Checklist for Comprehensive Risk Management

I. Development and Establishment of Comprehensive Risk Management System by Management

【Checkpoints】

- Comprehensive risk management refers to a self-control type of risk management based on a comparison of a financial institution's financial strength (capital) and all risks faced by the institution, including risks not counted in the calculation of the capital adequacy ratios (credit concentration risk, interest rate risk in the banking book, etc.) and assessed on a category-by-category basis (credit risk, market risk, operational risk, etc.). The "integrated risk management" is a type of comprehensive risk management based on a comparison of a financial institution's financial strength (capital) and the aggregate of various risks measured with uniform yardsticks such as VaR (value at risk). On the other hand, a comprehensive risk management method not using this universal-yardstick approach may conduct risk management by, for example, comparing a financial institution's financial strength (capital) and the overall risk level evaluated as a result of qualitative and quantitative assessments of the risks conducted with various methods according to the risk type.

- The development and establishment of the risk management system for a financial institution in its entirety is one of the key elements for ensuring the soundness and appropriateness of the institution's business. The institution's management is charged with and responsible for taking the initiative in the development and establishment of this system by deciding basic corporate management policies (business policies), determining strategic objectives based on these policies and developing an organizational framework for securing the effectiveness of the function of managing risks for the whole of the institution in a comprehensive manner.

- A financial institution should, with a view to ensuring the soundness and appropriateness of its business, make voluntary efforts to develop a comprehensive risk management system based on self-recognition of the need thereof, by taking account of the strategic objectives, the scale and nature of its business and its risk profile.

- When reviewing a financial institution's comprehensive risk management system, the inspector should, while paying as much respect as possible to the institution's voluntary efforts to develop and establish the system, check whether the system being developed and established is an appropriate one commensurate with the institution's strategic objectives, the scale and nature of its business and its risk profile as well as the levels of complexity and sophistication of the risk assessment method used by the institution.

It should be noted that the type and level of the risk assessment method to be used by a financial institution should be determined according to the institution's strategic objectives, the diversity of its business and the risks faced by it and therefore a complex or sophisticated risk management system is not necessarily suited to all financial institutions.

- The inspector should determine whether the comprehensive risk management system is functioning effectively and whether the roles and responsibilities of the institution's management are being appropriately performed by way of reviewing, with the use of check items listed in Chapter I., whether the management is appropriately implementing (1) policy development, (2) development of internal rules and organizational frameworks and (3) development of a system for assessment and improvement activities.

- If any problem is recognized as a result of reviews conducted with the use of the check items listed in Chapter II. and later of each of the checklists for the various risk management systems including this checklist, it is necessary to exhaustively examine which of the elements listed in Chapter I. of each checklist, including the elements listed in this checklist as necessary, are absent or insufficient, thus causing the said problem, and review findings thereof through dialogue between the inspector and the financial institution.

- If the institution's management fails to recognize weaknesses or problems recognized by the inspector, it is also necessary to explore in particular the possibility that the Internal Control System is not functioning effectively and review findings thereof through dialogue.

- The inspector should review the status of improvements with regard to the issues pointed out on the occasion of the last inspection that are not minor and determine whether or not effective improvement measures have been developed and implemented.

1. Policy Development

(1) Roles and Responsibilities of Directors

Do directors attach importance to comprehensive risk management, fully recognizing that a lack of such an approach could seriously hinder attainment of strategic objectives? In particular, does the director in charge of comprehensive risk management review the policy and specific measures for developing and establishing an adequate comprehensive risk management system with a full understanding of the scope, types and nature of risks, and the risk identification, assessment, monitoring and control technique as well as the importance of comprehensive risk management, and with precise recognition of the current status of comprehensive risk management within the financial institution based on such understanding? For example, does the director in charge understand the limitations and weaknesses of the method of assessing various risks in a comprehensive manner (including the assessment and measuring techniques and the assumptions thereof; hereinafter referred to as the "Comprehensive Risk Assessment Method") and consider countermeasures to supplement such shortcomings?

