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The OCC's Final Guidance for Recovery Planning: Getting Started Guide

*By Michael Nonaka and Randy Benjenk**

Recovery planning will be a key focus of the Office of the Comptroller of the Currency and other banking regulators in the coming months and years. This article is intended to help covered banks get started with recovery planning and preparing their inaugural plans for review by the OCC, by describing action items that should be completed as part of the recovery planning process.

The Office of the Comptroller of the Currency (“OCC”) issued final guidance for recovery planning (“Guidance”) in late 2016. The Guidance applies to insured national banks, federal savings associations and federal branches of foreign banks with average total consolidated assets of \$50 billion or more (covered banks). The Guidance has a phased-in compliance period: covered banks with at least \$750 billion in assets have been required to comply since July 1, 2017; covered banks with at least \$100 billion and less than \$750 billion have been required to comply by January 1, 2018; and covered banks with at least \$50 billion and less than \$100 billion are required to comply by July 1, 2018.

BACKGROUND

At its core, recovery planning consists of the development of scenarios, triggers and options. The scenario establishes the macroeconomic conditions and bank-specific conditions that reflect financial stress that adversely affects the bank's financial condition. The scenario causes the breach of various quantitative or qualitative recovery triggers that signal stress and set in motion certain governance processes internally that lead to the bank's evaluation of various recovery options. Recovery options, if implemented, are intended to respond to the financial stress experienced by the bank and to return the bank to a stable financial condition. However, despite this simple framework, recovery planning requires significant resources and attention from the board of directors and senior management.

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Similar to resolution planning, developing a recovery plan that complies with the Guidance requires input from several internal stakeholders within a covered bank as well as a concerted effort on the part of the bank's management to develop a plan that is comprehensive, appropriately supported by data and realistic assumptions, consistent with resolution, liquidity and capital planning analyses, and based on a thorough analysis of the bank's financial condition and the effects that various recovery measures would have on such condition.

Recovery plans focus on the information that signals severe financial stress to an institution and the remedial measures that the institution can deploy to avoid failure. Recovery planning often is described in conjunction with the resolution planning required of systemically important bank holding companies ("bank SIFIs") and nonbank systemically important financial institutions ("nonbank SIFIs"). Whereas resolution planning is focused on mitigating the risk to financial stability from an institution's failure, recovery planning is concerned with avoiding failure altogether. Resolution planning posits failure and requires the institution to plan its resolution in a rapid and orderly manner. Recovery planning assumes financial stress that, if not addressed, could lead to the institution's failure and requires the institution to consider how it would learn about that stress and respond to it.

Importantly, the Guidance does not have a formal submission date for a covered bank to submit its recovery plan to the OCC, unlike resolution plans that must be submitted to the Federal Deposit Insurance Corporation ("FDIC") and the Board of Governors of the Federal Reserve System ("Federal Reserve"). A covered bank's recovery plan will be reviewed by the bank's OCC supervisory team as part of the supervisory process, and the plan is required to be reviewed and approved by the covered bank's board of directors or a committee thereof.

The consequences for failing to comply with the Guidance include a potential public enforcement action if the covered bank does not submit a credible plan for complying with the Guidance. Both recovery planning and resolution planning are integral to the federal banking agencies' supervision of large and interconnected banking organizations.

This article is intended to help covered banks get started with recovery planning and preparing their inaugural plans for review by the OCC, by describing action items that should be completed as part of the recovery planning process.

ACTION ITEMS

Preparing to Develop the Plan

Developing the bank's first recovery plan from scratch may initially seem

overwhelming. However, dividing the process into various phases, each with a specific set of action items, can make the process more manageable and help produce a well-written and thought-out plan. The following framework may prove helpful in approaching this significant initiative.

PHASE	Preparing to develop the plan	Core recovery plan analysis	Production and implementation to business as usual (BAU)
ACTION ITEMS	<ul style="list-style-type: none">• Set up project• Involve board of directors and senior management• Collect data and information	<ul style="list-style-type: none">• Develop overview of the bank• Develop recovery scenarios• Identify recovery triggers• Identify and analyze recovery options• Analyze applicable governance and reporting processes	<ul style="list-style-type: none">• Integrate with related plans and processes• Develop communications plan• Implement or leverage existing testing framework• Be mindful of potential consequences of a deficient plan

Set Up Project

The overall success of a project with the magnitude of a recovery plan is often based on the planning and work performed before the project starts. It is essential to obtain the appropriate level of sponsorship from senior management and to set the “tone from the top” of the importance of the plan. Education and knowledge-sharing sessions on recovery planning conducted early in the process can help level set and clarify project objectives.

