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Treasury Management in Modern Challenger Banks: Designing a Regulatory-Compliant Operating Model

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Neophytos Kathitziotis
Doctoral Research Student, University of Hamburg

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Neophytos Kathitziotis

The Fintech landscape has evolved significantly over the past decade, initially characterized by technology-driven startups, but gradually extending into the banking sector. This expansion has given rise to the establishment of several financial institutions with a banking licence (World Bank 2022). However, building a bank from the ground up requires navigating a complex and often unfamiliar environment that demands a broad spectrum of skillsets. Unlike traditional banking literature, which predominantly addresses established institutions, there is a notable gap when it comes to guidance for new entrants—especially in the critical area of Treasury management.

Practitioners in newly established banks seeking insights often rely on informal networks, conferences, and personal experience rather than comprehensive literature or in-house experience as the entity lacks headcount and breadth initially. This paper aims to address this gap by focusing on key challenges in the Treasury function specific to newly established banking institutions. While not an exhaustive resource, it highlights common pain points identified by regulators—either through fines or private feedback—as well as challenges raised by industry peers.

This paper focuses on a key consideration during the licencing phase in setting up a regulatory approved Treasury operating model with a comparison of regulatory requirements across three jurisdictions (UK, EU, UAE).

Banking and banking-like institutions

Because the scope of banking and banking-like institutions established in the last decade is very broad we classify these into four categories (Singapore Fintech Association & BCG, 2020).

1. **Payment Institutions**: These are non-bank entities licensed under the Electronic Money Institution (EMI) regime that facilitate digital payments without requiring a full banking license. They focus on secure, efficient transactions, such as digital wallets and e-money, often offering services as for example peer-to-peer payments and remittances. (e.g. Monese, Qonto, Mangopay)
2. **Neo-Banks**: These entities operate without a traditional banking license, relying on partnerships or agency models to provide financial services. While they don't take deposits directly, neo-banks provide payment, lending, and budgeting tools (e.g., Stripe, Tide, pre-banking licence Revolut).
3. **Challenger Banks**: Challenger banks hold full banking licenses, and offer a comprehensive suite of banking services similar to traditional banks, including savings accounts and loans. These banks leverage technology to enhance user experience and lower costs and provide a digital-only experience often within a specific target customer segment (e.g., Griffin Bank, Allica Bank, Monzo)
4. **Branches or Subsidiaries:** Traditional banks often expand through branches or subsidiaries in new markets, a strategy that has become especially prominent post-Brexit in the EU as well as in growth regions as the Gulf-states (e.g., Standard Chartered, Nomura)

This paper focuses on Challenger Banks (iii) and newly established branches or subsidiaries of traditional banks (iv), as their possession of a banking license significantly impacts Treasury's objectives. Unlike Neo-banks and Payment Institutions, which prioritize product development and client growth, fully licensed entities must balance these goals with the demands of regulatory compliance, risk management, and governance.

While our focus is primarily on the UK, Europe and the UAE, many of the best practices discussed are applicable in other regions where we have witnessed growth of these business models, for instance Singapore.

The Target Operating Model during the Licencing Phase

The journey of establishing a new bank begins with the critical licensing phase, where a detailed business plan takes shape. This plan lays out the institution's financial viability and establishes the essential links between departments that will drive smooth operations. At the heart of this phase is the Target Operating Model for each department, setting a clear framework for how each area will function. For Treasury, the operating model defines the organisational structure, assigns roles and responsibilities, and maps out the bank's approach to financial resource management and risk control. Encompassing key domains—including governance, procedural workflows, technology frameworks, and reporting structures, it answers the fundamental questions of 'what' and 'how' in treasury management.

Organisational Structure – The strategic view

The Target Operating Model is designed to ensure clear accountability for risk, positioning Treasury operations within the broader risk management framework. A natural connection exists between the Target Operating Model and the Bank's Risk Directory. This directory provides a structured inventory of identifiable risks across the institution, covering key risk drivers and metrics and enables a comprehensive view of the bank's risk landscape. Treasury is tasked with oversight of several critical "Level 1" risks—high-priority exposures with significant implications for capital adequacy, liquidity, and profitability. Given their potential to impact financial stability and regulatory compliance, these risks require rigorous control measures. It is therefore essential that the structure and activities outlined in the Target Operating Model closely correspond to the risks documented in the Bank's Risk Directory, ensuring that Treasury's operational design aligns with its risk control priorities.

