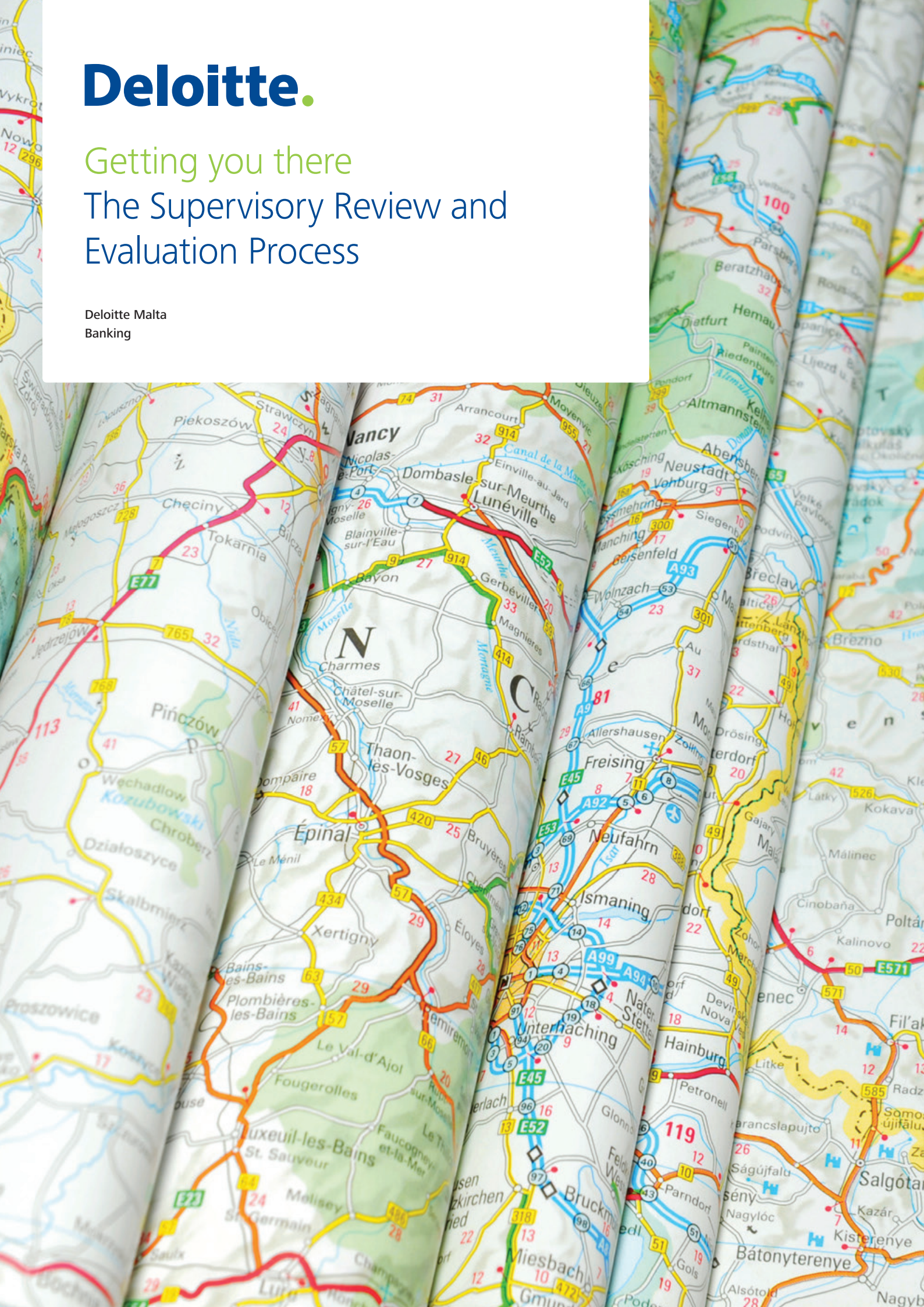


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## Getting you there The Supervisory Review and Evaluation Process

