

Breakout 1:
Bank Director 101: Risk Primer

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Bank Director
#BBTF24

Bank Board Training Forum

Risk Primer

What you should know

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US\$9.4bn



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The Why

FED NOTES

Why hundreds of U.S. banks may be at risk of failure

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FDIC Problem Bank List:

August 21, 2024 By Marco Santarelli

US Banks Paying \$470,000,000 To Regulators Over Widespread Recordkeeping Failures and 'Off-Channel' Communication Methods

Henry Kanapi • August 25, 2024 // REGULATORS



Problem Bank List: Is Your

- Obtaining a Lien Release
- Borrower's Guide
- Resources for Court Clerks and Law Enforcement Agencies

Republic First Bank dba Republic Bank	Philadelphia
Citizens Bank	Sac City

THE CONVERSATION

TD Takes \$2.6 Billion Hit on US Probe, Sells Schwab Shares

Collapse in 2024... Led to the Failure of Republic Bank

\$136 million... fine Citigroup... taking too long to fix internal control issues

Small Banks Are Teetering. Expect

U.S. banks are... secret report finds

Politics + Society Science + Tech Podcasts
of another US

Risk 101 Overview

What is Risk?



- Uncertainty of an outcome
- Negative consequences
- The possibility or frequency with which something bad happens.
- Risk and reward are intertwined.
- There are risks I may want to take - Risk Appetite
- But there are risks and levels of risk that I don't - Risk Tolerance

Risk Management: Basics



Identification

- Define the nature of risk
- Sources of risk
- Why they pose a threat



Assessment and Analysis

- Assess the likelihood and potential impact of each risk
- Prioritize those that need most attention



Mitigation

- Design and implement policies and processes to limit the chance of risks becoming threats and minimize any damage

Example types of risk facing a bank



Credit

Risk of default on a bank loan



Operational

Cyber, fraud, IT failure, Third Party



Market

Interest risk, currency risk, equity risk



Liquidity

Asset Liability imbalance



Legal and
Compliance

Regulatory sanctions

Federal Reserve Expectations:

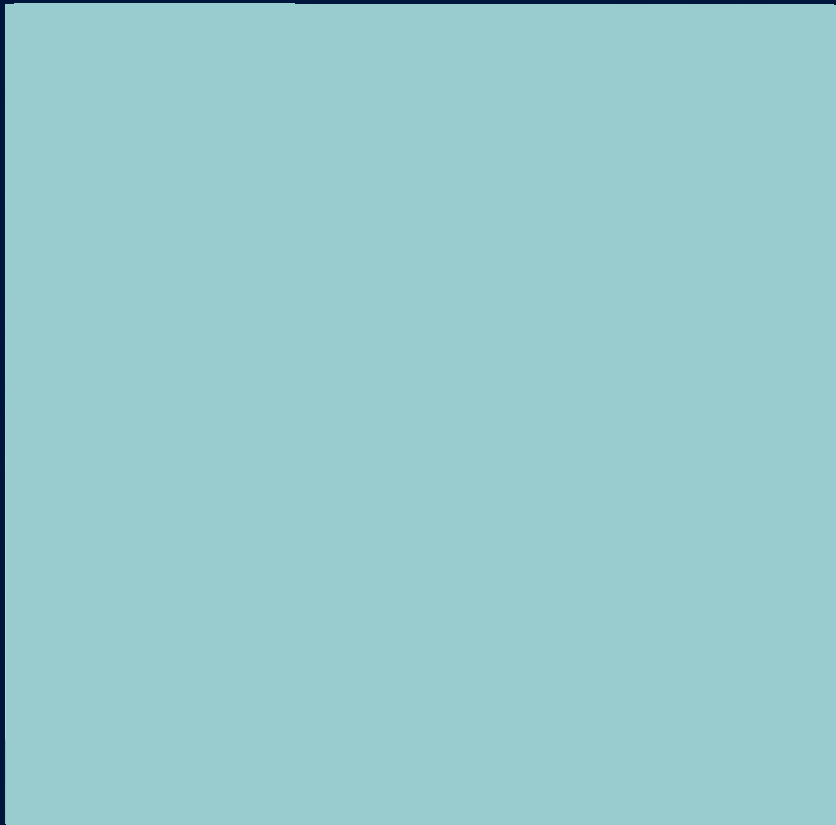
- Board and Senior Management Oversight
 - Policies, Procedures, and Limits
 - Risk Monitoring and Management Information Systems
 - Internal Controls
-
- 5-point rating systems: 1 is Strong, 5 is unsatisfactory
 - Rating can affect institution's CAMELS rating*