In terms of project structure, one suggested approach is the establishment of a project team (sometimes known as a working group) and a steering committee. The project team will take primary responsibility for completing the plan and meeting deadlines. Where feasible, the project team should leverage the existing risk governance structure and include functional representation from the bank’s Treasury (Liquidity, Capital, ALCO), Legal, Finance/Controllers, Stress Testing and Risk Management units. Given recovery planning’s close ties with resolution planning, the bank should consider leveraging existing resolution planning team members to access relevant knowledge and establish robust integration with resolution planning efforts, where applicable.

The steering committee, composed of a subset of senior leaders, will meet periodically to review progress and facilitate strategic decision-making. The project team should report progress to the steering committee at key milestones in the plan’s development, including, but not limited to, presenting the committee with a well-defined project scope; a detailed project plan; roles and

responsibilities; a timeline for deliverables; and potential scenarios, triggers and options.

Involve Board of Directors and Senior Management

The Guidance contemplates a significant role for the board of directors and senior management with respect to recovery planning, and OCC examiners may well focus on these roles in their initial compliance reviews. The board of directors is responsible for overseeing the bank's recovery planning process, while management is responsible for developing the plan. The Guidance requires the board, or a board committee, to review and approve the recovery plan at least annually and more frequently, if needed, to address significant changes made by management.

Senior management is required to review and update the plan at least annually and in response to material events. Such revisions should reflect material changes in the bank's size, risk profile, activities and complexity. Recovery planning requires a bank to make strategic choices regarding its recovery options and how they would be implemented, which may require input from senior management and potentially the board.

Recovery planning may also require gathering a considerable volume of data from different units at the bank, so it is critical to have buy-in and engagement from senior management in order to move along information requests. The board should understand how recovery planning relates to other contingency planning exercises such as capital planning and resolution planning. Banks should consider whether it is more appropriate for the board to assess different types of contingency plans in a single board session—to enable evaluation of these plans in an integrated manner—or at different times so that there is less opportunity for confusion and information overload.

Collect Data and Information

Financial institutions already have a significant amount of information readily available that can be leveraged for the creation of bank recovery plans. Gathering and assembling such existing information during the project initiation phase is time well spent. Not only does leveraging such information save time and effort, but it also helps to facilitate the broader plan integration and alignment process. The Guidance requires the bank to integrate its recovery plan into its risk governance function and to align the recovery plan with other plans of the bank and its holding company, such as business continuity plans, contingency funding plans, capital plans, liquidity plans, stress-testing documents and resolution plans.

In addition to gathering the aforementioned plans, as well as any related policies and procedures, the following types of information should be collected:

General Information	Financial Information	Operational Information
<ul style="list-style-type: none"> • Business overview, description of business units and operating segments • Overview of legal entity structure • Mapping of each of the above business units into the major legal entities in which it books assets, revenues or income • Description of risk management framework 	<ul style="list-style-type: none"> • Historical and forecasted financial statements, including balance sheet and income statement • Key financial metrics for each business line • Overview of funding and liquidity plans (including intercompany items) 	<ul style="list-style-type: none"> • Description of shared service functions • Inventory of key agreements (third party, customer and service level) • Financial and operational interconnectedness between legal entities and core businesses • Key performance indicators (KPIs)

CORE RECOVERY PLAN ANALYSIS

Develop Overview of the Bank

Each recovery plan begins with an overview of the bank. At first glance, it would seem easy to dismiss this section as perfunctory by copying language from another general description of the bank (e.g., securities disclosure) or including only a summary, high-level overview. However, there are several reasons to resist this temptation and to develop a comprehensive and thoughtful overview.

First, the overview section presents an opportunity to strategically frame the recovery analysis. For example, if the plan includes triggers relating to liquidity, and liquidity concerns form a key component of recovery plan scenarios, the background section could provide a high-level overview of the bank's sources of liquidity, ability to access additional forms of liquidity, and the bank's liquidity risk management and control frameworks.

