and sometimes paragraph numbers from this document, unless otherwise stated.

This letter is divided into seven more sections that deal with:

- *General Issues* of clarity, force and scope, and principles that should govern the regulation's present form and future evolution;
- *Transition and Timing Issues* surrounding the introduction of the proposed regulation;
- *Governance and Organization Issues* concerning the role of the Board vis-à-vis senior management and the definition of independence of the risk management function;
- *Data Issues* including scope, reconciliation, thresholds, relevance and evolving approach;
- *Capital Estimation and other Analytical Issues* including offsets for risk mitigation, reductions for correlation and diversification, indirect losses, the differences amongst methodologies, and the exclusion of expected operational losses;
- *Issues regarding Supervisory Practices and Regulatory Developments*, including home host country issues and alternatives to the AMA; and
- *Conclusion*.

The Working Group hopes that this comment letter proves useful to the Agencies as they work to finalize their regulatory proposal and associated supervisory guidance.

II. General Issues

*Increasing Specificity and Prescriptiveness*⁵ The final form of the regulation should contain far fewer mandatory rules for well-managed banks.

The ANPR contains many more specific prescriptions than CP3. For example, the ANPR:

- requires the internal control environment to exceed "Agency minimum standards." This is a new requirement that is unclear;
- suggests additional fields to be maintained for large losses in loss event databases:
 - Where loss is reported and expensed
 - Discovery date of the loss
 - Event end date
 - Management actions
 - Adjustments to the loss amounts
 - Product type;
- requires quantification, with documentation of model rationale and assumptions for expected loss (EL), even when it has been budgeted and/or reserved for;
- requires risk mitigation for insurance only, not other securities products, as was implied under CP3; and
- requires additional data maintenance practices to track losses when the impact is across multiple business lines.

⁵ CP3 is interpreted to include ideas in Basel's "Sound Practices" (February 2003) documents on operational risk.

Where the ANPR or the DSG needs to be specific and a rule is appropriate, it is helpful to make that rule as clear as possible. However, the Working Group believes there should not be so many mandatory rules and much of what is being prescribed should be left to management judgment and oversight.

Ambiguities and Inconsistencies The DSG in particular needs to be clarified extensively to reduce repetitiveness and internal inconsistencies, and definitions are needed for many key concepts in the ANPR and DSG.

The relationship between the two documents, and their relationship to CP3 and to principles of regulation and supervision is obscure. Although the ANPR states that the DSG is meant to explain more fully the material in the ANPR,⁶ that is not always the case.

In the DSG in particular, several subjects are treated more than once in language that is not always consistent. Redundancies should be removed. Many undefined terms are used in different contexts in different ways, making their meaning uncertain. More definitions are needed.⁷

These aspects of the current drafts make it hard to judge for example whether the balance between flexibility and fixed requirements is right, or the balance between supervision and regulation is appropriate – two of the questions on which the regulators have asked for comment.

Future Changes The regulation should be clear that future evolution will generally be toward more principles-based guidance and that change will be introduced gradually, to avoid undue implementation costs.

The Working Group is concerned about the timing, scale and direction of future change in the regulation and supervisory practices that are covered by the ANPR and the DSG in the years ahead. It is widely believed in the industry that the new Accord will be obsolete before the ink is dry and senior regulators have said they expect it to evolve – to be “evergreen.”⁸

⁶ See page 45940 footnote.

⁷ Among terms that are not defined and are used differently in different parts of the DSG are: operational risk management framework; operational risk management; principle, policy, standard, process and procedure; practice; independence (of one function from another); business environment factors; inherent risk and residual risk; and regulatory framework for operational risk.

⁸ In his testimony before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate June 18, 2003, Federal Reserve Vice Chairman Roger Ferguson' said, "...Basel II could evolve as best practice evolves and, as it were, be evergreen."

As we develop more specific knowledge in the industry about sound practices in operational risk management, the AMA should not become ever more prescriptive. It would be far preferable if it evolved toward a more principles-based and less rules-based body of guidance. Principles tend to be more durable than specific rules; their wider applicability can enhance fairness; their relationship to fundamental public policy imperatives establishes their legitimacy more clearly than any relatively unsupported enumeration of rules. In any event, the pace of change should generally be moderate and measured and set a balance between introducing improvements in a timely manner and limiting compliance costs to a reasonable level.

