



## What is Operational Risk?

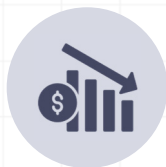


**The risk of loss**



**Damage to the bank's reputation**

## What is Operational Risk?



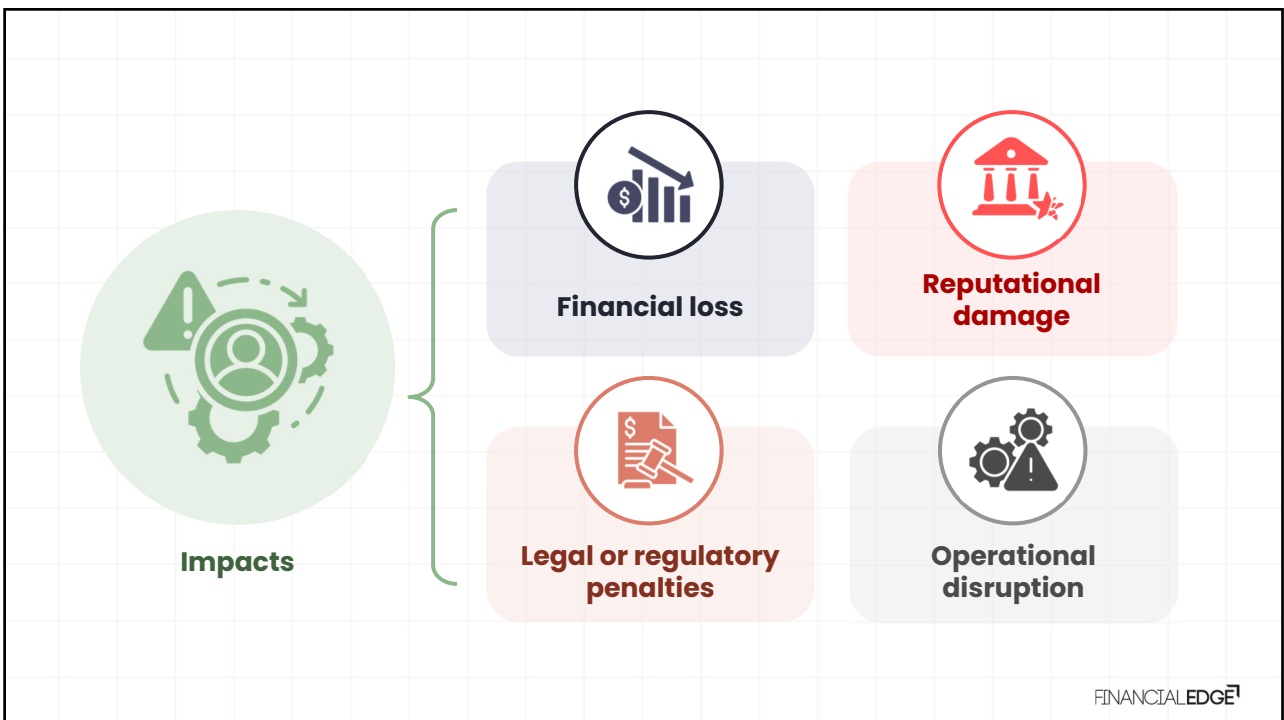
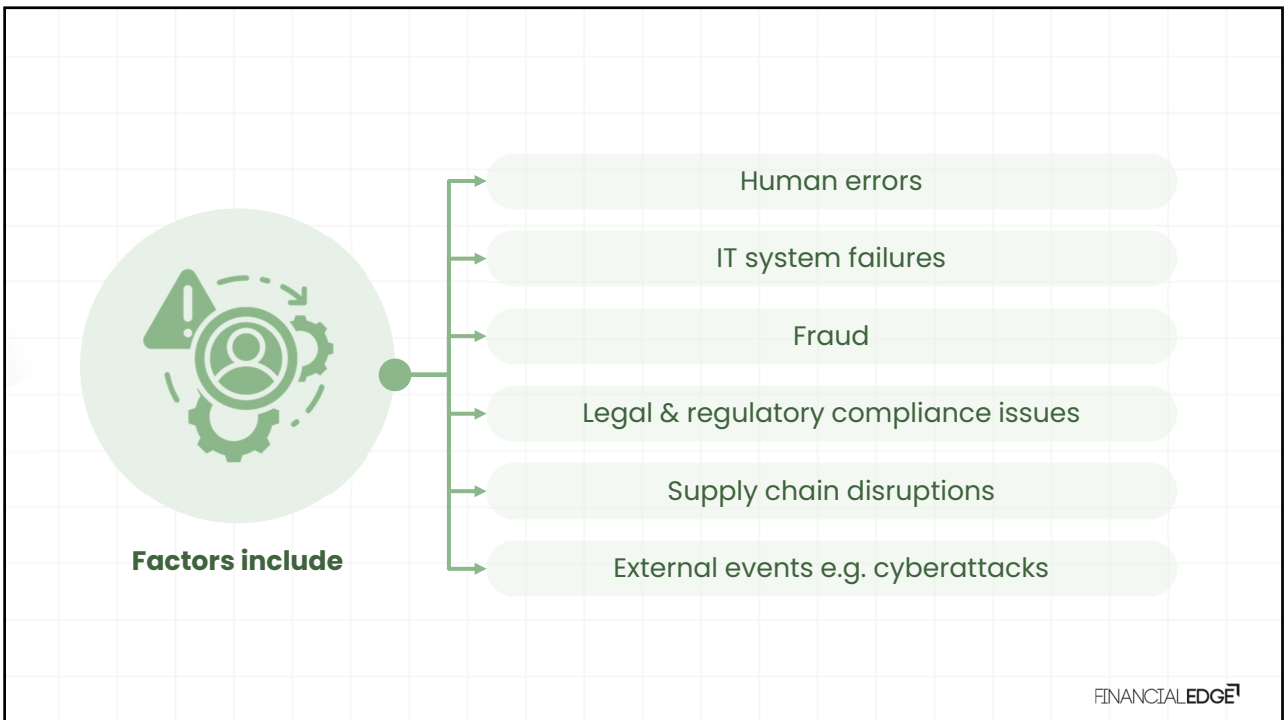
**The risk of loss**



Inadequate or failed internal **processes, people, systems** or **external events**



**Damage to the bank's reputation**





## Sources of Operational Risk

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### Basel risk event categories



Fraud (internal and external)

Employment practices

Clients, products, and business practices

Damage to physical assets

Business disruption and systems failures

Execution, delivery, and process management

Workplace safety and environmental incidents

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## Basel risk event categories




- Fraud (internal and external)
- Employment practices
- Clients, products, and business practices
- Damage to physical assets
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- Execution, delivery, and process management
- Workplace safety and environmental incidents

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## Basel risk event categories





- Fraud (internal and external)**
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### Internal Fraud


Risks arising from acts of fraud **committed by individuals within** the organization

e.g. embezzlement, insider trading, money laundering, and employee misconduct

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- Fraud (internal and external)**
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### External Fraud


Risks associated with fraudulent acts **committed by people external** to the organization

e.g. theft, forgery, hacking, identity theft, and other criminal activities

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### Basel risk event categories

- Fraud (internal and external)
- Employment practices**
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### Risks related to **employment practices**

e.g. discrimination, harassment, workplace accidents, and health and safety concerns

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### Basel risk event categories

- Fraud (internal and external)
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Risks associated with the organization's **products and services** and the **practices employed** in conducting business

e.g. mis-selling of products or services, inadequate disclosure, non-compliance with regulations, and product defects

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### Basel risk event categories

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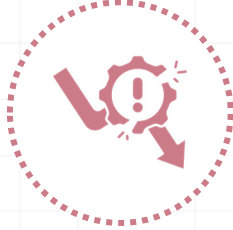
Risks arising from **physical damage** to the **organization's assets**, such as buildings, equipment, and infrastructure

e.g. natural disasters, fires, vandalism, and accidents

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### Basel risk event categories

- Fraud (internal and external)
- Employment practices
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- Execution, delivery, and process management
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Risks related to **disruptions in business operations and failures of internal systems and processes**

e.g. IT system outages, power failures, supply chain disruptions, and failures in business continuity planning

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### Basel risk event categories

- Fraud (internal and external)
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Risks associated with failures in the **execution, delivery, and management of processes and systems**

e.g. errors, delays, and inefficiencies in operational processes, inadequate monitoring, and control mechanisms

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### Basel risk event categories

- Fraud (internal and external)
- Employment practices
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Risks related to **accidents, injuries, and environmental incidents** occurring within the organization's premises

e.g. workplace accidents, occupational health hazards, and environmental pollution

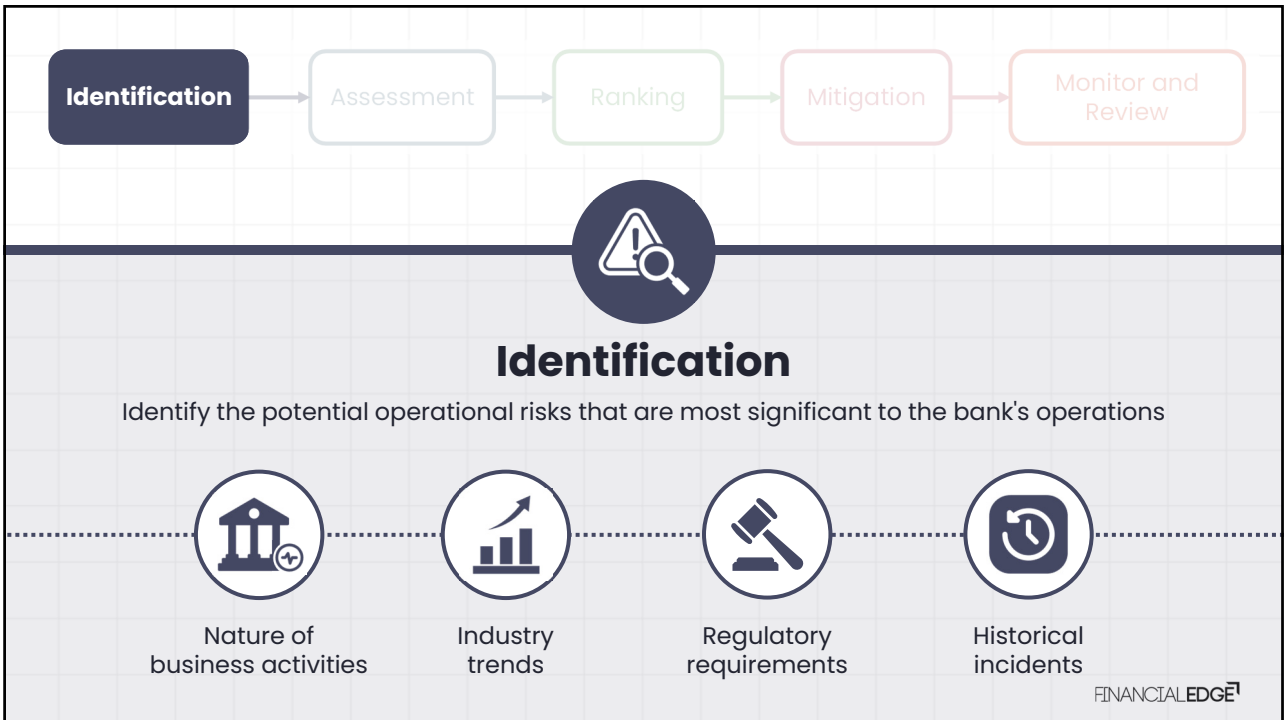
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# Top Operational Risks



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**Assessment**

Conduct a detailed risk assessment to evaluate the likelihood and potential impact of each risk

- Frequency and severity of past incidents
- Effectiveness of existing controls
- Emerging trends in the industry

