



Bank Of China USA

Fed Net Debit Cap Procedure


April 2021

BOCNY Fed Net Debit Cap Procedure
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1. Background

The purpose of the Fed Net Debit Cap Procedure (“the Procedure”) is to outline relevant departments’ responsibilities and the process to establish a net debit cap category for Bank of China USA (“BOCNY” or the “Bank”) according to Federal Reserve Bank’s (“Fed”) Payment System Risk Policy (“PSR”), and the process of using it when needed.

1.1. Rationale

Under Fed’s PSR policy, each institution that maintains an account at a Federal Reserve Bank is assigned or may establish a net debit cap, which limits the amount of intraday Federal Reserve credit that the institution may use during a given interval.

An institution’s net debit cap refers to the maximum dollar amount of daylight overdrafts that it may incur in its Federal Reserve account. An institution’s cap category and its capital measure determine the dollar amount of its net debit cap. An institution’s cap category normally does not change within a one-year periods. The policy defines six cap categories: zero, exempt-from-filing, de minimis, average, above average, and high. Each cap category is associated with a cap multiple, ranging from 0-2.25. To establish a net debit cap in the high, above average, or average category, an institution must perform a self-assessment of its creditworthiness, intraday funds management and controls, customer credit policies and controls, and operating controls and contingency procedures. The results of the applicable self-assessment should indicate the appropriate cap category for the institution.

To ease the burden on the small over drafters of engaging in the self-assessment process and to ease the burden on the Fed of administering caps, Fed allows institutions that meet reasonable safety and soundness standards to incur De Minimis amounts of daylight overdrafts without performing a self-assessment. According to Fed’s PSR, an institution may incur daylight overdrafts of up to 40% of its capital measure if the institution submits a board of directors’ resolution.

In addition, the FFIEC Handbook also requires the institution complies with the Fed’s PSR.

The procedure defines the roles and responsibilities of BOCNY related departments, and establishes the process for the annual Fed Net Debit Cap application & usage.

2. Scope

The scope of the Procedure applies to relevant Front Line Units (FLUs), Independent Risk Management (IRMs) and the Third Line of Defense, including CLD, FMD, FID, OSD, TRY, ORD, MRD, CRM, LCD and IAD.

The procedure focuses on the annual Fed Net Debit Cap application process to ensure the Bank complies with regulatory requirement.

3. Roles & Responsibilities

3.1. Procedure Governance

The Procedure is drafted and maintained by MRD. The respective stakeholders CLD, TRY, FMD, FID, CRM, ORD and MRD are the reviewers. BOCNY Market and Liquidity Risk Committee (“MLRC”) is the approval authority of this procedure.

The Procedure should be periodically reviewed and updated at least once a year to reflect any changes in the related policies and processes.

3.2. Procedure Implementation

Related departments’ employees are responsible for implementing the Procedure as below.

3.2.1. Roles and Responsibilities for FLUs and IRMs in applying for net debit cap

3.2.1.1. Leading / Coordinating Department

In this process, MRD is assigned as the leading / coordinating department with primarily roles and responsibilities as follow:

- Communicate with Fed on the normal information request and response, questions and answers.
- Coordinate the recommendation and information for executive management decision
- If Fed self-assessment is needed, lead the assessment process by coordinating with each related department to complete its own required assessment assigned by executive management.
- After the completion of all parts of the assessment, send all related documents to obtain the approval from the appropriate committee BOC Board of Directors (“Board”).

3.2.1.2. Executive Management

- Review the decision on the appropriate net debit cap category & usage when needed by considering the Bank’s liquidity profile and business strategy.
- If De Minimis Cap is decided, instruct the coordinating department to pursue the Board approval.
- If Average, Above Average or High Cap is decided, assign the appropriate FLUs to conduct self-assessment. The leading / coordinating department will consolidate the self-assessment results.

3.2.1.3. Related FLUs

FMD is responsible for collecting the BOC group’s financial information from HO and file FR 2225 (BOC group’s worldwide capital) to Fed.

If self-assessment is needed, relevant FLUs, including FMD, TRY, CLD, FID, BKD and OSD are responsible for providing information and conducting the self-assessment with regards to their business areas.

