Abstract

The client initiated a Basel II Credit Risk Mitigation (CRM) Policy project to ensure business processes and capital calculation processes for risk mitigation techniques were covered in a new policy which was compliant with the UK interpretation of Basel II. Avantage Reply was engaged to create the CRM Policy and a framework for its implementation and ongoing maintenance. The CRM Policy document was formally agreed by the relevant business stakeholders and approval was received by the FSA to use the CRM in the client’s loss given default estimates, which led to a significant capital reduction.

THE CLIENT
The client is a Global Banking Market Institution in London.

THE CHALLENGE
The Basel II Credit Risk Mitigation Policy project was initiated to embed a policy which reflects the institutional process and Risk Weight Calculation toward Credit Risk Mitigation.

As there are multiple CRM techniques available and many products this institution caters for in their Global Markets Division, the Client needed to ensure business processes and capital calculation processes for all products and risk mitigation techniques were covered in a new policy. There was a key focus within the business on using collateral as a mitigation technique. Furthermore, all policy requirements were to comply with the UK interpretation of Basel II.

The Client asked Avantage Reply to create the above CRM policy and a framework for its implementation and ongoing maintenance.

APPROACH AND SOLUTION
Initially, Avantage Reply developed a suitable framework to assist with policy development and future enhancements. This included the preparation of detailed business CRM procedures and aligning all policies with the group’s terms of reference.

Once the governance was established, Avantage Reply developed a straw man for the new policy, building on the existing policies and the UK FSA regulatory requirements.

A key new requirement related to “legal certainty”. As such, Avantage Reply worked closely with the Client’s legal department to ensure a consistent interpretation of Basel II requirements.

The straw man policy was discussed with various representatives from the business, finance and risk functions, mainly using workshops and facilitation techniques. The same forum was used to gain approval for implementation in the various departments.
Finally, Avantage Reply consultants documented in details the above framework to ensure that future changes will be appropriately handled and communicated.

RESULTS AND BENEFITS
The clear, comprehensible and wide-reaching CRM policy document was produced and formally agreed to by the relevant business stakeholders. The policy was developed to ensure that the Global Markets Division was compliant with both Basel II CRM and the Group’s regulatory requirements.

The success of the implementation of the policy was reflected in the approval received by the FSA to use the CRM in the Bank’s loss given default estimates, which in itself, led onto a significant capital reduction.