Statement of
Martin J. Gruenberg,
Acting Chairman,
Federal Deposit Insurance Corporation
On
"Examining Bank Supervision and Risk Management
In Light of JPMorgan Chase's Trading Loss"
Before the
Committee on Financial Services,
United States House of Representatives
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Chairman Bachus, Representative Frank and members of the Committee, thank you for the opportunity to testify this morning on behalf of the Federal Deposit Insurance Corporation on bank supervision and risk management as it concerns recent trading losses at JPMorgan Chase.

The recent losses at JPMorgan Chase revealed certain risks that reside within large, complex financial institutions. They also highlighted the significance of effective risk controls and governance at these institutions.

The four FDIC-insured subsidiaries of JPMorgan Chase firm have nearly $2 trillion in assets and $842 billion in domestic deposits. As the deposit insurer and backup supervisor of JPMorgan Chase, the FDIC staff works through the primary federal regulators, the Comptroller of the Currency and the Federal Reserve System, to obtain information necessary to monitor the risk within the institution.

The FDIC maintains an onsite presence at the firm, which currently consists of a permanent staff of four professionals. The FDIC staff engages in risk monitoring of the firm through cooperation with the primary federal regulators. Following the disclosure of JPMorgan Chase’s losses, the FDIC has added temporary staff to assist in our current review. The team is working with the institution’s primary federal regulators to investigate both the circumstances that led to the losses and the institution’s ongoing efforts to manage the risks at the firm. The agencies are conducting an in-depth review of both the risk measurement tools used by the firm and the governance and limit structures in place within the Chief Investment Office (CIO) unit where the losses occurred. Following this review, we will work with the primary regulators to address any inadequate risk management practices that are identified.

Following the announcement of these losses in May, the FDIC joined the OCC and the New York Federal Reserve Bank in daily meetings with the firm. Initially, these meetings focused on gaining an understanding of the events leading up to the escalating losses in the CIO synthetic credit portfolio. The FDIC has continued to participate in these daily meetings between the firm and its primary regulators. We are looking at the strength of CIO’s risk management, governance and control frameworks, including the setting and monitoring of risk limits. The FDIC is also reviewing the quality of CIO risk reporting that has historically been made available to firm management and the regulators. Our discussions have also focused on the quality and consistency of the models used in the CIO as well as the approval and validation processes surrounding them. Although the focus of this review is on the circumstances that led to the losses, the FDIC is also working with JPMorgan Chase’s primary federal regulators to assess any other potential gaps within the firm’s overall risk management practices.

As a general matter, and apart from the specifics of this situation, evaluating the quality of financial institutions’ risk management practices, internal controls and governance is an important focus of safety-and-soundness examinations conducted by the federal banking agencies. Onsite examinations provide an opportunity for supervisors to evaluate the quality of the loan and securities portfolios, underwriting practices, credit review and administration, establishment of and adherence to risk limits, and other matters pertinent to the risk profile of an institution. One important element of risk management is that senior management and the board receives accurate and timely information about the risks to which a firm is exposed. Timely risk-related information is needed by institution management to support decision making and to satisfy disclosure requirements -- and it is an important element of supervisory review.

Without speaking to the specifics of the case for which a review is underway, the recent losses attest to the speed with which risks can materialize in a large, complex derivatives portfolio. The recent losses also highlight that it is important for financial regulatory agencies to have access to timely risk-related information about derivatives and other market-sensitive exposures, to analyze the data effectively, and to regularly share findings and observations.

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