

# Operational Risk Management

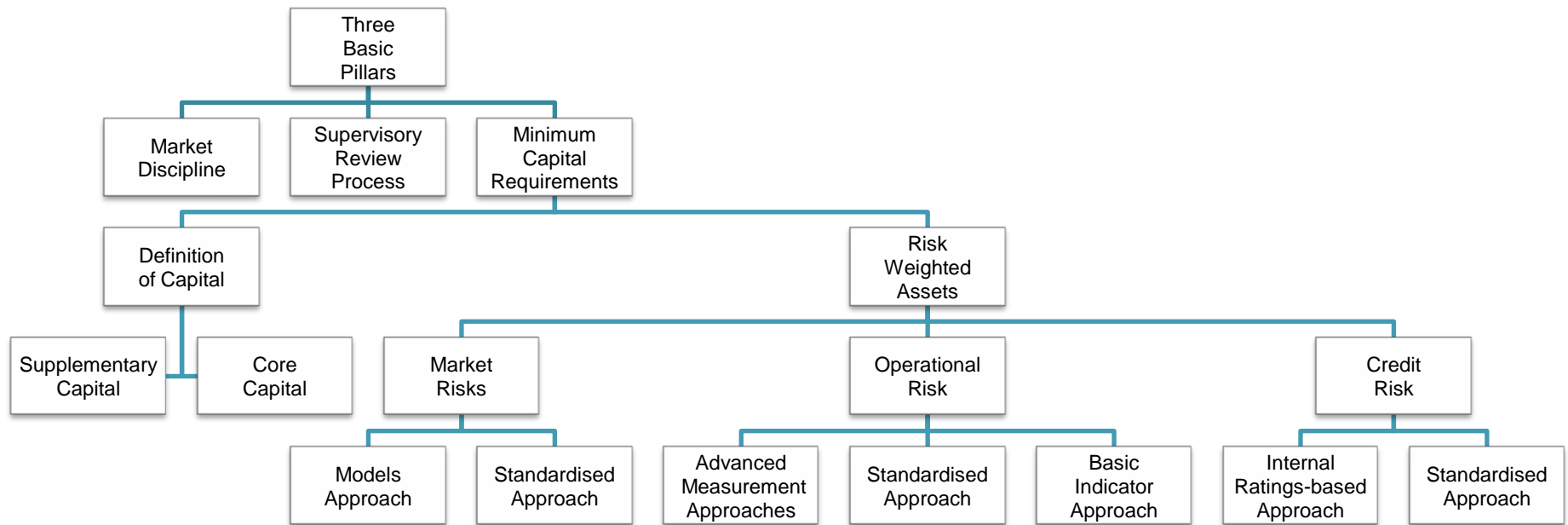
## Risk & Control Self-Assessment (RCSA) Workshop

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# Capital Requirements (Basel II)

- The new Basel Capital Accord specifically introduces a capital charge related to the operational risk an institution faces.
- Additionally, Corporate Governance requirements place a specific duty on directors to address operational risk issues.



# Key Success Factors

- Knowledgeable Facilitators
- Business – Subject Matter Expert Participation
- SELF ASSESSMENT !!! NOT AUDIT
- Part of Annual Performance - Attendance

# RCSA Models

- Scoring Models
- Pre Defined Models – Vendor Scoring Based
- Qualitative Models
- Hybrid Models