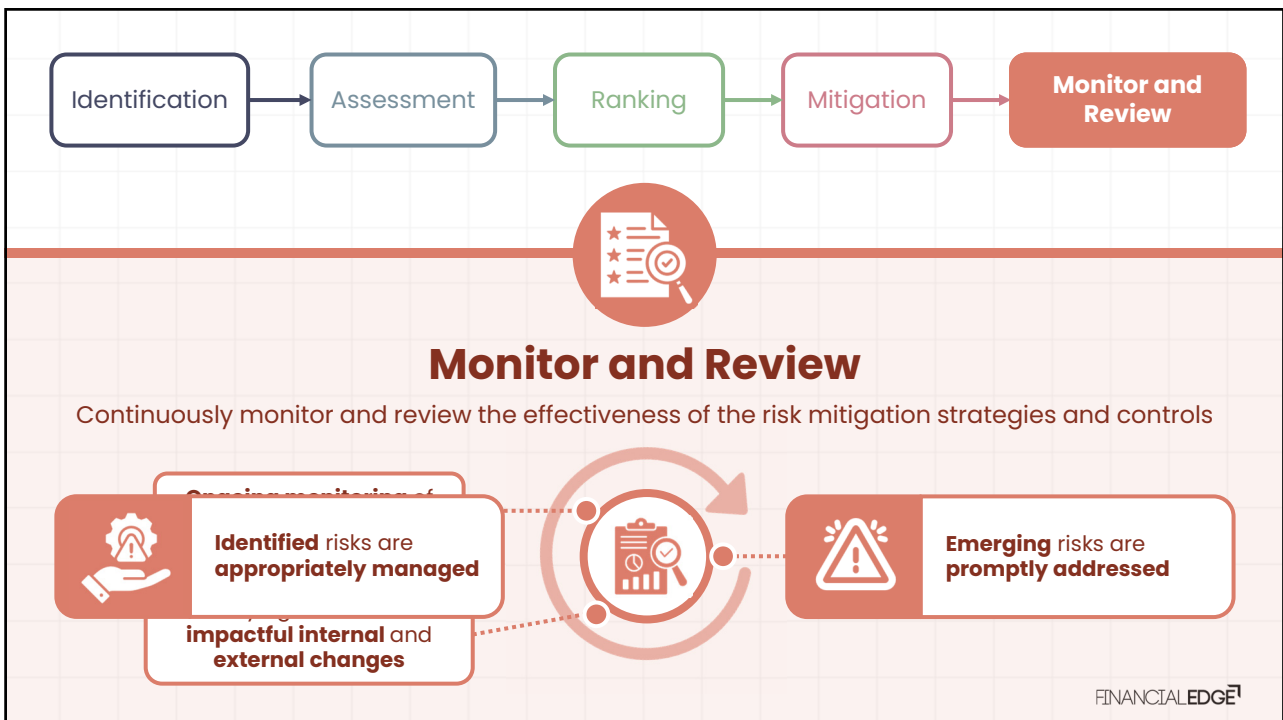
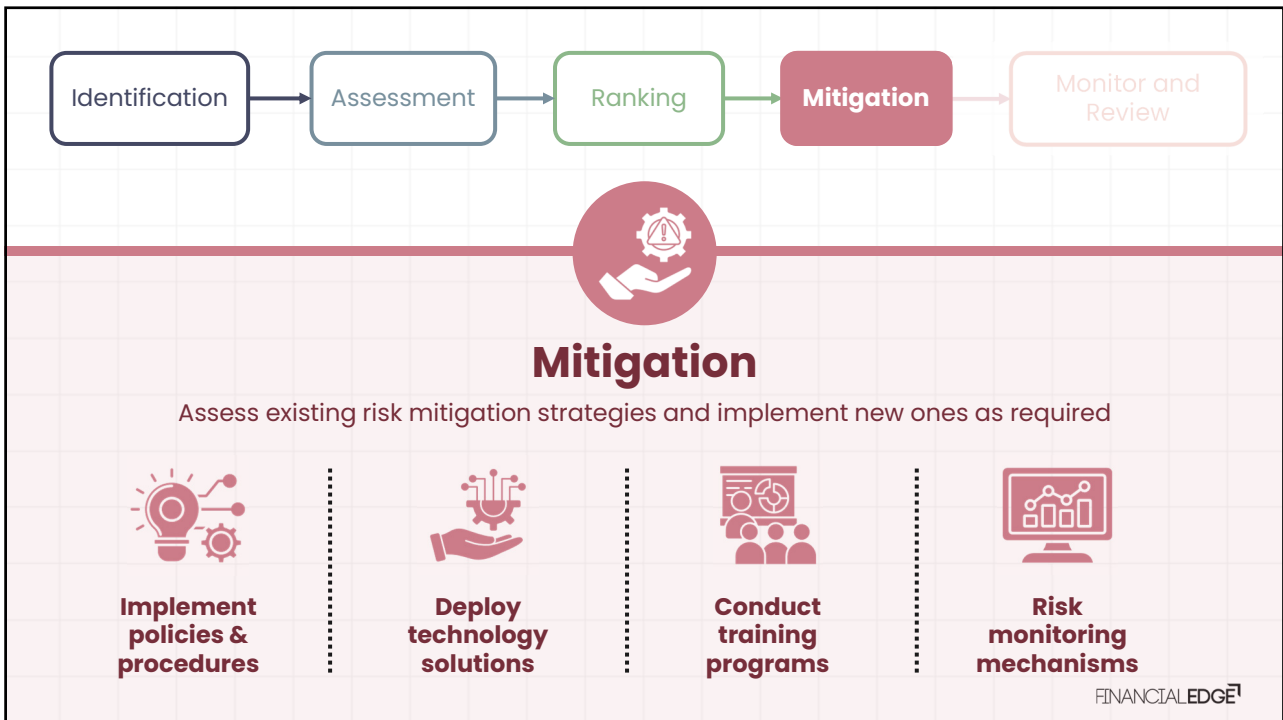
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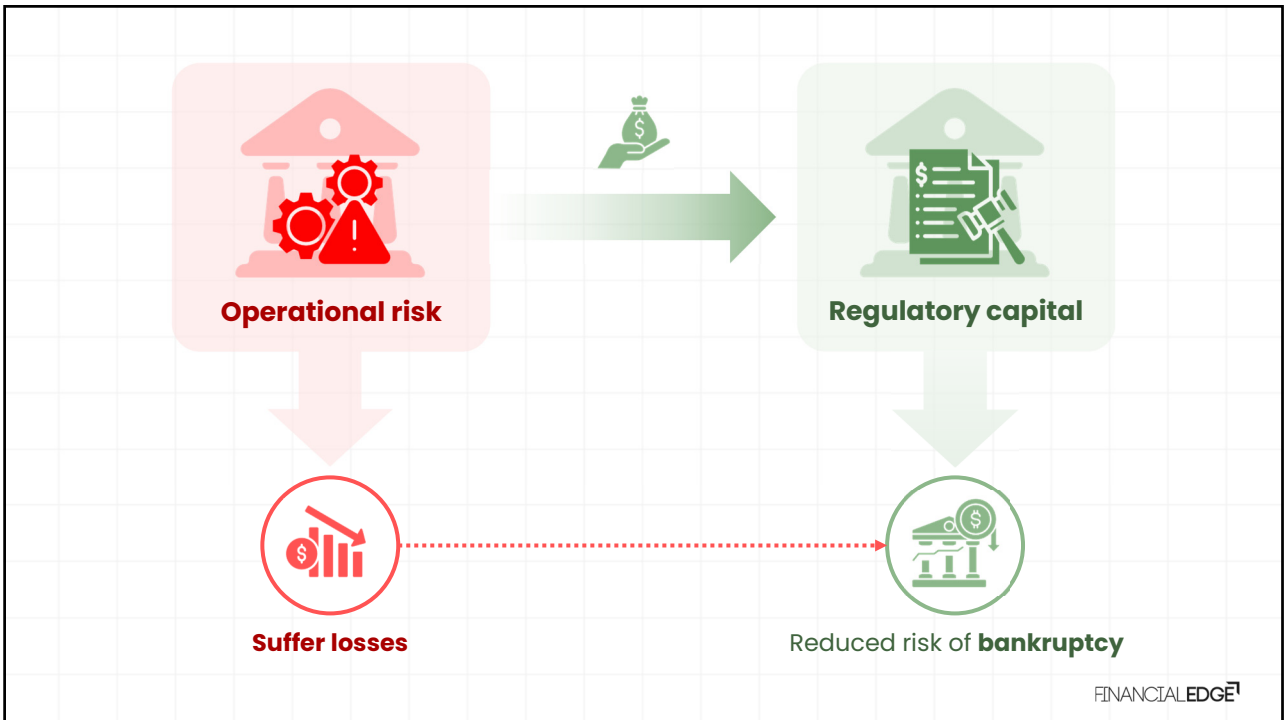
**Ranking**

Rank and prioritize the “top operational risks” according to their level of potential impact and likelihood

Allocate appropriate **resources** and **attention** to the **most significant risks**

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## How banks calculate regulatory capital...