For challenger banks in their early stages, Treasury typically manages two "Level 1" risks: Capital Risk and Liquidity Risk:

- **Capital Risk**: Treasury oversees capital adequacy by maintaining required capital buffers and coordinating capital planning to meet regulatory standards. This includes capital forecasting to ensure ongoing compliance with capital adequacy ratios.
- **Liquidity Risk**: Treasury plays a central role in liquidity risk management, overseeing the bank's liquid assets to meet the regulatory liquidity coverage ratio (LCR) and net stable funding (NSFR) requirements. This responsibility includes monitoring daily cash flows, arranging contingency funding sources, and managing short-term liquidity requirements.

As the bank's operations expand, Treasury may also take on Interest Rate Risk management, reflecting the institution's increasing complexity and exposure to duration. However, during the initial stages—when cash products are the primary focus—interest rate risk is generally

managed within a defined risk appetite or through balance sheet hedging, rather than an a separate Treasury function. Consequently, the initial Treasury structure is likely to prioritize liquidity and capital management, with interest rate risk management potentially integrated within 12 to 18 months of operations as the bank's exposure increases.

Ultimately, Treasury will come to manage three of the six or seven Level 1 risks that Challenger banks commonly face, the others being Financial Crime, Cybersecurity, Operational, and potentially Credit Risk. This underscores Treasury's central role in managing the bank's financial resources, positioning it as a foundational component of the institution's risk management framework.

Organisational Structure – Tactical implementation

A key operational consideration in defining the Treasury organisational structure is the segregation of responsibilities between the market-facing (front-office) and non-market-facing (back-office) Treasury functions. Regulators mandate that Treasury functions with risk exposure—such as liquidity management—remain separate from oversight activities to prevent conflicts of interest. As Choudhry et al. (2018) outline, effective Treasury management relies on the separation of profit-centre and control activities. For instance, the Supervisory Statement SS24/15 (PRA, 2018) outlines supervisory expectations for the segregation of Treasury activities where front-office Treasury responsibilities must remain distinct from back-office and non-market-facing roles. In the German-speaking framework, Enthofer and Haas (Treasurer Handbook, 2020) advocate for a distinct division between "market-facing" and "non-market-facing" Treasury activities, a structure that resonates with European regulatory standards for segregating execution and oversight functions. Both approaches emphasize the need for clear functional boundaries within Treasury to meet both operational and regulatory requirements.

For smaller or newly established entities, a phased approach to implementing Treasury activities can bring clarity in execution while maintaining regulatory compliance. By initially adopting a nimble structure, a Treasury department can progressively add complexity in response to business growth, thereby optimizing resource allocation. Therefore we propose a Treasury function typically divided into two main categories:

1. **Market-Facing Activities** – These are managed by the Front Office Treasury and include cash & position management (receiving, transferring, and optimizing cash flow and liquidity), and foreign exchange (FX) management.
2. **Non-Market-Facing Functions** – Managed by Asset and Liability Management (ALM) or Balance Sheet Management, these activities encompass capital management, liquidity planning, interest rate risk management, and governance (incl. policy) and reporting.

Table 1: Breakdown of key Treasury pillars between market facing and non-market facing sub-teams in Treasury

Treasury Function	**Activity**	**Description**	**Responsible Team**
Market-Facing	Cash & Position Management	Receiving, transferring, and managing excess cash and overall bank liquidity position. Executing funding transactions.	Front Office Treasury

	FX Management	Managing foreign exchange exposures and transactions	Front Office Treasury
Non-Market-Facing	Capital Management	Monitoring and maintaining adequate capital levels	ALM / Balance Sheet Management
	Liquidity Planning & Forecasting	Ensure adequate liquidity & funding planning and metrics controlling	ALM / Balance Sheet Management
	Interest Rate Risk Management	Managing structural interest rate exposures & instructing FO treasury for hedging	ALM / Balance Sheet Management
	Governance and Reporting	Ensuring policy compliance and internal / ALCO reporting	ALM / Balance Sheet Management

Operationalizing the Treasury Operating Model: A Comparative Analysis of Regulatory Requirements in the UK, EU, and UAE

Once a high-level Treasury operating model is established, a regulatory assessment is crucial to clearly define roles and responsibilities both a) within Treasury and b) between Treasury and the Second Line of Defense (SLOD). This ensures that these roles align with regulatory expectations. We analyze five key compliance themes commonly applicable across regulatory jurisdictions, detailed in table 2. Appendix 1 provides implementation examples for each theme to help Treasury managers visualize practical applications of these requirements.