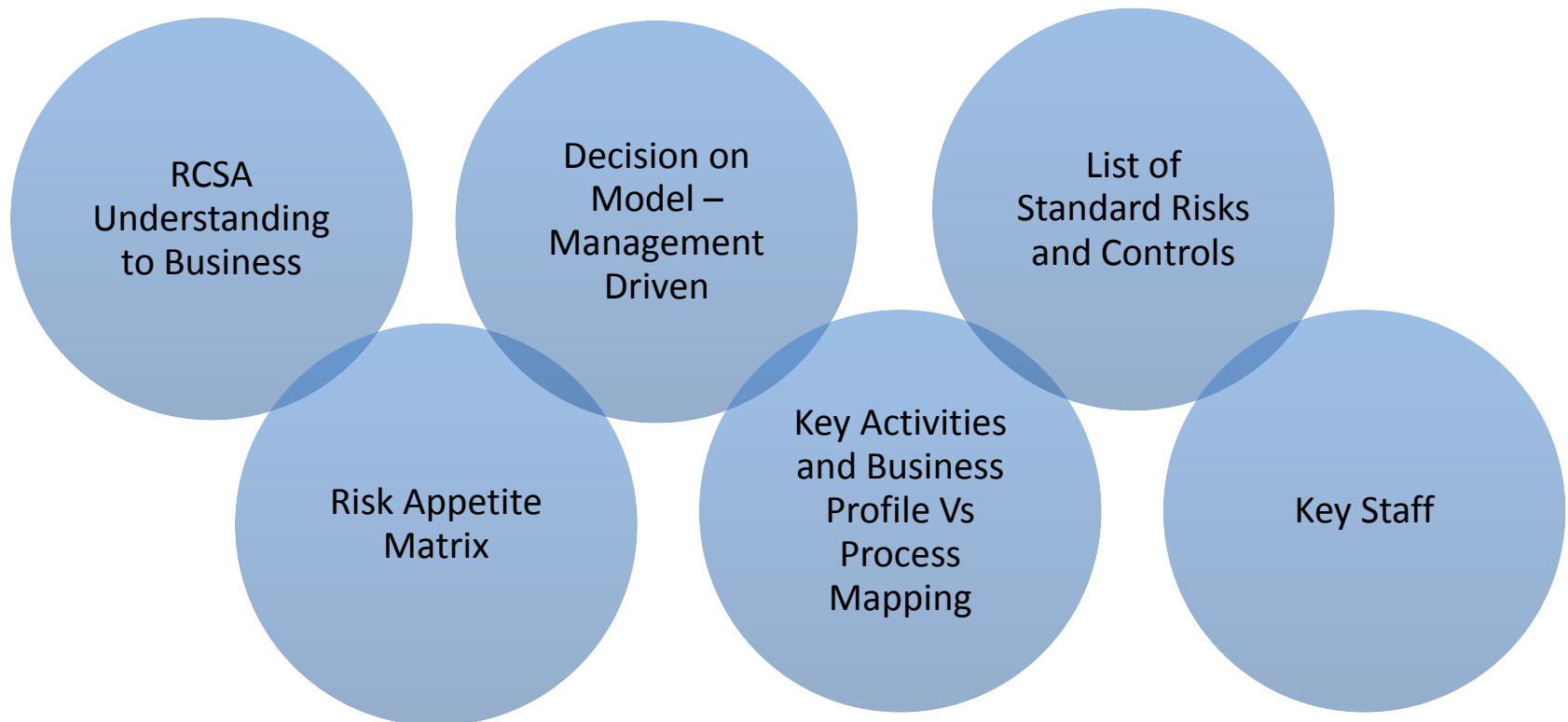
# RCSA Models

- Scoring Models
  - Scores Risks and Controls (Traditional Audit Approach)
  - Scoring 1- 10 linked to certain ranges
  - Total Score linked to overall Thresholds
- Pre-Defined Scoring Models
  - Scores Risks and Controls
  - Scoring Linked to financial ranges
  - Predetermined Weights for Control Effectiveness to arrive at residual risk
  - Inherent Risks – Control Score = Residual Risk