Deloitte Malta  
Banking

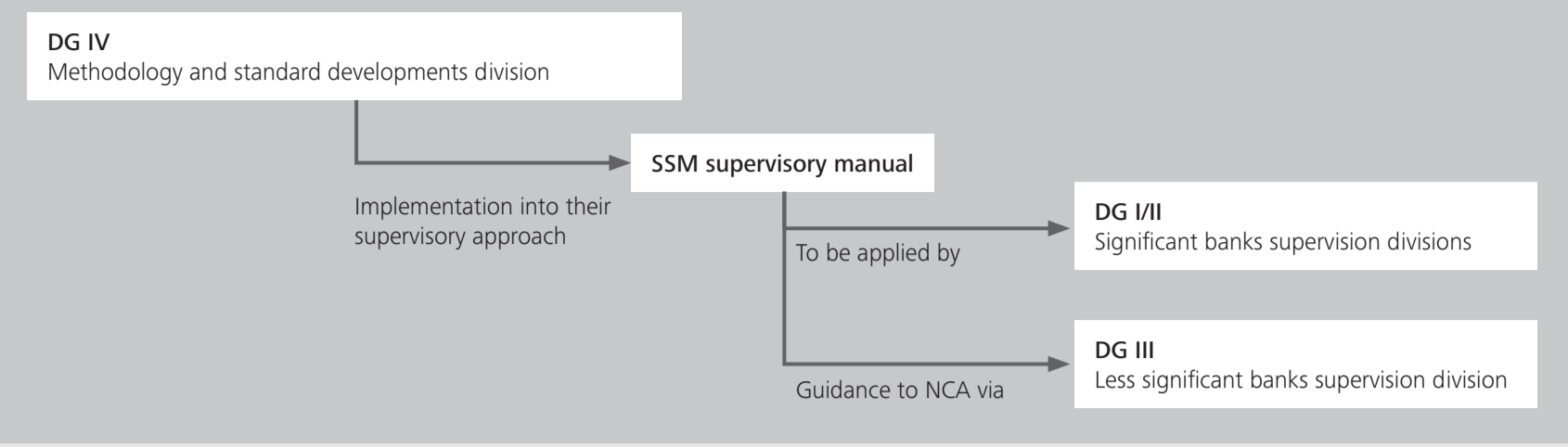


The SREP supervisory process will apply to all banks irrespective of size or complexity, through a common decision making process allowing for peer comparisons and transversal analyses on a wide scale

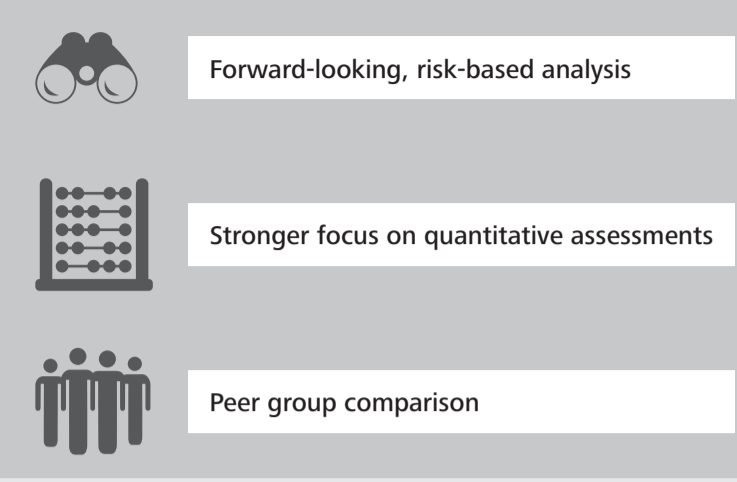
Regulators will specifically assess each of the eight SREP governance principles, and in doing so will adjust to factor in the specificities and business model of each bank

