



Regulatory training for internal audit

Abstract

The client is the Internal Audit function of a global bank.

Avantage Reply was asked to provide training to address specific regulatory issues and concerns around emerging regulation to enable the Audit Function to discharge its duties effectively.

Avantage Reply tapped into its extensive resources and network to deliver valuable SME insight, expert regulatory knowledge and supported internal audit through the regulatory haze. Regulatory training for internal audit.

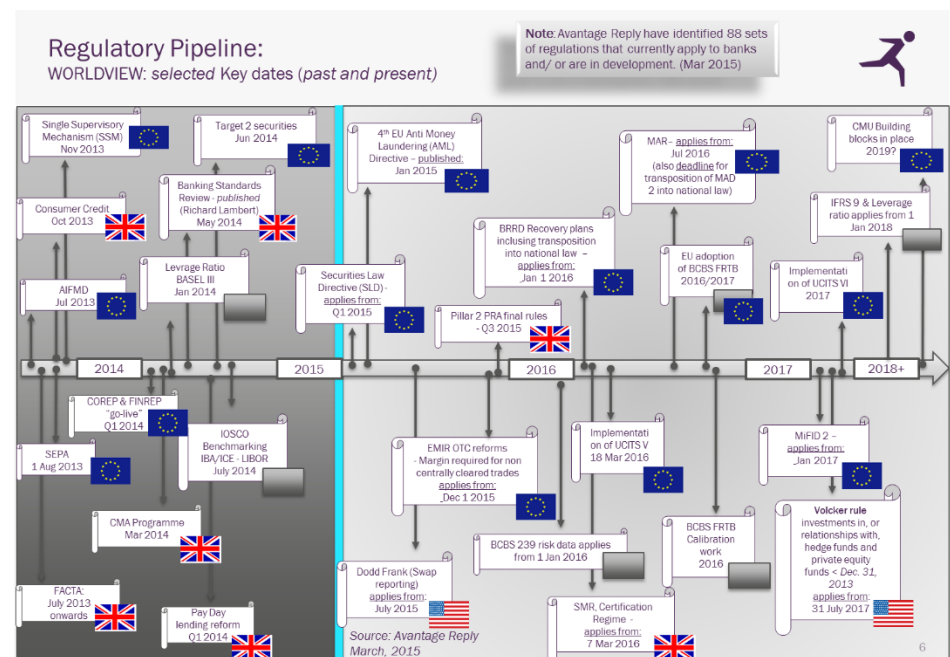
THE CLIENT

Our client was the Internal Audit Function of a global banking group. The function was responsible for third line of defence assurance of both Prudential and Conduct risks and focused its attention providing oversight of the second line of defence. The Audit team had grown from circa 40 auditors a year ago to an approved headcount of 100 within a year. As a result of this rapid expansion, the team was both understaffed and underskilled in terms of possessing sufficient risk and regulatory expertise to deliver its remit.

THE CHALLENGE

Avantage Reply was asked to provide training to address specific concerns about emerging regulatory issues faced by the bank with the objective of providing Audit with sufficient expertise to design and deliver audits of the areas affected.

The workshop addressed 15 regulatory topics, based on the pipeline of emerging regulatory change.



APPROACH AND SOLUTION

Avantage Reply planned and prepared the training off-site, then executed it on-site at the client's address. This was carried out with minimal fuss and demands on the client.

The approach and solution was divided into 2 (two) phases: 1. Planning and preparation; and, 2. Execution, Delivery and Presentation.

1. Planning and Preparation

Avantage Reply identified key resources and leading experts in each applicable regulatory field. The 'team' assembled was sourced from both the UK and continental Europe. A manager was appointed internally to organise, collate and drive the project to completion. By tapping into expert knowledge Avantage was able to engage 'clusters' of partners, managers and consultants to deliver valuable regulatory insight, subject matter expertise and audit acumen to help deal with the complexities of the issues involved.

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2. Delivery, Execution and Presentation

The training was divided into 15 Regulatory Topics and 7 regulatory Chapters. At the end of each Topic Avantage Reply organised a short Q&A session to brainstorm how regulatory compliance could be tested via Audit work. The client found this very useful. It was found to promote issue awareness, team co-operation, lateral problem solving and fresh ideas. Overall it helped the audit team gain a better understanding of what they should be looking out for.