(2) Development and Dissemination of Strategic Objectives

Has the Board of Directors developed strategic objectives covering institution-wide profit objectives, risk-taking strategy (the asset and liability management strategy and the risk-return strategy, etc.) in accordance with the institution's corporate management policy, and disseminated them throughout the institution? When developing such strategic objectives, does the Board of Directors give due consideration to the asset and liability structure (including off-balance sheet items) and various risks and take into account the status of the institution's capital? For example, does it pay attention to the following matters?

- Does it make clear whether to aim at minimizing the risk or to aim at making a profit by aggressively taking and managing a certain amount of risk in deciding the levels of risk-taking and profit objectives?
- Does it avoid setting institution-wide and division-specific strategic objectives that sacrifice risk management for profit? In particular, does it avoid setting objectives that pursue short-term profit by disregarding long-term risk or avoid setting a performance appraisal system that reflects such inappropriate objectives?

(3) Development and Dissemination of Comprehensive Risk Management Policy

Has the Board of Directors established a policy regarding comprehensive risk management (hereinafter referred to as the "Comprehensive Risk Management Policy") and disseminated it throughout the institution? Is the appropriateness of the Comprehensive Risk Management Policy being secured by way of, for example, clear statements on the following matters?

- The roles and responsibilities of the director in charge and the Board of Directors or equivalent organization to the Board of Directors with regard to comprehensive risk management
- The policy on organizational framework, such as establishment of a division concerning comprehensive risk management (hereinafter referred to as the "Comprehensive Risk

Management Division") and the authority assigned thereto

- The policy on organizational framework, such as establishment of an organization that comprehensively manages assets and liabilities and participates in the development and implementation of the strategy regarding Assets, Liabilities and Liquidity, etc. (hereinafter referred to as the "Asset and Liability Management [ALM] Committee") and the authority assigned thereto
- The policy regarding the setting of risk limits
- The policy regarding identification of risks to be managed
- The policy regarding comprehensive assessment of risks and the monitoring, control and mitigation of the assessed risks
- The policy regarding New Products, etc.[1]

(4) Revision of Policy Development Process

Does the Board of Directors revise the policy development process in a timely manner by reviewing its effectiveness based on reports and findings of various investigations on the status of comprehensive risk management in a regular and timely manner or on an as needed basis?

2. Development of Internal Rules and Organizational Frameworks

(1) Development and Dissemination of Internal Rules

Does the Board of Directors or equivalent organization to the Board of Directors have the Manager of the Comprehensive Risk Management Division (hereinafter simply referred to as the "Manager" in this checklist) develop internal rules that clearly specify the arrangements concerning comprehensive risk management (hereinafter referred to as the "Comprehensive Risk Management Rules") and disseminate them throughout the institution in accordance with the Comprehensive Risk Management Policy? Has the Board of Directors or equivalent organization to the Board of Directors approved the Comprehensive Risk Management Rules after determining if they comply with the Comprehensive Risk Management Policy and after legal checks, etc.?

(2) Establishment of Comprehensive Risk Management Division

(i) Does the Board of Directors or equivalent organization to the Board of Directors have a Comprehensive Risk Management Division established and have the division prepared to undertake appropriate roles in accordance with the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules?[2]

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1 See "Checklist for Business Management (Governance) (for Basic Elements)," I. 3. (4).

2 When the Comprehensive Risk Management Division is not established as an independent division (e.g.,

(ii) Has the Board of Directors allocated to the Comprehensive Risk Management Division a Manager with the necessary knowledge and experience to supervise the division and enabled the Manager to implement management operations by assigning him/her the necessary authority therefor?

(iii) Has the Board of Directors or equivalent organization to the Board of Directors allocated to the Comprehensive Risk Management Division an adequate number of staff members who have the necessary knowledge and experience to execute the relevant operations and assigned such staff the authority necessary for conducting the aforementioned operations?[3]

(iv) Does the Board of Directors or equivalent organization to the Board of Directors keep the Comprehensive Risk Management Division independent from the Office (Trading, Banking) Divisions, Marketing and Sales Divisions, etc. and secure a check-and-balance system of the Comprehensive Risk Management Division?