III. Transition and Timing Issues

During a planned transition to Basel II, regulation should allow banks to combine the AIR-B approach for credit risk capital with the BIA or the SA for operational risk.

Unlike their counterparts in other nations, the U.S. Agencies propose to implement the new Basel Capital Accord without offering the options of the Basic Indicator Approach (BIA) and the Standardized Approach (SA). The U.S. banks concerned will implement the Advanced Internal Ratings-Based Approach (AIR-B) for credit risk. The Working Group recognizes that banks should implement an approach to operational risk at the same time, because the AIR-B covers credit risk alone: there is no “gross-up” for operational risk as exists under the current framework. Therefore, as currently proposed, these banks have no choice and must implement the AMA as they implement the AIR-B.

The Working Group believes that this may prevent timely opting in by borderline banks that expect to be ready for AIR-B but not as ready for AMA.

Operational risk management and measurement is at a much earlier stage of development than credit risk management and measurement. There are significant open issues such as the relative value of internal data vs. external data vs. scenario analysis, and methodologies for converting external data into something usable internally. For this reason, some well managed banks have taken the very defensible strategic decision to develop their operational risk management capacity at a measured pace.

Therefore, regulators should allow banks a transition period during which they might use the AIR-B approach to estimate credit risk capital and the BIA or the SA for calculating operational risk regulatory capital. This transitional arrangement should be subject to certain conditions:

- The bank should comply with the finalized DSG sections titled “Corporate Governance” and “Operational Risk Management Elements”;
- The bank should have a well-articulated implementation plan for the AMA to which they are committed;
- The bank is capturing internal operational risk data, and effectively using internal data, external data, business environment and internal control factor assessments, and scenario analysis in the management of operational risk throughout the bank.

This would establish that the bank had a well-developed approach to measuring and managing operational risk and was on track to adopt AMA in a reasonable timeframe.

The Working Group understands that the BIA and SA are not accurate measures of operational risk and that, used for any protracted period, they could distort incentives. This is why the Working Group supports only their temporary use. Still, for a period of a few years, with a clear end point, the Working Group believes that the benefits that arise from wider use of the AIR-B far outweigh the negatives associated with the temporary and limited use of the BIA and SA.

The Working Group considers it is important to ensure the incentives for opting into Basel II encourage as many banks as possible to do so now and in the future.

Timing Following the recently announced delay in finalizing the Accord internationally, the implementation end date should be put back at least six months.

Following the October 2003 announcement by the Basel Committee that it would postpone finalization of the Accord for six more months, implementation should also be delayed by a similar period, to allow banks time to make the necessary investments in people, processes and systems to achieve compliance.

IV. Governance and Organization Issues

Board and Management Oversight The regulation should not mandate the exact manner in which the Board of a bank is involved in determining operational risk management policy, organization or implementation.

Unlike CP3, which was flexible in defining the respective roles of the Board of Directors and senior management⁹ in their oversight of operational risk management, the ANPR requires formal Board of Director approvals of the framework. The Working Group believes this is not necessary. It should be sufficient for senior executive management to review and approve the operational risk management framework to assure its scope and approach is appropriate, and that it is well implemented and properly audited. Then periodic updates to the Board can give the Board the opportunity to give overall guidance and support. The Working Group believes the adequacy of Corporate Governance should be evaluated under Pillar II.¹⁰

Independent Firm-wide Operational Risk Management Function The regulation should more clearly define independence.

The Working Group supports the idea of Firm-wide Operational Risk Management Function independence. The Operational Risk Management Function, Internal Audit and Compliance should have independent reporting lines and performance objectives. This is a prerequisite for Internal Audit and Compliance making objective determinations about

⁹ See footnote 4 of the Feb 2003 "Sound Practices" document.

¹⁰ See pages 45907, 45941, 45942, 45979-S2, 45980-S3.

the effectiveness of the Operational Risk Management Function. However, in the interests of efficiency, it is important that these three functions be free to coordinate certain aspects of their activity such as their development of standards, criteria and tools for assessing, identifying, measuring and monitoring risks. And it should be permissible for the analysis of the Audit and Compliance functions, such as audit scores, to be used by the business units and the Operational Risk Management Function in the assessment and management operational risks.

