

August 6, 2012

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551

**AMAG 2nd Supplemental Response
2012 Agency Information Collection Activities
Operational Risk Data Reporting FR Y-14A/Q/M – OMB Nos. 7100-0341**

Dear Ms. Johnson:

This letter and attachments comprise the second Supplemental Response from RMA's Advanced Measurement Approaches Group (AMAG)¹ on proposed changes to the operational risk aspects of Agency Information Collection Activities under FR Y-14A². It should be read in conjunction with the AMAG's earlier responses dated April 23, 2012 and May 24, 2012, respectively.

The AMAG reiterates the positions and recommendations outlined in its April 23, 2012 and May 24, 2012, letters including, but not limited to, the members' objection to providing legal reserve data as part of the FR Y-14A/Q/M.

In its original proposal the Federal Reserve Board (FRB) requested that AMA banks submit operational risk loss data based on a new quarterly operational risk loss data collection template. The FRB's request encompassed all operational risk loss data, including reserves for **pending** litigation, because the reserves tend to have a significant impact on the measurement of operational risk. Among other concerns in our previous April 23, 2012 and May 24, 2012 letters, the AMAG highlighted the extremely

¹ The Advanced Measurement Approaches Group (AMAG) was formed in 2005 by the Risk Management Association (RMA) to share industry views on aspects of Advanced Measurement Approaches (AMA) implementation with the U.S. financial services federal regulatory agencies. The members of AMAG are listed in Attachment B to this letter. They are listed for identification purposes only. This letter and attachment do not necessarily represent the views of RMA's institutional membership at large, or the views of the individual institutions whose staff have participated in the AMAG.

² Generally speaking, AMAG member firms understand and appreciate the regulatory community's interest and needs for collecting actual loss data. The Federal Reserve has stated its goals for the change as (1) assessing BHC's operational loss exposures in relation to the risks faced by them, (2) ensuring safety and soundness, (3) developing and calibrating supervisory stress test models, (4) evaluating the projections that BHCs submit as part of the FR Y-14A, and (5) supporting continuous monitoring and analysis of BHCs' operational loss activity and trends. Despite its support in concept, AMAG has concerns about some of the details of implementing this new proposal relative to FR Y-14A/Q submission requirements.

confidential and sensitive nature of the legal reserve data that would be required as part of quarterly submissions of operational risk loss data sets on the collection template, and explained why it would be inappropriate and potentially prejudicial, in the context of pending litigation, to include such information in these data sets.

Recent Dialogue with Regulators

Notwithstanding its objection to reporting such highly confidential and sensitive legal reserve information, the AMAG appreciates the opportunity to have engaged in a dialogue with the regulatory community about addressing this topic of reporting extremely sensitive information. Following the AMAG's April 23^d response, the Federal Reserve contacted The Risk Management Association (RMA), sponsor of the AMAG, for clarification of the Group's response on the question of including legal reserves in CCAR submissions.

The AMAG has also since participated with certain trade associations in teleconferences and meetings with the FRB. Notably, on July 16, 2012 representatives of the AMAG attended in person and participated by telephone in a meeting at the FRB in which three (3) FRB alternative Methods for reporting were discussed. At that meeting, the AMAG also had an opportunity to describe more fully its own two analytic alternative approaches outlined in our May 24, 2012 letter that should meet both the needs of the FRB and protect the confidentiality of these critical bank data. In light of that discussion, the AMAG believes that, in particular, one of the two approaches that we outlined in our May 24, 2012 has potential for further discussion and careful consideration as it would alleviate the AMAG members' concerns and further the interests of the FRB.

Analytic Alternatives

Following the July 16, 2012 meeting, the AMAG has also received brief descriptions of reporting Methods 4 and 5 as proposed by the FRB. Of these, Method 4 holds potential, subject to some modifications. For one, a reduction of the number of matrix cells (i.e., less granularity) would enhance protection of confidentiality (e.g., possibly collapsing the entire matrix to the aggregate bank level and submitting both legal reserve and all other data using this method). Also, reporting frequency data for periods in which reserves are established and increased would be a preferred approach, as opposed to reporting only one frequency entry when the reserve is first established.³

In the absence of these enhancements, however, the AMAG is using this Comment period to reiterate one of our two reporting alternatives outlined in our letter of May 24, 2012 (See Attachment A). The AMAG recognizes that these options are not without challenges for both banks and regulators. The AMAG stands ready, however, to work with the FRB to assess the merits and feasibility of its proposals in the spirit of satisfying U.S. banking agencies' need for insight into banks' operational risk exposures, while respecting the banks' and their stakeholders' own need for confidentiality of these critical data sets.

³ Note that the AMAG has participated with certain trade associations in developing detailed response commentary on the five reporting Methods offered by the FRB. See separate joint letter dated August 6, 2012.

Lastly, some AMAG members believe that banks should also be given the option of reporting such sensitive data either under one of the confidential reporting methods referenced herein, or reporting such data as it would all other operational risk data, if it so chooses.

Thank you, on behalf of AMAG, for the opportunity to continue a dialogue on possible solutions. The AMAG would be pleased to continue this discussion at your convenience.

Please contact us as appropriate.

Sincerely,

A handwritten signature in black ink, appearing to read "R. Phillips", with a stylized flourish at the end.

