






Risk Management Association
“Internal Loss Events: Embedding Internal
Loss Data in an Organization’s DNA”






Agenda

- Overview and Context
- Background on Loss Data
- Defining the Objectives
- Objectives of Collecting Loss Data
- Aggregating Loss Data
- Loss Data Categories





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Agenda (cont.)

- Boundary Risks
- Process
- Loss Event Data Elements
- Uses of Internal Loss Data





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Overview and Context

- Internal Loss Data is an important Component of an Operational Risk Program
- In order to evolve your organization's internal loss data collection program from a mere exercise to a key management tool for your businesses, the loss data collections objective must be known and well understood, the process must be clear and simple, and the analysis must be intuitive and insightful





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Overview and Context (cont.)

- This Web Seminar will explore the key concepts and issues around internal loss data and its collection





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Background on Loss Data

- A financial loss is defined as a loss to the business due to inadequate internal processes, people or systems
- A sound operational risk management framework is essential to identifying risk exposure
- Internal loss data tracking is a critical component of the framework






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Background on Loss Data (cont.)



- Internal Loss data management does not relate only on a firm's ability to keep records of internal loss data but also to evaluate the types of losses by categories
- Aggregation of internal losses by specific categories is based on industry standards and firm specific taxonomy






Defining the Objective



- Collecting and analyzing Internal Loss Data provides essential information to minimize or avoid losses through the following:
 - Creating transparency in the organization by determining the “root causes” and developing corrective actions
 - Rewarding employees for early detection and reporting of losses and near misses – “Don’t shoot the Messenger”
 - Promoting a risk aware culture
 - Developing corporate intelligence






Defining the Objective (cont.)



- Communicating the importance of loss data collection and analysis
 - Including the importance of loss data in Senior Management discussions
 - Ensuring senior management communicates broadly and frequently






Objectives of Collecting Loss Data



- By capturing and sharing Loss Data information, organizations are better able to:
 - measure risk exposure,
 - create corrective action plans for current control deficiencies,
 - design internal control processes to minimize or avoid potential losses,
 - identify trends and potential emerging issues, and
 - satisfy regulatory requirements for loss data information utilized for Capital Modeling.







Objectives of Collecting Loss Data (cont.)

- Robust risk management relies on a sufficient level of volume and quality of data for better analysis, more effective decision making, reduced losses, and more precise Capital Modeling.









Aggregating Loss Data


- The categories of losses are defined across the Basel Categories such as:
 - internal and external fraud,
 - employment practices & workplace safety,
 - client products & business practices,
 - damage to physical assets,
 - business disruptions & system failures,
 - execution delivery & process management.







Aggregating Loss Data (cont.)

- Company specific Taxonomy includes the above categories modified across a firm's Process, Risk, and Control hierarchy by Business, Product, and Support Group
- Consistency with the Firm's RCSA, KRI, and Scenario Analysis is key


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Loss Data Categories


- Internal and External Fraud:
 - Internal Fraud (credit fraud, forgery, check kiting, intentional mis-marking of positions, unauthorized transactions, transactions not reported, embezzlement, forgery, insider trading, bribes, kickbacks), and
 - External Fraud (theft/robberies, forgery, systems hacking, theft of client and/or corporate information)


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Loss Data Categories (cont.)



- Employment Practices & Workplace Safety:
 - employment losses associated with Employee Relations (terminations, benefits, compensation),
 - Safe Environment (accident liabilities, workers compensation),
 - Diversity/Discrimination litigation



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Loss Data Categories (cont.)



- **Clients, Products, & Business Practices:**
 - Fiduciary (appropriateness and suitability violations, account churning, breach of privacy, disclosure violations, KYC),
 - Improper Business or Market Practices (insider trading, money laundering, unlicensed activities, antitrust), and
 - Advisory (disputes over performance, exceeding client limit)







Loss Data Categories (cont.)



- **Damage to Physical Assets:**
 - Natural Disaster Losses, Terrorism, Vandalism
- **Business Disruption and System Failures:**
 - losses arising from disruption of business or system failures including hardware, software, telecommunications, utility outages







Loss Data Categories (cont.)


- **Execution, Delivery, and Process Management:**
 - Data Entry,
 - Accounting Errors,
 - Model and Spreadsheet Errors,
 - Inaccurate Disclosures,
 - Documentation shortfalls (e.g., collateral, loan), and
 - Client Account Management (unauthorized access to accounts, inaccurate client records),
 - Vendors and Suppliers (outsourcing, vendor disputes)







Boundary Risks


- Defining the losses between risk categories is an important aspect to understanding risk exposure
- Credit losses, Underwriting losses, Market Risk losses, Financial losses, Liquidity losses, Operational losses, etc. are to be appropriately categorized






Boundary Risks (cont.)


- Determining the Causal effect by appropriate risk category will allow a more effective set of solutions
- Establishing the appropriate Boundary risk will allow better accountability across the Three Lines of Defense and more effective prioritization






Process



- Collection of internal loss events through:
 - Direct Data Input
 - System Interface or Download
 - Accounting Staff review of Financial results






Process (cont.)



- Sources of Data Loss Events:
 - Legal/Litigation
 - Compliance
 - Business Units
 - Service Centers (Technology, Operations, Human Resources, Call Centers, Accounting, etc.)
 - Product Groups
 - Risk Management
- Threshold amount to be set







Loss Event Data



| | |
|--|--|
| <ul style="list-style-type: none"> • Originating Area: Business entity, Product, Service Area Location (Geography) • Loss Event Description: Occurrence Date Submission Date Type of Event Event Description | <ul style="list-style-type: none"> • Financial Impact: Accounting reference number Currency Loss Amount Recovery amount Insurance coverage, if any |
|--|--|







Loss Event Data (cont.)



| | |
|---|---|
| <ul style="list-style-type: none"> • Control Categorization: Level I Control type Level II Control type | <ul style="list-style-type: none"> • Corrective Actions: Assigned to an Accountable Executive Link to business Function and Risk Control Deficiency Enhancement Corrective Action Completion Date Compensating Controls |
|---|---|







Uses of Internal Loss Data

- Assess effectiveness of internal controls
- Training, education and risk awareness
- Refine existing key risk indicators and developing new ones
- Produce management reports with valuable statistics that outline frequency and severity by category





Uses of Internal Loss Data (cont.)

- Inclusion into internal data models for capital calculation, scenario analysis, stress tests and business analysis
- Establish priorities

