February 24, 2011

Comments on the Basel Committee's Consultative Document
Sound Practices for the Management and Supervision of Operational Risk

Japanese Bankers Association

We, the Japanese Bankers Association, would like to express our gratitude for this opportunity to comment on the Consultative Document, *Sound Practices for the Management and Supervision of Operational Risk*, released December 10, 2010, by the Basel Committee on Banking Supervision.

We hope that our comments below will assist the Basel Committee in its efforts to finalize rules going forward.

【General Points】

We understand that the sound practices paper review both is based upon lessons learned from the recent financial crisis and reflects progress made thus far with banks' operational risk management. Furthermore, we believe that, as described in the Consultative Document, the principles proposed should be adopted by banks in accordance with the nature, scale, complexity, and risk profiles of their operations, and that the principles will not mandate uniform risk management systems for all banks.

We hope that the following points will be considered in conducting future deliberations to further improve banks' sound operational risk management.

【Specific Points】

<u>Principle 2: Fundamental principle of operational risk management (Paragraph 27(e))</u>

In establishing operational risk frameworks for individual banks, item*(e) establish risk reporting and Management Information System (MIS)* should be clarified, and we request an illustration to clarify the definition and details of the Management Information System noted in this item.

<u>Principle 4: Governance and the Board of Directors (Paragraphs 30, 31)</u>

This principle would require that the board of directors approve a statement of risk appetite and tolerance for operational risk that the bank is willing to assume, as well as appropriate thresholds or limits for specific operational risk. However, we would like approval of appropriate thresholds and limits for specific operational risks to be optional.

Paragraph 30 states that *the board of directors should approve appropriate thresholds or limits for specific operational risks*. Further, Paragraph 31 notes that bank boards of directors should consider frequency, volume, or nature of limit breaches in reviewing the appropriateness of the overall operational risk appetite and tolerance statement.

However, adequate assessments of a bank's envisioned risk appetite and tolerance cannot be made solely by setting appropriate thresholds and limits for operational risk.

Therefore, in order to increase latitude and allow flexibility for individual banks in approving and reviewing risk appetite and tolerance, we request a description not restricted to setting thresholds and limits.

Principle 6: Risk Management Environment / Identification and Assessment of Operational Risk (Paragraph 39(a))

Paragraph 39 (a) notes that *[b]anks may also find it useful to capture and monitor operational risk contributions to credit and market risk related losses in order to obtain a more complete view of their operational risk exposure*. We seek a clarification of the meaning of *operational risk contributions*.

If *operational risk contributions* refer to a comparison between internal loss data classified as credit risk-related and internal loss data classified as market risk-related, we seek a further notation of this. Or, if the objective of *operational risk contributions* differs from the description above, we seek a more detailed description of the intended usage with examples when analyzing the relationship with credit and market risk related losses.

Principle 8: Monitoring and Reporting (Paragraphs 43-46)

This rule would require banks to conduct timely and comprehensive operational risk reporting for the board of directors in an effort toward continuous improvement. However, we would like authorities in individual countries to be cautioned against excessively high expectations regarding supervision and examination.

The following various considerations in regard to operational risk reporting are proposed, as described in Paragraphs 43-46.

- Reporting should be classified by normal and stressed market conditions
- The frequency of reporting should change depending on losses arising
- The reports should describe the compliance conditions of the bank’s risk appetite and tolerance statement, details regarding important internal operational risk losses, relevant external events and potential impact on operational risk capital.
- The reporting process should be reviewed periodically

However, the contents described in this principle should be considered best practices, and we feel uncomfortable calling for the principle to be uniformly implemented by all countries. Therefore, we request that the costs or burdens borne be considered when details of the principles are implemented.