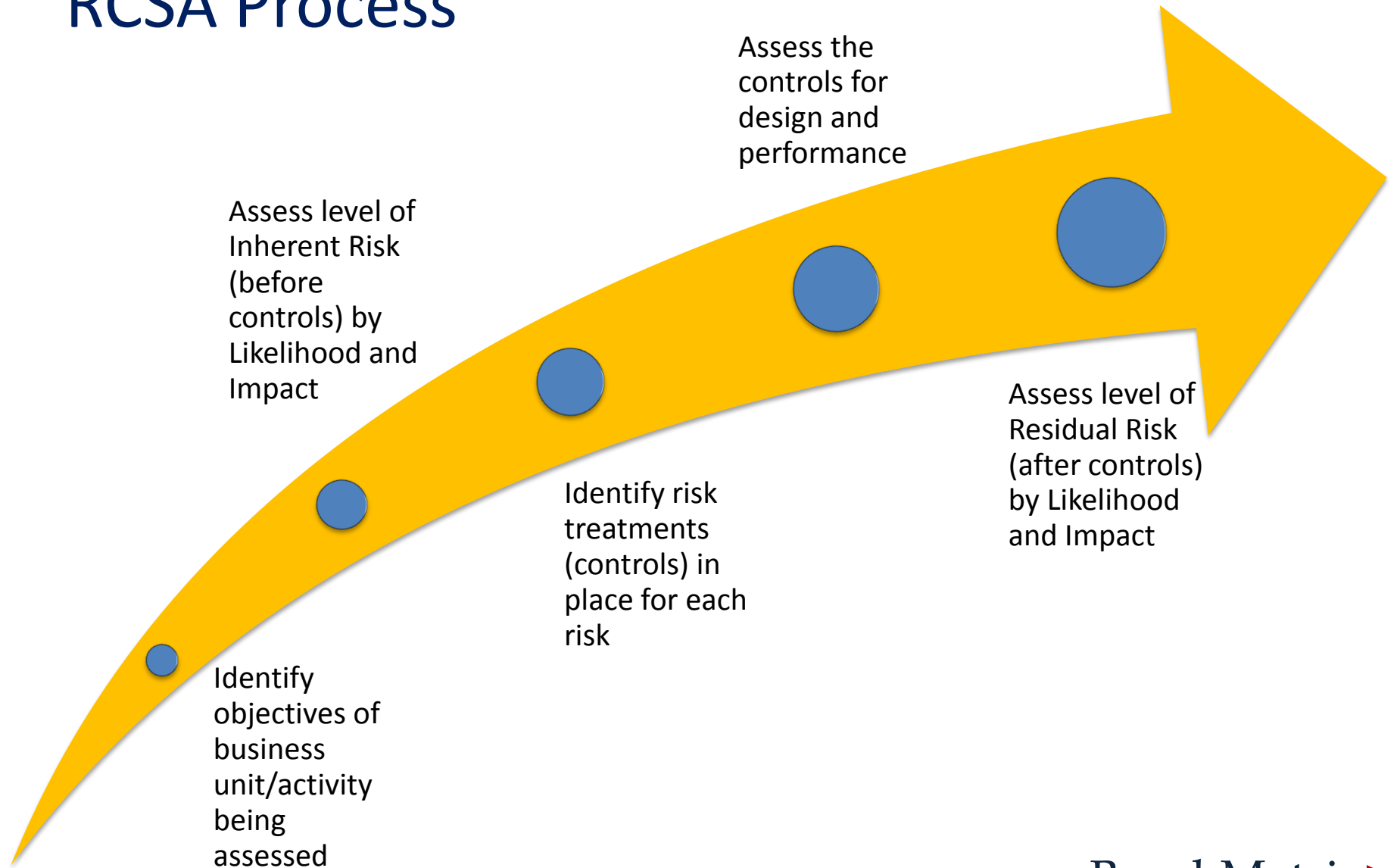
# RCSA Models

- Qualitative Models
  - High, Medium and Low (Traditional Risk Assessment)
  - Each Selection Defined Qualitatively (Subjective)
- Hybrid Models
  - High, Medium and Low (Traditional Risk Assessment)
  - Each Selection Defined Qualitatively (Subjective)
  - Each Selection Defined Quantitatively (Financial)
  - Over all Assessment Based on Financial and Non Financial
  - Inherent Risks – Residual Risks = Control Mitigation Value
  - Business Driven