Regulatory topics covered


Chapter	Topic	
Capital Markets Union	Topic 1	CAPITAL MARKETS UNION (CMU): Single Supervisory Mechanism (SSM) and the ECB
Prudential Regulatory Pipeline	Topic 2	Basel Capital Floors, Basel Leverage Ratio, IFRS 9
Pillar 2	Topic 3	Assessing capital adequacy under Pillar 2 - CP1/15
EBA consultations on model approaches	Topic 4	Fundamental Review of the Trading Book (FRTB)
	Topic 5	Standardised approach for Counterparty Credit Risk (CCR)
	Topic 6	The Internal Ratings Based (IRB) approach to Credit Risk
	Topic 7	Pillar 2: Interest Rate risk in the Banking Book (IRRBB)
	Topic 8	Operational Risk revisions to Standardised Approach and Advanced Measurement Approach (AMA)
Traded Products	Topic 9	Traded Products and CVA Capital charge
	Topic 10	Margining for non-cleared transactions
	Topic 11	Trade & Transaction reporting, including MiFID 2
Bank Recovery & Resolution	Topic 12	Recovery & Resolution Planning
Risk Governance & Conduct Risk	Topic 13	FCA Business Plan & Conduct Risk Outlook
	Topic 14	Senior Managers Regime (SMR) and Certification Regime (CR)
	Topic 15	The Role of the Second Line of Defence (2LOD)

Each Regulatory Topic had a summary slide (see below) which covered

- What it was and why is it happening?
- How is your business affected?
- Key dates to look out for
- Further reading
- Glossary of Terms

Example Topic Summary

TOPIC 10
New mandatory 'Margin requirements' for non-centrally cleared OTC derivatives (BCBS 261):
SUMMARY



What is it and why is it happening?

- Not all derivatives can be centrally cleared. Only 'standardised derivatives' can be centrally cleared. Derivatives which cant be standardised and therefore cant be centrally cleared are now mandated with minimum standards for margin requirements The paper was issued in March 2015.
- These new margin requirements are guided by the Basel committee's BCBS 261 and will become national law.
- This is happening again due to the financial crisis and is a response to the lack of liquidity available for counterparty margins posted. There are new mandatory margin requirements. For example new % requirements by asset class.

Key Dates

- Implementation dates vary between 2015-2020 and are 'based on your average notional amounts for March, April and May from the previous year.'

How is your business affected?

- Implementation dates will be phased in and dependent on your covered entities "aggregate month-end average notional amount of non-centrally cleared derivatives" and range from 1 Sep 2016 – 2020. Implementation includes "Initial Margin" and "Variation Margin".
- All asset classes are impacted, except physically settled Forward physically settled FX forwards and swaps.

Further Reading / Links

- BCBS 261 Margining for non cleared derivatives_Sep 2013

Glossary of Key Terms

- Margin / Independent Amount** – the margin or collateral used to cover drops in an assets value. (same as margin)
- Standardised Derivatives** – derivatives which meet uniform characteristics and standards across the industry.
- Initial margin** – initial collateral provided at the outset to cover potential future movements in the assets value
- Variation margin** – collateral 'top ups' to the initial margin (co-lateral) if the asset's value fall more than is covered by the initial margin.
- Non centrally cleared derivatives** – overt the counter (OTC) derivatives
- Covered entities** – All financial firms and "systemically important non-financial entities

RESULTS AND BENEFITS

Benefits delivered by the Training included:

- **Valuable insight in terms of regulatory awareness and upcoming legislation** – this enabled internal audit to stay up to speed with issues, best practice and identify key areas to focus on. This further provided valuable

insight for conducting future audits in often complex business and regulatory practices;

- **Valuable insight into best practice** – because Avantage Reply can access a wide network of expertise, knowledge and experience they were able to offer the client a view of current industry practice from other market participants and build on this regulatory knowledge to recommend benchmark best practice;
- **Regulatory reference** - the hard and soft copy training manual could be referenced at any time with follow up support provided by Avantage Reply;
- **Increased audit confidence and reduced risk** – Internal audit felt more confident challenging the business and questioning current practice. This resulted in a building of trust between team members and other key stakeholders within the audit team.

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