## Banking Union

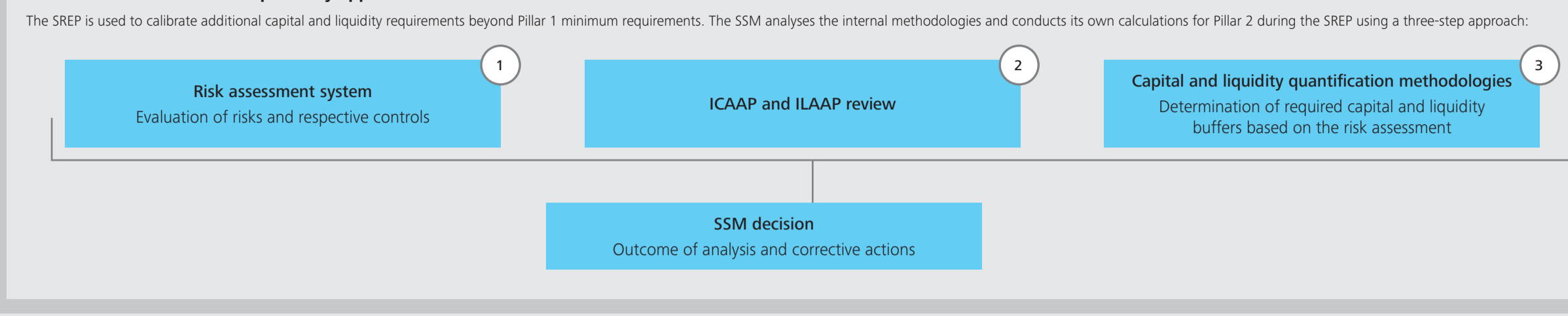
### Implementation of EBA SREP guidelines by the ECB



### Characteristics of the SSM supervisory approach



### Characteristics of the SSM supervisory approach



Single Resolution Mechanism (SRM)

Single Rule Book

## EBA guidelines for common procedures and methodologies for the SREP

### Categorisation of institutions

| Categories based on size, structure, internal organisation and nature, scope and complexity of activities | Systemically important (1)  | Medium to large (2)  | Small to medium (3)  | Other (4)  |
|---|---|--|--|--|
| Level of engagement and dialogue  | Ongoing engagement with institution's management body and senior management; engagement with institution for assessment of each element | Risk-based engagement with institution's management body and senior management as well as engagement with the institution for the assessment of material risk elements | Risk-based engagement with institution's management body and senior management as well as engagement with the institution for the assessment of material risk elements | Engagement with management body and senior management at least every three years |

### Key indicator monitoring



### Core process: SREP elements

#### Sources of information for assessments should include amongst others:

- Strategic plans
- Financial reporting
- Regulatory reporting
- Internal reporting
- Recovery plans
- ICAAP
- ILAAP
- Third party reports, e.g. external audits
- Other studies, e.g. macro-prudential reports

#### 1. Business model analysis (BMA)

- Preliminary assessment**: Identify main activities, product lines, geographies, market positions; identify the institution's peer group on the basis of the rival product/business lines targeting the same source of profits.
- Identification of the areas of focus for the BMA**: Identify the business lines which are most important for future business model sustainability and the ones most likely to increase vulnerabilities; assess supervisory reviews and findings, internal and external audits, strategic plans and peer comparisons.
- Assessment of the business environment**: Develop an understanding of macroeconomic and market trends as well as strategic peer group intentions (analysis of competitive landscape).
- Quantitative analysis of the current business model**: Analyse and assess the institution's profitability, balance sheet, concentrations and risk appetite taking the recent past and future trends into account.
- Qualitative analysis of the current business model**: Assess external and internal dependencies, reliance on reputation, strength of the relationships and areas of competitive advantage.
- Analysis of the strategy and financial plans**: Quantitative and qualitative analysis of strategic plans and projected financial performance, including the underlying success drivers and assumptions as well as execution capabilities.
- Assessment of the business model viability**: The institution's current business model's ability to generate acceptable returns over the following 12 months; assess the acceptability of returns against ROE, funding structure, risk appetite.
- Assessment of the sustainability of the institution's strategy**: The sustainability of the institution's strategy on its ability to generate acceptable returns over the next three years; assess the plausibility of assumptions and the risk level.
- Identification of key vulnerabilities**: Examples: unrealistic strategy, excessive concentrations or volatility, excessive risk taking, funding structure concerns and external issues.

Scoring 1 – 4

#### 2. Assessment of internal governance and controls

**Overall internal governance framework**

- Is the organisation fit for purpose?
- Does the management know the institution's structure and risks?
- Are adequate policies in place e.g. to avoid conflicts of interest, outsourcing?

**Corporate and risk culture**

- Has the institution a corporate and risk culture adequate for its business and risk appetite?
- Are there independent whistle-blowing processes?
- Is the culture clearly communicated across all levels?