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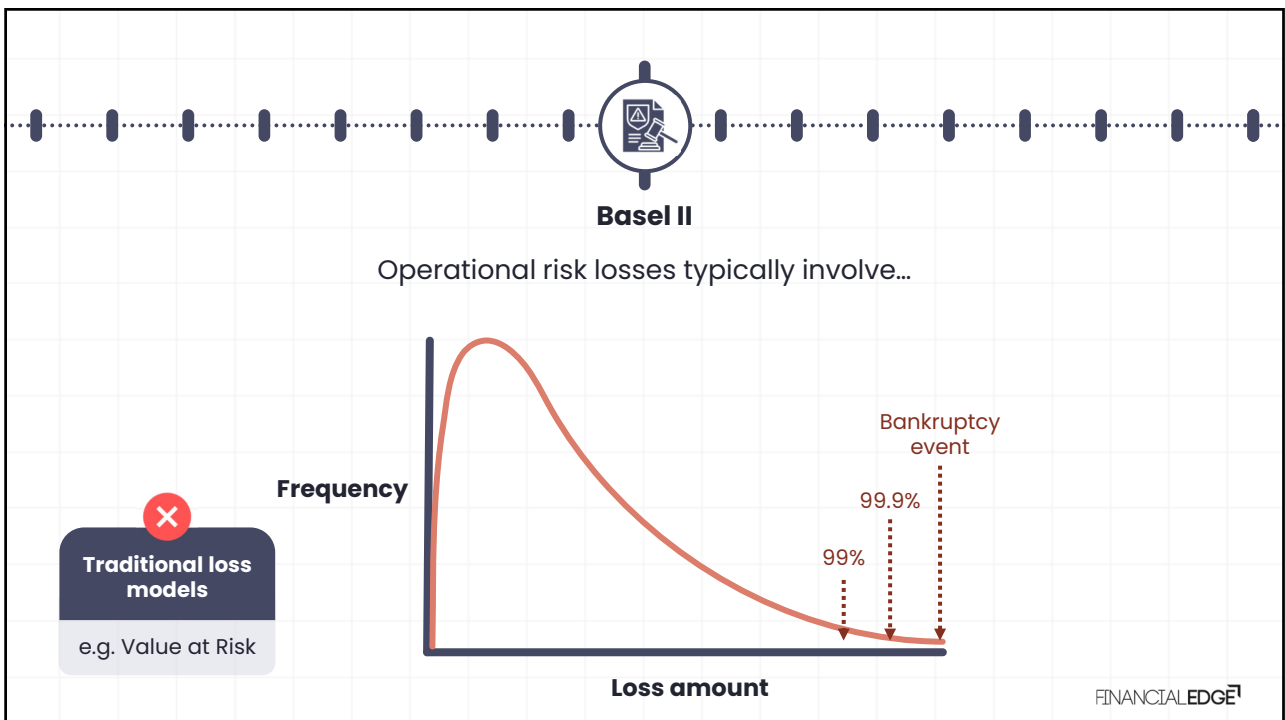
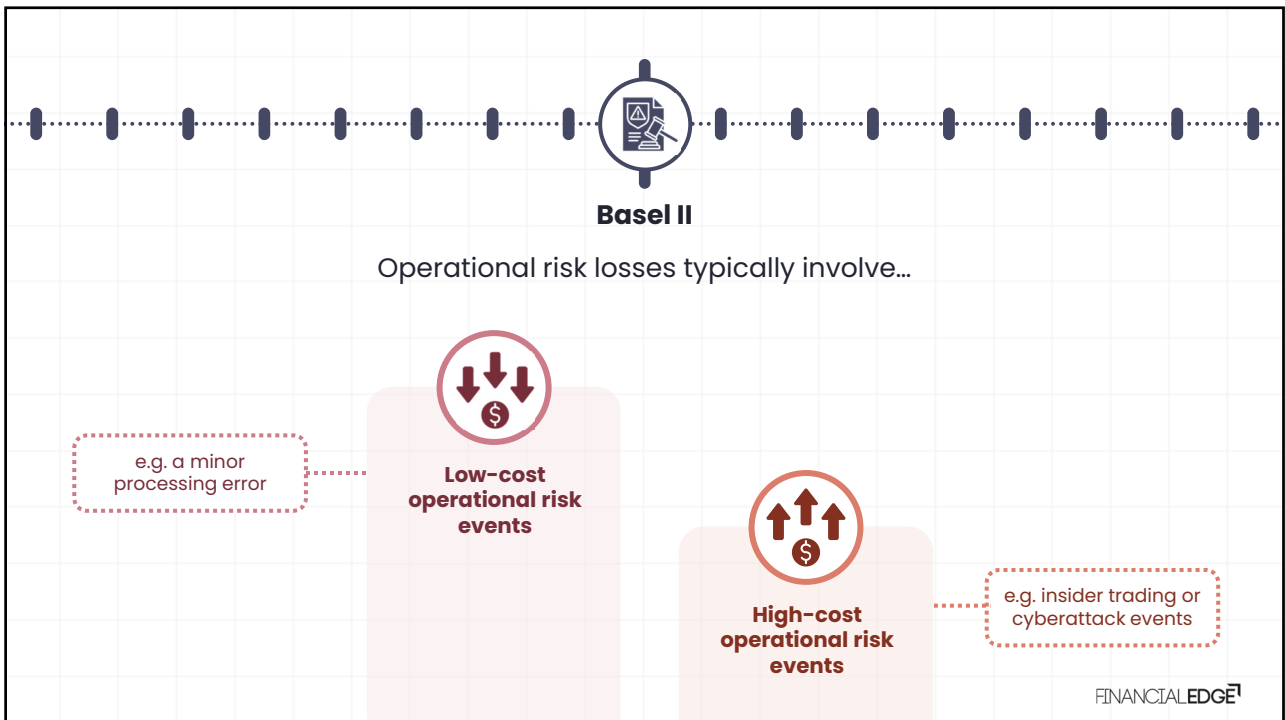


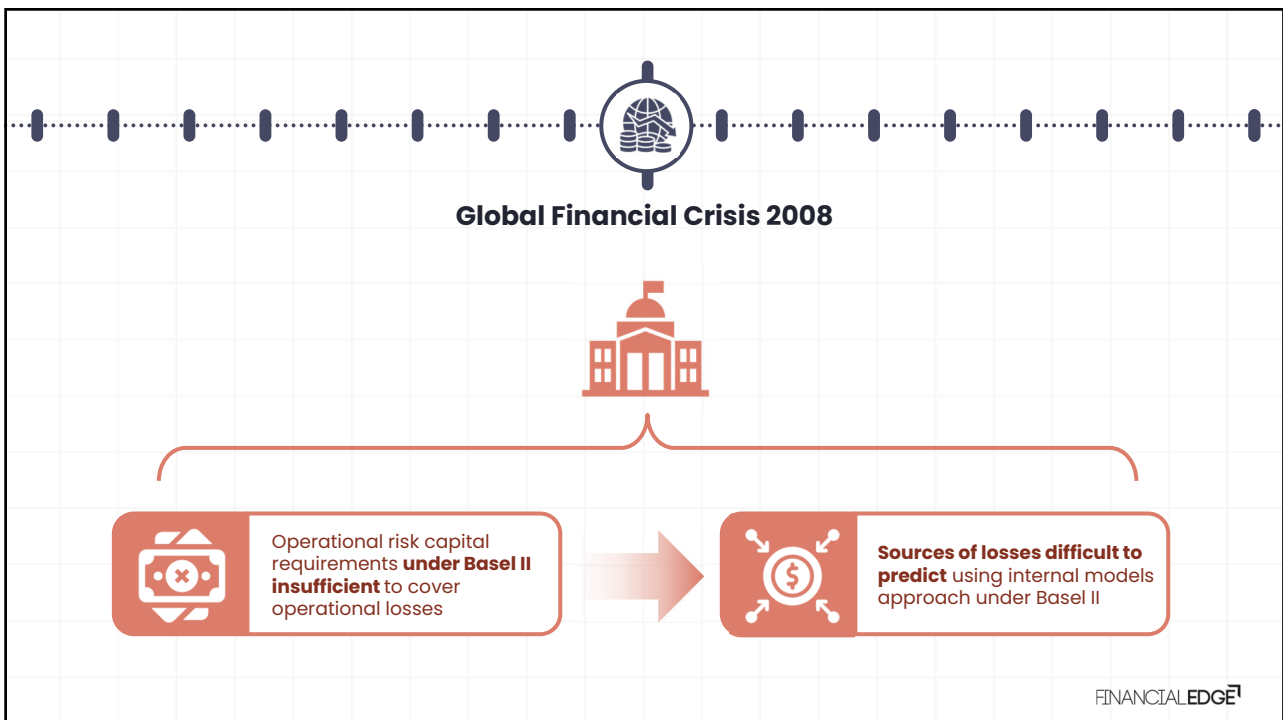
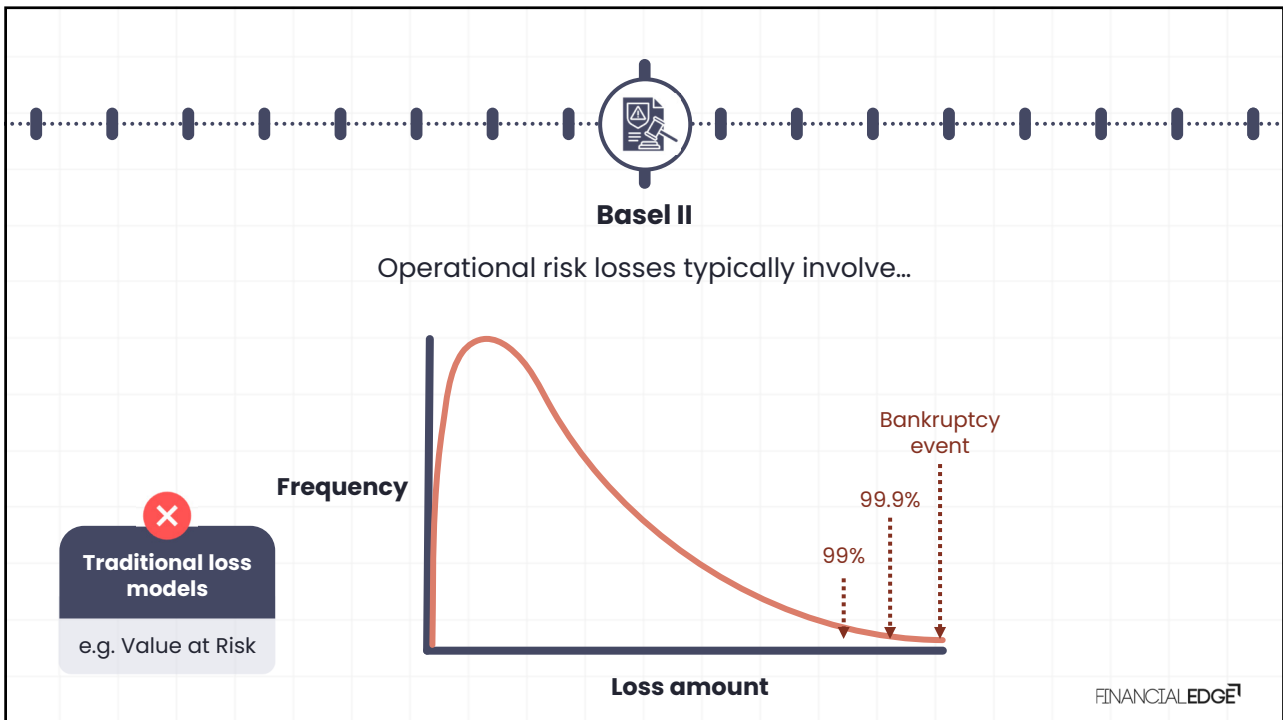
**Basel II**