The definition of independence used in describing the relationship of the operational risk management function to other parts of an institution should apply to purpose, reporting structure and scope of activity but permit cooperation in ways that would add to efficiency.

V. Data Issues

Definition of Operational Risk: Scope of Legal losses Regulation should exclude plaintive costs in operational losses.

The proposed definition of operational risk includes “...the exposure to litigation from all aspects of an institutions activities”.¹¹ This would include all litigation exposures, which the Working Group believes is inappropriate.

The term ‘exposure to litigation’ implies that the institution is a defendant in a legal action. However, technically this is not necessarily the case – ‘exposure to litigation’ could also include costs incurred by the institution as plaintiff. The Working Group believes it should be explicitly stated that those plaintiff-incurred costs not be considered as an operational risk.

The proposed definition would also seem to include settlements of baseless lawsuits as operational risk losses. As many times these settlements are made to control costs or to maintain customer relations, these would be more appropriately labeled business or strategic risks.

Definition of Operational Risk: Boundary Issues Between Credit and Operational Risk Guidance related to the classification of loss events should be clarified.

The proposed rules are unclear when applied to retail credit products.¹² In some institutions, losses associated with the fraudulent use of credit cards or the fraudulent use of homeowner equity lines of credit via a check have traditionally been treated as operational losses, as opposed to credit losses, because of their check/draft-like features. The Working Group believes that this treatment should remain appropriate, and that the guidance related to the classification of loss events should take such events into account.

¹¹ Page 45978, Section III, 2nd paragraph.

¹² See page 45904, “Boundary Issues” 2nd paragraph.

Loss Event Reconciliation Regulation should not generally require operational loss data be reconciled to the general ledger.

The definition and nature of operational risk losses should be clarified. Currently, operational risk losses must be “...recorded in the institution’s financial statements consistent with Generally Accepted Accounting Principles (GAAP)”¹³ Our concern is that this not be construed as requiring a reconciliation to be performed between all of an institution’s loss data and the general ledger. Many operational risk losses do not get posted to the G/L as discrete items, particularly in trading businesses. Requiring reconciliation of general ledger information with operational risk data would severely impact the quantity of usable loss data in certain business lines. The supporting information for the loss is often found in the narrative of the incident description as opposed to in a G/L posting document. And operational losses should be dated at the time of the event, even if the loss is accrued in the G/L over some extended period. The Working Group believes that many loss event database items will often, by their very nature, not be reconcilable to the general ledger.

Loss Event Data Thresholds Regulation should require thresholds be set so that enough loss event data is collected for AMA modeling.

The proposed regulatory standard for loss event data thresholds should be based on the required functions of the data. Currently, one of the requirements of loss data “....capture a significant proportion of the institution’s operational risk losses”.¹⁴ Given that the data will be used for risk measurement purposes in some manner in an AMA model, a better standard would be to state that the thresholds should provide data sufficient to perform this function.

External Data Regulation should require management to review relevant external data of admissible quality, but allow banks leeway to apply sound judgment in dealing with issues like applicability and scaling.

The guidance on the use of external data needs strengthening. Clarity should be provided under Supervisory Standard 21 on expectations relating to systematic review of external data to ensure an understanding of industry experience. The Working Group suggests incorporating language in this section acknowledging that effective use of relevant external data is in the early stages of development and that ongoing dialog during implementation is appropriate.

In addition, to meet the external data requirements, institutions have initiated a number of consortia and third party vendor efforts. Greater direction from the agencies regarding external loss data collection requirements would help to ensure that the data collected and distributed by the consortia are similar in quality, to avoid potential gaming through selective incorporation of external data.

¹³ See page 45978, Section III, 3rd paragraph.

¹⁴ See page 45982, Internal Operational Risk Loss Event Data, 9th paragraph.

VI. Capital Estimation and other Analytical Issues

Risk Mitigation Regulation should not restrict the offset for risk mitigation to 20% of capital.

The 20% ceiling on the amount of capital that can be offset by insurance appears arbitrary. The qualitative criteria necessary for insurance to qualify as a capital offset are particularly restrictive. The ceiling is a disincentive for financial institutions to utilize all the protection that may be available from insurance and other risk mitigants. The Working Group believes the size of any capital adjustment for insurance should not be restricted to 20 % but should be based on the quality and extent of insurance protection provided.

