Proposed Attestation Requirements for FR Y-14A/Q/M reports

Overview and Implications for Banking Institutions
**Background**

On September 16, 2015, the Board of Governors of the Federal Reserve System (“Federal Reserve”) published a proposal to make a number of revisions to the FR Y-14A/Q/M Capital Assessments and Stress Testing Reports. The proposed changes in this presentation are specific to those noted in the Federal Register / Vol. 80, No. 179. The comment period for proposed changes ends November 16, 2015.

This proposal includes the addition of an attestation requirement for select FR Y-14A/Q/M filers – the Large Institution Supervising Coordinating Committee (LISCC) respondents*. The proposal outlines the Federal Reserve’s increased expectations regarding accuracy and completeness for regulatory reports as well as specific accountability requirements. The increased expectations reflect the Federal Reserve’s ongoing concerns with data quality, overall, but also particularly for these reports.

The chief financial officer (CFO) or an equivalent senior officer of a LISCC respondent would be required to make an attestation for both the actual and projected risk and financial data. The FR Y-14 reports are expected to reconcile to the FR Y-9C.

This document highlights Deloitte’s point of view regarding the implications on attestation, materiality, internal control processes and expectations.

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* LISCC respondents represent financial institutions that may pose elevated risks to US financial stability and are supervised by the Federal Reserve. Refer to the following link for further details: [http://www.federalreserve.gov/bankinforg/large-institution-supervision.htm](http://www.federalreserve.gov/bankinforg/large-institution-supervision.htm)
Principal 6 defines the level of internal controls required throughout the capital planning process. The proposal will formalize the expectations already provided in CCAR supervisory guidance.

Existing CCAR supervisory guidance emphasizes the importance of internal control frameworks (COSO, SOX, etc.)

As part of CCAR submissions, regulators require banks with assets of $50B or more to file an annual capital plan document and the FR-Y14 A, Q, and M schedules.

The Capital Plan and FR Y-14A submissions are documents comprising current and forward-looking scenario based projections and analysis of capital adequacy. The FR Y-14Q and FR Y-14M are separate filings of detailed current period exposure and risk attribute data.

With the Federal Reserve’s continuous focus on data quality, integrity, and accuracy, the proposal to add an attestation requirement ‘to improve consistency of reported data across firms, address industry concerns, and improve supervisory modeling’ affecting certain large FR Y-14A/Q/M filers (LISCC respondents) appears to be a logical next step in the regulatory drive for adequate internal controls and accountability pertaining to CCAR process.
Overview of Proposed Requirements

The proposal establishes internal controls and data accuracy attestation requirements for LISCC respondents related to their FR Y-14A/Q/M reports, and also encourages enhancement to the internal control environment of all FR Y-14A/M/Q filers.

<table>
<thead>
<tr>
<th>Required Attestation</th>
<th>Affected institutions’ CFOs or equivalent senior officers would have to attest that:</th>
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<tr>
<td></td>
<td>▪ <strong>FR Y-14A/Q/M reports are prepared in conformance with the instructions</strong> issued by the Federal Reserve System, which implies adherence to US Generally Acceptable Accounting Principles (“GAAP”). This would cover <em>both projected and actual data</em> within the applicable FR Y-14A/Q/M reports</td>
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<td>▪ <strong>Reported actual data is materially accurate.</strong> Any material weaknesses in internal controls and any material errors or omissions should be reported promptly.</td>
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<td>▪ <strong>Internal controls over the FR Y-14A/Q/M preparation (actual data) are effective</strong> and include practices necessary to provide reasonable assurance as to the accuracy of data.</td>
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<td>▪ <strong>These internal controls are audited annually</strong> by internal audit or compliance staff and are assessed regularly by management</td>
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<td>Proposed attestation requirements would be effective beginning June 30, 2016</td>
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| Attestation Policy | Institutions should have a **policy for determining materiality** as related to management attestation over FR Y-14A/Q/M reports that the data is materially accurate and the internal controls are effective. The policy should include a comprehensive analysis of all relevant quantitative and qualitative considerations, including, but not limited to, the size and effect of the omission or misstatement on firms' projected regulatory capital ratios in stressed scenarios |

| Other Considerations | While only LISCC respondents would be required to provide an attestation, all FR Y-14A/Q/M filers are expected to meet regulators expectations regarding effective internal controls and ensure accurate and complete reporting |
Our Takeaways

The attestation proposal will impose additional due diligence on part of the firms to ensure the reporting processes have adequate controls.

