



July 23, 2024

Chief Counsel's Office  
Comment Processing  
Docket ID: OCC–2023–0008  
Office of the Comptroller of the Currency  
400 7th Street SW, Suite 3E–218  
Washington, DC 20219

James P. Sheesley, Asst. Executive Secretary  
Comments/Legal OES (RIN 3064–AF29)  
Federal Deposit Insurance Corporation  
550 17th Street NW  
Washington, DC 20429

Ann E. Misback, Secretary  
Docket No. R–1813, RIN 7100–AG64  
Board of Governors of the Federal Reserve  
System  
20th Street and Constitution Avenue NW  
Washington, DC 20551

Re: Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity; OCC Docket ID: OCC–2023–0008; Board Docket No. R–1813, RIN 7100–AG64; FDIC RIN 3064–AF29; 88 Fed. Reg. 64028 (Sep. 18, 2023)

Dear Ladies and Gentlemen:

Better Markets<sup>1</sup> appreciates the opportunity to provide additional comments on the above-captioned proposed rule (“Proposal”) issued by the Office of the Comptroller of the Currency (“OCC”), Board of Governors of the Federal Reserve System (“Fed”), and the Federal Deposit Insurance Corporation (“FDIC”), collectively (“Agencies”).<sup>2</sup>

The Proposal would make several valuable improvements to capital measures for large banks to more accurately reflect risk and shift the burden of that risk to the banks as well as their shareholders and away from the public. One of the key components of the Proposal is the addition

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<sup>1</sup> Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans’ jobs, savings, retirements, and more.

<sup>2</sup> Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity; RIN 1557-AE78, RIN 3064-AF29, RIN 7100-AG64; 88 FED. REG. 64028 (Sep. 18, 2023), <https://www.federalregister.gov/documents/2023/09/18/2023-19200/regulatory-capital-rule-large-banking-organizations-and-banking-organizations-with-significant>.

of a new standardized approach for operational risk measurement at the largest banks. This change would result in a more transparent and comparable risk measure.

Operational risk results from inadequate or failed internal processes, people, and systems, or from external events. The Agencies believe that operational risk is inherent in all banking products, activities, processes, and systems.<sup>3</sup> As Better Markets detailed in its prior comment letter on the Proposal, not only can operational risk result in large costs for banks, but it often has severe and damaging effects on consumers who are harmed by the risky operations.<sup>4</sup>

Bank CEOs and even some regulatory officials, however, have attempted to downplay the severity of operational risk and dismiss the need for capital allocation for it. Better Markets detailed this opposition in a supplemental comment letter to the Agencies and detailed reasons why it is not justified.<sup>5</sup> The truth is that operational risks are evolving and increasing from historical periods. In our prior comment letter, we cited research from the Federal Reserve Board and the Federal Reserve Bank of Richmond that proves these points.<sup>6</sup>

#### New Regulatory Reports Underscore the Severity of Operational Risk and the Need to Intensify the Scrutiny of and Protection Against It

***While regulators have consistently and clearly stated their concerns about operational risk generally,<sup>7</sup> a new report from the OCC showing that half—11 of 22—of the large banks it supervises have inadequate controls over operational risk<sup>8</sup> heightens the concern of its detrimental effects on Main Street Americans and the financial system at large. It also increases the urgency to appropriately allocate capital to protect against these effects.***

Operational risk ratings are part of the Agencies confidential bank ratings system and are normally not disclosed to the public. Instead, the public is left to trust that the regulators are

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<sup>3</sup> *Id.* at 64082.

<sup>4</sup> Better Markets Comment Letter, *Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity* 18-21 (Jan. 16, 2024), <https://bettermarkets.org/wp-content/uploads/2024/01/Better-Markets-Comment-Letter-Regulatory-Capital-Rule-1-16-24.pdf>.

<sup>5</sup> Better Markets Comment Letter, *Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity* 18-21 (May 16, 2024), <https://bettermarkets.org/wp-content/uploads/2024/05/Better-Markets-Supplemental-Comment-Letter-Regulatory-Capital-Rule.pdf>.

<sup>6</sup> Filippo Curti & Marco Migueis, *The Information Value of Past Losses in Operational Risk*, Board of Governors of the Federal Reserve System: Finance and Economics Discussion Series 2023-003 (2023), <https://doi.org/10.17016/FEDS.2023.003>.