The Working Group also believes that insurance provided by captive insurers should be allowed for a capital adjustment provided qualitative criteria are met.

Finally, regulations should provide flexibility, allowing for recognition of other risk mitigation products that emerge in the future. So, for example, securities products and other capital market instruments that are determined to be effective risk mitigation tools should be permissible offsets to operational risk regulatory capital requirements..

Correlation Regulation should allow capital reductions for correlation and diversification wherever there is a strong argument for assuming such effects are material, even if it is not a statistical argument.

It is important that the standard for establishing correlation and diversification is reasonable. Generally, the Working Group believes that insufficient data will be available to estimate correlations across business lines and event types statistically. Most assessments of correlations and the effects of diversity will be made from qualitative reasoning based on the underlying nature of the risks. The Working Group suggests the final regulatory language recognize that a sound qualitative judgment will be necessary and sufficient. Reasonable assumptions and inferences from institutions that are actively working to improve their understanding of available risk data should be acceptable.

It is important that overly conservative criteria not be applied regarding correlation assumptions so that banks using more risk-sensitive “bottoms-up” approaches to the quantification of capital are not penalized.

Opportunity Costs Regulation should not permit indirect losses and opportunity costs to be taken into account in calculating capital.

The ANPR requests comment on whether indirect losses (for example, opportunity costs) should be included in the definition of operational risk against which institutions would have to hold capital. The Working Group opposes consideration of indirect losses such as

opportunity cost in the definition of operational risk. Issues would emerge relating to the accuracy of measurement, uniformity in application, and immaturity of the data collection process that would compound an already complicated task.

Alternative Approaches during Transition Regulators should accept that equally valid but different methodologies may be used by different institutions.

The Advanced Measurement Approach (AMA) grants institutions considerable leeway in how they construct operational risk capital models, provided certain standards are met. The Working Group believes this is particularly appropriate given the nascent stage of operational risk measurement. For example, the proposed regulation implicitly allows great latitude in sources of external data and its use. This makes a great deal of sense.

However, this flexibility may lead different institutions to produce significantly different capital estimates in relation to comparable operational risks. With only a little over two years to achieve AMA compliance, institutions would appreciate a statement in the regulation to the effect that, within reason and at least for a period, the Agencies were willing to accept this possibility; that, late in the day, they will not insist on institutions adopting the methodologies that lead to particularly high operational risk capital charges.

Expected Loss Regulators should require only unexpected operational losses to be covered by regulatory capital for any bank where expected operational losses are consistently treated as an operating cost.

Supervisory Standard 28 requires capital for operational risk to be the sum of expected and unexpected losses unless the institution can demonstrate, consistent with supervisory standards, the expected loss offset. The Working Group believes the capital charge for operational risk should represent unexpected losses only. Further guidance is needed on how banks are expected to demonstrate to regulators that they have the appropriate coverage for expected losses. Expected losses for operational risk typically are budgeted and factored into the pricing for products and services.

The Basel Committee recently indicated expected losses will not be included in credit risk capital. To be consistent, we recommend this approach also be adopted for operational risk capital too.

VII. Supervisory Practices and Regulatory Issues

Flexibility The regulation should set clear standards on supervisory flexibility.

Supervisors should be able to take the circumstances of individual institutions into account – for example, in making reasonable, fair adjustments to the timetable for implementing AMA, depending on an institution’s recent history, or in adjusting capital adequacy levels to reflect unusual levels of diversification or concentration in its businesses or portfolios. However, they should treat like institutions in like manner where their circumstances are broadly the same. Moreover, this should be true regardless of

which country or Agency the supervisors come from so that, when confronted with similar institutions in similar situations, supervisors apply the same principles and reach similar conclusions. And, most certainly, Agencies should be consistent in the way they apply supervisory principles throughout the United States.

In general, the Working Group believes the flexibility on standards needs to be explained more clearly. One way to do this is to explain them in terms of universal basic principles and then discuss the degree of flexibility in their interpretation. If that's the approach, then it is helpful to understand if there are guidelines as to how supervisors should use their flexibility. Alternatively, flexibility could be articulated in terms of two sets of standards: those that apply universally; and those that apply only in specific defined circumstances. For example, it would be useful for the "must have" standards and criteria for compliance labeled as such and spelt out in the DSG, so the costs and challenges of implementation could be better understood.