Robin L. Phillips
Chairman,
Advanced Measurement Approaches Group

Attachments

- A – AMA Group Alternative Reporting Proposal
- B -- About the AMA Group

AMA Group Alternative Reporting Proposal

Following is a restatement and elaboration of one of the two possible alternatives offered by AMAG in May 2012. It is included herein for further consideration and discussion.

AMAG Processed Data Alternative – *Provide “processed” rather than highly confidential “raw” loss reserve data*

Rather than provide the “raw” loss data to the FRB, AMA banks could provide “processed” data. Undoubtedly, the FRB has plans to use the raw loss event data within a modeling process. We assume that its end-to-end modeling process will include a series of analytical / quantitative tasks. Our proposal would be for AMA banks to perform some of the initial analytical / quantitative tasks and submit the output to the FRB. Then, the FRB could take this output and perform the remaining tasks to complete the modeling process and produce the final results.

It is difficult to determine the exact nature of the tasks to be performed by the AMA banks without knowledge of the FRB’s modeling process. However, following are some examples on how this alternative approach could work based on some typical operational risk modeling processes.

Example A: LDA-type modeling, which focuses on determining parametric frequency and severity distributions using the empirical loss data.

- Determining Frequency distribution parameters: Loss amount information is not necessary for frequency modeling; therefore AMA banks could provide the number of loss event for each unit of measure without providing the loss amount. This information would not compromise the confidentiality of the reserve data and would not impede the FRB in modeling frequency of loss.
- Determining Severity Distribution parameters: Loss amount information is critical to determining severity distribution parameters. Therefore, the proposal would be for the FRB to provide the AMA banks with the specifications on how the loss data should be fitted. The AMA banks would be responsible for conducting the fitting process and submitting the results [i.e., fitted distribution parameters for each Unit of Measure (UOM)]. The loss amounts for individual events would not be submitted and the confidentiality of the reserve data would not be jeopardized. In addition, AMA banks could provide other statistics such as goodness-of-fit test results and other statistical properties of the empirical distribution (e.g., mean mode, median, variance).

Example B: Panel Regression analysis between Frequency of loss and macroeconomic factors (in line with the model used by the FRB for the recent CCAR analysis)

- This type of analysis would not require loss amount information as the regression analysis is performed against the frequency of loss. Therefore, AMA banks could submit the loss data without loss amounts.
- Once the number of losses for a given stress period is determined, the FRB would need some estimate of severity. In the recent CCAR analysis, the FRB used "sample averages by event type for each BHC" as the estimate of severity. The AMA banks could provide these statistics (along with other statistics) for each UOM without compromising the confidentiality of the reserve information.

This "Processed Data option" is similar in some respects to the FRB's Method 4 but with some additional important benefits. In fact, one could interpret the FRB's Method 4 as one example of "process data". A key difference, however, is that in the AMA bank-processed data alternative, the institutions could submit the Frequency matrix and the Total Loss Amount for a given period for all of the data (non-reserve losses and reserve losses). A second difference is that the level of "processing" would be less granular than that of FRB Method 4 (e.g., possibly collapsing the entire matrix to the aggregate bank level).

The benefits of submitting the information for all combined events would:

- Completely eliminate any potential for compromising the confidentiality of reserve information; and
- Remove the potential concern about "double counting" of losses when current reserves turn into actual settlements over time.

Furthermore, the AMAG alternative would allow the FRB to change the nature of the requested "processed data" over time. In this alternative, it is envisioned that the FRB would establish a set of processed data to be submitted, which could change over time (i.e., with appropriate amount of lead time, of course) as the FRB determines the need for a different set of information.

Notwithstanding members' objection to reporting any Legal Reserve data, and although the AMAG banks are conceptually supportive Method 4 as a possible option, banks are left to make a number of assumptions about FRB Method 4. Because of the difficulty of making such assumptions AMAG continues to believe that "the processed data" alternative should be given due consideration because it affords more long-term flexibility, is more protective of confidential nature of reserves, and potential less problematic to use in the FRB models.

About the AMA Group

The Advanced Measurement Approaches Group (AMAG) was formed in 2005 by the Risk Management Association (RMA) at the suggestion of the U.S. AMA-BQT (formerly the Inter-Agency Working Group on Operational Risk). The RMA is a member-driven professional association whose purpose is to advance the use of sound risk management principles in the financial services industry.

The purpose of the AMAG is to share industry views on aspects of Advanced Measurement Approaches (AMA) implementation with the U.S. financial services federal regulatory agencies. The Group consists of operational risk management professionals working at financial service organizations throughout the United States. The AMAG is open to any financial institution regulated in the United States that is either mandated, opting in, or considering opting in to AMA. A senior officer responsible for operational risk management serves as the primary representative of each member institution on the AMAG. Of the US financial service institutions that are currently viewed as mandatory or opt-in AMA institutions; nineteen were members of the AMAG at the time of this writing.

The members of AMAG are listed below. They are provided for identification purposes only. This paper does not necessarily represent the views of RMA's institutional membership at large, or the views of the individual institutions whose staff have participated in the AMAG.

Bank of America / Merrill Lynch
Bank of the West
BMO Financial Group
BNY Mellon
Capital One Bank
Citizens Bank
Deutsche Bank
Goldman Sachs
HSBC
JP Morgan Chase
Keycorp
Morgan Stanley
Northern Trust
PNC
State Street Corporation
SunTrust
TD Bank Financial Group
Union Bank
Wells Fargo

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