Remarks by

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The Globalization of Bank Supervision

I am honored to be the guest of your company and your country, and deeply appreciative of the many courtesies shown me since my arrival in Japan.

Whenever I travel abroad, I am reminded of how much smaller the world has become. This is perhaps not so striking to younger people, who take for granted the ability to exchange ideas in real time wherever an Internet connection exists. But for those of us of an earlier generation, the extent of global integration and the speed of communications are nothing short of astonishing. Among other things, technology has made possible the unparalleled efficiency of modern capital markets, which have stimulated commerce, economic development, and productivity, with a consequent improvement in living standards for more of the world's people.

The interconnected world, however, offers risks as well as opportunities. Almost every day brings evidence of the difficulty of preventing one country's problems from spilling over to affect neighbors and neighbor's neighbors. Lately, the world has rallied to the defense of the West African countries dealing with a dreaded virus, in hopes of stopping it at their shores. Global threats require a global response. But the steps we take collectively must be compatible with our respective national cultures and institutional frameworks.

That is equally true when the viruses are of the sort that compromise the security of our information systems. Leaders of business and industry increasingly tell us that hackers and cybercriminals represent the biggest threat to the global economy today. That is a plausible argument—although I would point out that the threat extends well beyond the realm of economics to the information systems upon which our governments, defense structures, and public utilities depend.

Still, cyber criminals are especially attracted to banks, for the obvious reasons that banks hold so much of the world's wealth and so much exploitable information about their customers. Banks in the U.S. and elsewhere have spent billions of dollars building and maintaining robust information systems and billions more to repair the breaches that seem to occur with alarming regularity. I need not point out that those are billions that would otherwise have been available to invest in economic expansion.

For these reasons, strengthening cybersecurity in the part of the U.S. banking system that the OCC supervises has been perhaps my foremost priority as Comptroller of the Currency. Hackers and cyber criminals, however, do not respect regulatory—or national—boundaries. That is why U.S. government bodies like the Financial and Banking Infrastructure Committee of the President's Working Group on Financial Markets, the Financial Stability Oversight Council (FSOC), and the Federal Financial Institutions Examination Council, or FFIEC, emphasize the importance of coordination and communication among financial regulators at home and abroad, and between the public and private sectors. It is also why, in my current capacity as chairman of the

FFIEC, I have advocated for the closest collaboration between the OCC and the other agencies with which we share responsibility for the safety and soundness of the U.S. financial system. Working together, we have stepped up monitoring of U.S. banks to assess their readiness to deal with cyberattacks. We issued guidance to help banks manage the risks with third-party providers, especially those providers with access to the banks' information systems. And we are using a variety of media to provide bankers with information on current threats and vulnerabilities, and advice on how best to address those challenges.

But there is growing recognition that cyber security is a global issue that requires a global response—a response that cuts across economic sectors and national borders. Regional institutions like the European Parliament and the South East Asian Central Bank (SEACEN) are sponsoring international conferences on cyber security, disseminating best practices, and encouraging banks to understand that information security is an area in which cooperation must trump competitive considerations. It is essential that we do everything possible to ensure that our information systems and all their interconnections are capable of withstanding cyberattacks, no matter where they are launched, what form they take, and what motivates the attackers.

There is, of course, another powerful contemporary example of how risk transcends borders. The financial crisis of 2007 and 2008 began in the United States, but it quickly became a global crisis, marked by plunging asset values and commodity prices, disruption of international trade, and rising unemployment across most advanced countries. The recession that began in the United States officially ended in 2009, but recovery in many countries has been dishearteningly slow, and the effects have been a drag on the entire global economy.

In the wake of the crisis, bank regulators and central banks were roundly criticized for failing to take effective preemptive action against speculation fueled by low interest rates. Some of this criticism was entirely justified. We need to learn from the experience how to do our jobs better, so that problems in the financial system can be contained and future meltdowns averted.

Fortunately, if globalization has increased the exposure to risk, sovereign nations no longer have to cope with it alone. They can—and do—draw upon the differing perspective and experiences of international colleagues.

The OCC has long provided technical assistance in response to requests from banking regulators in countries around the world. Last year, we asked a group of regulators from three countries to take a hard look at our supervisory work and offer recommendations for how we might improve. This "peer review" committee found much to admire about our approach to supervision. But they also found areas where they thought we could do better, and we are taking their recommendations very seriously.

To broaden our view of trends and emerging risks in the industry, they encouraged us to expand our use of "lead experts," typically, examiners who focus in a targeted manner on specific risk areas across multiple institutions. We are doing just that.

They recommended that we implement a rotation program to limit the time examiners spend at any one bank, thus ensuring that examiners bring a fresh perspective to their jobs.

