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European Banks Underestimate the Challenges of BCBS 239 Implementation

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In light of the discussion around BCBS[1] 239 – a document describing 14 principles aiming to establish effective risk data aggregation and risk reporting capabilities – we carried out a survey in January 2015 to give practitioners a snapshot of the industry's "current state". It shows that while banks understand the challenges of implementing BCBS 239, many of them underestimate the time, resources and costs involved.

BCBS 239 has its roots in the fact that the global financial crisis provided a sharp indication that banks' data infrastructure around the world were inadequate to support the early identification and timely management of financial risks. Far too many banks lacked the ability to aggregate risk exposures, identify concentrations quickly and report their findings. This had severe consequences for some banks and, because this affected some of the larger international players, the stability of the financial system was also put into jeopardy.

The 14 principles described in the BCBS 239 document cover four closely related topics: (1) data governance and infrastructure; (2) risk data aggregation capabilities; (3) risk reporting practices; and (4) supervisory review and tools and are initially addressing global systemically important banks (G-SIBs), requiring them to comply within three years. National supervisors will apply them to banks identified as being domestic systemically important banks (D-SIBs) and make the principles part of general guidelines for prudent risk management at a national level.

For the coming years it can be expected that the principles for effective risk data aggregation and risk reporting will become best practice and that they will foster leaner risk management structures and more agile banks.

1 Basel Committee on Banking Supervision

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A new standard with far-reaching implications

A resilient IT environment and robust data-aggregation capabilities enable effective risk management, which relies on accurate, complete and timely data, informing the relevant people of the right information at the right time. However, in periods of stress - for example, during the 2008/2009 financial crisis - it became painfully evident that data aggregation was (and still is) a central issue: It limits banks' risk-management capabilities, as many of them still lack the ability to aggregate exposures in a matter of hours, or even days. Fragmented IT infrastructures and an overreliance on manual workarounds were among the factors that impair banks' ability in this regard.

Supervisors globally have repeatedly criticised weaknesses in banks' risk data aggregation and reporting capabilities (e.g., the Senior Supervisors Group in 2009[2] and 2010[3]). In January 2013, the Basel Committee on Banking Supervision (BCBS) issued a document presenting a set of 14 principles to strengthen banks' risk data aggregation capabilities and risk reporting' practices. These principles, commonly referred to as "BCBS 239", which covers four closely related topics:

» Overarching governance and infrastructure;

» Risk data aggregation capabilities;

» Risk reporting practices; and

» Supervisory review, tools and cooperation.

The Basel Committee expects that the principles will support banks' efforts to[4]:

» Enhance the infrastructure for reporting key information regarding risks;

» Improve the decision-making process throughout the organisation;

» Improve information management across the banking group and facilitate a comprehensive assessment of risk exposure at a consolidated level;

» Reduce the likelihood and severity of losses resulting from risk-management weaknesses;

» Speed up the way in which information becomes available and decisions can be made; and

» Enhance a bank's strategic planning and the ability to manage the risks that new products and services pose.

The following graph illustrates how the principles relate to the four topics.

2 SENIOR SUPERVISORS GROUP, Risk Management Lessons From The Global Banking Crisis Of 2008, October 2009, p. 25.
3 SENIOR SUPERVISORS GROUP, Observations On Developments In Risk Appetite Frameworks And IT Infrastructure, December 2010, p. 10.
4 BCBS, Principles for effective risk data aggregation capabilities and risk reporting, January 2013, p. 3.

A strong governance framework, risk-data architecture and IT infrastructure are preconditions for banks to comply with BCBS 239 as they are critical for risk-data aggregation capabilities and risk reporting practices especially during times of stress. Strong risk data aggregation capabilities need accurate, complete and timely data. This ensures that risk-management reports reflect the risks reliably and can address ad-hoc requests that can come from changing internal or external needs. Risk reports based on risk data have to be accurate, clear and complete to ensure a bank's board and senior management can confidently rely on the aggregated information to make critical decisions. The supervisor should review compliance with the principles across banks to determine whether the banks are achieving the desired outcome and, whether effective and timely remedial action is needed to address the deficiencies in the bank's risk data aggregation capabilities and risk reporting practices.

Who will be subject to BCBS 239?