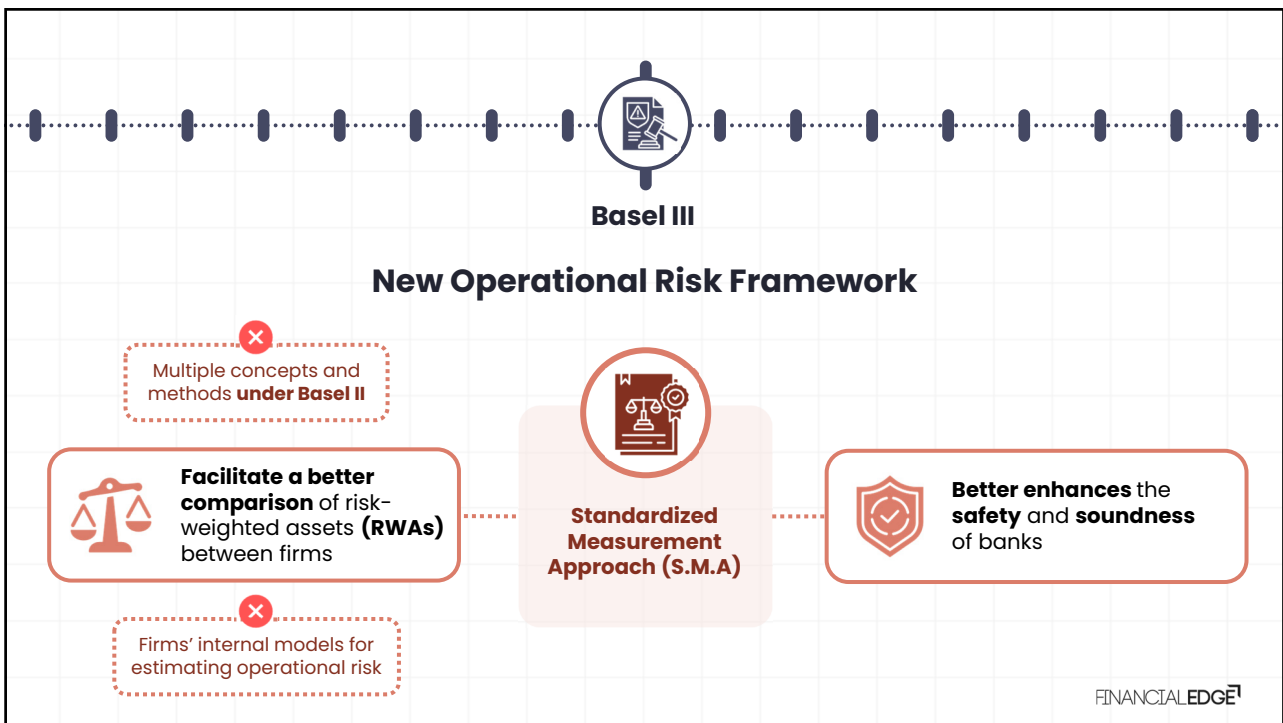
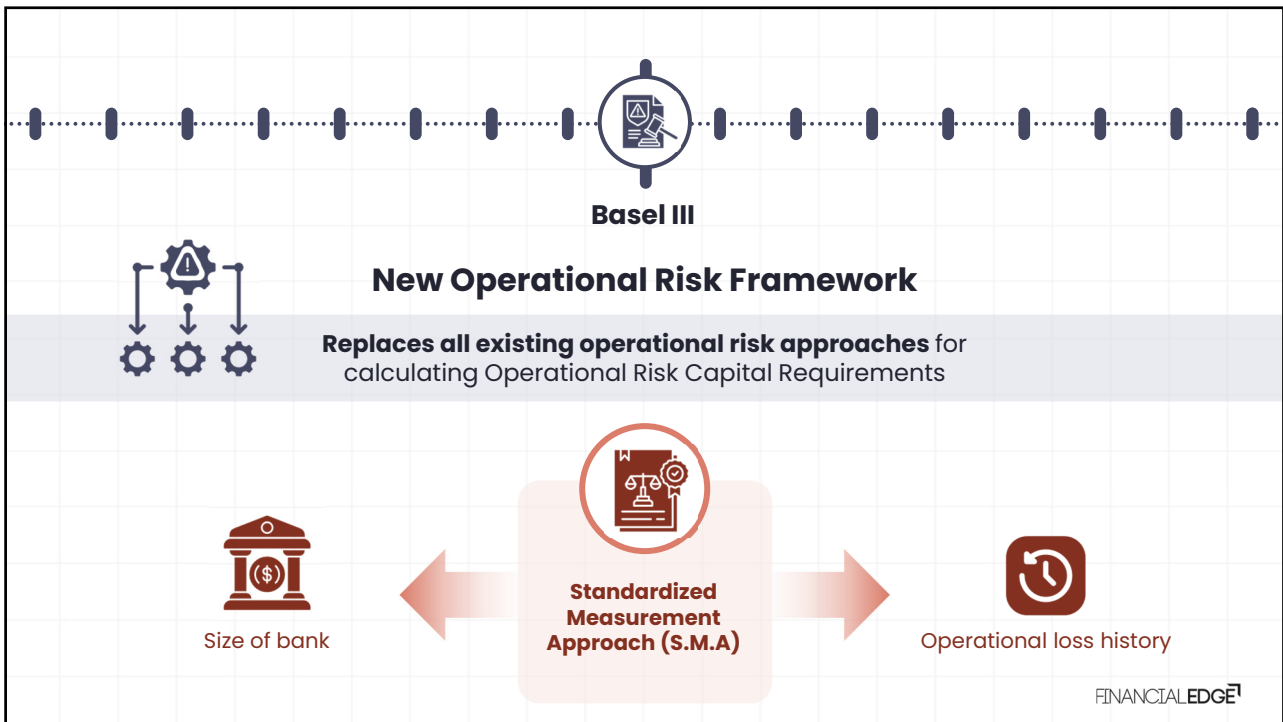
- Three options** to calculate the required amount of regulatory capital of operational risk
- Ranging in **complexity**
- Similar** to the methods for calculating **credit** and **market** risk



The **nature** of **operational risk** is very **different**









# Operational Risk Capital Requirement

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## Calculating Operational Risk Capital Requirements

Under Basel III

**Operational Risk  
Capital Requirement**

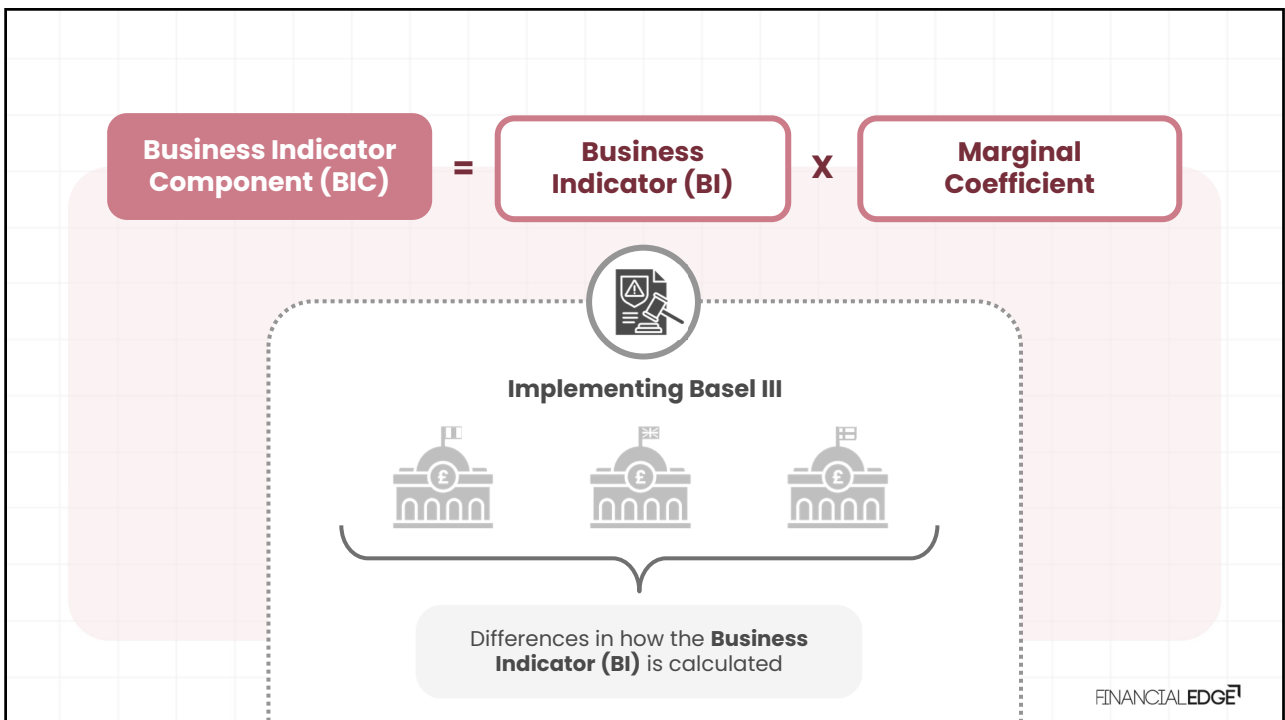
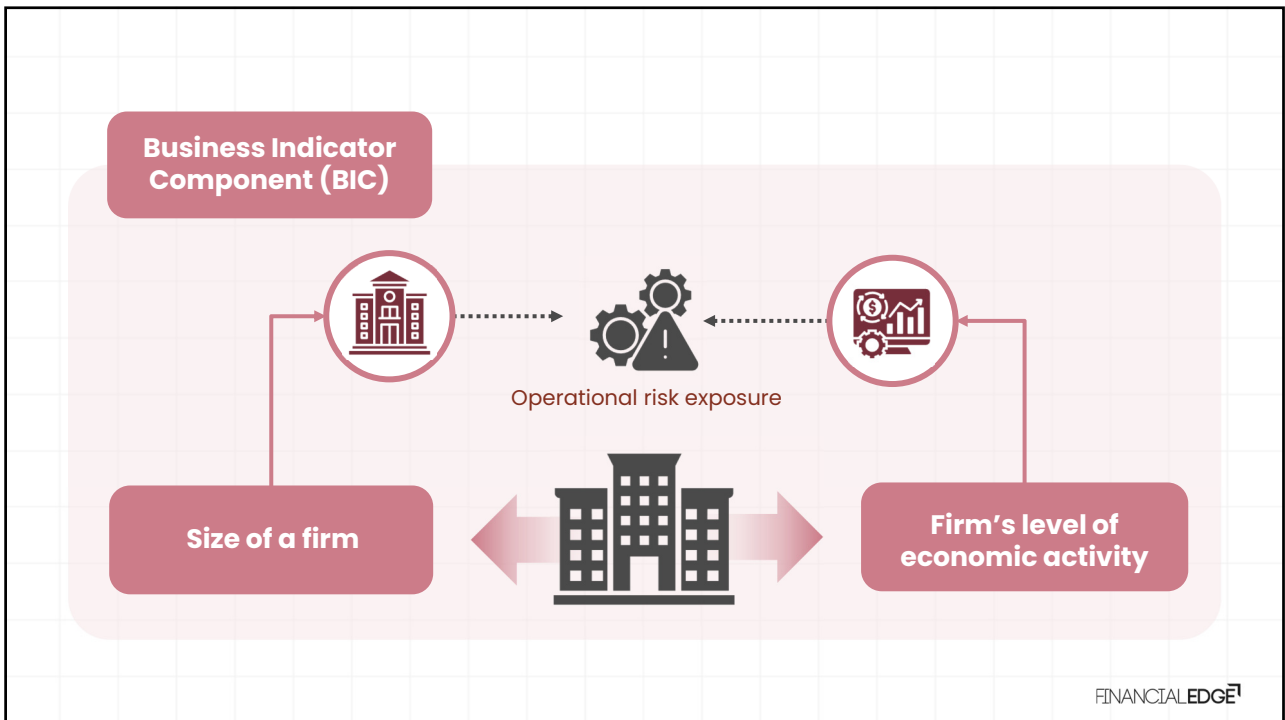
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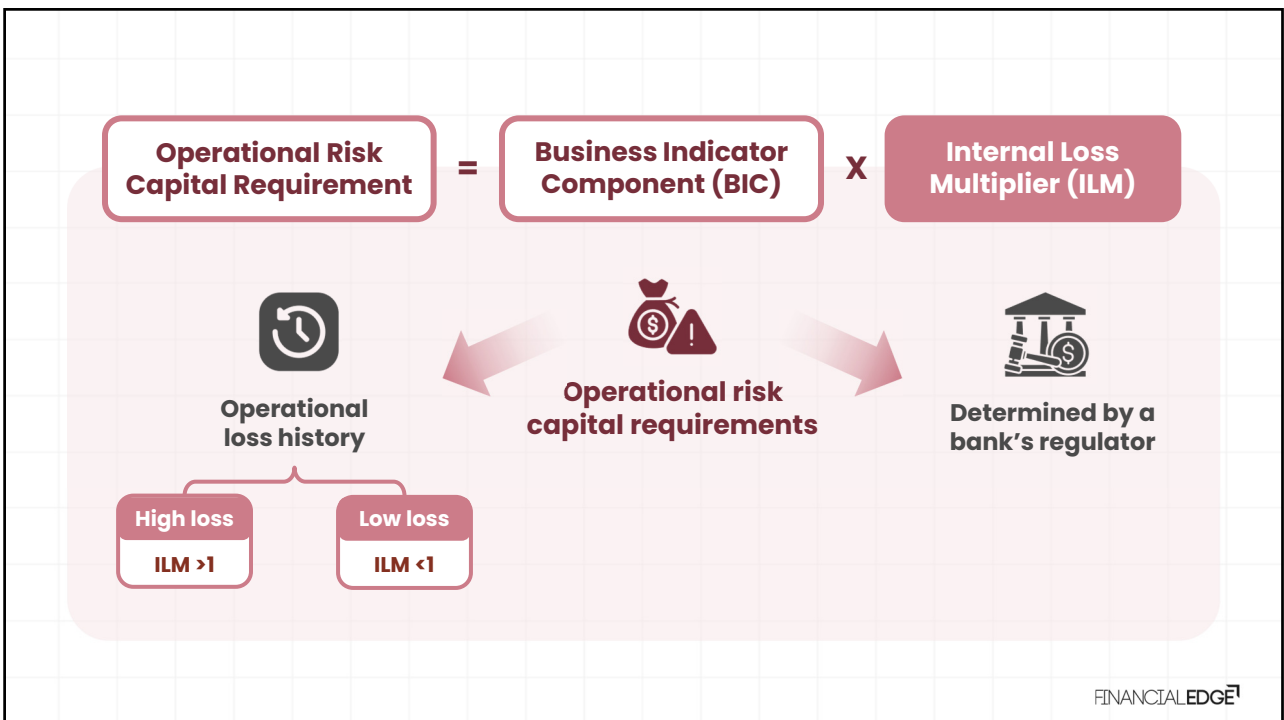
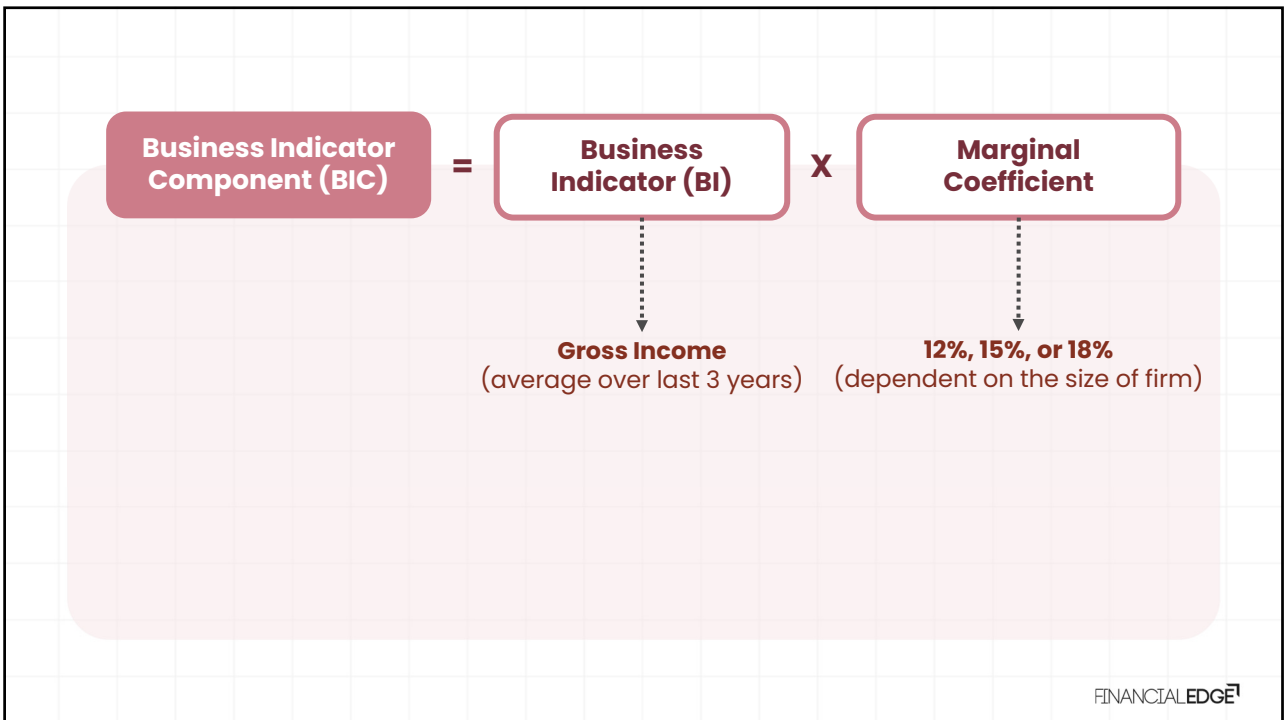
**Business Indicator  
Component (BIC)**