<table>
<thead>
<tr>
<th>1</th>
<th>Attestation</th>
<th>Attestation is more than a sign-off and is grounded in end-to-end accountability for data:</th>
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<tr>
<td></td>
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<td>• FR Y-14A/Q/M attestation brings a <strong>higher level of accountability</strong> to the CFO function, requiring a <strong>coordinated bank-wide effort</strong> to ensure the CFO has enough information to make the attestation.</td>
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<td>• For projected data, the focus is expected to center on <strong>adequacy of the forecasting process</strong> from both <strong>management and internal audit perspectives</strong>. Determining the right level of work required to provide assurance over “fair presentation” is key.</td>
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<td>• Similar attestation is already part of “traditional” regulatory reports (FR Y-9C, Call Reports). However, FR Y-14A/Q/M reports bring an <strong>added challenge due to complexity</strong> of CCAR processes and the diverse volume of data.</td>
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<th>2</th>
<th>Internal Controls</th>
<th>The COSO framework can be used as a baseline:</th>
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<td>• The proposal references COSO as an appropriate framework for establishing internal controls. Per COSO, the design of controls needs to be at the right level of materiality and granularity to ensure appropriate coverage of FR Y-14A/Q/M processes.</td>
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<td>• Based on this, Internal Audit will have to enhance coverage of FR Y-14 reporting to support the proposed annual attestation.</td>
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<th>3</th>
<th>Materiality</th>
<th>A consistent &amp; systematic approach with both qualitative &amp; quantitative considerations:</th>
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<td>• A formalized and consistent approach should be used to determine the of errors, omissions, and necessary restatements.</td>
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<td>• Materiality is a known concept to both financial and regulatory reporting and can serve as a reference point in designing a materiality framework for FR Y-14 reports</td>
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Attestation
Attestations already exist for internal controls for financial statements, e.g., SOX, FDICIA, and FR Y-9C and FFIEC031/04 (“Call Reports”). However, FR Y-14A/Q/M attestation represents a new dynamic through the inclusion of both risk and financial data at granular levels of detail. This attestation would be end-to-end, from a business line to control function perspective, and will require documentation and sign-off that is already grounded in an existing accountability framework for regulatory reporting.

### Sarbanes-Oxley Attestation Requirements
- **CEO and CFO attest that they:**
  - Are responsible for disclosure controls
  - Have designed controls to ensure that material information is known to them
  - Have evaluated the effectiveness of controls
  - Have presented their conclusions in the filing
  - Have disclosed to the audit committee and auditors significant control deficiencies and acts of fraud
  - Have indicated in the report significant changes to controls
  - Are responsible for establishing and maintaining adequate internal control structure and procedures for financial reporting

### FR Y-9C Attestation Requirements
- **Board of directors and senior management attest that they:**
  - Are responsible for establishing Internal Controls
  - Maintain an effective system of Internal Controls

- **The CFO, or equivalent, attest that:**
  - The FR Y-9C & supporting schedules are prepared in accordance with report form instructions
  - Information on FR Y-9C is true and correct, to best of knowledge & belief
Attestation is a much more comprehensive process than just a sign-off. It includes effective challenge, continuous monitoring and ensuring that the CFO, or designate, have enough information to make an informed decision. Attestation brings a higher level of accountability.

The complexity of CCAR processes, diverse volume of data (risk, financial, qualitative) and the introduction of attestation for projections pose inherent challenges. The extent of effort needed for a CFO to gain an understanding that the report is a fair presentation is unknown.

### Front to Back Considerations

- To support attestation of actual and projected data for both risk and finance, institutions will be required to reinforce or establish new processes and controls
- A re-assessment of the front to back control framework and governance model over the processes / accountability supporting the eventual attestation is likely required
- It may include both bottom-up and horizontal sub-attestations from designates in lines of business and corporate functions based on their accountability model (designated responsibilities)
- A distributed sub-attestation model based on **first line of defense governance model** will provide greater accountability across the units and provides a higher degree of comfort to the CFO
- Specifically, a corporate function responsible for generating FR Y-14A/Q/M reports will likely have to provide its attestation for the underlying actual “materially accurate data” and effectiveness of controls, plus “fair presentation” of projections (given the significant amount of data)
- Quality Assurance at the corporate and business unites level along with data integrity testing across the data flow should provide desired coverage as the **second line of defense** – and will include risk, finance, compliance functions
- As the **third line of defense**, Internal Audit may have to significantly expand its program to incorporate all the components required for the attestation; certain activities can also be performed by the Compliance function – noted above
Internal Controls Framework
Regulatory Expectations around Internal Controls