(3) Development of Comprehensive Risk Management Systems in Office (Trading, Banking) Divisions, Marketing and Sales Divisions, etc.

(i) Does the Board of Directors or equivalent organization to the Board of Directors provide a system to fully disseminate the relevant internal rules and operational procedures to the divisions involving risks to be managed (e.g. the Office (Trading, Banking) Divisions, Marketing and Sales Divisions, etc.) and ensure that such divisions observe them? For example, does the Board of Directors or equivalent organization to the Board of Directors instruct the Manager to identify the internal rules and operational procedures that should be observed by the Office (Trading, Banking) Divisions, Marketing and Sales Divisions, etc. and to carry out specific measures for ensuring observance such as providing effective training on a regular basis?

(ii) Does the Board of Directors or equivalent organization to the Board of Directors provide a system to ensure the effectiveness of comprehensive risk management in the Office (Trading, Banking) Divisions, Marketing and Sales Divisions, etc. through the Manager or the Comprehensive Risk Management Division?

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when the division is consolidated with another risk management division to form a single division or when a division in charge of other business also takes charge of comprehensive risk management or when a Manager or Managers take charge of comprehensive risk management instead of a division or a department), the inspector shall review whether or not such a system is sufficiently reasonable and provides the same functions as in the case of establishing an independent division commensurate with the scale and nature of the institution and its risk profile.

[3] When a department or a post other than the Board of Directors or equivalent organization to the Board of Directors is empowered to allocate staff and assign them authority, the inspector shall review, in light of the nature of such a department or post, whether or not the structure of the Comprehensive Risk Management Division is reasonable in terms of a check-and-balance system and other aspects.

(4) Establishment of ALM Committee, etc.

Does the Board of Directors or equivalent organization to the Board of Directors have an ALM Committee established that comprehensively manages assets and liabilities and participates in the development and implementation of the strategy regarding Assets, Liabilities and Liquidity, etc. or an organization that provides an equivalent function (hereinafter collectively referred to as an "ALM Committee, etc.") based on the Comprehensive Risk Management Policy? If not, does it have in place an alternative risk management process?

(5) System for Reporting to Board of Directors or equivalent organization to Board of Directors and Approval

Has the Board of Directors or equivalent organization to the Board of Directors appropriately specified matters that require reporting and those that require approval and does it have the Manager report the current status to the Board of Directors or equivalent organization to the Board of Directors in a regular and timely manner or on an as needed basis or have the Manager seek the approval of the Board of Directors or equivalent organization to the Board of Directors on the relevant matters? In particular, does it ensure that the Manager reports to the Board of Directors or equivalent organization to the Board of Directors without delay any matters that would seriously affect corporate management?

(6) System for Reporting to Corporate Auditor

In the case that the Board of Directors has specified matters to be directly reported to a corporate auditor, has it specified such matters appropriately and do they provide a system to have the Manager directly report such matters to the auditor?[4]

(7) Development of Internal Audit Guidelines and an Internal Audit Plan

Does the Board of Directors or equivalent organization to the Board of Directors have the Internal Audit Division appropriately identify the matters to be audited with regard to comprehensive risk management, develop guidelines that specify the matters subject to internal audit and the audit procedure (hereinafter referred to as "Internal Audit Guidelines") and an internal audit plan, and approve such guidelines and plan?[5] For example, does it have the following matters clearly specified in the Internal Audit Guidelines or the internal audit plan and provide a system to have these matters appropriately audited?

- Status of development of the comprehensive risk management system

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[4] It should be noted that this shall not preclude a corporate auditor from voluntarily seeking a report and shall not restrict the authority and activities of the auditor in any way.

[5] The Board of Directors or equivalent organization to the Board of Directors only needs to have approved the basic matters with regard to an internal audit plan.