Initially, the principles for effective risk data aggregation and risk reporting address G-SIBs only. They apply at the group level and to all of the group's material business units or entities. The G-SIBs comprise the world's 30 largest financial institutions, which have been working since the beginning of 2013 to comply with the principles by 1 January 2016. A recent self-assessment published by the BCBS in January 2015 showed that many of the G-SIBs continue to encounter difficulties in establishing strong data-aggregation governance, architecture and processes, with the banks themselves reporting that they often have to rely on manual workarounds[5].

The Basel Committee also strongly suggests that national supervisors apply the principles to D-SIBs three years after their designation as such by their national supervisors[6]. Even though these D-SIBs have not been nominated yet, it is expected that the largest banks in each country, in the Euro area, or those under the direct supervision of the European Central Bank will have to implement the principles for effective risk data aggregation and risk reporting. Banks in Canada and Germany are preparing for this earlier than in other countries.

5 BCBS, Progress in adopting the principles for effective risk data aggregation and risk reporting, January 2015, p. 3.
6 BCBS, Principles for effective risk data aggregation and risk reporting, January 2013, p. 4.

Industry snapshot: Current state of play

In advance of the regulatory development, many European banks are facing significant challenges in implementing BCBS 239. Moody's Analytics ran a survey in January 2015 to give practitioners a snapshot of the industry's "current state". It reveals that many banks underestimate the time, resources and cost involved to implement BCBS 239.

All principles

50% of the respondents intend to address all principles simultaneously

75%

of the respondents expect to see improved operational efficiency

Internal

75% of the respondents plan to comply by extending the framework internally

<€5M

34% of the respondents believe that the total budget to achieve BCBS 239 compliance will not exceed €5 million

>3 years

38% of the respondents do not believe that banks will achieve compliance with BCBS 239 within three years

Data

A major challenge when implementing the requirements of BCBS 239

69%

of the respondents have already begun a project or at least developed a road map

Resources

The lack of skilled resources is considered to be the project's biggest obstacle

Survey Results

The survey aimed to gain a better understanding of how banks are planning to comply with: (1) the principles for effective risk data aggregation and risk reporting; (2) the challenges that they face; and (3) the resources necessary to achieve this objective. The survey consolidates the views from about 40 banks from ten countries regarding how they are approaching the challenges that they face. Banks were requested to answer 14 questions across four main areas:

» Survey demographics

» Ownership and expectations

» Challenges

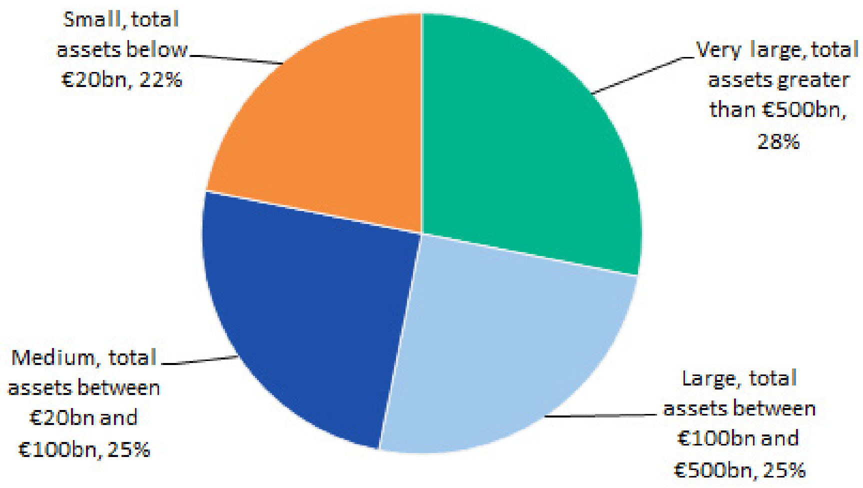
» Resourcing and costs

Section 1 – Survey demographics

Key findings:

» We sampled a cross-section of institutions in terms of size and regional coverage. The survey's results prove that BCBS 239's requirements are on the agenda, regardless of the bank's size or location.

QUESTION 1: WHAT ARE THE TOTAL ASSETS OF YOUR BANK?



QUESTION 2: IN WHICH COUNTRY IS YOUR BANK DOMICILED?

Country	Share in Survey (%)
Austria	14
Belgium	4
France	7
Germany	36
Greece	7
Italy	4
Netherlands	11
Switzerland	4
United Arab Emirates	4
United Kingdom	11

Section 2 - Ownership and expectations

Key findings:

» The implementation of BCBS 239 is firmly on the agenda of banks' senior management. Typically, the chief risk officer is in charge of overseeing the project along with the chief financial officer, or a combination of C-level executives are in charge.