The absence of a clear articulation of where and how flexibility might be exercised in either the ANPR or the DSG makes it hard to assess the flexibility of the proposed rules.

Roles and Responsibilities of Supervisors Regulation should clearly delineate the respective roles of the different US financial supervisory bodies.

The interpretation and implementation of Sarbanes-Oxley, Basel II, FIDCIA and other legislation and regulation should be coordinated to remove potential duplications and contradictions, saving compliance costs.

Currently, it is unclear what the roles of the Fed, OCC, FDIC, NASD and SEC will be in supervision of operational risk management. Where there are differences in interpretation between agencies, how will they be resolved? How will the SEC lead role in assessing operational risks of bank broker dealer businesses be coordinated with the federal bank regulator supervision of operational risk management overall? How will the supervisory interpretation of governance standards in Sarbanes-Oxley and the ANPR be reconciled and applied?

The banking and other regulatory agencies concerned should expeditiously review overlaps in their rules and regulations flowing from recent and established law and regulatory initiatives. It would be helpful if the language of the DSG and that of other agency rules and regulations could be normalized. It is important that the roles, responsibilities and scope of action of the various US supervisory bodies be clarified prior to the finalization of the DSG. This would reduce unnecessary regulatory burden and greatly help affected institutions plan their implementation of the necessary changes in the systems, organization and processes.

Home/Host Country Rules For operational risk as well as credit risk, the home country supervisor should generally set capital standards for internationally active Bank Groups.

Provided the home country supervisor acts in accordance with international supervisory standards established by the Basel Committee, the home country supervisory should set standards for the measurement of risk and the estimation of capital requirements for the entire Bank Group and host country supervisors should accept a top-down allocation scheme for apportioning capital to the separate national and legal entities within the Group.

This is consistent with the Basel Concordat and the Core Principles of Banking Supervision enunciated by the Basel Committee in earlier documents. So an institution's home country supervisor, and not any of its host country supervisors, should generally:

- determine the adequacy of an institution's capital in relation to its operational risk profile;
- assess an institution's internal methodologies for calculating operational risk and allocating associated capital;
- approve an institution's use of advanced methodologies under Basel II;
- decide whether to require an institution to hold regulatory capital for operational risk in excess of the minimum called for under Basel II and, if so, what the appropriate level of regulatory capital should be;
- establish "target" ratios for supervisory action against an institution, which may be greater than the minimum called for under Basel II;
- decide whether, and if so how, to intervene to prevent capital from falling below required levels; and
- require action by an institution to restore its capital in the event it falls below the minimum requirement.

In any event, with regard to the estimation of capital required in national and legal subsidiary entities, it will often be impossible to make independent capital estimates, entity by entity and, therefore, it is critical that a top-down allocation approach be generally permissible.

Alternatives to AMA The Agencies may wish to consider a simpler alternative to setting operational risk management capital standards.

Given the US regulatory decision to forego either of the less rigorous alternatives to AMA in their implementation of Basel II, the Agencies may wish to consider something significantly different to AMA before committing to final implementation.

One alternative that has been recently articulated was published in December last year as the "New General Approach to Capital Adequacy."¹⁵ That approach proposed that regulators guide banks in their development of proposals for capital adequacy levels not by setting rules of calculation but by creating strong and clear incentives for banks to make their best faith efforts independently. It focused less on how capital levels should be estimated and more on the results and consequences.

¹⁵ "A New General Approach to Capital Adequacy," Charles Taylor, CSFI, December 2002.

That approach was framed as an alternative for setting capital standards for all types of risk. But there is no reason why it should not be applied, perhaps in the first instance, just to operational risks. Indeed, the New General Approach was based on a similar 1996 proposal developed just for market risk. Applying it to a single area of risk seems quite feasible and it may, therefore, provide an alternative that the Agencies should consider seriously.

VIII. Conclusion

A risk-based approach to setting capital adequacy standards will make America's banking system more competitive and stable. The Working Group would be very happy to discuss and expand on its comments with the Agencies at their convenience to support that goal.

The Working Group wishes to thank the Agencies for the opportunity to comment.

Attachment 1

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Working Group on Operational Risk Regulation
Members

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