- Status of observance of the Comprehensive Risk Management Policy, Comprehensive Risk Management Rules, etc.
- Appropriateness of the comprehensive risk management processes commensurate with the scale and nature of the business and risk profile
- Appropriateness of the use of the comprehensive risk assessment method based on the limitations and the weaknesses thereof
- Appropriateness of the Comprehensive Risk Assessment Method
- Accuracy and completeness of the data used in comprehensive assessment of risks
- Appropriateness of stress test scenarios, etc.
- Status of improvement of matters pointed out in an internal audit or in the last inspection

(8) Revision of Development Process of Internal Rules and Organizational Frameworks

Does the Board of Directors or equivalent organization to the Board of Directors revise the development process of internal rules and organizational frameworks in a timely manner by reviewing their effectiveness based on reports and findings on the status of comprehensive risk management in a regular and timely manner or on an as needed basis?

3. Assessment and Improvement Activities

1) Analysis and Assessment

(1) Analysis and Assessment of Comprehensive Risk Management

Does the Board of Directors or equivalent organization to the Board of Directors appropriately determine whether there are any weaknesses or problems in the comprehensive risk management system and the particulars thereof, and appropriately examine their causes by precisely analyzing the status of comprehensive risk management and assessing the effectiveness of comprehensive risk management, based on all information available regarding the status of comprehensive risk management, such as the results of audits by corporate auditors, internal audits and external audits, findings of various investigations and reports from various divisions? In addition, if necessary, does it take all possible measures to find the causes by, for example, establishing fact findings committees, etc. consisting of non-interested persons?

(2) Revision of Analysis and Assessment Processes

Does the Board of Directors or equivalent organization to the Board of Directors revise the analysis and assessment processes in a timely manner by reviewing their effectiveness based on reports and findings on the status of comprehensive risk management in a regular and timely manner or on an as needed basis?

2) Improvement Activities

(1) Implementation of Improvements

Does the Board of Directors or equivalent organization to the Board of Directors provide a system to implement improvements in the areas of the problems and weaknesses in the comprehensive risk management system identified through the analysis, assessment and examination referred to in 3. 1) above in a timely and appropriate manner based on the results obtained by developing and implementing an improvement plan as required or by other appropriate methods?

(2) Progress Status of Improvement Activities

Does the Board of Directors or equivalent organization to the Board of Directors provide a system to follow up on the efforts for improvement in a timely and appropriate manner by reviewing the progress status in a regular and timely manner or on an as needed basis?

(3) Revision of Improvement Process

Does the Board of Directors or equivalent organization to the Board of Directors revise the improvement process in a timely manner by reviewing its effectiveness based on reports and findings on the status of comprehensive risk management in a regular and timely manner or on an as needed basis?

II. Development and Establishment of Comprehensive Risk Management System By Manager

【Checkpoints】

- This chapter lists the check items to be used when the inspector reviews the roles and responsibilities to be performed by the Manager and the Comprehensive Risk Management Division.

- If any problem is recognized as a result of reviews conducted with the use of the check items listed in Chapter II., it is necessary to exhaustively examine which of the elements listed in Chapter I. are absent or insufficient, thus causing the said problem, and review findings thereof through dialogue between the inspector and the financial institution.

- If the institution's management fails to recognize problems recognized by the inspector, it is also necessary to strictly explore in particular the possibility that the systems and processes listed in Chapter 1. are not functioning appropriately and review findings thereof through dialogue.

- The inspector should review the status of improvements with regard to the issues pointed out on the occasion of the last inspection that are not minor and determine whether or not effective improvement measures have been developed and implemented.

1. Roles and Responsibilities of Manager

(1) Development and Dissemination of Comprehensive Risk Management Rules

Has the Manager, in accordance with the Comprehensive Risk Management Policy, identified the risks, decided the methods of assessment and monitoring thereof and developed the Comprehensive Risk Management Rules that clearly define the arrangements on risk control and mitigation, based on a full understanding of the scope, types and nature of the risk and the relevant comprehensive risk management technique?

Have the Comprehensive Risk Management Rules been disseminated throughout the institution upon approval by the Board of Directors or equivalent organization to the Board of Directors?