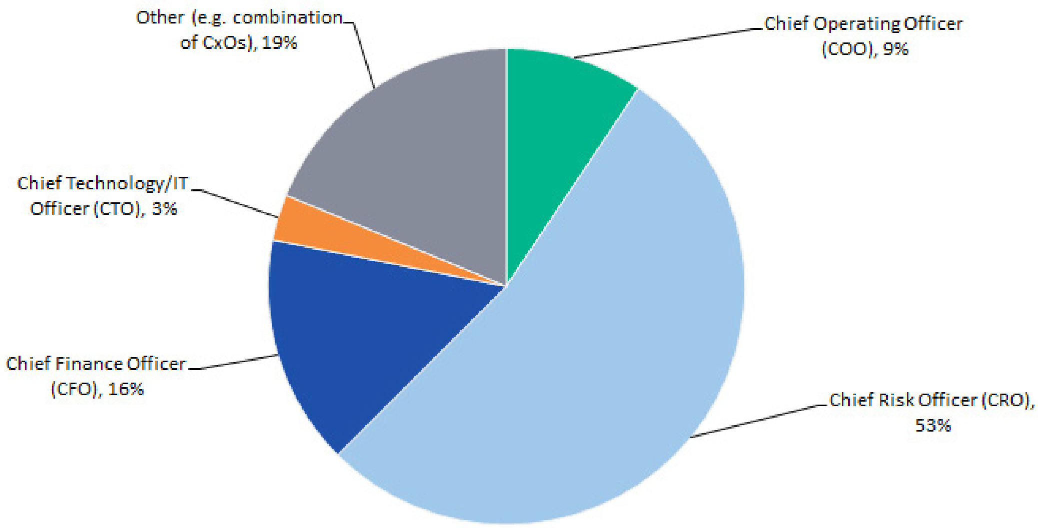
» Most banks consider the principles of BCBS 239 to be equally important and plan to address them simultaneously. About a third of the banks that we interviewed consider the need to revise the data infrastructure as being the most pressing requirement.

» Two-thirds of the interviewed banks have either already begun, or are preparing a project to implement BCBS 239.

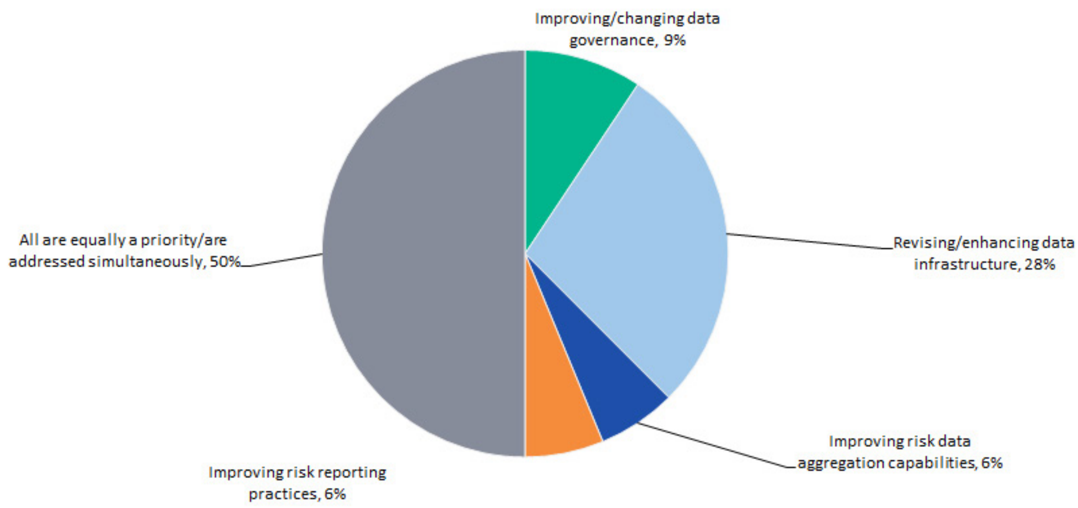
» Operational efficiency and better quality of data are seen as the main business benefits of BCBS 239.

» Three-quarters of the banks intend to enhance existing internal solutions to meet the requirements of BCBS 239.