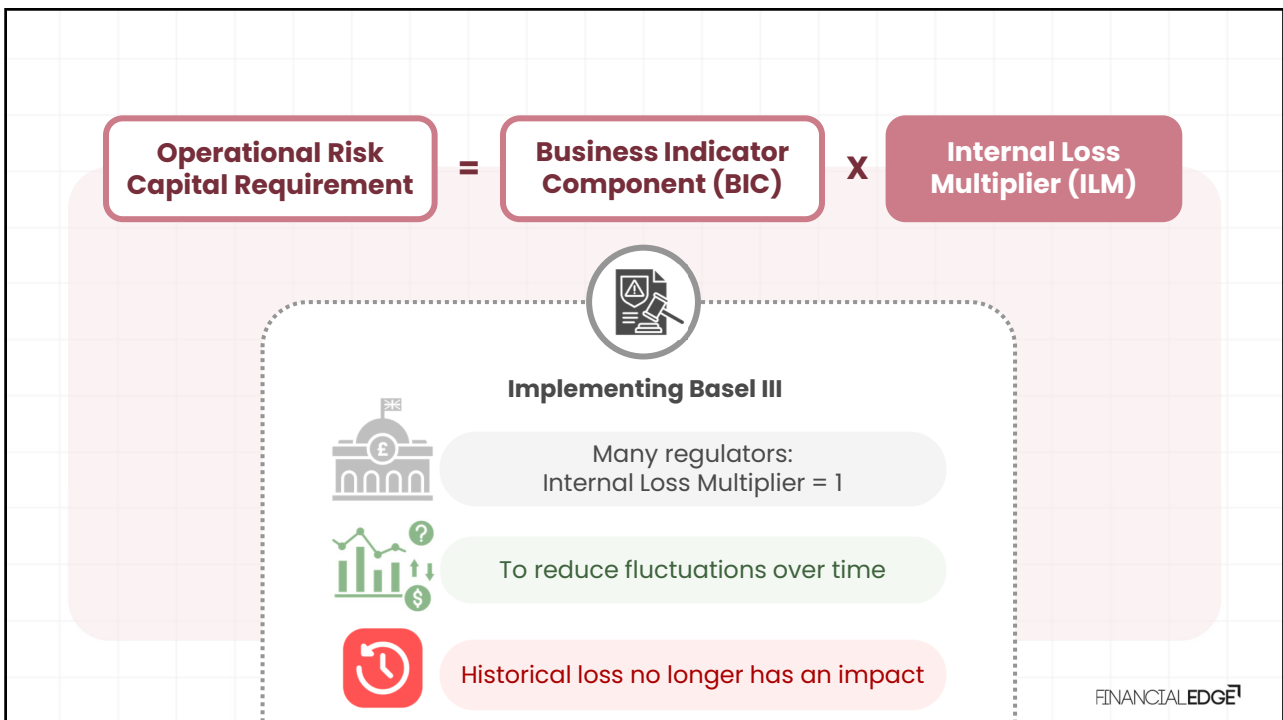
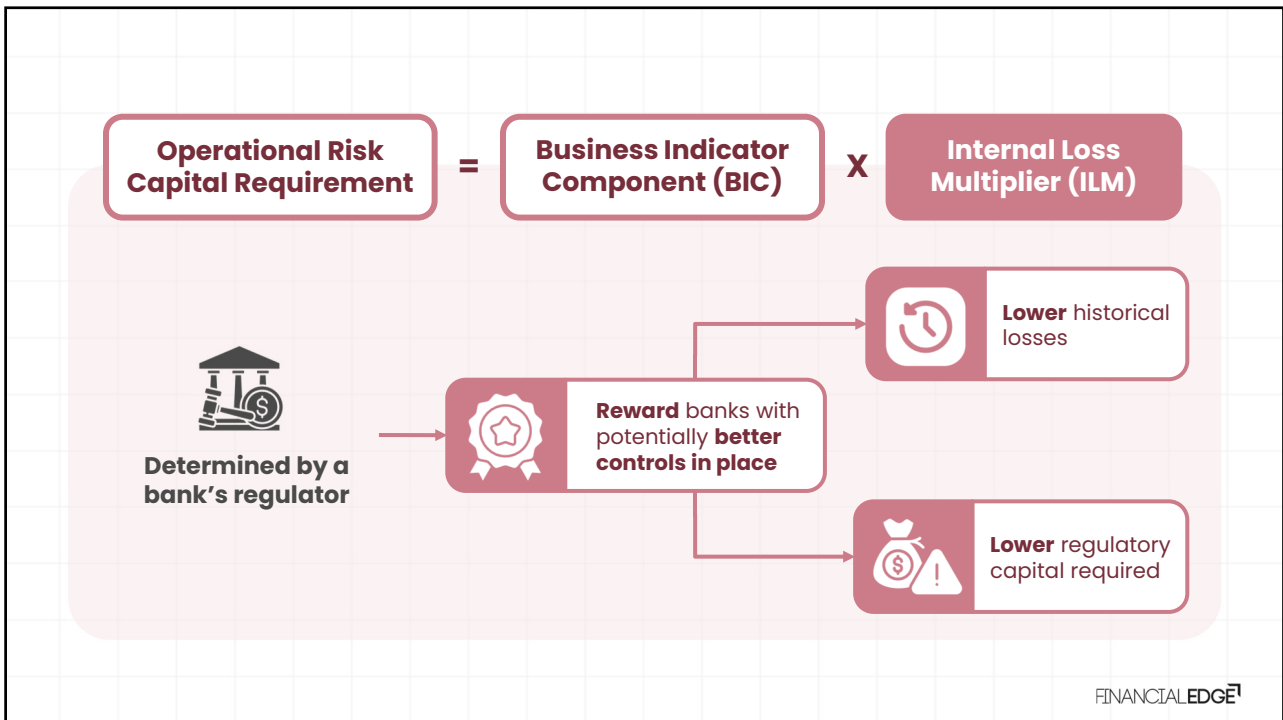
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**Internal Loss  
Multiplier (ILM)**

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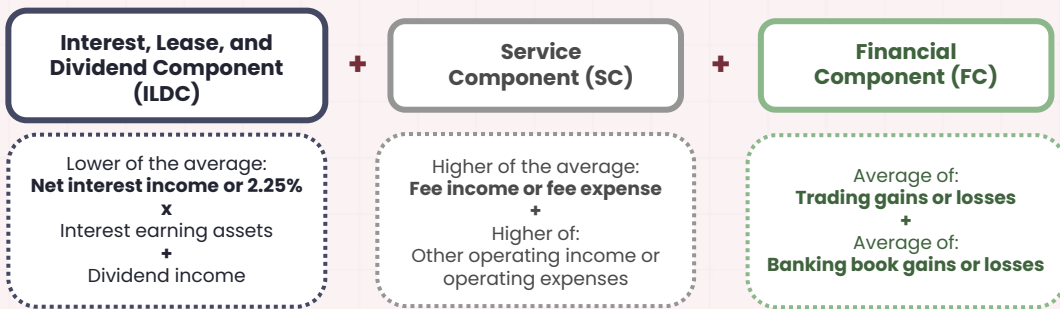




# Business Indicator Calculations

## Business Indicator (BI)

Based on **three components** (averages over 3 years)



Remove the possibility that a bank **making a loss** ends up with a **lower regulatory capital requirement**



