

AMA framework and determining its operational risk exposure.

S 14. The institution must have clear standards for the collection and modification of the elements of the operational risk AMA framework.

S 15. The institution must have at least five years of internal operational risk loss data¹⁷ captured across all material business lines, events, product types, and geographic locations.

S 16. The institution must be able to map internal operational risk losses to the seven loss-event type categories.

S 17. The institution must have a policy that identifies when an operational risk loss becomes a loss event and must be added to the loss event database. The policy must provide for consistent treatment across the institution.

S 18. The institution must establish appropriate operational risk data thresholds.

S 19. Losses that have any characteristics of credit risk, including fraud-related credit losses, must be treated as credit risk for regulatory capital purposes. The institution must have a clear policy that allows for the consistent treatment of loss event classifications (e.g., credit, market, or operational risk) across the organization.

S 20. The institution must have policies and procedures that provide for the use of external loss data in the operational risk framework.

S 21. Management must systematically review external data to ensure an understanding of industry experience.

S 22. The institution must have a system to identify and assess business environment and internal control factors.

S 23. Management must periodically compare the results of their business environment and internal control factor

assessments against actual operational risk loss experience.

S 24. Management must have policies and procedures that identify how scenario analysis will be incorporated into the operational risk framework.

S 25. The institution must have a comprehensive operational risk analytical framework that provides an estimate of the institution's operational risk exposure, which is the aggregate operational loss that it faces over a one-year period at a soundness standard consistent with a 99.9 per cent confidence level.

S 26. Management must document the rationale for all assumptions underpinning its chosen analytical framework, including the choice of inputs, distributional assumptions, and the weighting across qualitative and quantitative elements. Management must also document and justify any subsequent changes to these assumptions.

S 27. The institution's operational risk analytical framework must use a combination of internal operational loss event data, relevant external operational loss event data, business environment and internal control factor assessments, and scenario analysis. The institution must combine these elements in a manner that most effectively enables it to quantify its operational risk exposure. The institution can choose the analytical framework that is most appropriate to its business model.

S 28. The institution's capital requirement for operational risk will be the sum of expected and unexpected losses unless the institution can demonstrate, consistent with supervisory standards, the expected loss offset.

S 29. Management must document how its chosen analytical framework accounts for dependence (e.g., correlations) among operational losses across and within business lines. The institution must demonstrate that its explicit and embedded dependence

assumptions are appropriate, and where dependence assumptions are uncertain, the institution must use conservative estimates.

S 30. Institutions may reduce their operational risk exposure results by no more than 20% to reflect the impact of risk mitigants. Institutions must demonstrate that mitigation products are sufficiently capital-like to warrant inclusion in the adjustment to the operational risk exposure.

S 31. Institutions using the AMA approach for regulatory capital purposes must use advanced data management practices to produce credible and reliable operational risk estimates.

S 32. The institution must test and verify the accuracy and appropriateness of the operational risk framework and results.

S 33. Testing and verification must be done independently of the firm-wide operational risk management function and the institution's lines of business.

Dated: July 17, 2003.

John D. Hawke, Jr.,

Comptroller of the Currency.

By order of the Board of Governors of the Federal Reserve System, July 21, 2003.

Jennifer J. Johnson,

Secretary of the Board.

Dated at Washington, DC, this 11th day of July, 2003.

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Executive Secretary.

Dated: July 18, 2003.

By the Office of Thrift Supervision.

James E. Gilleran,

Director.

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¹⁷ With supervisory approval, a shorter initial historical observation period is acceptable for banks newly authorized to use an AMA methodology.