(2) Comprehensive Risk Management Rules

Do the Comprehensive Risk Management Rules exhaustively cover the arrangements necessary for comprehensive risk management and specify the arrangements appropriately in a manner befitting the scale and nature of the financial institution's business and its risk profile? Do the rules specify the following items, for example:

- Arrangements on the roles, responsibilities, and organizational framework of the Comprehensive Risk Management Division
- Arrangements on the risk limits
- Arrangements on the identification of risks to be subjected to comprehensive risk management
- Arrangements on the comprehensive risk assessment method and assessment methods used for the each risk areas
- Arrangements on the comprehensive risk monitoring method
- Arrangements on periodic reviews of the comprehensive risk assessment method
- Arrangements on approval process for New Products, etc.
- Arrangements on reporting to the Board of Directors or equivalent organization to the Board of Directors

(3) Development of Organizational Frameworks by Manager

(i) Does the Manager, in accordance with the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules, provide for measures to have the Comprehensive Risk Management Division exercise a check-and-balance system in order to conduct comprehensive risk management appropriately?

(ii) Does the Manager provide a system to prevent any lapse in the risk management for the financial institution as a whole so as to ensure an appropriate comprehensive risk management? Does the Manager ensure that the Manager of each risk management division promptly reports to the Comprehensive Risk Management Division when detecting any weakness or problem that may affect comprehensive risk management?

(iii) Does the Manager ensure that on a risk category-by-category basis, each risk management division identifies risks inherent in New Products as specified in the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules and reports them for the purpose of the screening of New Products?[6]

(iv) Does the Manager understand the limitations and weaknesses of the comprehensive risk assessment method and provide a system to make risk management more sophisticated in a manner commensurate with the scale and nature of the financial institution’s business and its risk profile?[7]

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[6] See “Checklist for Business Management (Governance) (for Basic Elements),” Chapter I. 3. (4)

[7] It should be noted that sophistication of risk management includes not only expansion of scope of risk measurement and improvement in precision and other aspects of risk management but also enhancement of measures to complement the limits and weaknesses of the management and the technique of utilizing measurement results.

(v) Does the Manager have in place a comprehensive risk management computer system[8] with the high reliability suited to the scale and nature of the financial institution's business and its risk profile?

(vi) Does the Manager ensure the provision of training and education systems to enhance the ability of employees to conduct comprehensive risk management in an effective manner, thus developing human resources with relevant expertise?

(vii) Does the Manager provide a system to ensure that matters specified by the Board of Directors or equivalent organization to the Board of Directors are reported in a regular and timely manner or on an as needed basis? In particular, does the Manager provide a system to ensure that matters that would seriously affect corporate management are reported to the Board of Directors or equivalent organization to the Board of Directors without delay?

(4) Revision of Comprehensive Risk Management Rules and Organizational Frameworks

Does the Manager conduct monitoring on an ongoing basis with regard to the status of the execution of operations at the Comprehensive Risk Management Division?

Does the Manager review the effectiveness of the comprehensive risk management system in a regular and timely manner or on an as needed basis, and, as necessary, revise the Comprehensive Risk Management Rules and the relevant organizational framework, or present the Board of Directors or equivalent organization to the Board of Directors with proposals for improvement?

2. Roles and Responsibilities of Comprehensive Risk Management Division

1) Risk Identification and Assessment

(1) Identification of Risks to Be Managed

(i) Does the Comprehensive Risk Management Division have each Risk Management Division exhaustively identify all risks faced by the bank on a category-by-category basis and identify the risks to be subjected to comprehensive risk management commensurate with the size and nature of the identified risks? Does the Manager ensure that the identification process covers the full scope of business including those of overseas offices, consolidated subsidiaries and consignees, in addition to exhaustively covering the risk categories such as credit risk, market risk and operational risk?

(ii) Does the Comprehensive Risk Management Division apply comprehensive risk management to the credit concentration risk and the interest rate risk in the banking book and is it considering whether to apply comprehensive risk management to the risks not included in the calculation of the capital adequacy ratio? When there are risks not covered by comprehensive risk management,

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[8] It should be noted that the computer system may be a centralized dataprocessing environment system, distribution processing system, or EUC (end user computing) type. The same shall apply hereafter.

has the Comprehensive Risk Management Division determined whether their effects are negligible?