Second, the recovery plan needs to be a stand-alone document with sufficient background information to inform the reader about the bank and its legal entities, organizational structure, critical operations, core business lines and core management information systems. The plan should be sufficiently clear to "tell the story" to the bank's board, senior management and the OCC. The OCC will review the content and efficacy of the plan in the course of its supervisory work. In certain instances, the OCC review team may not have specific knowledge of the bank and its activities, so it is important that the bank provides a clear and cohesive plan.

Develop Recovery Scenarios

Each recovery plan should include a range of bank-specific and market-wide stress scenarios, considered individually and in the aggregate, that are immediate and prolonged. These scenarios should be extreme but plausible and should reflect the bank's specific vulnerabilities based on the nature of its business activities.

The recovery plan should assess how each scenario would impact the bank, particularly its capital, liquidity, funding, profitability, material legal entities, critical operations and core business lines. This should also include an analysis of the impact to internal operations more broadly along with access to market infrastructure.

Examples of Aspects of Stress Scenarios	
Market-wide	Bank-specific
Disruption of domestic and global financial markets, failure or impairment of systematically important financial industry participants, significant changes in debt or equity valuations, currency rates, interest rates, interruption of critical infrastructure	Fraud or litigation loss, portfolio shock, significant cyber-attack or other wide-scale operational event, accounting or tax issue, reputational crisis, failure of significant affiliate

The successful development of credible recovery scenarios is critical to testing the effectiveness of the bank's chosen recovery options—in particular, their scale, speed, flexibility and suitability. In fact, the impact of the scenarios on the metrics tracked as part of the bank's recovery triggers and early warning indicators may lead to a recalibration of the scenarios, triggers or both.

Additional items for consideration in the development of scenarios include the following:

Additional Items for Consideration in the Development of Scenarios
<ul style="list-style-type: none"> • Length of time required to recover from specific scenarios and reach financial stability • Potential internal contagion effects (business line impacts may compromise franchise value) • Potential issues associated with the failure of significant business, operations or affiliates designated as "core," "critical" or "material."

Identify Recovery Triggers

Recovery planning should include the identification of triggers that indicate a crisis scenario and need for recovery actions. Banks should consider potential quantitative and qualitative triggers. Banks should also align their triggers, to the greatest possible extent, with their existing risk governance framework.

Leveraging existing metrics and utilizing information that is already monitored will help facilitate the transition to business as usual (“BAU”) and mitigate the need for new processes.

Examples of Various Trigger Types	
Capital	Liquidity
<ul style="list-style-type: none"> • Decrease in capital ratio(s) • Sustained decrease in profitability 	<ul style="list-style-type: none"> • Decrease in liquidity coverage ratio (LCR) • Withdrawal of deposits/funding sources • Increased collateral requirements
Credit/Market	Operational
<ul style="list-style-type: none"> • Widening of the bank's credit default swap (CDS) spreads • Decrease in interbank or treasury rates • Default of top counterparty • Significant draws on lines of credit by customers • Credit rating downgrade 	<ul style="list-style-type: none"> • Idiosyncratic events that result in a severe financial loss (e.g., cyber-attack or other events); recovery options should address the financial, not operational, impact of these events

Triggers most suitable for a bank will include those that are not only plausible to occur, but are also severe enough that they could reasonably be expected to threaten the bank's ongoing viability if the bank does not implement recovery options.

The trigger framework should enable timely activation of the recovery plan and include escalation procedures tied to the governance process and pre-established actions designed to confirm that a breach of a trigger is brought to the attention of senior decision-makers. In addition to triggers, many recovery plans often include less severe monitoring thresholds (sometimes known as “early-warning indicators”) that serve to heighten awareness and identify potential financial stress for the bank.

Identify and Analyze Recovery Options

Recovery options must be suitable for achieving recovery in the selected scenarios and have a materially positive impact on capital or liquidity, within executable time frames. Recovery options can be viewed as a menu of material actions available to be taken in isolation or in concert.