**Organisation and functioning of the management body**

- Is the number of members of the management body adequate and do they demonstrate a sufficient level of commitment and independence?
- Is the management body effective?
- Adequacy of internal control procedures?

**Risk management framework, including ICAAP & ILAAP**

- Review an institution's ICAAP and ILAAP and determine their (1) soundness, (2) effectiveness and (3) comprehensiveness
- Review of stress testing programs and determine the appropriateness of, e.g. scenarios, assumptions and methodologies

**Internal control framework, including internal audit function**

- Do independent control functions and clear decision making processes exist?
- Are adequate risk reporting policies and compliance functions established, approved by the management body?

**Information systems and business continuity**

- Does accurate and reliable risk data exist (up-to-date, complete)?
- Can on-demand data requests be met?

**Remuneration policies and practices**

- Is the remuneration policy in line with the risk profile, corporate values and risk appetite?
- Ratio of variable and fixed remuneration is appropriate – are the provisions on the limitation of the variable component complied with?

**Recovery plan arrangements**

- Are adequate recovery plans available?

**In addition, the following aspects are assessed on the consolidated level:**

- Is the legal structure transparent?
- Does an institution-wide strategy and information system exist?
- Implementation of group policies on subsidiary level?

Scoring 1 – 4

#### 3. Assessment of risks to capital

**Measuring risk to capital**

| Credit and counterparty risk   | Market risk  | Operational risk   | Interest Rate Risk in the Banking Book (IRRBB)  |
|--|--|--|---|
| 1. Assessment of materiality of risk   | 2. Evaluation of the nature, composition and sub-categories of risk categories                                   | 3. Evaluation of the accuracy and prudence of methodologies  | 4. For credit and counterparty risk, e.g. assessment of the quality of the credit portfolio, the applied credit risk mitigation techniques, the level of loan loss provisions and CVA |
| 5. For market risk, e.g. evaluation of profitability and market concentration risk | 6. For operational risk, e.g. assessment of the significance of operational risk exposures and reputational risk | 7. For interest rate risk in the banking book, e.g. evaluation of scenario analysis and stress testing results |   |

**Assessment of risk management and controls**

| Policies and procedures  | Risk identification and measurement | Risk management, monitoring, reporting |
|--------------------------|-------------------------------------|--|
| Organisational framework | Internal control framework          | Respective risk strategy and appetite  |

**Assessing whether own funds suffice to cover risks to capital**

| Capital requirements  | Determining total SREP and overall capital requirements  | Additional considerations   |
|---|--|---|
| Overall capital requirements: CRD IV counter-cyclical buffer (0–2.5%), CRD IV conservation buffer (2.5%), Macro-prudential requirements (0–5%), Total SREP capital requirements (TSCR), CRD own funds requirements (8%), SREP additional own funds requirements | SREP own funds depend on the identified risks to capital while taking expected and unexpected losses over a one year horizon as well as model and governance deficiencies into account. SREP CRD IV and macro-prudential buffers have to be reconciled to avoid double counting. | Excessive leveraging is assessed by: Comparing the leverage ratio to peers, Evaluating its distance to the regulatory minimum, Considering stressed events. Analysis whether OCR and TSCR can be held stable over the economic cycle and stress scenarios |

Scoring 1 – 4

#### 4. Assessment of risks to liquidity and funding

**Risk to liquidity**

**Risk to funding**

Are liquidity buffers sufficient? Funding profile and plan. Is funding stable & market access assured?

- Identify the short and medium term liquidity needs by:**
  - Calculating the liquidity needs and availability over different time horizons
  - Assessing if the LCR is appropriate and reflects the liquidity needs adequately
- Evaluate whether the liquidity buffer and counterbalancing capacity are sufficient to meet the liquidity needs by assessing:**
  - Volume of assets to be liquidated
  - Quality and classification of liquid assets, using the LCR specifications
  - Capability to sell liquid assets swiftly
- Conduct independent liquidity stress tests to assess liquidity needs and buffers**

**1. Analyse the funding profile by evaluating:**

- Sufficiency of stable funding instruments
- Maturity mismatches
- Funding metrics, e.g. loan/deposit ratio and NSFR
- Concentration in funding sources
- The impact of an increased demand for unsecured debt due to asset encumbrance