## Business Indicator Ranges and Marginal Coefficients

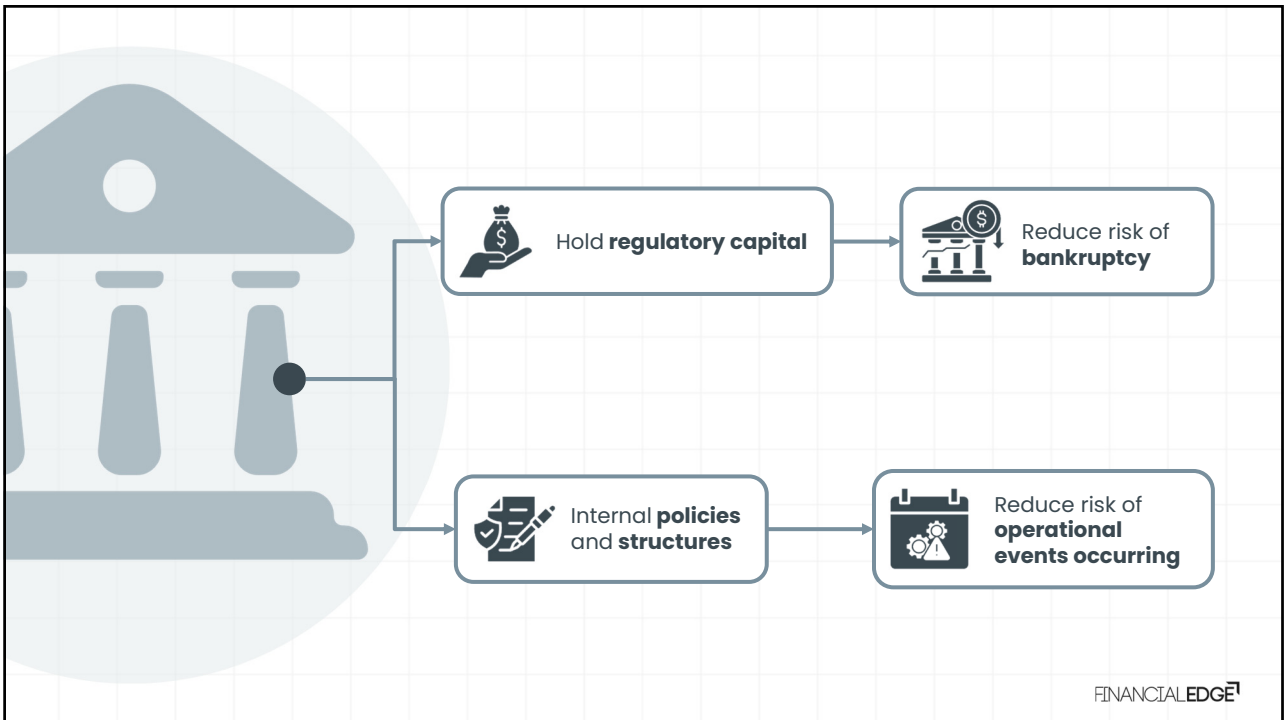
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### Marginal Coefficient

Based on an organization's **Business Indicator (BI) number**


Bucket	BI range (2025)			BI marginal coefficients
	US (\$bn)	EU (€bn)	UK (£bn)	
1	≤1.0	≤1.0	≤0.9	12%
2	1.0 ≤ BI ≤ 30.0	1.0 ≤ BI ≤ 30.0	0.9 ≤ BI ≤ 26.0	15%
3	> 30.0	> 30.0	> 26.0	18%

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**The Basel Committee on Banking Supervision**

- ✓ \_\_\_\_\_
- ✓ \_\_\_\_\_
- ✓ \_\_\_\_\_
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Relevant for banks to consider when **determining** how **operational risks are managed**

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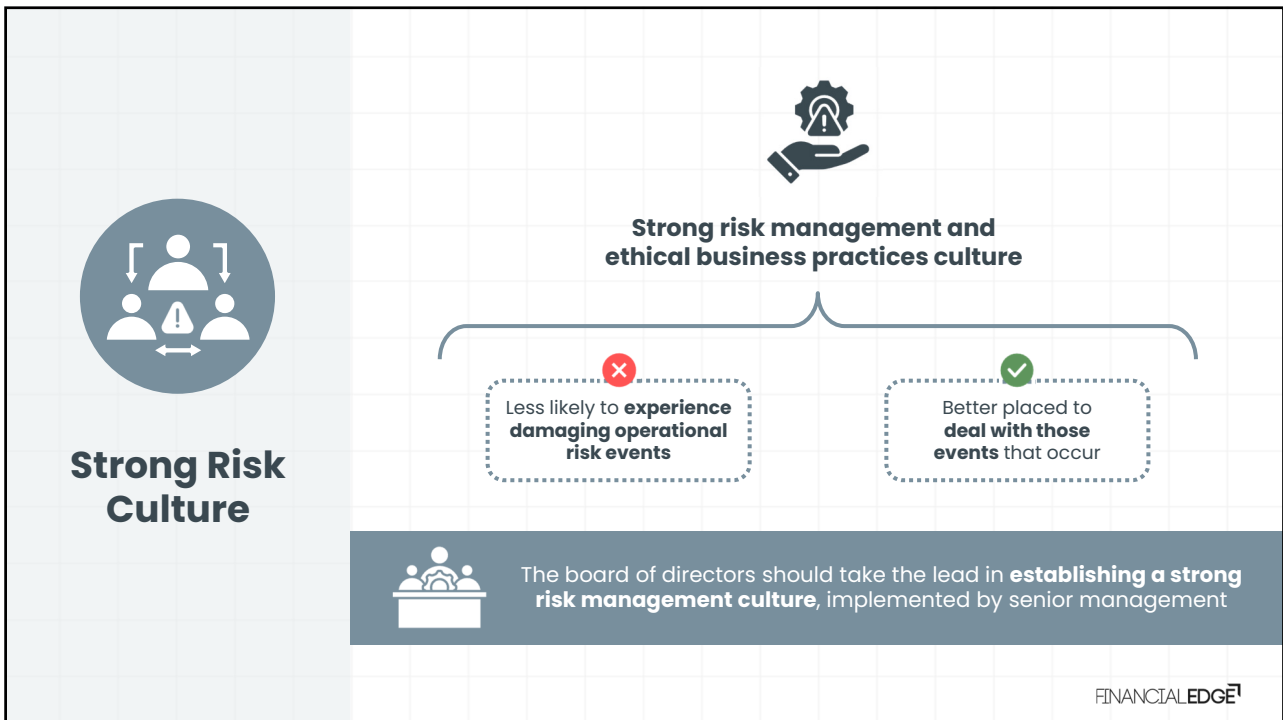



**Strong Risk Culture**




**Comprehensive Operational Risk Management Framework (ORMF)**

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The board of directors should establish a **code of conduct** or an **ethics policy** to address conduct risk




**Strong Risk Culture**



**Policy**

- \_\_\_\_\_
- \_\_\_\_\_
- \_\_\_\_\_



Expected standards of behavior

- Applicable to both **staff** and **board members**
- High standard of **integrity** and **ethical values**
- Identify **acceptable business practices**
- Prohibit **conflicts of interest** or the **inappropriate provision of financial services**

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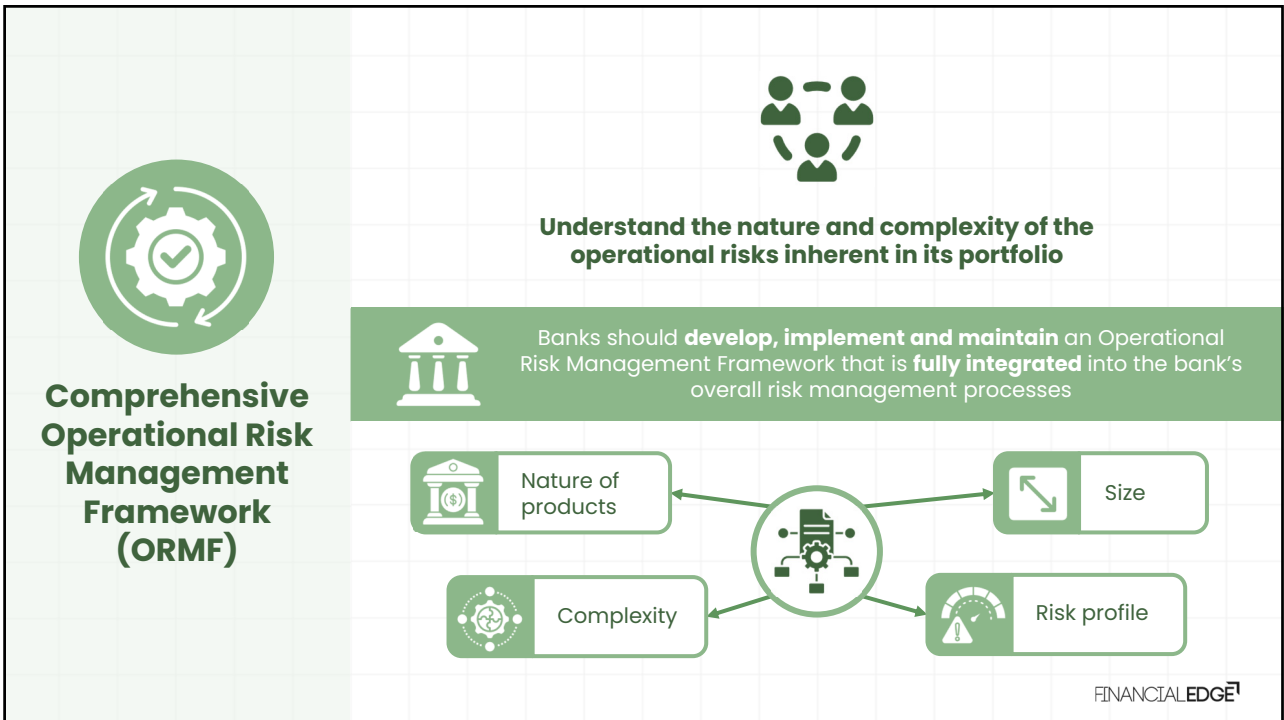
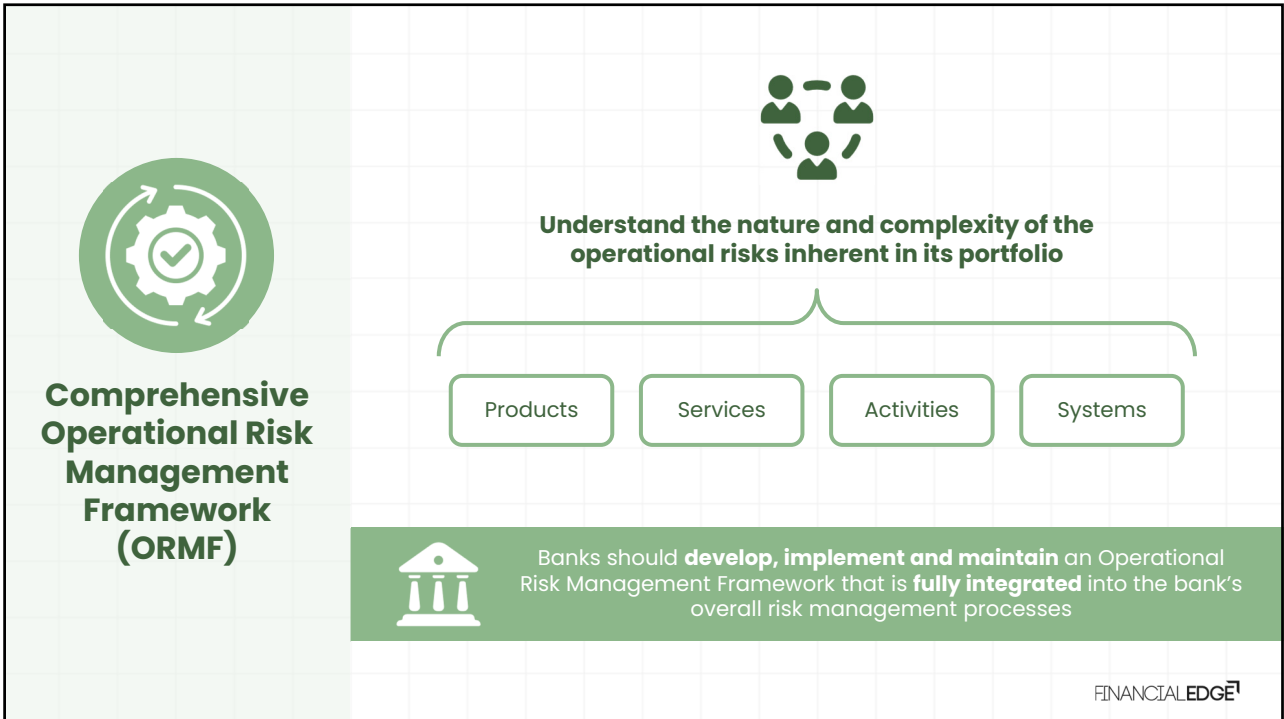