3.2.1.4. Independent Risk Management

If the self-assessment is required, the IRMs are responsible for the following.

- CRM is responsible for 1) Providing credit risk related information such as credit policies and procedures; 2) Review the FLUs' self-assessment related with credit risk area.
- ORD is responsible for 1) Providing operational risk related information such as operational risk policies and procedures; 2) Review the FLUs' self-assessment related with operational risk area.
- MRD is responsible for 1) Providing liquidity risk related information such as liquidity risk policies and procedures; 2) Review the FLUs' self-assessment related with liquidity risk area. 3) MRD is also responsible for reviewing and updating this procedure. In addition, MRD takes the roles and responsibility as the leading/coordinating department stated above.

3.2.2. The enhanced process of using net debit cap

Usage Amount

The usage of net debit cap utilization amount shall be aligned with the bank's business needs, and historical intraday liquidity stressed events. Therefore the bank sets up \$3 Billion and \$8 Billion Fed net debit cap usage thresholds in the USD clearing system to better monitor and manage the usage level. The implemented thresholds are recalibrated according to the bank's business needs and management decision.

Net debit cap shall be used as the last resort of the bank's intraday liquidity source according to the bank's liquidity risk management policy, and prudently managed to prevent from overnight overdraft.

Roles and Responsibilities

- CLD is responsible for 1) Process payments by following related procedures; 2) Monitor Fed account balance and sent intraday position report; 3) Notify and escalated to related departments and executive managers when thresholds are triggered.
- TRY is responsible for 1) Project Fed account end of day balance; 2) Assess overnight overdraft risk and conduct contingent funding plan to meet potential liquidity shortfalls.

Monitoring and Controls

- 1) Fed account balance triggers the threshold of \$2 Billion.
 - CLD sends out notification to TRY immediately and provide: (1) Unsettled payments in system and critical payments clients already notified; (2) Known OSD custody security settlement payments need to process; (3) Projected usage level of Fed net debit cap.
 - CLD notifies related departments.
- 2) Fed account balance drops below zero, and Fed net debit cap starts to be used.
- 3) Fed net debit cap usage reaches \$3 Billion.
 - CLD continues to send out notification and updates timely.
 - CLD holds on all non-time-sensitive payments while continues to manually release time-sensitive payments.
- 4) Fed net debit cap usage reaches \$8 Billion.
 - CLD continues to manually release time-sensitive payments.
 - CLD escalates to related EVPs and department heads through email and phone call notification.

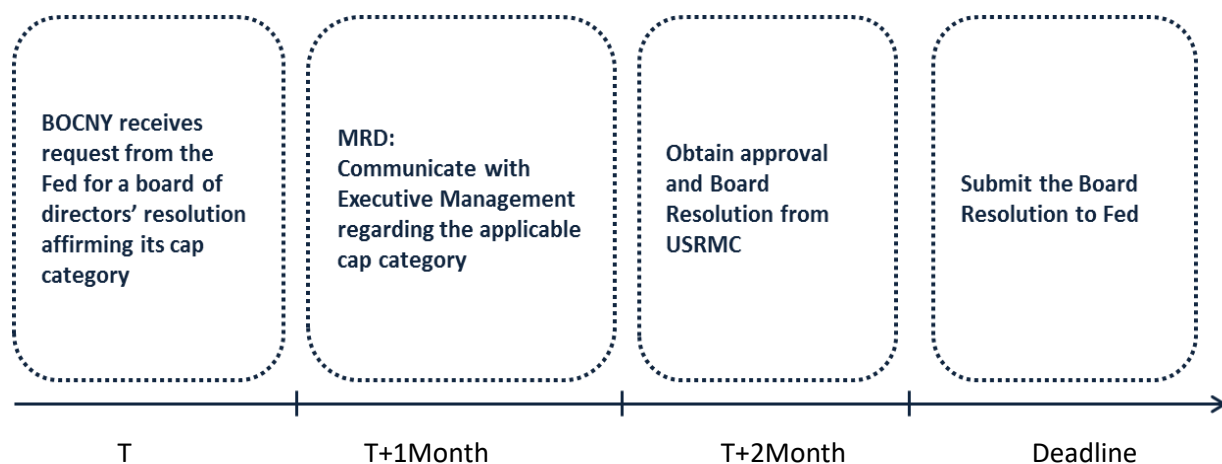
- TRY notifies MKD to conduct overnight repo with same day settlement on the available unencumbered assets before 10:30 AM, intending to prevent overnight overdraft at Fed account balance.

