



Key messages summary

These are informal notes from discussions held during the conference, reflecting the views of individuals invited to the Conference. They should not be taken as statements of policy from either the regulators, supervisors or members of ECIIA.

1. Technological transformation and new Banking Business Models: challenges and opportunities

- The events of the last decade have impacted the Financial System drastically.
- The new regulations significantly increased banks' capital requirements, while profit margins suffered.
- While Banks were dealing with the aftermaths of the crisis, the digital transformation kicked-in, the traditional business model changed, and customers behaviours changed. The banks are continuing to try to catch up, making huge investments in IT to ensure their on-going sustainability..
- We have observed a change in the Banks' DNA: shifting from real estate and HR investments to IT investments whilst maintaining the focus on cost reduction and process optimisation.
- New entrants also arrived: Fintech and Open Banking, which change the way financial services are structured and consumed. Consequently, we went from a closed organization to an interconnected "open" system and the banks became very fragile with new risks such as, cyber fraud, data management, reputation. Banks report a wide and growing range of cyber incidents, detected more often by third parties.
- But digitalization also creates opportunities: increasing use of algorithms, data analytics, artificial intelligence etc to improve core processes, particularly in the areas of financial crime and fraud detection.
- The controls functions are also impacted, they may need fewer people in the future and may be more concentrated on controls over systems and machines than performing detailed testing.
- The digital work must be part of the culture of the bank and impacts the relations between the different lines (especially 2nd and 3rd). But it also requires new skills and we must attract these people (data experts, data analysts, digital process experts...) that all sectors need!

- We must strengthen the partnership among Banks and Supervisors, enhance the supervision of 3rd party service providers to facilitate the interactions between the different lines and benefit from the digital revolution.

2. Latest developments on governance and outsourcing from EBA

The latest developments include:

- ✓ CRD V/CRR2 - update of the regulatory framework
 - ✓ Governance and remuneration
Review RTS identified staff, update of fit and proper requirements re independence and AML aspects, inclusion of holding companies
 - ✓ Waivers for the application of deferral and pay out in instruments
 - ✓ Fintech Roadmap (Cyber risks, ICT risks, Innovation hubs, Sandboxes)
 - ✓ IFD/IFR - Separate rulebook for investment firms
 - ✓ Sustainable finance (ESG factors)
Challenges ahead due to change of the whole economy impacting banking products and credit risks
Financial inclusion, diversity, human rights: products not discriminating against customers
- The EBA guideline on outsourcing will come into force on 30th September 2019. All institutions must have robust governance arrangements and manage their risks with all third parties.
 - The operation risks should be thoroughly assessed when assessing outsource risks
 - The register of all outsourcing arrangements is crucial for the Regulator but also for internal auditors
 - It is highly recommended to have a plan to exit the outsourcing partnership if needed. In this context, a strong Business continuity plan is important and must be tested
 - The internal auditors must provide coverage of the whole outsourcing process: pre-outsourcing phase, contractual phase, monitoring phase and exit phase.

3. Panel discussion with the on-site inspections (OSI) ECB and European CAEs

- The challenge over the last few years has been to set up a common and uniform on-site inspection function operating across the Eurozone. A new concept has been launched by the OSI group: harmonizing the OSI missions by carrying out the same mission on the same topics in different banks: 'the campaigns'. The current 'campaign' reviews cover credit risks: residential, commercial real estate, market risks, IT risks, business continuity and shortly cyber risks will come.
 - There is a common ground on purpose from ECB and the internal audit profession: helping organizations to run sustainable strategy with a reasonable risk appetite. Therefore, an open dialogue is crucial.
 - ECB teams look at strategy, governance, risks and they have useful benchmarks of the industry.
-