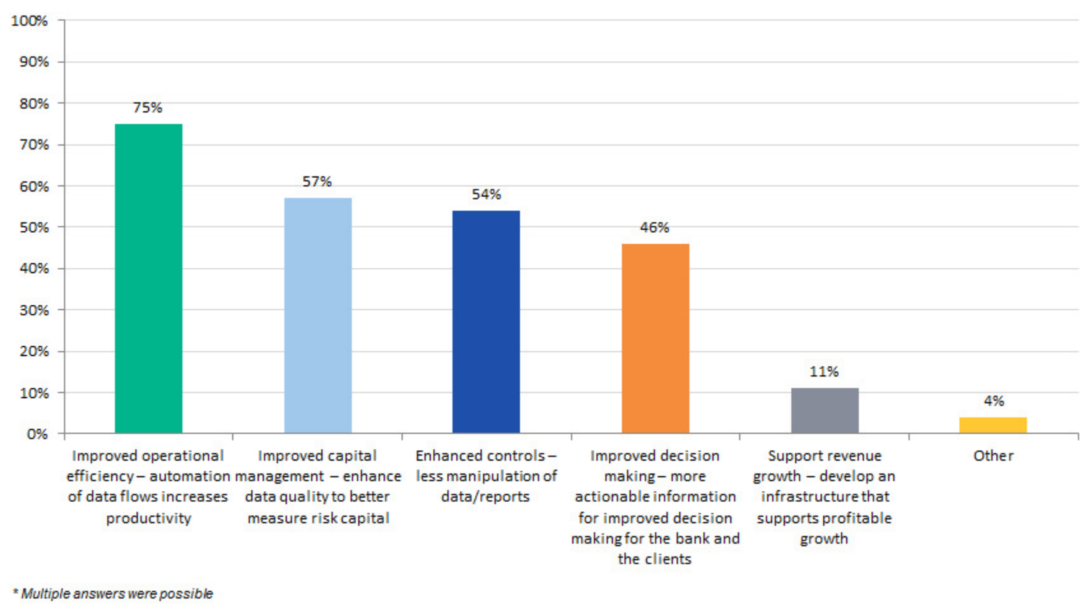
QUESTION 3: WHO "OWNS" THE OVERALL BCBS 239 PROJECT IN THE ORGANISATION?



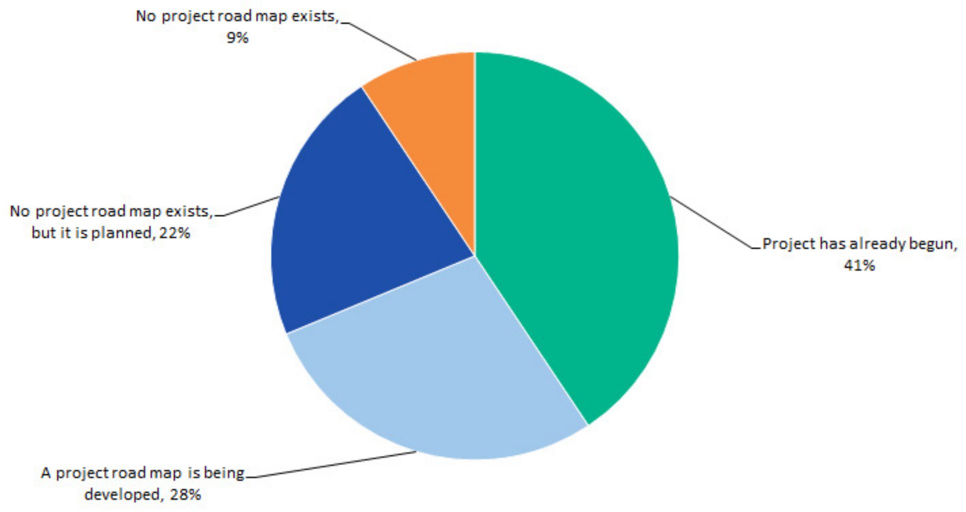
QUESTION 4: WHICH SEGMENT OF BCBS 239 HAS PRIORITY/WILL BE ADDRESSED FIRST?