**2. Assess the stability of the funding profile, e.g.:**

- Significance of certain asset classes
- Quality and classification of liquid assets, using the LCR specifications
- Capability to sell liquid assets swiftly

**3. Examine the current and future market access:**

- The volume of funding demands on certain markets or counterparties compared to the capacities of these institutions

**4. Compare the funding risk to the funding plan**

**Governance and risk management requirements**

| Appropriate framework to identify, measure, manage, monitor and report risks | Consistency between policies/procedures and the liquidity risk tolerance | Adequate implementation of liquidity stress tests |
|--|--|---|
| Integration into the overall risk strategy                                   | Effective internal limit and control system                              | Adequate liquidity contingency plan               |
|  |  | Sufficient technical and human resources          |

Scoring 1 – 4





# Regulatory and Risk training by Deloitte

## We can tailor our training to your needs

The inseparability of strategy, risk and regulation has elevated the role of a bank's risk function.

The CRO, risk team, BoD and risk committee need to be equipped with the right mix of risk and regulatory know-how to be able to influence and challenge decision making.

With risk management under the spotlight, investing in training and development is critical

With risk management under the spotlight, investing in risk people is critical to gaining a competitive advantage. Our training solutions may be the key to aligning your risk function in the most affordable manner.

We are offering a free session to discuss what we believe to be the key areas impacting the industry.

Be it the risk committee members or the CRO, we will tailor our discussion accordingly.

**Should you be interested in tailored training sessions, please do not hesitate to contact us for a consultation meeting.**

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# Regulatory and Risk training by Deloitte

## We can tailor our training to your needs

### Training catalogue

|  |  |
|--|--|
| Introduction to the new regulatory and supervisory environment | <ul style="list-style-type: none"><li>• Introduction to the Single Supervisory Mechanism (SSM), and an overview of their supervisory methodology (SREP);</li><li>• An overview of why regulators are expected to focus on converging the banks' business models with ICAAP and ILAAP processes.</li></ul>  |
| Capital requirements   | <ul style="list-style-type: none"><li>• Definition of Tier 1 and Tier 2 capital;</li><li>• Discussion on the effects of the quality and size of capital to loan and investment portfolios;</li><li>• Overview of how Forbearance and Non-Performing Loans impact capital requirements;</li><li>• Interpretation of Risk Weighted Assets.</li></ul>           |
| Liquidity requirements   | <ul style="list-style-type: none"><li>• Overview of the new CRR liquidity requirements;</li><li>• Explanation of the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR).</li></ul>   |
| Optimising risk exposure to maximise Return on Equity (ROE)    | <ul style="list-style-type: none"><li>• Overview of the options available for the Bank to increase its risk exposure;</li><li>• Discussion on de-risking and de-leveraging vs issuing new capital.</li></ul>   |
| ICAAP & ILAAP in the context of SREP                           | <ul style="list-style-type: none"><li>• Overview of the ICAAP and ILAAP as management tools;</li><li>• ICAAP and ILAAP stress testing;</li><li>• Liquidity monitoring and funding strategy.</li></ul>  |
| Recovery planning  | <ul style="list-style-type: none"><li>• Overview of recovery plans under the Bank Recovery and Resolution Directive (BRRD);</li><li>• Recommended approach for recovery plans, including scenario planning and recovery option development;</li><li>• Governance around recovery planning.</li></ul>   |
| Stress testing   | <ul style="list-style-type: none"><li>• Defining 2016 stress testing scope as per ECB requirements and EBA guidelines;</li><li>• Developing a stress testing plan and methodology.</li></ul>   |
| FATCA and CRS  | <ul style="list-style-type: none"><li>• Introduction and rationale to FATCA;</li><li>• Overview of entity classification and registration;</li><li>• Discussion on due diligence and reporting requirements;</li><li>• Introduction to CRS: wider exchange of information;</li><li>• Insight into the main features of CRS and its implementation.</li></ul> |
| Anti-Money Laundering (AML)                                    | <ul style="list-style-type: none"><li>• Introduction of the Bank's AML requirements, and potential reputational risk;</li><li>• Overview of the key principles of client acceptance;</li><li>• Discussion of the Bank's policy on initial and ongoing due diligence.</li></ul>   |

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