



# Governance and Risk Mitigation A Supervisor's Perspective

IOR OpRisk Forum 2013

16 May 2013 | Cologne

Bernd Rummel | Principal Policy Expert, EBA

# The role of EBA – main objectives and tasks

## European Banking Authority:

- > Founded 01.01.2011
- > Successor of CEBS

## Main objectives:

- > Establishing EU single rule book
- > Promoting and enhancing quality and consistency of supervision

## Main tasks:

- > Develop binding technical standards, guidelines, recommendations
- > Enhancing effectiveness colleges
- > EU-wide risk assessments
- > Emergency Situations

# CRD IV

## Institutions shall have robust governance arrangements:

- > clear organisational structure with well-defined, transparent and consistent lines of responsibility,
- > effective processes to identify, manage, monitor and report the risks
- > adequate internal control mechanisms
- > remuneration policies and practices that are consistent with and promote sound and effective risk management.

# Frequent weaknesses in the financial crisis

- > Too complex organisation
- > Unclear definition of roles within the organization
- > Lack of committee structures (audit, risk, nomination, remuneration)
- > Conflicts of interests (e.g. role of CRO and CFO mixed up)
- > Low standing of risk management function and CRO
- > No holistic view
- > Overreliance on risk models

# Governance and operational risk

## Operational risk losses often result from weak governance

breach of law

rogue trading

external fraud

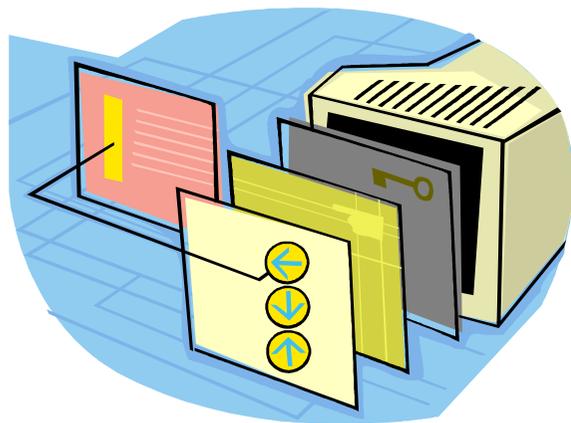
lack of knowledge

giving wrong advice

weak controls

lack of business continuity capacity

discrimination



**Processes**



**People**



**Systems**



**External events**

# Supervisory Expectations

## Risks shall be kept under control

- > Banking comprises risk taking
- > Capital alone is not sufficient to keep risks under control, a precondition is that risk is appropriately managed
- > Setting and implementing of a business and risk strategy
- > Identification and assessment: quantitative and qualitative risk management tools; scenario analysis and stress tests
- > Measures to ensure that risks are kept in line with strategy/limits
- > Possible measures: avoid, accept, mitigate (or take) risks

# CRD IV

## Management body is responsible for the treatment of risk

- > Management body approves and periodically reviews the strategies and policies for taking up, managing, monitoring and mitigating the risks the institution is or might be exposed to

# Governance and Risk

**ICAAP – sound strategies and processes to assess and maintain the internal capital that is appropriate to ongoing cover the risks**

- > Assessment of all relevant risks (e.g. credit, market, operational, concentration, liquidity, reputation, interest rate, macroeconomic risk)
- > Assessing the appropriateness of internal governance
- > Assessment of mitigating factors
- > Assessment of risk bearing capacity

**Competent authority performs Supervisory Review and Evaluation Process (SREP)**

# Two dimensions of risk mitigation

## Frequency and Severity of potential losses

- > Strong governance keeps risk under control
  - reduces the frequency of risk events
  - limits the overall exposure
- > Specific Risk Mitigation tools
  - collateral, CDS, diversification, netting
  - insurance (e.g. oprisk, relevant in Pillar II and AMA)
- > Specific risk mitigation tools considered in the SREP, but use not mandatory as long as risks are appropriately managed and covered