Examples of Various Recovery Options		
Dispositions	Capital/Liquidity	Business Tools
<ul style="list-style-type: none"> • Business lines • Country operations • Legal entities • Sale of trading assets/portfolio 	<ul style="list-style-type: none"> • Raising non-equity capital • Conducting liability management exercises • Reducing dividends • Raising fresh equity 	<ul style="list-style-type: none"> • Reducing new lending • Putting part of the business into runoff

Once the bank identifies its possible list of options, it should evaluate each option based on a series of success probability factors such as ease of execution, expected impact, feasibility and dependencies. As part of this exercise, the bank should quantify the expected impact of each recovery option on its capital and liquidity, calculate the timing of execution, and assess the probability of success. Other items for consideration include the following:

- Clarifying the role of the bank's holding company;
- Assessing horizontal and downstream implications (e.g., potential impact on other recovery options), understanding the business' inter-connectedness and interdependencies;
- Appraising potential response by key counterparties, clients, and regulators; and
- Identifying any barriers to implementation and clarifying how the bank plans to overcome them.

Based on the evaluation of such criteria, banking organizations often prioritize recovery options in accordance with (1) the financial, operational and strategic impacts they would have and (2) when within the life cycle of financial stress they would be implemented.

Analyze Applicable Governance and Reporting Processes

One objective of recovery planning is to require the bank to think through how its corporate governance framework would apply to decisions that need to be made during financial stress events. For example, how would information suggesting that a recovery trigger has been breached be escalated to management or the board? What bodies would make the decision of whether to implement a recovery option? These questions show that the exercise of recovery planning has a very practical application.

Each bank should develop governance procedures that could be executed and implemented efficiently and expeditiously in a crisis. A breach of a trigger must

be treated seriously and be met with appropriate analysis by senior-level managers in the bank. The recovery plan should include “escalation procedures” for bringing the breach of a trigger to the attention of senior management or the board and provide for relevant data and information to be reported to management or the board in order to inform the action to be taken upon the breach of a trigger. Each bank needs to critically assess its existing policies and procedures, management information systems, and reporting functions to determine whether they would function adequately in a recovery scenario and whether any changes should be made to enhance existing governance processes.

A plan should not commit the bank to take any action without management or the board first evaluating relevant information and deliberating on the best course of action. “Playbooks”—detailed lists of possible recovery actions—can be helpful tools when management and the board think through their recovery options, but should not bind or limit the bank when stress actually occurs.

PRODUCTION AND IMPLEMENTATION TO BAU

Integrate with Related Plans and Processes

The OCC is acutely aware that recovery planning is not being required in a vacuum. Indeed, there are a number of other risk management and compliance processes that relate to recovery planning: capital and liquidity planning, contingent funding, stress testing, and resolution planning. It is important for the bank when doing the initial scoping of its recovery plan to involve subject-matter experts responsible for these processes so that these other processes are properly taken into account before, and not after, the recovery plan is developed.

The bank may determine that it makes sense to incorporate in its recovery plan analyses and other materials from these other processes because doing so is efficient and preserves consistency. For example, the bank may use some analysis or assumptions from stress testing performed as part of Dodd-Frank Act Stress Test (DFAST) or Comprehensive Capital Analysis and Review (CCAR) exercises. Or, the bank may decide that it wants to leverage the critical operations, core business lines and material entities identified in its resolution plan to analyze how it needs to deploy recovery options to best mitigate risk to counterparties and financial stability. When a decision is made to borrow materials or concepts from another area, the bank should be careful to verify that they satisfy the Guidance.

There is no codified requirement for recovery planning assumptions, analyses and findings to be consistent with the other related processes in the bank. However, the fact that recovery forms just one component of a bank's operating

continuum (between BAU and resolution) highlights the need for planning processes to be well integrated and consistent. Integrated and consistent planning processes are key to achieving sustainability and further demonstrate that the bank has a cohesive risk management and planning strategy; the bank's financial projections and stress testing are based on a common set of assumptions agreed upon by senior management; and the bank's various processes are leveraging a consistent pool of current data in a timely manner. Indeed, one of the OCC's motivations for requiring bank-level recovery plans was to establish that management's plans for the bank in a recovery scenario are not at odds with its plans for the holding company.