**Strong Risk Culture**



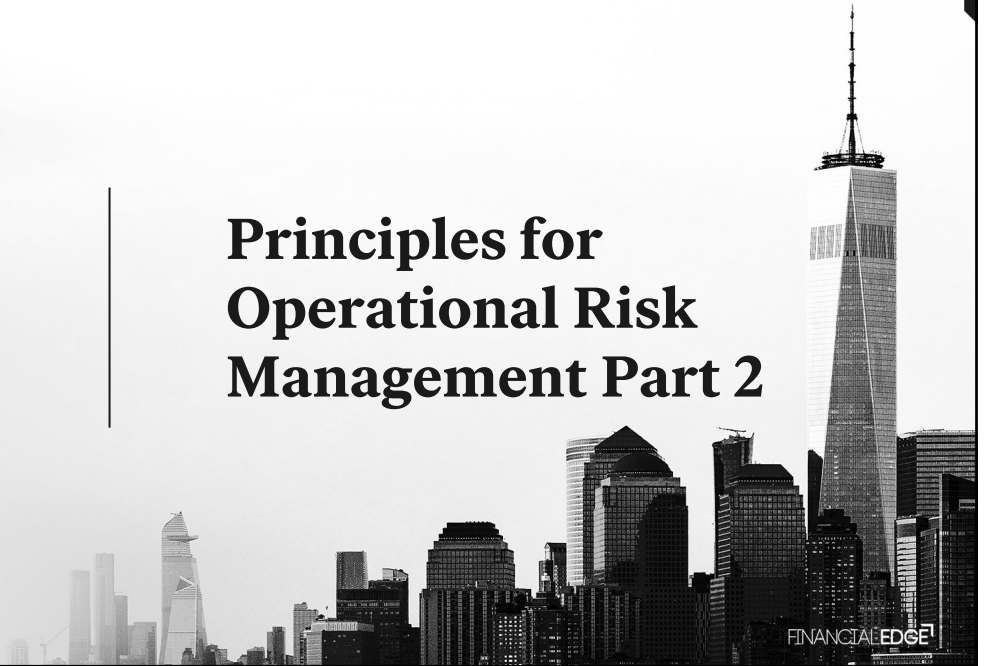
**Comprehensive Operational Risk Management Framework (ORMF)**

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# Principles for Operational Risk Management Part 2



**Governance**



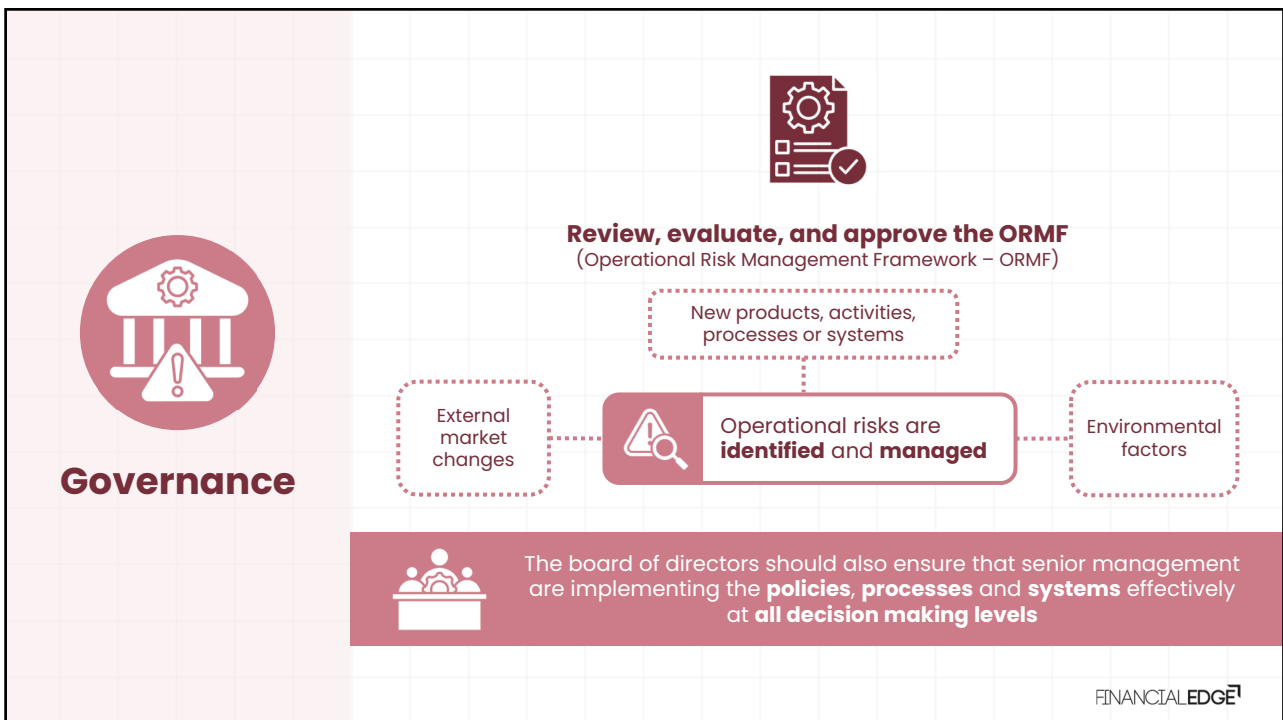
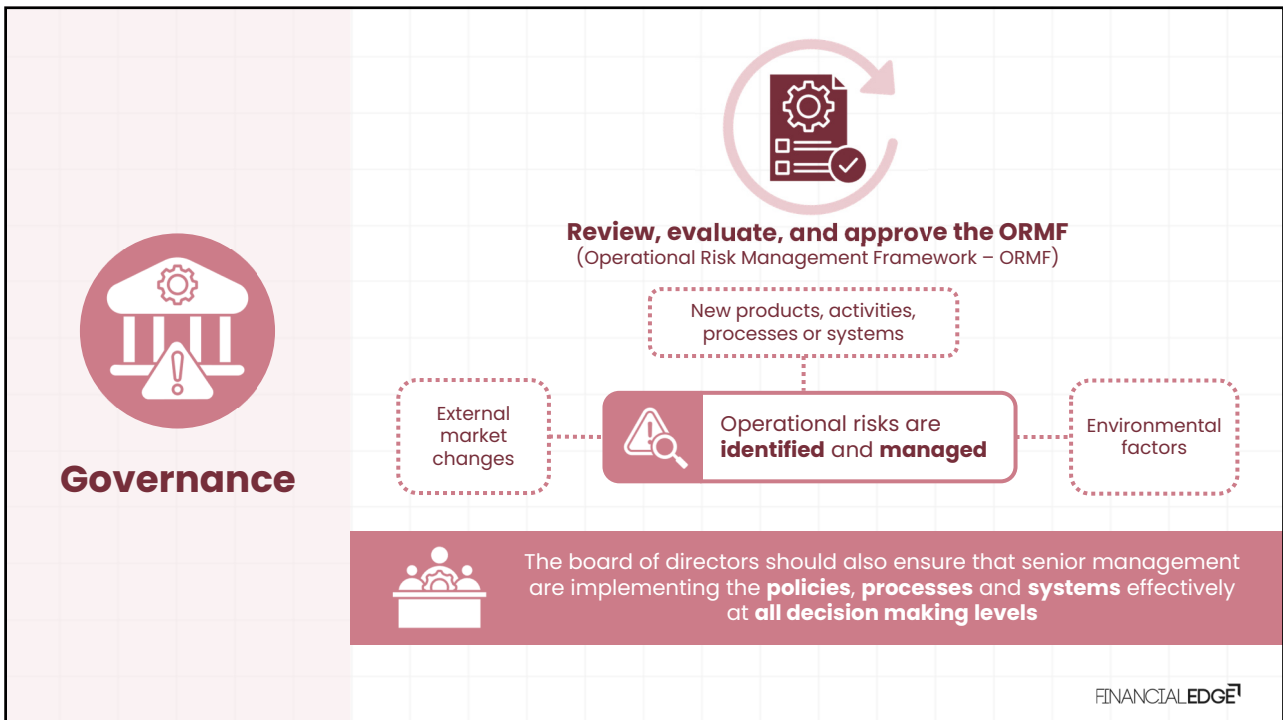
**Governance Structure**