- The follow up of ECB recommendations is crucial and it is interesting to combine the exercise with the internal audit departments' findings and recommendations, external auditors' (EA) recommendations and define "lessons learned" for the risk assessment exercise. An improvement has been observed over the last years.
- There is a pressure on documentation, methodology: the formalisation is important for internal auditors.
- Only the most efficient banks (cost controls aspects), who properly manage their risks will survive.
- Credit risks have been a key subject for OSIs and will remain so. There are 2 types of missions for this subject: process analysis and assets quality reviews (credit file reviews). IA should also continue to focus on Credit risk, including credit file reviews.
- A dedicated IT tool (to facilitate more efficient credit file reviews) is under development at the ECB and the objective will be to standardise the data requirements requested within the 'loan tapes' and in doing so this should give time for the Banks to prepare documentation on the different loan types.
- The interactions between IA and EA should be reinforced and IA should be more involved in the risk assessment process.
- When preparing an OSI mission, the reports of the IA are reviewed as well as any relevant information. Interviews are conducted with IA from the beginning or when an observation must be discussed. The Compliance Officer is also usually involved from the beginning.
- Regarding the reliance of OSI on IA work, the recommendation towards IA is to ensure that all relevant work is highlighted to the OSI in the planning phase of the inspection (this will usually be part of the standard information request anyway). The OSIs testing maybe reduced if IA is reliable.
- Regarding the timing of OSI missions, the signature of the final report takes 8 to 16 weeks and no longer than 6 months and the follow up of the recommendation letter is issued within 2 months (as such no inspection should take more than 8 months end to end)

4. Panel discussion with JST, ECB and European CAEs

- The JST's independent assessment includes different dimensions: report of OSI, other inputs for independent assessments.
- There have been many opportunities to interact with IA and so far, the exchanges are of a good quality despite the methodology differences (no one size fits all solution).
- The JST try to understand why IA did not find the weakness they found. The various explanations are: the possibility to improve, the challenges, the issues of resources (cost cutting), the quantity and quality issues, good analytical tools
- The efforts must be coordinated, starting with the IA planning and the JST annual program. The top down and bottom up approaches for risk assessments are recommended.
- We must continue the good and open dialogue both ways and better understand the risk profile, the quality of the control environment and the impact of the changes in the financial landscape. As the size of banks varies, a tailor-made solution is required.
- The effectiveness of the Bank's IA function is considered within the Governance Pillar of the SREP.
- There is a need for a close collaboration, openness between the 2^d, 3rd lines and the Supervisor. IA must be proactive to build up the dialogue.
- A key question is how to best allocate the resources in the future? IA must address the "old risks" in different ways (data analytics...) while addressing the new ones (cloud services, cyber...). The

access to the data is becoming difficult (confidentiality clauses). There is “big elephant in the room”: IA must get ready!

- Regarding sustainability, IA must support the Management Board with a review of the risk (compliance, reputation, operational....) and the assessment of the other lines.
- There is a need for new competences and Banks and Supervisors need a similar profile!
- The expectations for IA in banks: demonstrate sufficient organisation independence, give a strong outcome to the Board, have the adequate resources (skills, competencies) to assess new risk with new tools, have an effective QAS internally and externally, prepare a multiyear audit cycle plan with comprehensive risk map and solid risk process, have an IA sufficiently empowered and that effectively follows up on all findings.
- The alignment of objectives between IA and the Supervisor is key. Both have common objectives to improve the Bank’s internal processes, the internal controls and ensure a risk-based approach!
- For the risk mapping, a top down and bottom up approaches seem ideal to avoid overlapping and ensure completeness of the Bank business and value chain.
- It is important for IA to attend the various meetings with JST (entry, exit, workshop...)
- Brainstorming, open forum, not formalised exchanges must be promoted between IA and the Supervisor to discuss new topics, set up a sounding board and get interesting input.
- In terms of ICAP, the coverage of IA can improve (sequential guidelines over the years and big efforts for banks to comply with the different approaches): expectations communicated long in advance but not in the radar of IA function in many banks!

5. Breakout sessions (results in appendix 1)

6. Conclusions

The key messages of the day are:

IA must balance resources between regulatory requirements and business requirements

There is a need for more discussion, more direct discussion on interactions with the Regulators: more constructive, more inclusive

To go with the exchanges, a group has been started on LinkedIn: [ECIIA Banking Committee](#).