

CONFIDENTIAL

FEDERAL RESERVE BANK OF NEW YORK

NEW YORK, N.Y. 10045-0001

AREA CODE 212-720-5000

August 4, 2006

Ms. Michelle A. Vinnedge  
Board of Governors of the  
Federal Reserve System  
Division of Banking Supervision  
and Regulation  
Surveillance Section  
Mail Stop 198  
Washington, D.C. 20551



Dear Ms. Vinnedge:

Please find enclosed a copy of the following examination letter report:

<u>Name</u>	<u>Start Date</u>	<u>RSSD #</u>	<u>Event #</u>
Citigroup, Inc.	05/08/06	1951350	489059

Target area: Risk Control Self Assessment  
Risk Factors - Operational Risk

Examiners for the Federal Reserve Bank of New York and the Office of the Comptroller of the Currency conducted this examination jointly.

Sincerely,

A handwritten signature in cursive script that reads "Jim Robbins".

Jim Robbins  
Staff Leader  
Bank Supervision

Enclosure

RESTRICTED FR

FEDERAL RESERVE BANK OF NEW YORK

NEW YORK, N.Y. 10045-0001

AREA CODE 212-720-5000

July 13, 2006

RCSA # 1951350  
Event# - 489059  
S/D 5/18/06

BOARD OF GOVERNORS  
OF THE FEDERAL RESERVE SYSTEM



Ms. Susan A. Locke  
Managing Director  
Global Risk Management and Compliance  
Citigroup  
399 Park Avenue  
3rd Floor  
New York, NY 10022

COPY

Dear Ms. Locke:

Examiners from the Federal Reserve Bank of New York with the participation from the Office of the Comptroller of the Currency completed a review of Citigroup's Risk and Control Self Assessment (RCSA) framework. The primary goal of the review was to evaluate the effectiveness of the existing RCSA process as a control tool across five dimensions including; quality, comprehensiveness, aggregation and reporting, validation, and corrective action plans. Examiners also discussed with management efforts underway to enhance the RCSA framework, particularly as it relates to the technology initiatives.

Citigroup's current RCSA framework is an effective tool for identifying key risks and their associated controls, and for assessing the effectiveness of said controls. Management's recent efforts to rationalize the self assessment processes across the firm with the establishment of the RCSA and Operational Risk Council, as well as to develop an automated firm-wide RCSA platform signal a strong commitment towards ensuring that RCSA remains a key pillar of its control framework.

Examiners did note, however, inconsistent execution of the RCSA mandate. Specifically, examiners observed a large number of applications at the business level used to carry out the firm-wide RCSA process, and inconsistent approaches for incorporating the risks engendered by new products into the RCSA framework. Additionally, examiners identified areas in need of further clarification related to risk acceptance and documentation practices of Audit and Risk Review (ARR) as they relate to RCSA audits. These and other points are discussed in more detail below.

**Technology Supporting RCSA Preparation**

A myriad of technologies currently support RCSA preparation across the firm with varying levels of functionality available within each application. Management has identified approximately

thirty technology applications across the firm and has acknowledged the need for a single RCSA technology solution. We are pleased with management's initiative in this regard.

Given the sheer scope of the RCSA technology initiative, a granular project plan detailing resources, milestones, dependencies, and outlining clear project governance to facilitate the escalation of issues is essential. Management has indicated that it will deliver a detailed plan to examiners in the near term. That said, between now and the scheduled deployment date of this firm-wide RCSA technology, business units will continue to develop and enhance their existing applications to support RCSA efforts.

### **New Product Approval**

Variation in the risk profile of a given business area can be driven by the introduction of new products. In exploring the linkages between new product approval processes and RCSAs, examiners found extensive variation across sectors regarding the methods used to incorporate new product risk into the RCSA framework. For example, some sectors formally reconciled new products to RCSA activities on a quarterly basis; however, this was not a firm-wide practice. Examiners did note that staff involved in the new product approval process often contribute to the preparation of RCSAs. Where this is the case, RCSA preparers were aware of new products and risks introduced into the business unit. Current RCSA policy does not provide guidance on how risks introduced through the new product approval processes should be linked to the RCSA process, and, as such, business units are responsible for establishing and documenting their own procedures. Management is encouraged to explore more disciplined approaches for incorporating the risks associated with new products into RCSAs.

### **Risk Acceptance**

Management does not have an explicit risk acceptance process embedded in its RCSA framework; a practice observed at other large institutions. Implicit in the RCSA guidance is an assumption that all residual risks will be addressed through a corrective action plan (CAP). With risk acceptance, there is recognition of the fact that there may be instances where a CAP may not be effective in fully mitigating the inherent risk due to, for example, limitations stemming from legal or country requirements or industry practices. In these cases, it would be important for a business to document that it has explicitly accepted the residual risk in addressing the control deficiency. A risk acceptance policy would ensure that management is apprised formally of the risks undertaken by the business line.

### **Audit Documentation**

Among other items, ARR develops a planning memo and a Tailored Review Program (TRP) when conducting RCSA-related audits. The TRP is derived from the Standard Audit Program (SAP) for RCSAs. Based on the sample reviewed, in most cases, audit followed the SAP template for

COPY

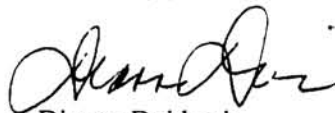
Ms. Susan A. Locke  
July 13, 2006

RCSA testing. However, it was observed that at times the SAP components related to RCSAs were excluded from the TRP without supporting rationale in the planning memo. Audit is encouraged to enhance such documentation going forward.

Please provide a written response to the matters discussed above within 45 days of receipt of this letter. In closing, please note that this letter contains confidential material and should be treated accordingly by your organization. As such, the contents of this letter are subject to the rules of the Board of Governors of the Federal Reserve System regarding the disclosure of confidential supervisory information. Under no circumstances shall the company, its agencies, or any of its directors, officers, or employees disclose or make this information public in any manner. We would like to express our appreciation for the courtesies and cooperation extended to the review team by Citigroup's management and staff. Should you have any questions, please feel free to contact Eric Caban at (212) 720-2411, or myself at (212) 527-0217.

COPY

Very truly yours,

Dianne Dobbeck  
Vice President

Cc: D. Bushnell M. Helfer B. Howard L. Kaden S. Krawcheck T. Rollauer  
M. Zuckert