<sup>7</sup> *See, e.g.*, OFFICE OF THE COMPTROLLER OF THE CURRENCY, SEMIANNUAL RISK PERSPECTIVE 29-32 (Spring 2024), <https://occ.gov/publications-and-resources/publications/semiannual-risk-perspective/files/semiannual-risk-perspective-spring-2024.pdf>; FEDERAL DEPOSIT INSURANCE CORPORATION, RISK REVIEW 59-60 (2024), <https://www.fdic.gov/analysis/risk-review/2024-risk-review/2024-risk-review-full.pdf>.

<sup>8</sup> *See, e.g.*, Hannah Levitt & Katanga Johnson, *Secret Bank Ratings Show US Regulator's Concern on Handling Risk*, BLOOMBERG (July 21, 2024), <https://www.bloomberg.com/news/articles/2024-07-21/secret-bank-ratings-show-us-regulator-s-concern-on-handling-risk>.

measuring and monitoring the risks appropriately and implementing corrective actions when banks have outsized levels of risk. The recent reporting of insufficient and weak management of operational risk raises serious questions about how much the regulators know about the failure of banks to manage operational risk.

One recent example of large banks' failure to manage operational risk was exposed by the Fed's climate scenario analysis exercise.<sup>9</sup> The results of the exercise revealed dangerous risks and grossly deficient regulation, management, and preparation.<sup>10</sup> The banks tested were six of the largest banks in country, but they were shown to have significant data and modeling challenges when attempting to simply estimate their climate risk for an 'exploratory' test. Furthermore, most of the banks had to rely on third parties because they had serious gaps in information needed for the exercise. These very basic deficiencies are shocking and inexcusable because banks are already required to measure and monitor all relevant risks, no matter the source, and the Fed is supposed to make sure that they do.

At a minimum, the OCC report on operational risk support the Fed's research<sup>11</sup> which concludes that operational risk at the largest banks is persistent over time and a consequence of greater amounts of institutional complexity and moral hazard at too-big-to-fail institutions. Standardized models are unquestionably needed to guard against operational risk because banks' risk appetite is unlikely to change quickly because it is engrained within the culture of a firm.

We urge the Agencies to implement the proposed standard measures for operational risk in the Basel capital framework as soon as practicable. Additionally, regulators must immediately implement corrective actions at the 11 banks with identified operational risk management failures. These failures could range from threats from employee mistakes to legal problems to cybersecurity vulnerabilities. Bank customers and Main Street Americans deserve nothing less than the highest level of vigilance and urgency to protect against such threats.

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<sup>9</sup> Press Release, Board of Governors of the Federal Reserve System, *Federal Reserve Board Releases Summary of the Exploratory Pilot Climate Scenario Analysis (CSA) Exercise That it Conducted With Six of the Nation's Largest Banks* (May 9, 2024), <https://www.federalreserve.gov/newsevents/pressreleases/other20240509a.htm>.

<sup>10</sup> Press Release, Better Markets, *Fed's Big Bank Climate Scenario Results Reveal Dangerous Risks and Grossly Deficient Regulation, Management and Preparation* (May 10, 2024), <https://bettermarkets.org/newsroom/feds-big-bank-climate-scenario-results-reveal-dangerous-risks-and-grossly-deficient-regulation-management-and-preparation/>.

<sup>11</sup> Filippo Curti, W. Scott Frame, & Atanas Mihov, *Are the Largest Banking Organizations Operationally More Risky?*, Federal Reserve Bank of Dallas Working Paper 2016 (Mar. 3, 2020), <https://doi.org/10.24149/wp2016>.

We hope these comments are helpful as the Agencies finalize this Proposal.

Sincerely,



Dennis Kelleher  
Co-founder, President and CEO  
[dkelleher@bettermarkets.org](mailto:dkelleher@bettermarkets.org)

Shayna M. Olesiuk  
Director of Banking Policy  
[solesiuk@bettermarkets.org](mailto:solesiuk@bettermarkets.org)

Better Markets, Inc.  
2000 Pennsylvania Avenue, NW  
Suite 4008  
Washington, DC 20006  
(202) 618-6464  
<http://www.bettermarkets.org>