



Mrs Kerstin af Jochnick  
Chair  
CEBS  
Committee of European Banking Supervisors  
Floor 18, Tower 42  
25, Old Broad Street  
London EC2N 1HQ

**By e-mail : cp21@c-eps.org**

## **Compendium of supplementary guidelines on implementation issues of operational risk, CP 21, Febelfin comment**

Brussels, 06/04/2009,

Dear Madam,

Febelfin, i.e. the Federation which regroups four trade associations from the Belgian financial industry<sup>1</sup>, welcomes the opportunity to express its views on the consultation paper mentioned above. Following the decision of our Board meeting on 27<sup>th</sup> March 2009, we would like to make the following remarks.

We welcome the Compendium of supplementary guidelines for operational risk, however we need to point out they do not provide sufficient comfort in specific areas, reason for which we advocate further guidance and the establishment of minimum requirements concerning collection of incidents, scenario-analysis and risk and control self assessment.

In particular as from which moment on certain losses need to be taken into account ('pipeline' risks); and the identification and measurement of operational loss categories such as 'pending losses', 'near misses', 'operational risk profit/gains', 'opportunity cost/lost revenues' and 'timing impacts' are areas where banks would welcome more detailed guidance.

As operational risk measurement is still a young discipline and consequently far from standardised, we ask that, before any final guidelines are published a new consultation could be organised to find a consensus on a suitable guidance leaving sufficient flexibility in its application.

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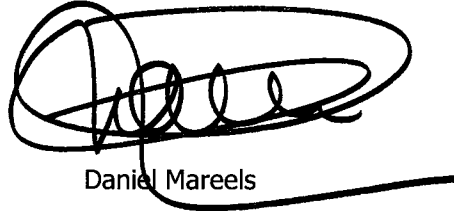
<sup>1</sup> The following trade associations are part of Febelfin: the Belgian Bankers' and Stockbroking Firms' Association (ABB/BVB); the Professional Union of Credit Providers (UPC/BVK); the Belgian Asset Management Association (BEAMA); the Belgian Leasing Association (BLA).

Our more detailed remarks can be found in the enclosure to this letter. We hope these remarks will be taken into account. Please do not hesitate to contact our services and our working group, should you want any further information.



Michel Vermaerke

Chief Executive Officer



Daniel Mareels

Director Taxation and Prudential,  
Legal and Compliance

Enc.

cc. Mr. J.P. Servais, Chairman of the Banking, Finance and Insurance Commission

## Compendium of supplementary guidelines on implementation issues of operational risk, CP 21, Febelfin comment, annex

### General remarks:

- At the moment there exists a range of practices concerning **operational loss definition practices**. In order to harmonize these, there is a **need for detailed regulatory guidance** in this field.
- We are of the opinion that there is need to **establish minimum requirements** concerning at least the following items:
  - **Collection of incidents;**
  - **Scenario-analysis;**
  - **Risk & control self assessment.**
- **The scope of operational risk loss:** in order to be able to implement the regulatory requirements in a proper way, **additional guidance is necessary in order to know at what moment certain losses need to be taken into account**. The treatment of these **'pipeline' risks**, and the relationship with the accounting treatment under IFRS are a major stumbling block in the creation of an operational loss database. More precisely we wonder how the recognition under the operational risk framework relates to the treatment of provisions under the IFRS-framework (need to establish differences between conditions such as 'probable', 'remote',...?) In particular, we wonder how potential losses are evaluated for each of the different stages an pipeline event can pass through? In this regard it would be useful to receive minimum requirements to estimate potential losses in each of the possible stages.
- **Type of elements/items that can result from an operational risk event:** as rightfully mentioned in the introduction of the Compendium, the identification of operational risk events is not a straightforward task. We agree with the classification of 'direct charges to P&L and write-downs', 'external costs incurred as a consequence of the event' and 'specific provisions taken following the occurrence of a risk event' as operational risk events. However, **defining other categories such as 'pending losses', 'near misses', 'operational risk profits/gains', 'opportunity costs/lost revenues' and 'timing impacts' as operational risk events creates huge problems of identification and measurement for banks**. In our opinion these categories should only be optional. Should regulators maintain their opinion that these categories are to be seen as operational risk events, we ask for more detailed guidance by way of examples on each of these categories. In particular, the category of 'pending losses' is hard to describe. The definition provided in footnote 8 of the document is in our opinion rather vague and insufficiently clear to be usable in determining an operational risk framework of an institution.
- We are also looking for **more guidance on the events to be classified as operational losses**. In particular we are looking for further clarification on:
  - § 18: *Examples to be included in the scope of strategic risk*. We do not agree that *'sums of money paid back to customers as a result of a firm's own decision (no breach of rules, regulations or ethical conduct occurred)'* are part of strategic risk. In our opinion these belong to the operational losses. In this regard we are looking for more guidance how to deal with dispute settlements related to the investor profile under MiFID?
  - § 18 *Examples to be included in the scope of operational risk*: While we agree that compensation paid to employees is to be included into the scope of operational risk, we wonder how they should be treated. In order to answer this question, it is in our opinion needed to make a difference between those countries where:
    - Resignation amounts are established via a specific formula;
    - Resignation amounts are freely negotiable;
    - Resignation amounts are legally fixed.

**Detailed remarks:**

- § 10: The wording of this paragraph is ambiguous. We wonder how regulators evaluate the establishment of an individual operation risk loss profile in relation to the industry practices. More guidance on this issue would be welcome.
- § 17: We do not agree with the draft EBF position that *'the portion of the loss due to adverse market conditions'* should not be included into the scope of operational risk loss.
- § 18 *Examples to be included in the scope of strategic risk: 'losses relating to decisions made by the competent decision making body which are not compatible with the firm's risk tolerance level and deviate from its core business activities'*. We believe that this paragraph should be rewritten as follows:

*'losses relating to decisions made by the competent decision making body which are not compatible with the firm's risk tolerance level and deviate from its core business activities, unless the body itself is competent or duly delegated to decide on the procedure'*

- § 18 *Examples to be included in the scope of operational risk: 'expenses stemming from law cases or from interpretations of the regulations which proved to go against corporate practice'*. We propose to replace the words 'corporate practice' with 'industry practice' as these practices are not governed or supported by internal corporate documents.
- § 21: As mentioned before, we do not agree to include 'pending losses' in the scope of operational risks with the exception if there should be a sufficiently detailed guidance be available to delimitate these losses.
- § 22: More guidance is also needed on the scenario analysis to include pending losses in the scope of operational risk losses.