(iii) With regard to New Products as specified by the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules, does the Comprehensive Risk Management Division identify their inherent risks in advance through each risk management division and report to the new product committee, etc. in a timely manner?[9]

(2) Assessment of Various Risks

(i) When some risks to be controlled through comprehensive risk management cannot be quantified, does the Comprehensive Risk Management Division appropriately assess them by conducting graded assessment of their effects and self-assessment of the levels of management and control to the scope achievable? Or does the Comprehensive Risk Management Division have each risk management division provide necessary information concerning the specific risk areas to be managed in an appropriate and timely manner in such a case?

(ii) Does the Comprehensive Risk Management Division determine the validity of the risk assessment and measurement techniques used by the Risk Management Divisions and the assumptions thereof? Or does it make sure that each risk management division examines the validity of the techniques and assumptions? Does it determine the following items, for example?:

- Are the treatment of core deposits and the technique of measuring the optionality inherent in assets and liabilities (nonlinear risks such as the risks of early termination and early redemption) appropriate when measuring the interest rate risk in the banking book?
- When the scenario approach is employed in measuring risk, are the scenarios used appropriate?
- When VaR, a uniform yardstick for measuring risk, is employed, are the measuring techniques, the holding periods and the confidence levels applied in a manner befitting the financial institution's strategic objectives and risk profile?
- When the integrated risk measurement technique is employed, is consistency between the employed measurement techniques ensured?

(3) Comprehensive Assessment of Risks

(i) Does the Comprehensive Risk Management Division comprehensively assess and measure risks including those existing at sales branches, etc.[10] consolidated subsidiaries and subcontractors with important operations?

(ii) Does the Comprehensive Risk Management Division comprehensively assess and measure the

[9] See "Checklist for Business Management (Governance) (for Basic Elements)," I. 3. (4).

[10] Sales branches and overseas offices

various risks to be controlled through comprehensive risk management? When the various risks to be thus managed are integrated, is the integration method appropriate? When the integrated risk measurement technique is used, are the various risks integrated in light of the check items listed in Chapter III. 1. 3) (1) of this checklist?

(iii) Does the Comprehensive Risk Management Division comprehensively assess and measure risks based on stress scenarios that cover incidents capable of having serious effects on the financial institution?

2) Monitoring

(1) Comprehensive Monitoring of Overall Risks

Does the Comprehensive Risk Management Division, in accordance with the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules, conduct monitoring with regard to the status of overall risks comprehensively and with an appropriate frequency in light of the financial institution's internal environment (risk profile, the status of the use of risk limits, etc.) and external environment (economic cycles, markets, etc.)? Does the division conduct monitoring with regard to the status of internal and external environments and the appropriateness of the assumptions?

(2) Monitoring of Compliance with Risk Limits

Does the Comprehensive Risk Management Division regularly monitor the status of compliance with the risk limits and the risk capital limits (in the case where capital allocation management is employed) and the status of the use thereof?

(3) Reporting to Board of Directors or equivalent organization to Board of Directors

Does the Comprehensive Risk Management Division, in accordance with the Comprehensive Risk Management Policy and the Comprehensive Risk Management Rules, provide in a regular and timely manner or on an as needed basis information necessary for the Board of Directors or equivalent organization to the Board of Directors to make an appropriate assessment and judgment with regard to the status of the comprehensive risk management and the status of the risks assessed comprehensively? Does the division report the following items, for example?

- The risk profile and the trend thereof
- The status of compliance with the risk limits and the risk capital limits (in the case where capital allocation management is employed) and the status of the usage thereof
- The status of external environment such as economic cycles
- The validity of the comprehensive risk assessment methods and the limitations and weaknesses thereof

(4) Coordination with the Capital Management Division

Does the Comprehensive Risk Management Division communicate, in a timely and appropriate manner, information determined as necessary by the Capital Management Divisions such as data on the status of risks, the status of compliance with the risk limits and the risk capital limits (in the case where capital allocation management is employed) and the status of the use thereof as well as the validity of the risk assessment and measurement techniques and the assumptions thereof?