# RCSA Pre-Requisites



# RCSA Process





# Help with Assessing Gross Risks

- **Assessment:** Frequency and impact should be assessed on a **Gross** (before the application of controls) basis
- **Impact:** Impact of a risk refers to the level to which the risk will affect the financial results of a business. UGB shall use the following dimensions for the impact buckets used for assessment:

S. No	Impact	Description
1	Catastrophic	This risk would probably have a very <b>significant financial severity</b> if it was to occur, or, this risk would cause severe reputation damage to the business.
2	High	This risk would probably have a <b>material financial severity</b> if it was to occur, or, would cause reputation damage to the business.
3	Moderate	This risk would probably have a <b>moderate financial severity</b> if it was to occur.
4	Low	This risk would probably have a <b>low financial severity</b> if it was to occur, or, would cause minimal reputation damage to the business.

# How to View IMPACT

- Inherent Risk
    - Controls (Standard Industry)
  - Residual Risk
    - Controls (Company Specific – An in control of the firm)
  - Target Risk
    - Desired Risk (Considering cost/benefit balance)
- 
- Consider Value – Average Transaction Size
  - Consider Room Temperature ! – Current environment other than specific controls
  - Consider activity outside your location or another bank
  - Consider going on long vacation – A new guy on the job takes over responsibility
  - Consider High Risk by admin/office boy and High Risk by Treasury (both on same report)

# How to View Frequency/Likelihood

- **Frequency:** Frequency of a risk refers to the chances of that risk occurring. UGB shall use the following dimensions for the frequency buckets used for assessment:

S. No	Frequency	Description
1	Frequent	Monthly (12)
2	Likely	Semi Annual (2)
3	Unlikely	Annual (1)
4	Remote (0.25)	1- 4 Years

- Consider Volumes
- Consider Number of Activities

# Help with Assessing Controls

- **Assessment:** A control shall be assessed based on its design and performance. A flaw in either component will result in a poor or ineffective overall control score.
- **Control Design:** Consider how well the control should work in theory, if it is always applied in the way intended.
- **Control Performance:** Consider the way in which the control is operated in practice, if it is applied when it should be and in the way intended by its designer.

# Help with Assessing Controls

Assessment	Description
Poor	Control is not effective in mitigating the portion of the risk it is designed for. <b>The control needs to be replaced.</b>
Inadequate	Control is not effective in mitigating the portion of the risk it is designed for. <b>Significant improvement is needed.</b>
Adequate	Control is mostly effective in mitigating the portion of the risk it is designed for. <b>Minor improvement is needed.</b>
Strong	Control is fully effective in mitigating the portion of the risk it is designed for. <b>For controls rated strong for a specific risk, the risk must be fully mitigated.</b>

# Risk Appetite Matrix

High Risk (Asset Management ) = High Risk (Administration)

Subjective Assessments = Subjective Value Addition ( ??? At the top)

Measurable Assessment = Difficult (Value addition)

RULE OF THUMB (Below)

Sample RAM				
Total Revenue	Low	Moderate	High	Catastrophic
	2 weeks	One month	Two Month	Three Months
<b>120 Million</b>	5 Million	10 Million	20 Million	30 Million

Addition Floor and Caps

# Risk Appetite Matrix

(will be discussed in the RCSA Workshop)

Investment Banking				
Total Revenue	Low	Moderate	High	Catastrophic
	2 weeks	One month	Two Month	Three Months
XXXX				

Asset Management				
Total Revenue	Low	Moderate	High	Catastrophic
	2 weeks	One month	Two Month	Three Months
XXXX				

# Heat Map

- Heat maps will be used to plot inherent and residual risks and assess their impact on the overall risk profile of the Bank.

Inherent Assessment Corporate Level				
Likelihood			2	1
				4
		8	6	
	15			9
Impact				

Residual Assessment Corporate Level				
Likelihood			1	1
		18	8	
	17	5		
Impact				



# RCSA Deliverables

- Top 20-30 Risks Identified with Associated Controls
- Management Decision on Acceptability of Risks not within Appetite or Decision on its Mitigation
- Action Plans with clear deadlines and responsible person

Thank You! Questions?