They offered suggestions for revising and enhancing our risk assessment system, which we use to evaluate risks within and across the banks we supervise, so that banks have a clearer understanding of our supervisory expectations. Those initiatives are now underway.

The recent work of the Basel Committee on Banking Supervision and other international regulatory groups offers a compelling illustration of what can be accomplished through collective action. Of course, the Basel Committee this year marked the 40th anniversary of its founding as the international standard-setter and sounding board for global supervisors, so it is hardly a newcomer to the scene. But the crisis has lent urgency, as it should have, to the Basel process and lent credibility to the Basel core principles of bank supervision. Recognizing the global character of risk, countries increasingly contribute to, and rely on the Basel Committee's work and on its support to strengthen the supervisory arrangements in their respective countries.

The latest Basel III standards and the Dodd-Frank Act in the United States were developed in parallel and were based on the same essential approach to reducing the threat to financial stability posed by systemically important financial companies. Even so, U.S. regulators have faced a particular challenge reconciling the two regimes. Basel III provided for a narrower definition of capital, higher minimum capital levels, a capital conservation buffer, and higher risk-weighted asset amounts on certain assets. Dodd-Frank required U.S. regulators to adopt higher prudential standards for systemically important financial institutions. Among the many steps U.S. regulators have taken to address this Dodd-Frank mandate was to increase non-risk weighted leverage ratios. Thus, this past April, U.S. regulators finalized the enhanced supplementary leverage ratio, which requires the largest, most systemically important holding companies to maintain a 5 percent leverage ratio in order to be free from certain restrictions on distributions and their U.S. depository institution subsidiaries to maintain a 6 percent leverage ratio in order to be considered "well capitalized."

Standard-setting for liquidity risk management took a very similar path. Basel's updated 2013 standards provided that, starting in January 2015, internationally active banks must hold sufficient High Quality Liquid Assets (HQLA) to meet their liquidity needs during a 30-day stress scenario. Again, U.S. regulators built on the Basel standards and adapted them to U.S. circumstances. Our final rule, which was adopted this past September, is more stringent than the Basel standard in several areas, including the range of assets that will qualify as HQLA, the assumed rate of outflows for certain types of funding, the calculation of total net cash outflows, and the required compliance timeline. We have defined "covered companies" to exclude community banks, as well as bank holding companies with substantial insurance operations, "bridge banks" that may be used in the course of bank resolutions, and federal branches and agencies.

The result, we believe, is a rule that accomplishes Basel's goal of promoting the short-term resilience of major financial institutions while accommodating the United States' unique banking structure and climate.

With the finalization of the liquidity risk rule, attention is turning to other important items on the Basel Committee's agenda. The agenda includes capital standards for interest rate risk and disclosure standards. For capital standards on interest rate risk, U.S. and Japanese experts, including the Japanese leader of the Basel Task Force on Interest Rate Risk, have worked hand-in-hand, arguing against overly prescriptive formulas, favoring instead more flexible rules that give appropriate discretion to national regulators. In particular, these experts have worked together to broaden the discussion to include strengthening of supervisory practices, as well as the development of possible additional international capital standards. We have also argued together for the considered and thoughtful development of new standards on bank disclosure.

No one should be surprised by the close confluence of viewpoints between our two countries on these important issues. Among other things, it reflects the close relationship U.S. and Japanese bank supervisors have built over the years. That relationship has brought my predecessors and me to Japan to address this group whenever the invitation has been extended to us. It reflects the frequent exchanges, both formal and informal, that occur between representatives of the OCC and the Japanese Financial Services Agency. We attend each other's conferences and participate in each other's "supervisory colleges," which I believe is a very promising approach to supervising global banks and developing multilateral responses to large bank-specific crises.

Yet I think the alignment of U.S. and Japanese views on supervisory matters have other important root causes. Because both countries have highly developed financial institutions and markets, we face similar regulatory and supervisory challenges when it comes to detecting emerging risks and maintaining financial stability. It should not be surprising, therefore, that our two countries operate from very similar principles of bank supervision.

Japan's FSA aims to "develop an environment in which people can use a wide range of financial instruments and services with a sense of security and trust." The OCC's mission statement speaks to the responsibility of ensuring the banks under its supervision operate “in compliance with laws requiring fair treatment of consumers and fair access to credit and financial products.” The FSA aims to “continuously ensure the stability of the financial system . . . to facilitate the supply of funds for various investment needs both within and outside Japan,” a function it discharges through “strict inspection and supervision” of financial institutions. That would also be a fair description of the OCC’s mission and the approach we take to achieve it.

Given the myriad of risks we face in our increasingly interconnected world, maintaining a resilient financial sector is undoubtedly a formidable challenge. Constructive relationships like the one between our two countries are essential to meeting that challenge. May that relationship continue to flourish.

Thank you.