# EBA Guidelines on Internal Governance

Update planned in 2015 to accommodate CRD IV

Corporate structure  
and organisation

Management body

Risk management

Internal control

Systems and  
continuity

Transparency

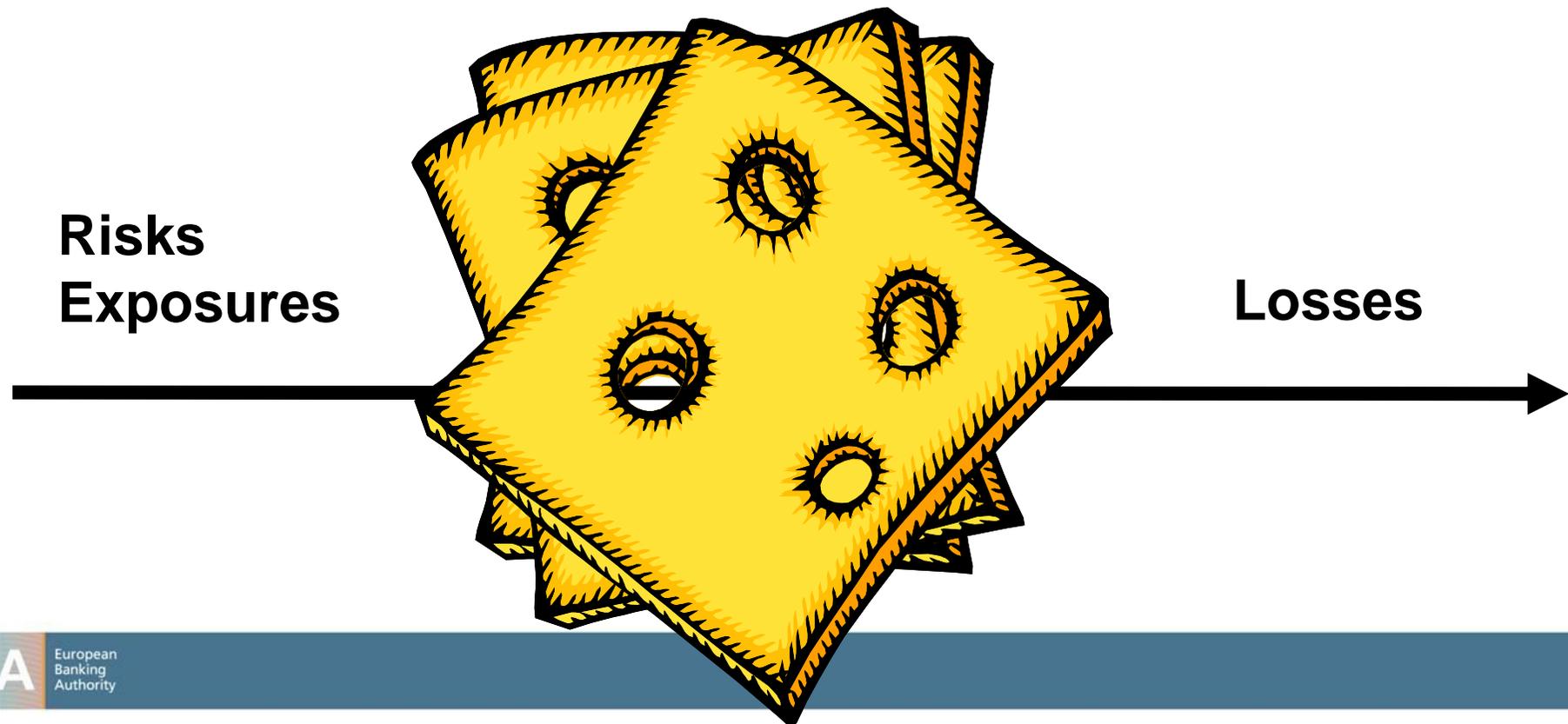
# Three lines of defence

## Risk strategy and risk management/control to be implemented

1) Risk management within business line

2) Independent risk control

3) Internal audit



# Risk management

## Develop a risk culture in line with the risk tolerance/appetite

- > business strategy and risk appetite to be implemented
- > awareness and clear responsibilities regarding risk management
- > holistic risk management framework – group and solo level
- > strong change processes (products, processes and systems)
- > business continuity requirements

# Risk Control Function

## Chief Risk Officer (CRO) should be appointed

- > responsible for providing comprehensive, understandable and well interpreted risk information
- > qualification requirements apply
- > removal of CRO to be disclosed
- > replacement only with approval of non-exec. directors
- > supervisory authority to be informed about the reasons

# Conclusions

- > Banking Business Comprises Risks, expressed in banks strategy
- > Capital is important, but not sufficient for risk management purposes
- > Sound governance enables risk management and control
- > Appropriate measures to identify and assess risks and to keep the risks with institutions strategy – including risk mitigation
- > Risks, governance and risk mitigation assessed within SREP

# Contact Information

Bernd Rummel

Floor 9 | Tower 42 | 25 Old Broad Street

London EC2N 1HQ | United Kingdom

t +44 (0)20 7382 1767

f +44 (0)20 7382 1771

[info@eba.europa.eu](mailto:info@eba.europa.eu)

[www.eba.europa.eu](http://www.eba.europa.eu)