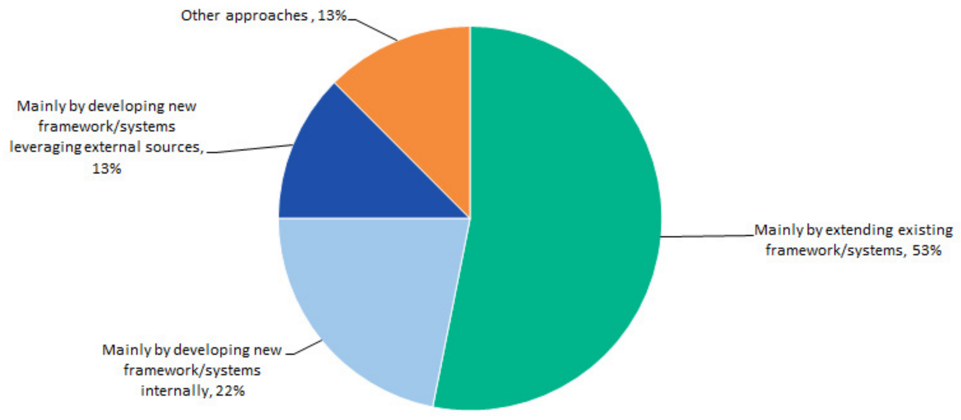
QUESTION 5: WHAT ARE THE PRIMARY BUSINESS BENEFITS THAT BCBS 239 WILL GENERATE FOR YOUR FIRM?(MULTIPLE ANSWERS WERE POSSIBLE)



QUESTION 6: WHAT IS THE CURRENT STATUS OF YOUR BCBS 239 PROJECT?



QUESTION 7: HOW DOES YOUR ORGANIZATION PLAN TO ACHIEVE BCBS 239 COMPLIANCE?



Section 3– Challenges

Key findings:

» Bad decisions made in the past have led to fragmented IT infrastructures that are becoming painfully visible, as incomplete data architectures and taxonomies, as well as weak data-management standards are the key challenges with regards to the principles on governance and infrastructure.

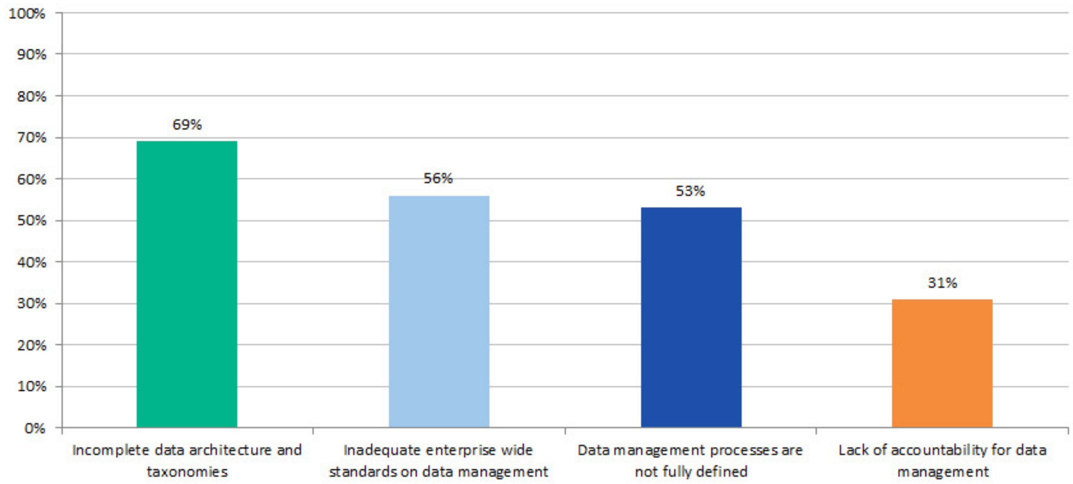
» Data-quality issues and inconsistencies are seen by the respondents as the key impediments for banks to aggregate their data, leading to far too many manual workarounds.

» The reliance on manual workarounds and the lack of a single data inventory with high quality data hinders the banks when they are trying to report in a timely and accurate fashion.

» In light of the known problems, only two-thirds of the interviewed banks believe that they will be able to achieve compliance with BCBS 239 during the given timeframe. These tend to be the banks that either already begun a BCBS 239 project very early on, or that simply underestimate the amount of work required.