Develop Communication Plan

As part of the recovery plan development process, banks should develop communication plans and protocols aligned to specific recovery triggers and recovery options. These communication plans should be consistent with existing risk governance and crisis management frameworks, effectively extending existing communication processes across the crisis continuum. A risk-focused and well-integrated strategy enables organizations to communicate efficiently and in a timely manner during periods of extreme stress to prepare leadership, control misinformation, set expectations and mitigate potential obstacles associated with the execution of recovery options.

Communication plans should establish a process for notifying stakeholders and articulating key messages to both internal and external audiences, including potential communication with employees, customers, rating agencies, financial market utilities (FMUs), agent banks, external service providers, creditors, shareholders, depositors and, of course, regulators. With regard to regulators, communication plans should include processes for notifying relevant agencies of significant trigger breaches.

Communication plans should clearly articulate the ownership of various activities within the communication process, including the specific roles, responsibilities and authorities of participants. Additionally, communication plans should explicitly define the information required to support specific communications and the associated reporting necessary to generate that information. The bank should consider updating its communication plan on an annual basis, or when material changes occur, in conjunction with the recovery plan.

The communication strategy and related messaging should be proactive, transparent and tailored to the severity of recovery scenarios, as well as specific triggers, options and recipients. Communication plans should customize the frequency of, and mechanisms (i.e., distribution channels) for, communications to specific stakeholders. Additionally, communication plans should facilitate a

well-coordinated internal review and approval process so that messaging is consistent and accurate and ongoing communications are monitored.

Typical Steps in the Communication Planning Process

- Understanding the strategy, stakeholders, and procedures for delivering effective communications;
- Determining communication objectives, key messages, and protocols for enacting communication plans;
- Facilitating the review, testing, and approval process;
- Disseminating communications across appropriate channels; and
- Managing and assessing the need for ongoing communications.

Implement or Leverage Existing Testing Framework

As with resolution plans, testing is key to demonstrating the credibility of a bank recovery plan, including the validity of the plan’s underlying assumptions and strategy and the effectiveness of operational capabilities necessary for implementation. Testing also helps educate key stakeholders on their roles and responsibilities during a recovery scenario, and provides an assessment of the quality and usefulness of the tools and documentation to which they will have access in recovery. Banks can use test results to further refine and inform their recovery plan strategies and any required remediation efforts.

Recovery plan testing, like other testing processes, is an ongoing process covering multiple phases, including the following:

- Test design, preparation and execution;
- Test evaluation and closure; and
- Revise strategy and plan, as warranted.



Many institutions have already developed testing frameworks as part of their resolution planning process. Where possible, banks should look to leverage existing testing frameworks, align their testing with established governance processes, and involve all three lines of defense in the process. The second and third lines of defense (Independent Risk Management and Internal Audit) are often included early in the process, provide credible review and challenge, and share the testing responsibilities.

Be Mindful of Potential Consequences of a Deficient Plan

The OCC issued the Guidance as a safety and soundness standard that is an appendix to Part 30 of its regulations and pursuant to Section 39 of the Federal

Deposit Insurance Act, meaning the Guidance is enforceable by formal enforcement actions. Because the OCC issued the Guidance as a “guideline” and not as a “regulation,” the OCC has discretion to decide whether a bank that fails to comply with the Guidance should become subject to a non-public enforcement order that requires the bank to submit a plan specifying the steps it will take to comply (a Part 30 Order).

If the OCC determined that it would be appropriate to issue a Part 30 Order requiring a compliance plan, the agency would initiate this process by issuing a notice of deficiency. If the bank failed to submit a compliance plan or failed to implement the compliance plan approved by the OCC, the OCC would be required to issue a “notice of intent to issue an order” pursuant to Section 39—in this case, a public enforcement order—and the bank would be required to respond with a corrective action plan within 14 days. Based on the bank’s corrective action plan, the OCC could decide to issue a formal, public order that is enforceable in federal district court. In such circumstances, the OCC could also impose a civil money penalty on any bank that violates an order.

CONCLUSION

Recovery planning will be a key focus of the OCC and other banking regulators in the coming months and years. Some banks will be preparing a recovery plan for the first time to comply with the Guidance. Other banks may have more experience preparing recovery plans or similar plans, but may need to revisit their plans to comply with the Guidance and make adjustments based on their size or complexity. No matter the size or type of bank, recovery planning is a complex, interdisciplinary process that requires early and sustained engagement from banks.