

## **Risk Management: From Regulatory Compliance to Value Creation**

### **Sagora, the Risk Management Company**

Mathias Schmit<sup>1</sup> and Marie-Paule Laurent, relying on a network of associates, set up SAGORA Lease & Risk Management. Sagora offers consultancy services in risk management to financial institutions. The network aims at merging the extensive banking experience and strong analytical skills of its members. They review credit and operational risk management to ensure endorsement by internal management bodies and banking supervisors in respect to the implementation of new EU banking regulations, namely the Capital Requirement Directive (CRD being the EU version of the Basel II Accord). In this perspective, SAGORA defines risk management frameworks in financial institutions including model specifications, operational and organisational aspects that meet the requirements of Pillars I & II of the CRD. Their frameworks include the many EU specificities that have been introduced by the EU regulators.

### **Basle II & CRD: an issue for all EU financial institutions**

The implementation of the **EU directive** requires much more attention than the Basel II accord since its application **affects all EU financial institutions whatever their size** and not only internationally active institutions. Additionally, the EU directive has outstanding issues that crucially impact the financial institutions whatever the approach they choose to implement the Directive. These issues include the definition of exposures, requirements to apply for credit risk mitigation techniques, collateral appraisal requests, risk management policies and governance, stress testing etc...

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<sup>1</sup> Mathias worked previously at Leaseurope at head of economic affairs and acts now as an external advisor. He strongly contributed to a more suitable regulatory framework for the leasing industry regarding the implementation of Basel II accords in the EU.

## State-of-the-Art Approach

In order to achieve appropriate implementation of new EU regulations, SAGORA sets up proprietary methodologies. These do not only rely on pure implementation. **Our innovative approach embeds risk processes into a firm-wide risk management framework.**

**This framework integrates:**

1. **Description of strategic request and business case** including information relative to alternative options, economic capital, regulation considerations and potential impacts.
2. **The methodology and risk management design** to ensure that the use of risk management framework and its policies are developed in line with the institution objectives and user's acceptance criteria (specific business specifications, methodological choices, testing and policies definition).
3. **Usage policies** that describe how the risk management framework is applicable to the different parties and within which processes.
4. **Maintenance and review of the risk management framework on an on-going basis.** Indeed, monitoring reports should be defined as inputs to review and check specific requests to be in line with the institution's objectives, policies and implementation aspects.
5. **Organisational and internal governance** consistent with the risk management framework implementation so that the structure of the organisation is clear and transparent to both the institution's own staff and to the relevant supervisory activity. For instance, the institution should:
  - Clearly define the roles and responsibilities of risk management and business lines
  - Integrate decision making process and not rely on silos
  - Ensure a buy-in from all involved parties
  - Implement conditions to separate risk control, compliance and internal functions of the business lines they monitor and control
  - Implement effective processes for analyzing and reporting risks
  - Define profiles required and key success factors to promote adequately the institution

All these steps should be endorsed to make sure that risk management development and implementation guidelines are properly followed, policies approved and decisions relative to their governance adequately made in line with the specificities of the institutions.

**Proper internal validation** is essential before the external validation phase starts by the supervisor.

## Creating New Business Opportunities

The objective of SAGORA is about helping institutions to deliver quality throughout their organisation to **create opportunities in line with the objectives of the financial institution** that comes on top of pure regulatory compliance. Its areas of expertise include:

- Implementation of the EU Capital Requirement Directive and Basel II
- Definition and description of a proper vision upfront prior to any implementation
- Definition of a roadmap to migrate from today's to tomorrow's environment to be supported by the supervisors
- Elaboration of a risk management framework in line with predefined process for consistency, harmonization and transparency purposes taking into account the institution's objectives, strengths and internal constraints:
  - Development, specification and validation of risk policies
  - Specification for the recognition of credit risk mitigation techniques
  - Asset management
  - Regulatory and economic capital allocation
  - Specification and optimization of internal objectives
  - Improvement of measurement performance

The implementation of adequate processes will attract most of the potential benefits in the medium term. Indeed, building on suitable risk management frameworks, management will find out more about **new opportunities to optimise business benefits driven by new financial regulatory pressure**.

## Contacts

Sagora, Risk Management  
Rue de haverskercke 28  
B-1190 Brussels  
Belgium  
Dr. Mathias Schmit  
Dr. Marie-Paule Laurent  
Tel: +32 496.93.22.70  
E-mail: [sagora@skynet.be](mailto:sagora@skynet.be)