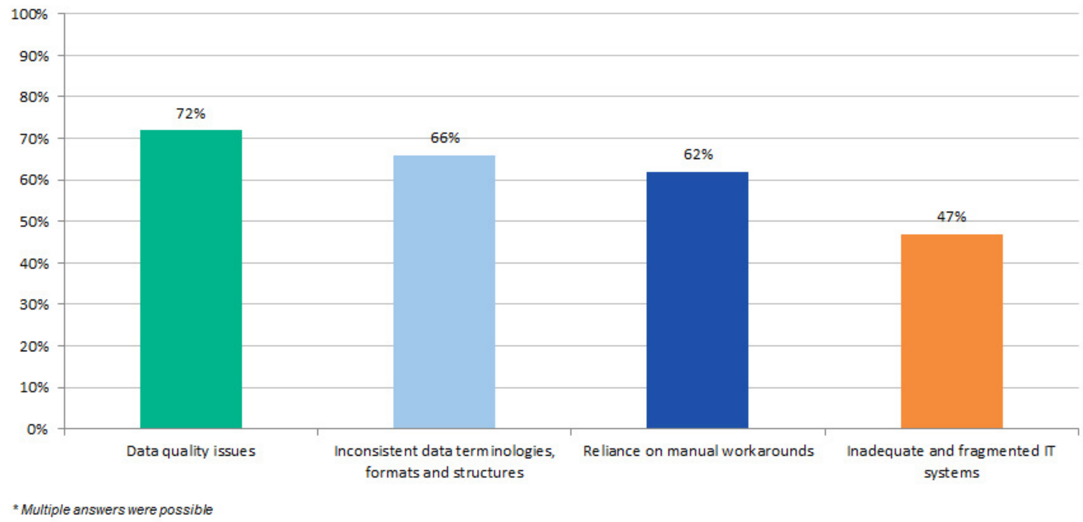
» The lack of skilled resources is the biggest risk that could jeopardize the implementation of BCBS 239.

QUESTION 8: WHAT ARE THE KEY CHALLENGES IN THE SEGMENT "GOVERNANCE AND INFRASTRUCTURE"?

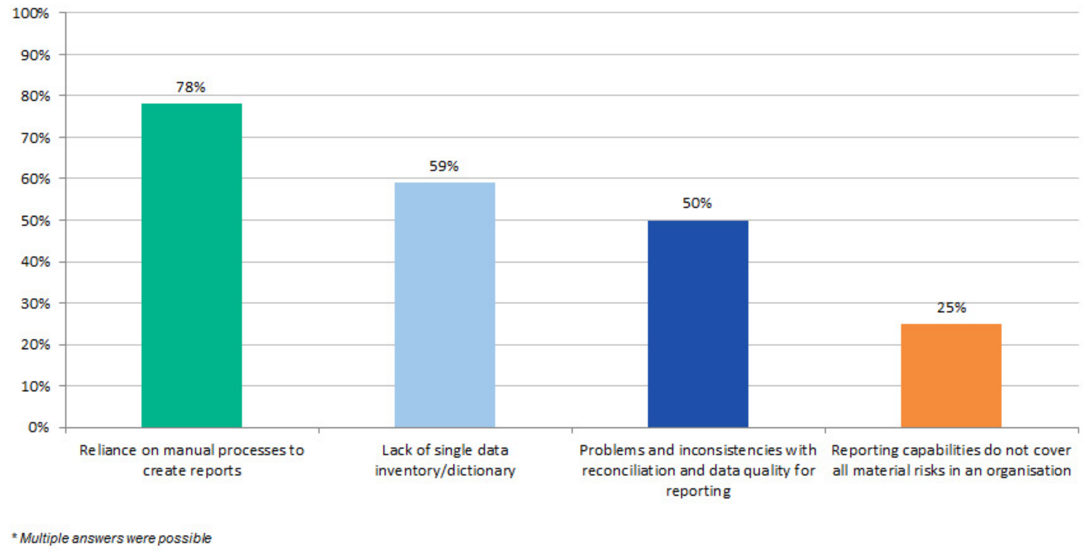


** Multiple answers were possible*

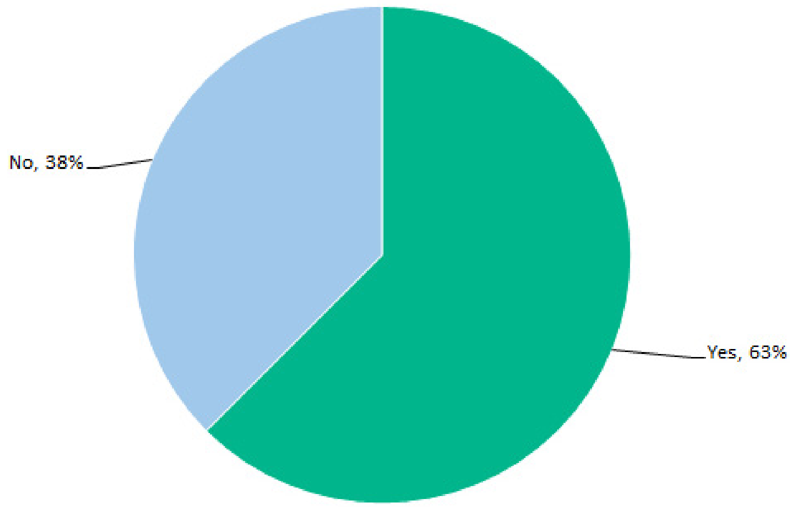
QUESTION 9: WHAT ARE THE KEY CHALLENGES IN THE SEGMENT "RISK DATA AGGREGATION CAPABILITIES"?