*Capital Adequacy, Asset Quality, Management, Earnings , Liquidity and Sensitivity

Board versus Senior Management role

- Boards of directors have **ultimate responsibility** for the level of risk taken by their institutions. Accordingly, they should **approve** the overall business strategies and significant policies of their organizations, including those related to **managing and taking risks**, and should also **ensure** that senior management is fully capable of managing the activities that their institutions conduct.
- Senior management is responsible for **implementing** strategies in a manner that **manages, monitors, and mitigates risks** associated with each strategy and that **promotes compliance** with laws and regulations on both a long-term and day-to-day basis.

Three Lines of Defense



Distributed/Ad Hoc
Owns and
Manages
deliberate
testing



Board Conversations: How does management know that they have identified ALL the most important risks?

- Sources of information
- Risks in response to change
- Risk associated with internal developments
- Hot Lines and customer complaints
- Regulatory guidance
- External Factors
- Peers
-



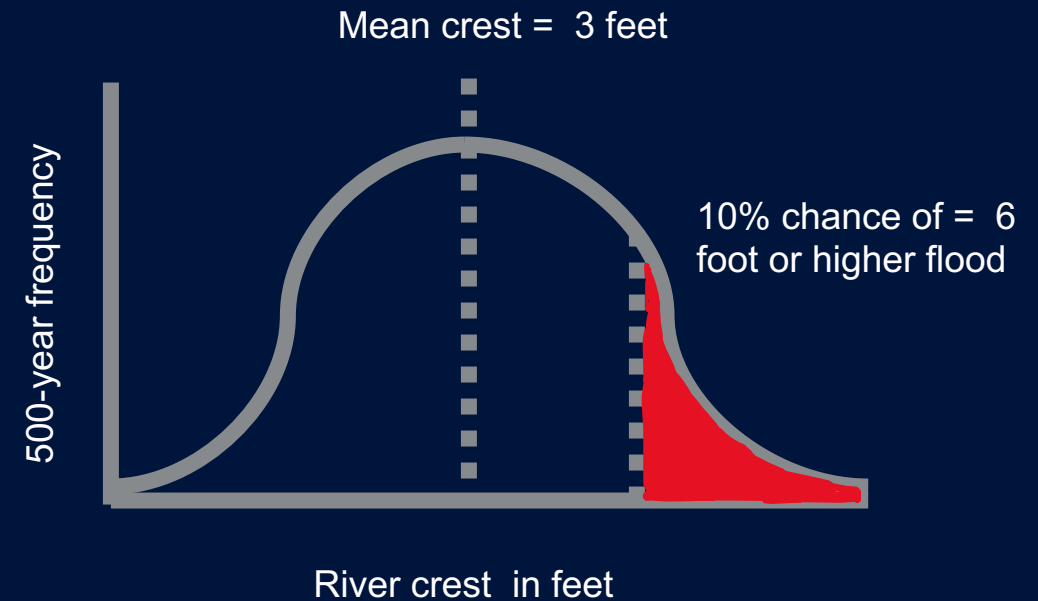
Board Conversations: How does management know all risk have been properly assessed and evaluated?

- What is the approach to measuring risk
- What are our key assumptions
- Have we considered black swan events
- Do we do scenario and "what if" analysis
- How do we know risk modelling is effective
- What's been our experience of loss events
-

Board Conversations: How does management know all risk are mitigated effectively?

- Is our risk appetite appropriate
- Are risk tolerances appropriate
- Are our risk reporting systems effective
- How do we know controls are operating
- Are we organized effectively
- What does Internal / External Audit say
- Is our control environment efficient

Real life – it gets more complicated



- Risk is not binary
- Using experience of loss
- We can calculate and model the Value At Risk
- This is used to make informed risk decisions

But keep sight of the wood despite the trees



- Banks cannot make money without taking risk
- The Board's role in risk management is fundamental
- Agree Risk Appetite and Risk Tolerance
- Understand the three lines of defense
- Ask good questions of Management
- Acknowledge that Risk Management is not always simple



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