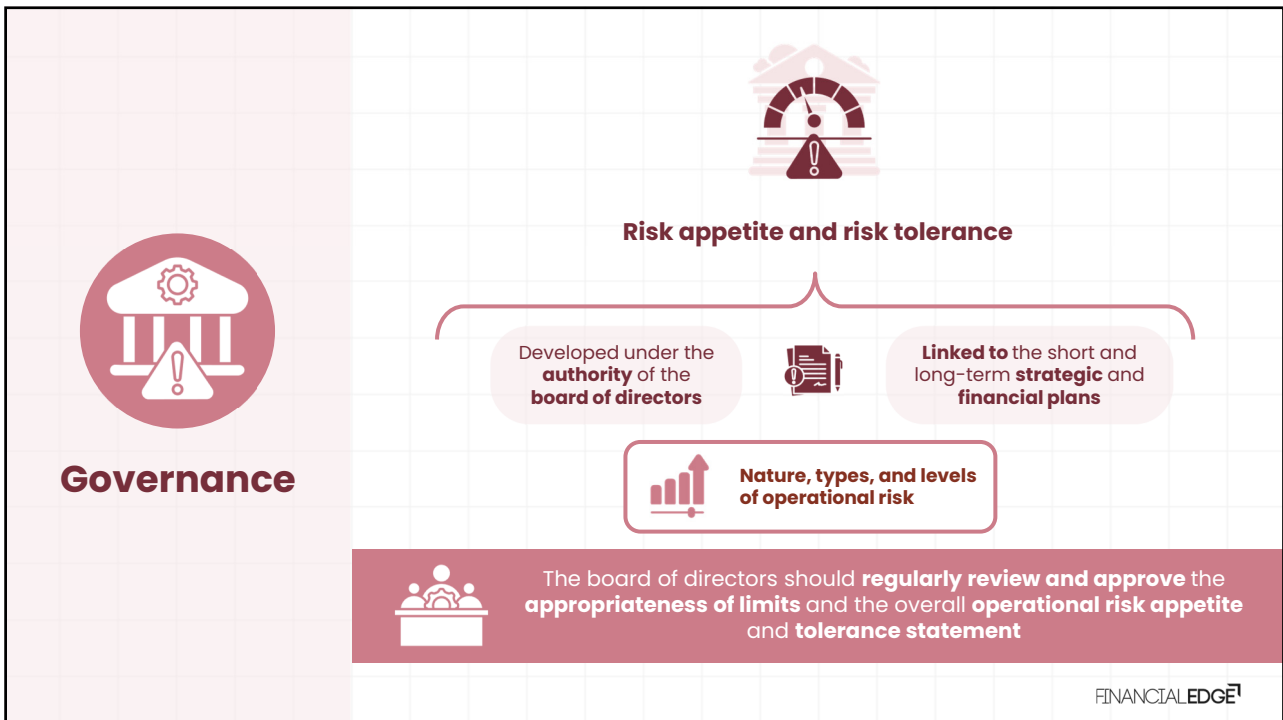


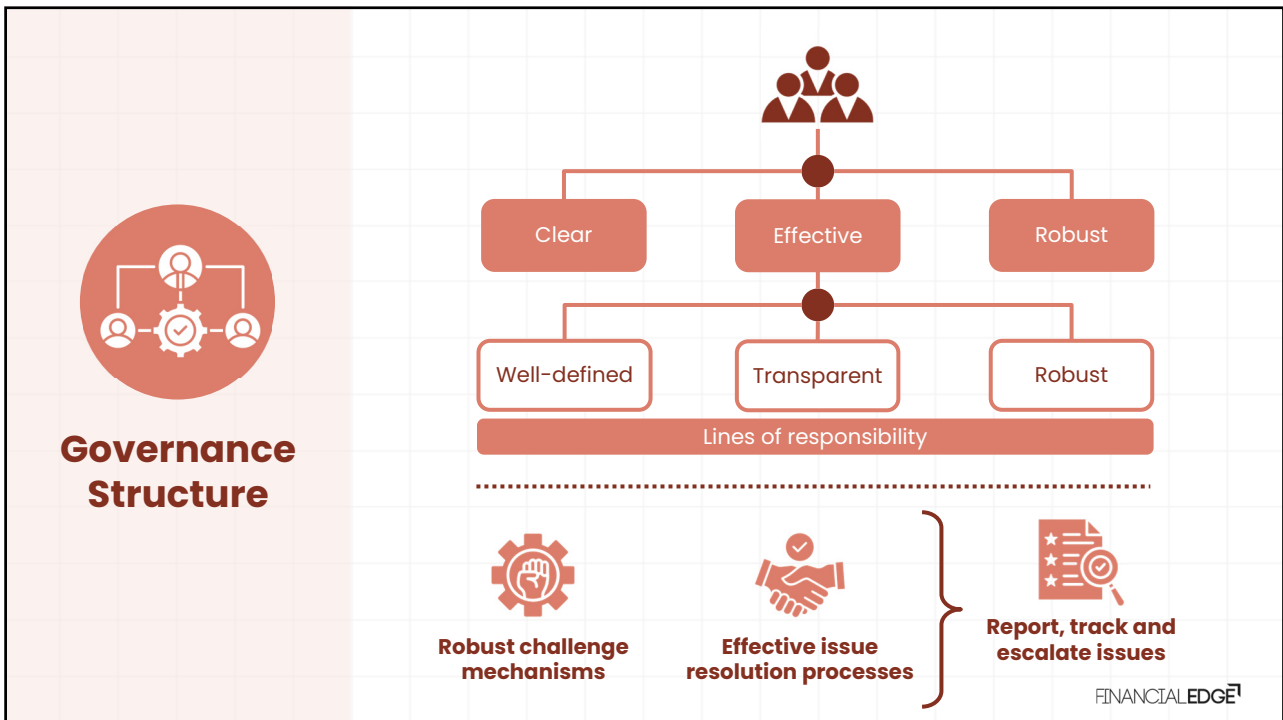
**Identification & Assessment**

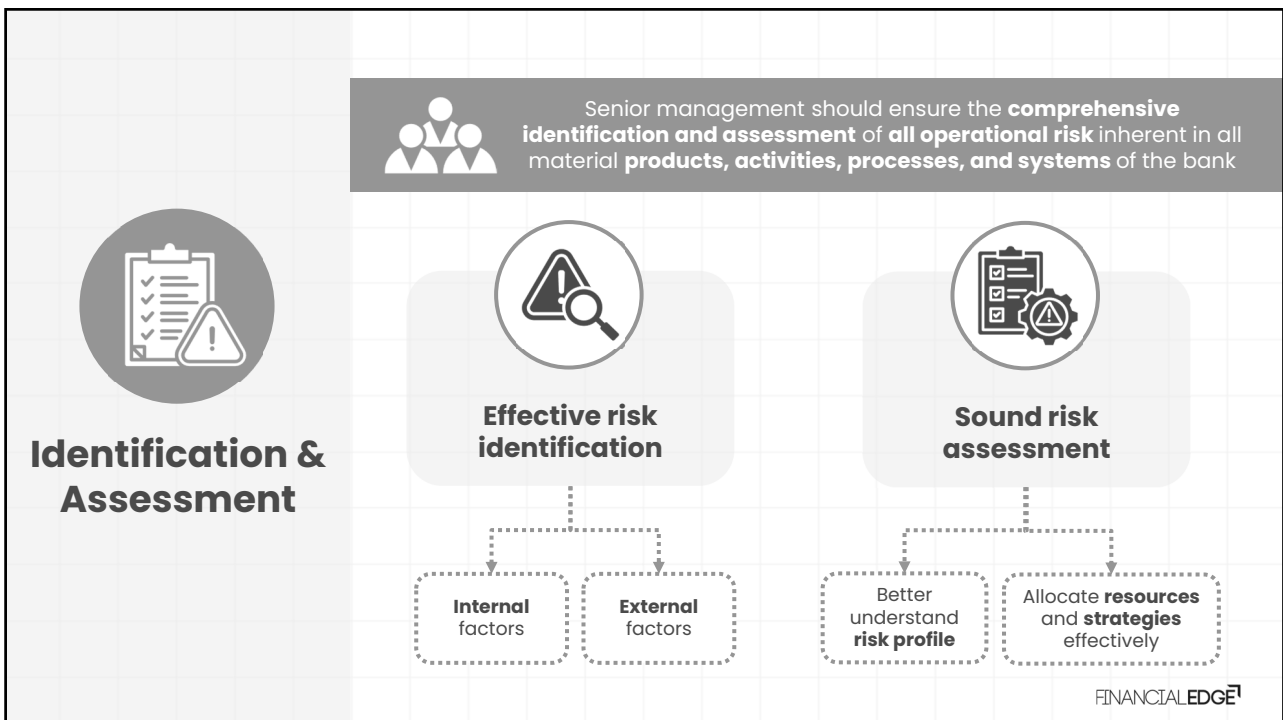
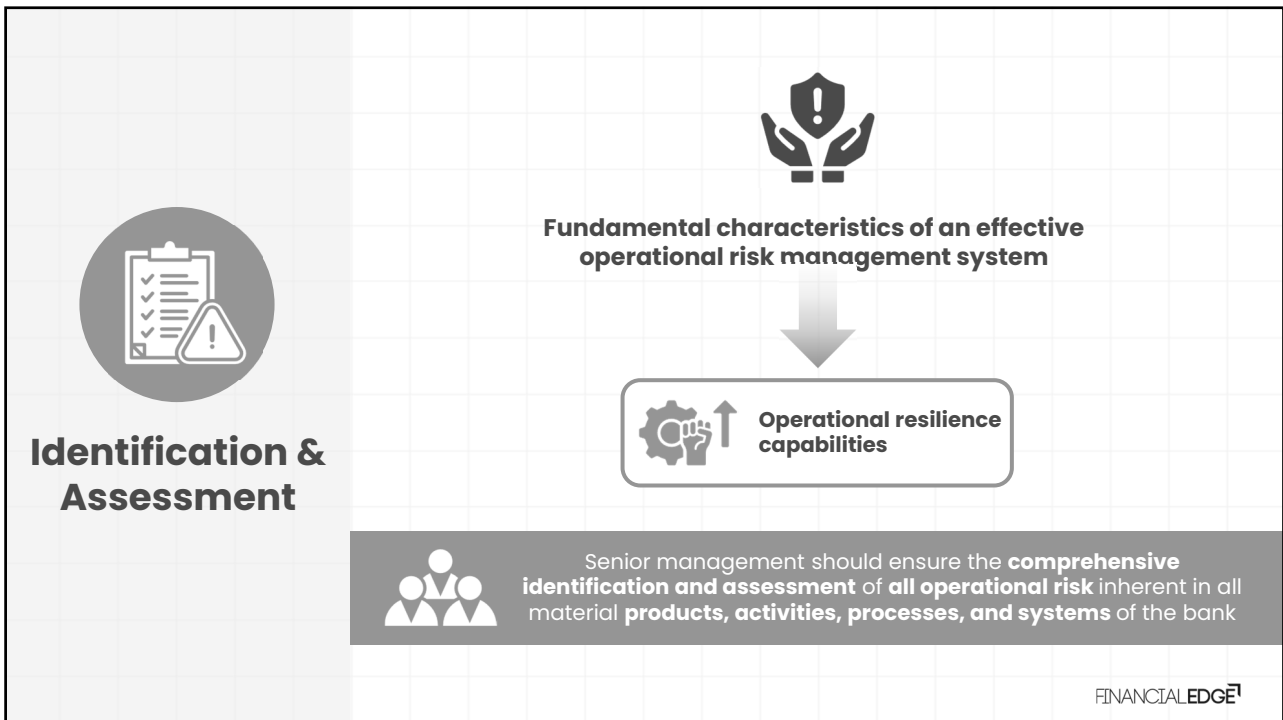


**Change Management**





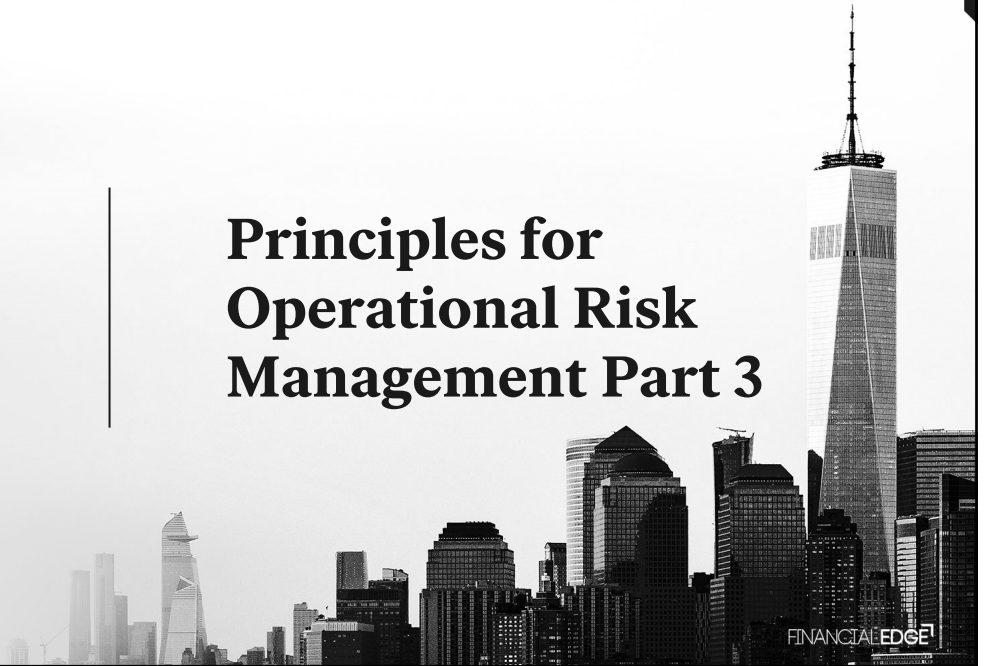








# Principles for Operational Risk Management Part 3



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**Monitoring  
& Reporting**




**Control  
& Mitigation**




**Information &  
Communication  
Technology (ICT)  
Risk**

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## Monitoring & Reporting




Senior management should implement a process to **regularly monitor operational risk profiles** and the material operational exposures within the bank

### Reports


- Comprehensive
- Accurate
- Consistent
- Actionable



**Board of directors**




**Senior management**




**Business unit**

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## Monitoring & Reporting



Senior management should implement a process to **regularly monitor operational risk profiles** and the material operational exposures within the bank

### Reports

- Comprehensive
- Accurate
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**Business unit**

Ensure **effective reporting** on any residual **operational risks**:

- Operational risk events
- Control deficiencies
- Process inadequacies
- Non-compliance with operational risk tolerances

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