Current State & Industry Trends

- Banks continue to conduct controls and compliance activities in silos, potentially resulting in redundancy, overlap, and an increased burden on the business
- Multiple frameworks followed to meet regulatory requirements (SOX, Regulatory Reporting, CCAR)
- Lack of well-defined end-to-end Capital Planning assurance process over reporting data accuracy and effectiveness of underlying controls, inclusive of self-assessment, validation and reporting
- Inadequate controls designed to address end-to-end reporting
- Disconnect between the risk reporting, financial reporting, and regulatory reporting controls due to inadequate granularity
- Improper classification of underlying data for regulatory reporting

Regulator Expectations

- **Governance and oversight**: High expectations for board’s engagement, understanding and oversight of regulatory reporting processes
- **Review and Approval**: Management review and approval of various regulatory reports
- **Effective risk assessment**: Comprehensive understanding of potential risks and prioritize identification of risks to focus resources on policies, processes, data, and controls to ensure risks are aligned with the enterprise risk appetite
- **Strong foundation of internal controls**: Banks are expected to develop and maintain a well-controlled capital planning environment
- **Data and reporting integrity**: Heavy focus on upstream and downstream reporting processes to confirm accuracy and integrity of various (FR Y-14A/M/Q) submissions
- **Implement and demonstrate progress**: Implement key controls for priority processes in the short-term and develop plans to demonstrate continued progress to regulators in the medium-term

Strengthening Governance and Controls

- Strengthening overall governance of the regulatory reporting processes
- Emphasizing accountability of key stakeholders including Lines of Business (LOB) and improving coordination between impacted groups
- Investing in change management and change control processes to enable integrity of reported results
- Increased focus on sign-off and attestation
- Integrated Governance and Internal Control Framework
Integrated Governance & Controls Framework

Bank Holding Companies (BHCs) should have a strong CCAR Data and Process Controls Integrated Framework ("CCAR Integrated Framework") that helps govern its internal capital planning processes and addresses the COSO principles.

The integrated framework should include:

1. Regular and comprehensive review by capital management;
2. Robust and independent model review and validation practices;
3. Comprehensive documentation, including policies and procedures; and
4. Effective Challenge and change controls

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<th>COSO Elements</th>
<th>Potential Alignment with CCAR and Regulatory Reporting Expectations</th>
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| Control Environment | ▪ Enterprise governance structure with the board and senior management involvement and top-to-bottom accountability  
▪ Written policies across regulatory reporting, stress testing and capital assessment processes provide clear guidance and set expectation for compliance |
| Risk Assessment | ▪ Define objectives and identify risks to ensure coverage across reports and processes  
▪ Employ sound methodologies for measuring all material risks pertaining to underlying reports and processes  
▪ Prioritize based on sound methodologies to take into account risk tolerance/materiality as well as the size and complexity of the underlying processes |
| Control Activities | ▪ Design controls throughout the reporting process flow to mitigate the risks identified in the risk assessment and cover both business processes and technology |
| Information & Communication | ▪ Ensure adequate lines of communication/escalation are established for internal and external purposes  
▪ There should be sufficient level of information around adequacy of internal controls, including reporting metrics and reports |
| Monitoring | ▪ Establish effective monitoring processes to assess control activities and evaluate effectiveness of internal controls; this may include evaluations to determine whether components of internal controls are present and are functioning as intended  
▪ This may also include assessment of whether there is oversight and critical evaluation of the framework, key assumptions, results, uncertainty and limitations by senior management and the Board  
▪ Finally, there should be a mechanism to communicate internal control deficiencies |
Internal Controls Considerations – Three Lines of Defense

Key components of an effective Internal Controls Framework pertaining to FR Y-14A/Q/M reporting may include the following:

- Periodic risk assessments and design of effective controls over the report preparation processes and data to address relevant risks
- Detailed documentation of the end-to-end report preparation processes and controls
- On-going and periodic controls effectiveness testing, validation of risk assessments, and adequacy of reporting documentation
- Independent (from report production) Quality Assurance (QA) and Data Integrity function at the corporate and lines of business level, coordination with SOX teams
- Process to analyze and mitigate issues/errors identified by monitoring activities
- Internal Audit coverage of end-to-end FR Y-14A/Q/M reporting, including first and second lines of defense