(5) Feedback to Risk Management Divisions

Does the Comprehensive Risk Management Division feed back the results of its assessment, analysis and review with regard to the status of risks to each risk management division as necessary?

3) Control and Mitigation

(1) Response to Case Where Unmanageable Risks Exist

In the case where risks not covered by comprehensive risk management have non-negligible effects or where risks to be controlled through comprehensive risk management cannot be managed appropriately, does the Comprehensive Risk Management Division provide information necessary for the Board of Directors or equivalent organization to the Board of Directors to make decisions as to whether the financial institution should withdraw from or downsize the business affected by those risks?

(2) Handling with the Case Where Risk Limits are Exceeded

In the case where the financial institution has exceeded the risk limits or the risk capital limits (in the case where capital allocation management is employed), does the Comprehensive Risk Management Division provide information necessary for the Board of Directors or equivalent organization to the Board of Directors without delay to make decisions as to whether to take steps to mitigate risks or alter the limits?

4) Review and Revision

(1) Sophistication of Risk Management

Does the Comprehensive Risk Management Division conduct a review to grasp the limitations and weaknesses of the comprehensive risk assessment method and devise countermeasures to complement the method? Does it conduct investigations, analysis and consideration commensurate with those limitations and weaknesses with a view to making risk management more sophisticated commensurate with the risk profile?

(2) Review and Revision of Comprehensive Risk Management Method

Does the Comprehensive Risk Management Division grasp the limitations and weaknesses of the comprehensive risk assessment method as well as changes in the internal and external environments, and regularly review whether the method suits the institution-wide strategic objectives, the scale and nature of the business in question and the risk profile of the financial institution in its entirety, and revise the method? Does the division review and revise the following items, for example:

- Validity of the identification of risks to be subjected to comprehensive risk management
- Validity of the comprehensive risk assessment method
- Appropriateness of the operation of the comprehensive risk assessment method commensurate with its limitations and weaknesses

III. Specific Issues

【Checkpoints】

- This chapter lists the check items to be used in the inspection of financial institutions that employ the “integrated risk measurement technique” which measures various risks with uniform yardsticks such as VaR and measures the aggregated risks.

- If any problem is recognized as a result of reviews conducted with the use of the check items listed in Chapter III., it is necessary to exhaustively examine which of the elements listed in Chapters I. and II. are absent or insufficient, thus causing the said problem, with the use of the checklists in those chapters, and review findings thereof through dialogue between the inspector and the financial institution.

- If the institution’s management fails to recognize problems recognized by the inspector, it is also necessary to strictly explore in particular the possibility that the systems and processes listed in Chapter 1. are not functioning appropriately and review findings thereof through dialogue.
- The inspector should review the status of improvements with regard to the issues pointed out on the occasion of the last inspection that are not minor and determine whether or not effective improvement measures have been developed and implemented.

1. Check Items to Be Used When Integrated Risk Measurement Technique Is Employed

1) Establishment of Integrated Risk Measurement System

(i) Is the integrated risk measurement system conceptually sound and has it been properly implemented?

(ii) Is the role of the integrated risk measurement technique (model) clearly positioned under the Comprehensive Risk Management Policy and operated based on the understanding of the items listed below? Does it determine if there is no problem with the application of the technique to consolidated subsidiaries?

(a) The financial institution’s strategic objectives, the scale and nature of its business and its risk profile

(b) The fundamental design concept of the integrated risk measurement technique based on (a)

(c) Identification and measurement of risks based on (b) (scope, technique, assumptions, etc.)

(d) Nature (limitations and weaknesses) of the integrated risk measurement technique that derive from (c) and the validity of the technique

(e) Details of the method of validating with respect to (d)

(iii) In the case where capital allocation management[11] is employed, has the policy of capital allocation management been developed based on the results calculated by way of the integrated risk measurement technique? When there are risks which are not measured with this technique are there any reasonable grounds for excluding them from the measurement? Is the risk capital allocated with due consideration for the risks excluded from the measurement?

2) Appropriate Involvement of Directors and Corporate Auditors

(1) Understanding of Integrated Risk Measurement Technique

(i) Do directors understand that decisions concerning the integrated risk measurement technique as well as the risk limits and the risk capital limits (in the case where capital allocation management is employed) have serious implications for the financial institution's corporate management and financial conditions?

