Statement Of

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Chairman Reed, Ranking Member Bunning, and members of the Subcommittee, my name is Tim Long and I am the Senior Deputy Comptroller for Bank Supervision Policy at the OCC. I appreciate this opportunity to discuss the OCC's views on risk management – the role it plays in the banks we supervise, the weaknesses and gaps that we've identified in risk management practices and the steps we're taking to address those issues, and how we supervise risk management at the largest national banks.

Recent events have revealed a number of weaknesses in banks' risk management processes that we and the industry must address – and we are taking steps to ensure this happens. More importantly, these events have reinforced that even the best policy manuals and risk models are not a substitute for a strong corporate governance and risk management culture – a tone and approach to business that must be set at the top of the organization and instilled throughout the company.

While risk management practices are, legitimately, the focus of much current attention, risk management is hardest when times are good and problems are scarce. It is in those times when bank management and supervisors have the difficult job of determining when accumulating risks are getting too high, and that the foot needs to come off the accelerator. These are never popular calls to make, but in retrospect, we and bankers erred in not being more aggressive in addressing our concerns. However, we must also not lose sight that banks are in the business of managing financial risks. Banks must be allowed to compete and innovate – and this may, at times, result in a bank incurring losses. The job of risk management is not to eliminate risk but to ensure that those risks are identified and understood so that bank management can make informed choices.

Among the lessons we've learned are: underwriting standards matter, regardless of whether loans are held or sold; risk concentrations can excessively accumulate across product and business lines; asset-based liquidity is critical; backroom operations and strong infrastructure matters; and, robust capital and capital planning are essential. As described in my written testimony, we are taking steps to address all of these issues. Because the current problems are global in nature, we are working closely with my colleagues here and internationally. Critical areas of focus are on improved liquidity risk management, stronger enterprise-wide risk management, including rigorous stress testing, and further strengthening the Basel II capital framework.

Risk management is a key focus of our Large Bank Supervision program. Our program is organized with a national perspective – it is centralized and headquartered in Washington and structured to promote consistent and uniform supervision across the banking organizations. We establish core strategic objectives annually, based on emerging risks. These objectives are incorporated into the supervisory strategies for each bank and carried out by our resident on-site staff, with assistance from specialists in our policy and economics units. Examination activities within a bank are often supplemented with horizontal reviews across a set of banks – this allows us to look at trends not only within but across the industry.

Through our resident staff, we maintain an on-going program of risk assessment, and communication with bank management and the board of directors. Where we find weaknesses, we direct management to take corrective action. For example, we have directed banks to make changes in personnel and organizational structures to ensure that risk managers have sufficient stature and ability to constrain business activities when warranted. Through our examinations and reviews, we've directed banks to be more realistic about recognizing credit risks; to improve their valuation techniques for certain complex transactions; to aggressively build loan loss reserves; to correct various risk management weaknesses; and to raise capital as market opportunities permit.

Finally, the Subcommittee requested the OCC's views on the findings that Ms. Williams from the GAO will be discussing with you today. Because we only recently received the GAO's summary statement of findings, we have not had an opportunity to review and assess their full report. We take findings from the GAO very seriously and will be happy to provide the Subcommittee with a written response to this report once we receive it. My preliminary assessment, based on the summary we were provided, is that the GAO raised a number of legitimate issues, some of which I believe we are already addressing and others, as they pertain to the OCC, may require further action on our part.

Thank you. I'll be happy to answer questions you may have.