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<tbody>
<tr>
<td>- Implementing attestation framework</td>
<td>- Independent &amp; objective</td>
<td>Program expansion to address attestation framework:</td>
</tr>
<tr>
<td>- Establishing materiality thresholds (actual data)</td>
<td>- Effective challenge</td>
<td>- Reporting data accuracy and integrity</td>
</tr>
<tr>
<td>- Designing and implementing effective controls over data accuracy and underlying processes</td>
<td>- Data validation</td>
<td>- Effectiveness of key reporting controls</td>
</tr>
<tr>
<td>- Defining “Fair Representation” (projected data)</td>
<td>- QA coverage</td>
<td>- Adequacy of attestation process and second line of defense activities</td>
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<tr>
<td>- Ensure compliance with report instructions</td>
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Considerations for Internal Audit Functions

While the CFO attestation of the FR Y-14A should not significantly increase the Internal Audit requirements for their coverage of CCAR (as the CCAR requirements already require a comprehensive coverage of all seven principles of a capital adequacy process), Internal Audit should assess if their current testing coverage of the internal controls around the CFO attestation needs to be strengthened.

- Internal Audit should formally determine its materiality thresholds. This may be challenging due to the qualitative factors that should be considered.
- Internal Audit should assess their defining factors for a material weakness as it relates to the CFO attestation, both a quantitative and qualitative perspective.
- Internal Audit should consider performing a ‘readiness assessment’ or, at a minimum, perform continuous monitoring routines to support any required changes, including changes to the technology infrastructure over the preparation and reporting of the FR Y-14A.
- Internal Audit should review its current testing approach over CCAR to determine if additional internal control and/or transactional testing of the FR Y-14A is needed.
- Internal Audit should review the structure for the reporting (e.g., timing of report, communication of deficiencies) of its testing results of the FR Y-14A internal control framework.
- Internal Audit should ensure there is adequate time for remediation of deficiencies to assist the CFO in its attestation.
Materiality
Qualitative and Quantitative Materiality Factors

Responsible CFOs or equivalent senior officers would have to attest that the underlying FR Y-14A/Q/M reporting data is materially accurate and related controls are effective. The framework for determining materiality in context of the attestation will have to be stipulated in a policy document.

The initial step in determining materiality related to regulatory reports is to implement a consistent and systematic approach to the treatment of regulatory reporting errors, omissions, and the determination of potential restatement (refiling). In determining whether or not a potential reporting error or omission is deemed material, it needs to be both qualitatively and quantitatively evaluated.
Industry Practices Related to Materiality around CCAR

An issue may be considered material if its omission or misstatement makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement.

While materiality as defined by SOX process can be a starting point, regulatory reporting materiality, including FR Y-14A/Q/M are generally at a more granular level.

For the purposes of internal controls, materiality should also be considered when evaluating regulatory reporting controls at a process and data level.

One of the acceptable practices is to establish ranges for threshold categories that can be used to determine the appropriate level of materiality.

<table>
<thead>
<tr>
<th>Potential Threshold Categories</th>
<th>Other Considerations</th>
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<tbody>
<tr>
<td>Tier 1 Capital</td>
<td>Influence on loss models, projections and ratios</td>
</tr>
<tr>
<td>Total Assets</td>
<td>Evaluate Dollar ($) amount and percentage (%)</td>
</tr>
<tr>
<td>PPNR</td>
<td>Materiality assessment processes</td>
</tr>
<tr>
<td>Total Credit Losses</td>
<td>Memorandum Items</td>
</tr>
<tr>
<td>Total AUM</td>
<td>Impact of line items across multiple schedules and other reports</td>
</tr>
<tr>
<td>Notional Value</td>
<td>Materiality assessment processes</td>
</tr>
<tr>
<td>Off-Balance Sheet</td>
<td>Impact on Prior Period(s)</td>
</tr>
<tr>
<td>Impact on Prior Period(s)</td>
<td>Average Daily Transaction Values</td>
</tr>
</tbody>
</table>

Materiality should be consistent and aligned to FR Y-9C reporting. Materiality for FR Y-9C follow:
- SEC Staff Accounting Bulletin No. 99, Materiality (SAB 99)
- FASB Concepts Statement No. 8
- Management evaluation on a schedule and line item level

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