Business & Computing Examinations (BCE)
LONDON (UK)

BCE Capital Adequacy Plan

BCE Capital Adequacy Plan requires the following checks:
- minimum capital requirements;
- the extent of total shareholder funds required to meet BCE's strategy and maintain minimum capital requirements;
- ensuring that material risks of the organisation are understood by its board, and that there is sufficient and appropriate risk management.

Four crucial elements in Capital Adequacy Plan are:
- identification and measurement of the risks the organisation is, or may be, exposed to;
- application of mitigation techniques that may help to lower capital requirements;
- stress-testing techniques;
- role of the board and CEO.

BCE ensures that risks are presented to, and discussed by, the board to ensure its acceptance and understanding. BCE must also consider any other internal risks that the organisation may face which may result in losses such as fraud, examination leakage, candidate impersonation, Centre malpractices or strategy failure.

The preparation of a capital plan incorporate all risks, and requires the cooperation of, and collaboration with, all functional units. BCE Capital Adequacy Plan is customised taking into account the particular risks and information available. **The process consists of the following stages:**
- **Identifying risks** - List all material risks, interview personnel and assess the probability of risks occurring.
- **Assessing capital** - How much capital would a risk require?
- **Forward capital planning** - Assess how the capital calculated from the capital assessment might be altered by its business plan, i.e. perform stress and scenario analyses.
- **Conclusion** - What are the ranges of capital identified, and how much internal capital should a firm hold?

Line Managers also consider the following risks:
- **credit risk** - probability of loss from a debtor's default. Risk of loss arising from a borrower who does not make payments as promised.
- **market risk** - The value of investments may decline over a given time period simply because of economic changes or other events that impact large portions of the market.
- **operational risk** - loss occurring from the internal inadequacies of a firm or a breakdown in its controls, operations, or procedures.
- **liquidity risk** - loss arising from a situation where there will not be enough cash and/or cash equivalents to meet the needs of the business
- **concentration risk** - loss arising from a large position in a single ASSET or market exposure.

- **residual risk** - A risk that remains after all efforts have been made to mitigate or eliminate risks associated with a business process or investment.
- **business risk** - the probability of loss inherent in an organization's operations and environment (such as competition and adverse economic conditions)
- **interest rate risk** - probability that the market interest rates will rise significantly higher than the interest rate earned on investments
- any other risks identified.

BCE Statement of Attitude to Risk
An underlying cause of the recent financial crisis was a severe failure in risk assessment – by financial institutions, regulators and investors. Major risks were underestimated or ignored, and so they were managed either badly or not at all.

This has led to growing demands since the crisis for better risk reporting in the hope that it will encourage improvements in both risk assessment and risk management, and so make future crises less likely. Such demands have not been aimed only at the financial sector, but have extended to organisations in all sectors.

- *Tell stakeholder bodies what they need to know* - Users of corporate reporting want information about the organisation's risks so that they can make their own assessment of risk.
- *Focus on quantitative information* - more information on the breakdown of activities, geographically and by sector, and on their assets, liabilities and commitments.
- *As far as possible, integrate information on risk with other disclosures* - risk is forward-looking and cannot be fully understood except in the context of broader forward-looking information about the organisation's performance, plans and prospects.
- *Think beyond the annual reporting cycle* - many risks stay the same from one year to the next.
- *Highlight current concerns* – ensure what is being currently discussed is objectively verifiable
- *Review risk experience* - What went wrong? What lessons have been learnt? How do their experiences match up with the risks that they had previously reported?

Business Strategy
Corporate strategies are essentially about what the business wants to achieve. Business strategy is about how those corporate objectives are to be achieved.

Business strategy is concerned with deciding which markets and activities the business should be involved in; where it wants to be; and how it is going to get there. Strategy is about making high-level decisions and forms the management game plan for:

- Satisfying customers (meeting customer needs)
- Running the business (organising resources in the most efficient and effective way)
- Beating the competition (strategies and tactics to gain competitive advantage)
- Achieving corporate objectives

Risk Assessment
The process of determining the likelihood that a specified negative event will occur. CEO and line managers use risk assessments to determine things like whether to undertake a particular

venture, what rate of return they require to make a particular investment and how to mitigate an activity's potential losses.

Examples of formal risk assessment techniques and measurements include:

- reducing the likelihood of incurring large losses;
- evaluating the risks from certain Centres
- analysing potential Centres' financial data
- analysing state of certain countries (internal conflicts/political stability, attitude to foreign organisations, relationship with European countries)

Capital Planning
The process of budgeting resources for the future of an organisation's long term plans. Capital planning for a business would include budgeting for new and replacement machinery, research and development and the production of new products, new plants and other major capital expenditures.

A plan for the organisation's capital expenditures. Capital expenditures are payments made over a period of more than one year. They are used to acquire assets or improve the useful life of existing assets; an example of a capital expenditure is the funding to renovate offices. Making a capital budget must account for the potential profitability of the plans involved. Calculating the net present value or the internal rate of return are two methods for determining a capital budget.

Stress and Scenario Testing
A simulation technique used on asset and liability portfolios to determine their reactions to different financial situations. Stress tests are also used to gauge how certain stressors will affect a company or industry.

Stress testing is an important risk management tool that is used as part of internal risk management and capital adequacy framework. Stress testing alerts management to adverse unexpected outcomes related to a variety of risks and provides an indication of how much capital might be needed to absorb losses should large shocks occur. Moreover, stress testing is a tool that supplements other risk management approaches and measures. It plays a particularly important role in:

- providing forward-looking assessments of risk;
- overcoming limitations of models and historical data;
- supporting internal and external communication;
- feeding into capital and liquidity planning procedures;
- informing the setting of the organisation's risk tolerance; and
- facilitating the development of risk mitigation or contingency plans across a range of stressed conditions.

A stress test is also used to evaluate the strength of an organisation. For example, BCE could run stress tests on qualifications to determine their currency condition, reliability and changing factors including, industry requirements or progression routes.