4. Procedure Instructions

4.1. Fed Net Debit Cap Application process

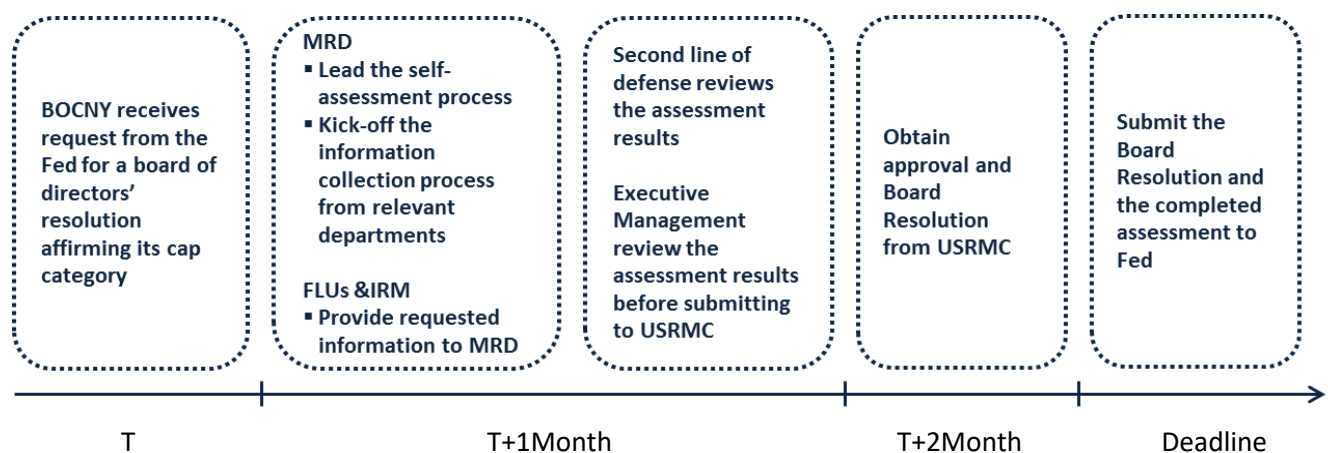
This is an annual process carried out by relevant departments and the process flow is illustrated as the figure below.

Figure 1. Process Flow for Fed net debit cap application without self-assessment requirement



Note: the Bank may request Fed for the extension of the deadline.

Figure 2. Process Flow for Fed net debit cap application with self-assessment requirement