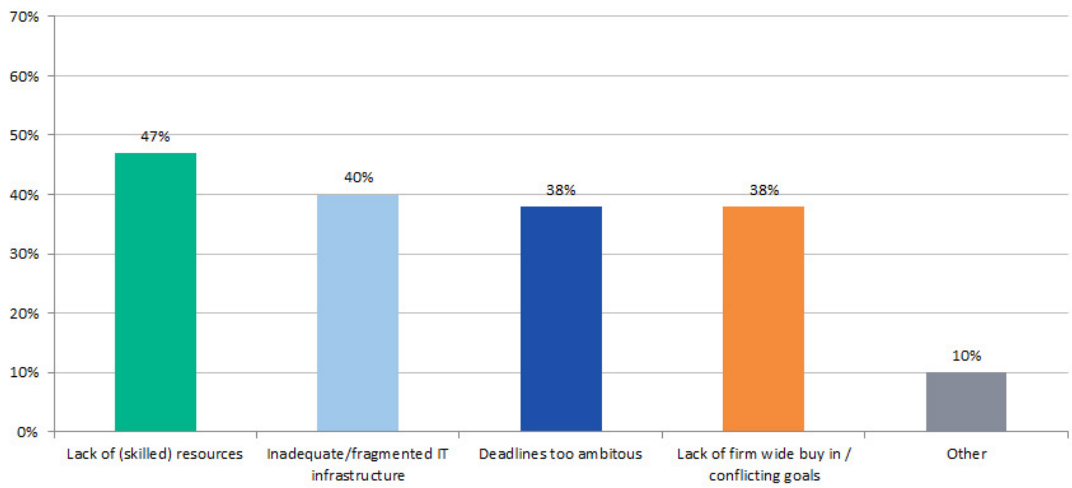
QUESTION 10: WHAT ARE THE KEY CHALLENGES IN THE SEGMENT "RISK REPORTING PRACTICES"?



QUESTION 11: THE BASEL COMMITTEE HAS GIVEN THE BANKS A THREE YEAR DEADLINE FOR THE IMPLEMENTATION OF BCBS 239. IS THIS TIMELINE ACHIEVABLE?



QUESTION 12: WHAT COULD JEOPARDIZE/SLOW DOWN THE OVERALL IMPLEMENTATION OF BCBS 239?



* Multiple answers were possible

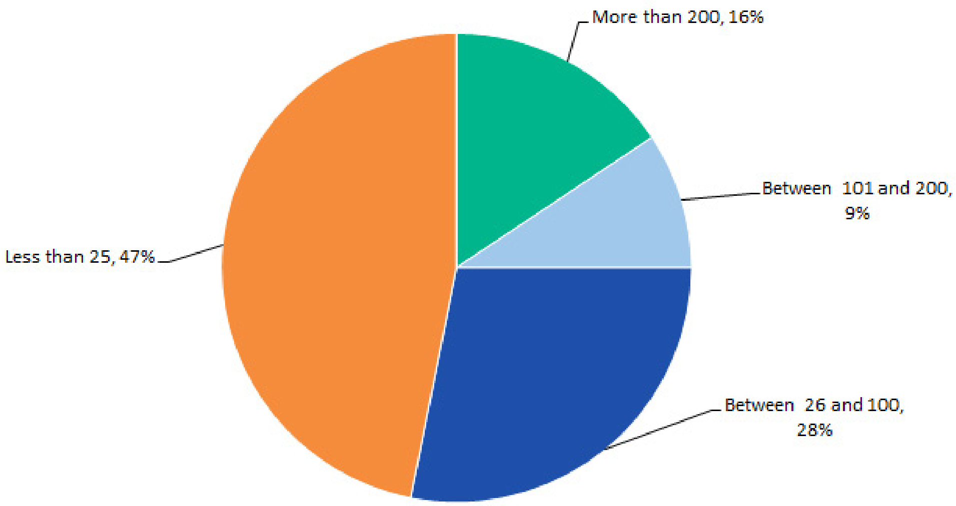
Section 4– Resourcing and cost

Key findings:

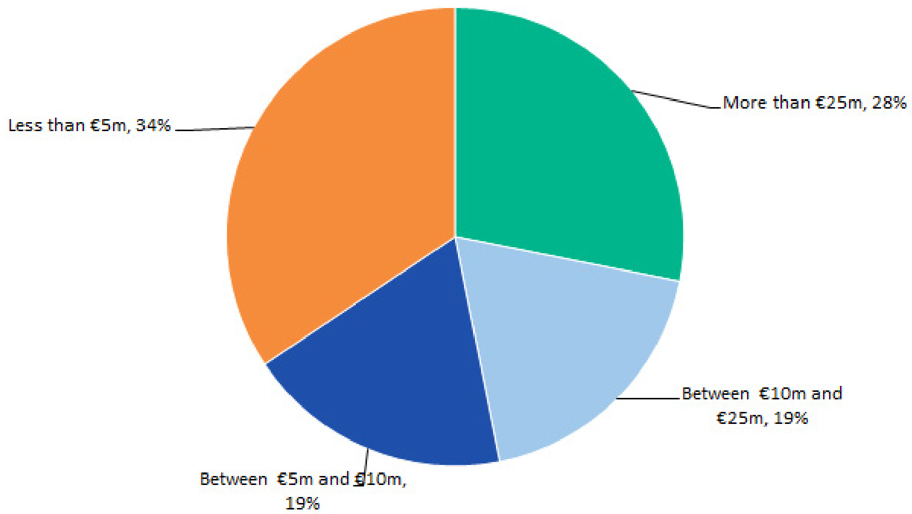
» Almost half of the respondents believed that less than 25 employees will be required to be directly involved in the implementation of BCBS 239. This does not correspond with observations from banks that have already initiated BCBS 239-related projects, which report far higher numbers.

» A third of the banks in the survey believed that the cost of implementing BCBS 239 will not exceed €5 million. Similar to the finding of question 13, this does not correspond with observations from banks that have already initiated BCBS 239-related projects, which estimate that their expenses will exceed €25 million.

QUESTION 13: HOW MANY EMPLOYEES ARE (EXPECTED TO) BE DIRECTLY INVOLVED IN THE IMPLEMENTATION OF BCBS 239?



QUESTION 14: WHAT IS THE (EXPECTED) TOTAL BUDGET FOR THE IMPLEMENTATION OF BCBS 239?



Summary: Many banks underestimate the challenges

Our survey provided a snapshot on the current state of play with regard to the implementation of BCBS 239 among European banks. Many institutions have begun or are about to begin projects to comply with the principles for effective risk data aggregation and risk reporting. Common challenges that resonate through the survey are weak data management standards, data quality issues and reliance on manual workarounds which are considered to be the key problems when addressing the principles of BCBS 239. In order to tackle these issues about three quarters of the respondents intend to turn to rather tactical solutions by enhancing existing internal systems to meet the requirements of BCBS 239 instead of utilizing this opportunity to establish a new strategic data infrastructure. Short term operational efficiency is viewed as the main business benefit of BCBS 239 whereas the long term ability to build a leaner, more agile bank is not on the radar screen of banks yet.

From an operational point of view the survey showed that many banks seem to underestimate the work, resources and investment required to achieve compliance with BCBS 239. Almost half of the respondents believed that fewer than 25 employees will be required to be directly involved in the implementation of BCBS 239 and about a third of the banks believe that the cost will not exceed €5 million. This does not correspond with observations of banks that have already initiated BCBS 239-related projects and report far higher staffing levels and estimate the project expenses to exceed €25 million.

References

» Basel Committee on Banking Supervision (2013), *Principles for effective risk data aggregation and risk reporting*, Bank for International Settlement.

» Basel Committee on Banking Supervision (2015), *Progress in adopting the principles for effective risk data aggregation and risk reporting*, Bank for International Settlement.

» Senior Supervisors Group (2009), *Risk Management Lessons From The Global Banking Crisis of 2008*.

» Senior Supervisors Group (2010), *Observations on Developments in Risk Appetite Frameworks and IT Infrastructure*.

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