(ii) Does the director in charge of integrated risk management understand the integrated risk management technique required for the business of the financial institution and have a grasp on the nature (limitations and weaknesses) thereof?

(iii) Do directors and corporate auditors seek to enhance their understanding of the integrated risk management technique by participating in training courses or through other means?

(2) Approach to Integrated Risk Management

Do directors involve themselves actively in integrated risk management based on the integrated risk measurement technique?

3) Integrated Risks Measurement

(1) Appropriateness of Measurement Technique

(i) With regard to the various risk measurement techniques used by the Comprehensive Risk Management Division, is the validity of each of them ensured, and is consistency among those techniques secured with a view to measuring risks appropriately in an integrated manner?

(ii) Are the assumptions that underlie the risk measurement conducted by the Comprehensive Risk Management Division reasonable in light of the strategic objectives and the risk profile?

(iii) Is the technique used by the Comprehensive Risk Management Division to aggregate various risks with different risk nature and loss distributions appropriate? When correlations among various risks (distribution effect) are taken into consideration, does the division regularly validate the correlations?

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[11] See "Checklist for Capital Management."

(2) Ongoing Validation and Stress Test

(i) Does the Comprehensive Risk Management Division regularly analyze the appropriateness of the measuring techniques through ongoing validation (back testing, etc.)? Are revisions of the measuring techniques conducted in accordance with the internal rules?

(ii) Does the Comprehensive Risk Management Division grasp the stress status of various risks individually and the risks as a whole through stress tests based on a comprehensive and appropriate stress scenarios and make appropriate use of the test results?

(3) Systems for Validating and Managing the Integrated Risk Measurement Technique

Were the integrated risk measurement technique and the assumptions thereof validated during the development of the technique and thereafter on a regular basis by a person or persons with no involvement in the development and with sufficient capabilities? If any deficiency is recognized in the integrated risk measurement technique or the assumptions thereof, is a corrective action taken appropriately?

Are there frameworks and internal rules to prevent the integrated risk measurement technique and the assumptions thereof from being altered on unreasonable grounds, and is the integrated risk measurement technique managed appropriately in accordance with the internal rules?

4) Records on Integrated Risk Measurement Technique

Are systems developed for the purpose of keeping records for future reference on the review process with regard to the selection of the integrated risk measurement technique and the assumptions thereof and the grounds for the selection process in order to enable follow-up verification and utilize the records to make the measurement more sophisticated and elaborated?

5) Audits

(1) Development of Auditing Program

Is an auditing program that exhaustively covers the auditing of the integrated risk measurement technique in place?

(2) Scope of Internal Audits

Is auditing conducted to check the following items?

- Consistency of the integrated risk measurement technique with the strategic objectives, the scale and nature of business and the risk profile
- Appropriateness of the business in light of the nature (limitations and weaknesses) of the integrated risk measurement technique

- Records on the integrated risk measurement technique are appropriately documented and updated in a timely manner
- Appropriate incorporation of alterations to the process of integrated risk management into the risk measurement technique
- Appropriateness of the scope of the risks measured by the integrated measurement technique
- Absence of any deficiency in the information system for the management
- Validity of the integrated risk measurement technique and the assumptions thereof
- Validity of the method of aggregating various risks
- Accuracy and completeness of the data used in integrated risk measurement
- Adequacy of the process and results of ongoing verification (backtesting, etc.)

(3) Utilization of Auditing Results

Does the Comprehensive Risk Management Division appropriately revise the integrated risk measurement technique based on the results of auditing?

6) Utilization of Management Indicators with Due Consideration for Risks

Does the Comprehensive Risk Management Division utilize management indicators such as return on equity not only for the purpose of grasping performance but also for that of enhancing risk management? [12]When management indicators are utilized, are they used to review the reasonableness of the risk-return strategy, etc. and help formulate strategies?

[12] It should be noted that the level of utilization of return on equity and other management indicators varies according to the corporate management policy, strategic objectives, etc.