


Financial institutions use quantitative models to translate the complex world around us into information that suits their daily business requirements. If a model reflects reality incorrectly, this can have major financial consequences. The Model Validation department evaluates the risk models that are used within the ING Group. For quite some time now, Zanders has been supplying the department with consultants that have a fresh take on models.

A fresh take on risk models

The Model Validation department hasn't been around for that long. In response to the Basel II Accord, financial institutions recently committed themselves to taking additional steps in the area of risk management. The quantification of risks on the basis of internal models can be seen as a core issue in this context. One of the findings of research in this area was that the strict separation of the development and evaluation of models was insufficiently safeguarded within ING. In order to achieve a more explicit separation of these two activities, the Group established the Model Validation department.

The department, which started its work in the first quarter of 2006, currently employs over 17 FTEs. "We resort directly under

"We have a broad scope," Hemerijck continues. "We focus both on models dealing with market risks, credit risks and operational risks of our banking activities and on risk models for our insurance department. We make an independent evaluation of each of these models - and there are definitely more than a hundred. This means that there is a tremendous amount of work to be done. Originally, our primary focus within the context of the Basel II Accord was on the Pillar 1 (credit risk and operational risk) and Pillar 2 (economic capital) models for our banking activities. We are now also shifting our focus in the direction of our insurance division, in response to the new external requirements introduced in connection with the disclosure of risk figures in the annual report as well as Solvency II."



the Chief Risk Officer, who is a member of ING Group's Board of Directors," explains Monique Hemerijck, who heads the department. "To my knowledge, this is a unique situation within the world of banking. It's a clear message where our priorities are. In my opinion, it communicates very clearly the importance we attach to independent model validation within the Group."

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Checks and balances

It's not an afternoon's work to finish the validation of one of these models. The complex models go through a fixed evaluation procedure with numerous checks and balances. Once Hemerijck and her colleagues issue their stamp of approval, the model can be considered reliable, compliant with internal and external regulations and ready for use. In addition, it has become clear what the model's weaknesses are.

Each year, the models are subjected to a review. "We definitely don't serve as a kind of examining board," states Hemerijck. "We primarily check whether the model has gone through a structural development process. Have all the different stages been concluded? Did the developers choose the right methodology? Is it based on sound assumptions? And how does the model perform over time?" Furthermore, Hemerijck's people definitely don't live in an ivory tower. "On the contrary. There's always room for dialogue. We carry out desk research, but also talk with various stakeholders - like the people who have to use a model on a daily basis. This is very useful. Because, if it turns out that the users don't trust the results of a model, or if they don't know how to interpret the results, this is a sign that the model is perhaps not yet working optimally."

The findings of the department are summed up in a handy report that also includes recommendations and improvement sugges-



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tions. Hemerijck: “This is how we try to encourage the ongoing improvement of the models used by ING. Our department’s assessments are binding up to the level of the Chief Risk Officer, who ultimately makes the decision. This means that people tend to listen to us. Generally speaking, developers recognise the added value of a separate validation department - a department that they can spar with and that speaks their language.”

Model expertise is scarce

Solid, experienced experts are thin on the ground. Hemerijck has noticed this too. “It’s very difficult to get the right expertise on board. Expertise that is not just based on theoretical knowledge, but also incorporates knowledge of the business. I find this combination very important.” Zanders has been providing people for the Model Validation department since it was first set up in 2006. The first two Zanders consultants have since been replaced by two other consultants, including Yvonne Sijm. Yvonne is part of Hemerijck’s team on behalf of Zanders for just over two days a week. “The nice thing about Yvonne - and this applies to all colleagues from Zanders - is that she simply works along with us in our day-to-day job. As a result, she feels more like a member of the team than an external consultant. In addition, Zanders offers a broad range of expertise in the area of risk models.”

touch the heart of a bank’s business. Every time round, it’s interesting to set to work on a model for the first time and find out how it works and what it does. And to determine how an abstract, theoretical model will work out in daily practice. It never becomes boring, because each model is different: basically, they’re all little projects in themselves.”

Sijm is getting an increasingly clear picture of the connections between the individual models. “A lot of models are closely connected or make use of each other. There are a lot of interfaces. We use our position to try and find a connecting theme. This way, we hope to bring models closer together.” Sijm spends a relatively large amount of time on her initial scrutiny of a model. When the models land back on her desk a year later for the annual review, the assessment takes considerably less time. “That’s a very nice part of the job,” says Sijm. “Because after a year, you can see quite clearly what kind of effect our recommendations have had.”

For the moment, Hemerijck’s reason for employing the services of external consultants is that it is difficult to find the required expertise. “Nevertheless, I expect to continue engaging external people on a regular basis,” she says. “If only because this prevents a kind of tunnel vision developing within the department. People from outside often have a fresh take on things.” <

▲ Zanders consultant Yvonne Sijm and Monique Hemerijck, head of the Model Validation department at ING Group.

“It’s a nice challenge,” remarks Yvonne Sijm. “Models really