Banking and Finance Law Daily Wrap Up, FINANCIAL STABILITY—March 2023 events prompt OCC to propose revised recovery planning guidelines, (Jun. 25, 2024)

Banking and Finance Law Daily Wrap Up

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The OCC seeks to ensure that banks with assets in the $100 billion to $250 billion range can effectively "respond to the financial effects of severe stress, particularly in light of the contagion effects and systemic risks they may pose."

The Office of the Comptroller of the Currency (OCC) has proposed revised recovery planning guidelines. The revised guidelines are to apply to certain large insured national banks, federal savings associations, and federal branches. According to the OCC's notice, public comments on the proposal are due within 30 days after the notice's publication date in the *Federal Register*.

Three objectives. As described by the OCC, the proposal's three main objectives are to:

- expand recovery planning guidelines to apply to banks with at least $100 billion in assets;
- incorporate a standard for testing recovery plans; and
- clarify the role of operational and strategic (*i.e.*, non-financial) risk in recovery planning.

2008 financial crisis. The OCC's notice of proposed rulemaking began with the observation that large-scale financial crises, including the 2008 crisis, have demonstrated how severe stress can have a destabilizing effect on financial entities, capital markets, the federal banking system, and the U.S. and global economies. The OCC said it observed that many financial institutions were not prepared to respond effectively to the 2008 crisis. Lack of planning "threatened the viability of some financial institutions." Many were forced to take significant actions without a well-developed recovery plan. The OCC said it recognized that recovery planning would reduce risk and increase the likelihood that a bank would return to financial strength after severe stress.

2016 guidelines. The OCC said it initially expected recovery planning to assist bank boards and management to focus on risk governance and lessening fallout from future severe stress. Toward that end, in 2016, the OCC issued "Guidelines Establishing Standards for Recovery Planning by Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches of Foreign Banks (Guidelines)." Under those Guidelines, covered banks would have a recovery plan including:

- risk indicators reflecting its particular vulnerabilities;
- a range of credible response options; and
- an assessment and description of how such options would affect it.

2018 amendments. The OCC reviewed how it amended the Guidelines in 2018 to raise the applicability threshold to banks with total consolidated assets of $250 billion, up from $50 billion. However, in March 2023, the OCC found that several insured depository institutions with total consolidated assets under the $250 billion threshold, who were not subject to recovery planning, failed. The OCC said this "made clear" the importance of recovery planning at below the $250 billion threshold. The proposed revision to applicability will primarily require banks with average total consolidated assets of $100 billion or more to engage in recovery planning.

Consolidated assets. The OCC also proposes to change what is meant by consolidated assets in order to:

- clarify the definition of "average total consolidated assets" such that calculating them will be based on the "total assets" line of the Call Report, not the "average total consolidated assets" line of the Call Report, such that this may effect the quarter in which a bank becomes a covered bank;

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- change the reservation of authority paragraph to potentially apply the Guidelines to banks with average total consolidated assets of under $100 billion if the bank is "highly complex or otherwise presents a heightened risk that warrants application of the Guidelines."

The OCC invited comment on the proposed $100 billion threshold and whether and why the OCC should use some other threshold.

Testing. The OCC stressed the importance of testing recovery plans to ensure they will be effective during periods of severe stress. Testing may involve simulating various scenarios involving both financial and non-financial stress pertinent to a covered bank's "particular vulnerabilities." The OCC said its proposal does not specify a testing format or method; however, testing ought to be "risk-based and reflect the covered bank's size, risk profile, activities, and complexity." Here, the OCC asked the public to respond to a variety of questions about whether and how the OCC should be more specific about recovery plan validation, implementation, impact assessment, and frequency of testing.

Non-financial risk. The OCC observed that covered banks also need to consider non-financial risks, like operational and strategic risks, because they have generally been less successful in addressing them. Neglecting non-financial risks "overlooks the very real threats that non-financial risks can pose to a bank's financial strength and viability." Innovation and digitization are two wild cards.

Here, the OCC proposes the following changes to the Guidelines:

- additional language stating that a covered bank's recovery plan should consider both financial and non-financial risks.
- conforming changes to the definitions of "recovery" and "trigger" to the recover plan elements of "trigger" and "impact assessment."
- integration of a covered bank's recovery plan into other risk governance functions and alignment with the bank's other plans, to make it clear that recovery should complement and not replace other risk governance and planning functions, including those that address non-financial risks, *e.g.*, business continuity and operational resilience planning.

Here, the OCC requested public comment on, among other things, whether its proposed guidelines are sufficiently clear and specific and whether it should identify specific risks like those used in the Comptroller's handbook.

Compliance. The OCC said it understands it will take time for covered banks to implement the proposed changes. The OCC is proposing that currently covered banks would have 12 months to comply with changes. Newly covered banks will have 12 months to comply, apart from 18 months to comply with testing requirements. Here, the OCC posed various questions to the public about whether the OCC should adopt a shorter or longer compliance date or whether the compliance dates should differ for non-financial risks and plan testing.

Comment submission. The OCC urged the public to submit comments through the Federal eRulemaking Portal under "Docket ID OCC-2024-0008" and using the title "OCC Guidelines Establishing Standards for Recovery Planning by Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches." Mailing or hand delivering comments are also possible. The public is asked to refer to "regulations.gov" or the OCC's notice for more details.

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