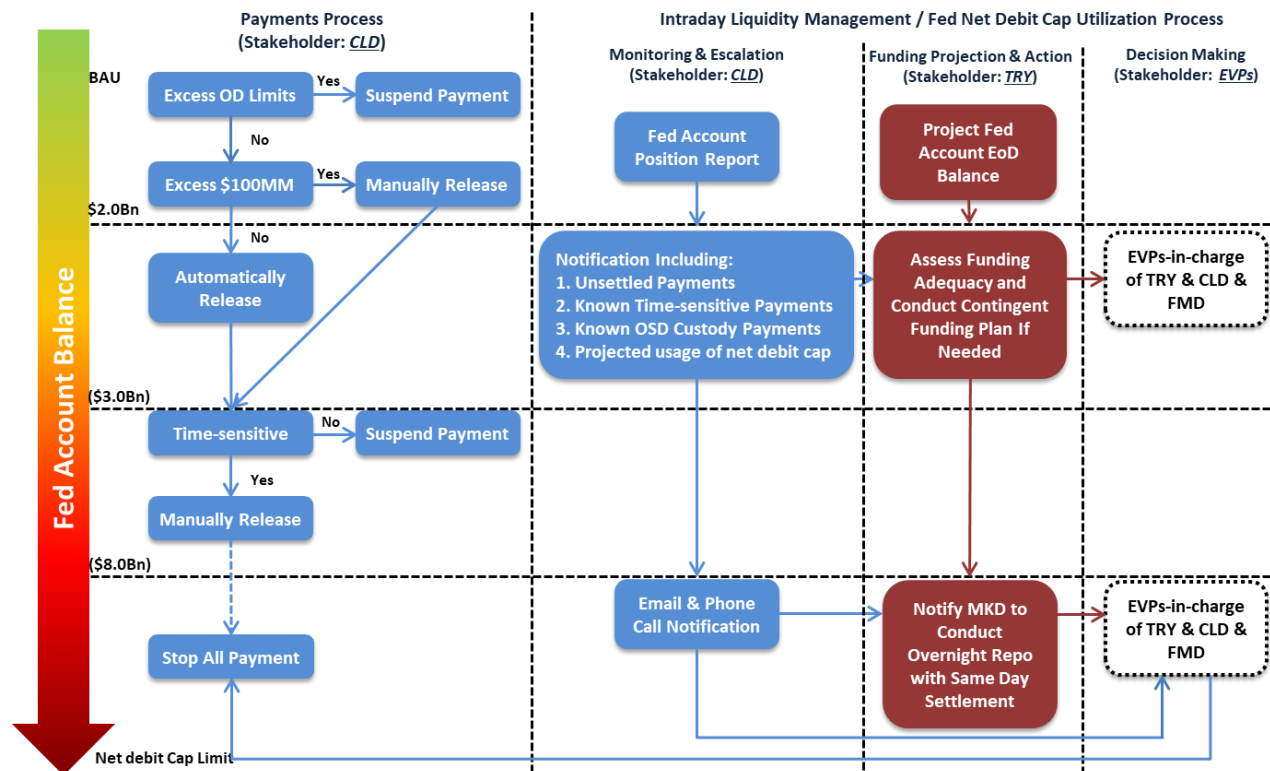
Note: the Bank may request Fed for the extension of the deadline.

4.1.1. Executive Management Review

The EVPs-in-charge can also review the self-assessment results before sending to the Head Office for approval.

4.2. Enhanced Monitoring Process and Controls

The process of monitoring and controls for intraday liquidity management are illustrated as below per internal discussion and management decision.



5. Update Requirements

This Procedure will be reviewed and approved at least every three years, and will be updated any time on a need basis. Material revision will require the approval of Executive Management in charge of the Department.

6. Exceptions & Exemptions

Exceptions and exemptions to the Procedure must be managed under the exception framework established in the associated policy.

7. Reference Information

7.1. External Regulations

- Federal Reserve, Policy on Payment System Risk Policy
- Federal Reserve, Prudential Standards for Large Bank Holding Companies, Savings and Loan Holding Companies and Foreign Banking Organizations; Final Rule (12 CFR Part 252)
- Federal Financial Institutions Examination Council (FFIEC), IT Examination Handbook: Wholesale Payment Systems

7.2. Other Related Branch Policies, Procedures, and/or Guidance

- BOCNY Liquidity Risk Management Policy
- BOCNY Credit Risk Management Policy

8. Glossary

The glossary lists definitions of terms and acronyms used in the policy.

| Abbreviation | Name |
|--------------|--|
| BKD | BOCNY Banking Department |
| BOCNY | Bank of China New York Branch or Bank of China USA |
| CLD | BOCNY Clearing Department |
| CRM | BOCNY Credit Risk Management Department |
| FID | BOCNY Financial Institution Department |
| FLU | First Line Unit |
| FMD | BOCNY Financial Management Department |
| IAD | BOCNY Internal Audit Department |
| IRM | Independent Risk Management |
| LCD | BOCNY Legal and Compliance Department |
| MKD | BOCNY Global Market Department |
| MRD | BOCNY Market Risk Management Department |
| ORD | BOCNY Operational Risk Management Department |
| OSD | BOCNY Operational Service Department |
| TRY | BOCNY Treasury Department |