GUIDELINES ON THE USE OF THE STANDARDIZED APPROACH IN COMPUTING THE CAPITAL CHARGE FOR OPERATIONAL RISKS

(Appendix to Sec. 125)

Banks applying for the use of The Standardized Approach (TSA) must satisfy the following requirements/criteria:

General Criteria

1. The use of TSA shall be conditional upon the explicit prior approval of the Bangko Sentral.

2. The Bangko Sentral will only give approval to an applicant bank if at a minimum:

    a. Its board of directors (or equivalent management committee in the case of foreign bank branches) and senior management are actively involved in the oversight of the operational risk management framework;
    b. It has an operational risk management system that is conceptually sound and is implemented with integrity; and,
    c. It has sufficient resources in the use of the approach in the major business lines as well as in the control and audit areas.

3. The above criteria should be supported by a written documentation of the board-approved operational risk management framework of the bank which should cover the following:

    a. Overall objectives and policies
    b. Strategies and processes
    c. Operational risk management structure and organization
    d. Scope and nature of risk reporting/assessment systems
    e. Policies and procedure for mitigating operational risk

4. This operational risk management framework of the bank should be disclosed in its annual report, as provided under *Appendix 59.*

Mapping of Gross Income

5. Banks using TSA in computing operational risk capital charge must develop specific written policies and criteria for mapping gross income of their current business lines into the standard business lines prescribed under *Appendix 59*. They must also put in place a review process to adjust these policies and criteria for new or changing business activities or products as

appropriate.

6. Banks must adopt the following principles for mapping their business activities to the appropriate business lines:

(a) Activities or products must be mapped into only one (1) of the eight (8) standard business lines, as follows:

1. *Corporate finance*– This includes banking arrangements and facilities [e.g., mergers and acquisitions, underwriting, privatizations, securitization, research, debt (government, high yield), equity, syndications, Initial Public Offering (IPO), secondary private placements] provided to large commercial enterprises, multinational companies, NBFIs, government departments, etc.

2. *Trading and sales*– This includes treasury operations, buying and selling of securities, currencies and others for proprietary and client account.

3. *Retail banking*– This includes financing arrangements for private individuals, retail clients and small businesses such as personal loans, credit cards, auto loans, etc. as well as other facilities such as trust and estates and investment advice.

4. *Commercial banking*– This includes financing arrangements for commercial enterprises, including project finance, real estate, export finance, trade finance, factoring, leasing, guarantees, bills of exchange, etc.

5. *Payment and settlement*– This includes activities relating to payments and collections, inter-bank funds transfer, clearing and settlement.

6. *Agency services*– This refers to activities of the banks acting as issuing and paying agents for corporate clients, providing custodial services, etc.

7. *Asset management*– This includes managing funds of clients on a pooled, segregated, retail, institutional, open or closed basis under a mandate.

8. *Retail brokerage*– This includes brokering services provided to customers that are retail investors rather than institutional investors.

(a) Any activity or product which cannot be readily mapped into one (1) of the standardized business lines but which is ancillary[1] to a business line shall be allocated to the business line to which it is ancillary. If the activity is ancillary to two (2) or more business lines, an objective criteria or qualification must be made to allocate the annual gross income derived from that activity to the relevant business lines.

(b) Any activity that cannot be mapped into a particular business line and is not an ancillary activity to a business line shall be mapped into one (1) of the business lines with the highest associated beta factor eighteen percent (18%). Any ancillary activity to that activity will follow the same business line treatment.

(c) Banks may use internal pricing methods to allocate gross income between business lines: *Provided*, That the sum of gross income for the eight (8) business lines must still be equal to the gross income as would be recorded if the bank uses the Basic Indicator Approach (BIA).

(d) The process by which banks map their business activities into the standardized business lines must be regularly reviewed by party independent from that process.

7. In computing the gross income of the bank, the amounts of the income accounts reported in the operational risk template[2] must be equal to the year-end balance reported in the FRP. Any discrepancy must be properly accounted and supported by a reconciliation statement.

Application Process for the Use of TSA

8. Banks applying for the use of TSA should submit the following documents to their respective Central Points of Contact (CPCs) of the Bangko Sentral:

(a) An application letter signed by the president/CEO (or equivalent management committee in the case of foreign bank branches) of the bank signifying its intention to use TSA in computing the capital charge for operational risk;

(b) Written documentation of the Board- approved operational risk management framework as described in paragraph 3.

(c) Written policies and criteria for mapping business activities and their corresponding gross income into the standard business lines as described in paragraphs 5 to 7.

(d) An overall roll-out plan of the bank including project plans and execution processes, with the appropriate time lines.

Initial Monitoring Period

9. The Bangko Sentral may require a six (6)-month period of initial monitoring of a bank's TSA before it is used for supervisory capital purposes.

Reversion from TSA to BIA

10. A bank which has been approved to use TSA in computing its capital charge for operational risk will not be allowed to revert to the simpler approach, i.e., the BIA. However, if the Bangko Sentral determines that the bank no longer meets the qualifying criteria for TSA, it may require the bank to revert to BIA. The bank shall be required to repeat the whole application process should it opt to return to the use of TSA, but only after a year of using the BIA.

These guidelines shall take effect on 21 July 2007.

(Circular No. 890 dated 02 November 2015)

Footnotes

1. Ancillary function is an activity/function that is not the main activity of a given business line but only as support activity
2. Part V of the revised CAR report template