1. **Segregation of Duties and Independence**: Regulators mandate that Treasury functions with risk exposure—such as liquidity management—remain separate from oversight activities to prevent conflicts of interest. This promotes operational independence between risk-taking functions (e.g., front-office Treasury) and control functions (Second Line of Defence / Risk Management).
2. **Governance Framework**: A robust governance framework aligned with the firm's risk management strategy is essential. Regulators expect senior management oversight, with Treasury operations subject to review and control by independent risk and compliance teams (Comprehensive Management Information suite and ALCO Terms of Reference)
3. **Independent Risk Assessment and Reporting**: Treasury activities related to liquidity and funding must operate within defined risk limits, monitored independently. Reporting lines must be clear to prevent Treasury from influencing its own risk assessments, with liquidity and funding reports directed to independent bodies such as the Asset and Liability Committee (ALCO) or the Management Board.
4. **Oversight of Front-Office and Treasury Operations**: Effective regulatory compliance necessitates controls that monitor and limit exposures created by front-office activities, including cash and funding management. Treasury operations need to ensure alignment with the firm's risk appetite and remain accountable within a controlled risk framework. (Risk Appetite Statements with triggers defined for Level 1 and Level 2 risks)
5. **Tailoring for Proportionality**: Many regulatory frameworks account for proportionality, adjusting risk management requirements based on the firm's size, complexity, and risk profile. This flexibility allows smaller firms to maintain essential segregation of duties and independence within a streamlined structure, meeting regulatory expectations without imposing undue complexity. (Make use of 'Small and non-complex institution' rules).

Conclusion

In this paper, we have emphasized the importance of regulatory requirements in shaping a robust Target Operating Model (TOM) for treasury management. This regulatory-centric approach is critical for several reasons. First, during the bank's licensing phase, regulators dedicate significant attention to assessing whether the proposed governance framework and compliance measures align with legal mandates. At this stage, the focus is more on strict regulatory adherence than on operational flexibility, ensuring that the bank meets the formal standards required for licencing approval.

Additionally, within the bank, key internal functions such as the Second Line of Defence (SLOD) and Audit play crucial roles in validating that the treasury setup is not only compliant but also well-structured to address future regulatory scrutiny. This ensures that the model is both practical and defensible from a regulatory perspective.

In Part II of our series, we will shift focus to the operationalization of the treasury function post-launch. Here, we will address the essential activities required for managing liquidity, cash flow, and positioning as the bank enters its initial stages of live operations. This transition from regulatory design to real-time treasury management will underscore how a strong compliance foundation will support the development of an agile treasury function.

Table 2: Compliance Considerations for Treasury organisation across Jurisdictions

Guidance Area	**High-Level Interpretation**	**Organisational Structure (Teams)**	**Governance/Reporting Lines (C-Level Roles)**	**UK Regulations (PRA)**	**MaRisk (Germany) and EU Regulations (including EBA)**	**UAE Regulations**
Segregation of Duties and Independence	Risk control and monitoring of liquidity must be independent from the front-office team that executes or manages liquidity.	Cash Management (Front Office Treasury); Liquidity Risk Control (Risk Management)	Front Office Treasury reports to CFO; Risk Management reports to CRO	**PRA SS24/15, Paragraph 3.1**: Requires separation between liquidity management and risk control activities	**MaRisk AT 4.3.2**: Segregation in Risk Management **CRR Art. 74**: Internal control framework for risk management **EBA Guidelines on Internal Governance (GL44)**: Emphasizes segregation of duties in risk management	CBUAE Circular No. 33/2015, Articles 22 and 23: Independent liquidity risk management
Governance Framework	Establish a governance framework with oversight committees, such as ALCO, to regularly review and approve liquidity management practices.	Asset and Liability Committee (ALCO) with representation from Treasury, Risk, and Finance	ALCO reports findings and escalations to CRO and CFO, with periodic updates to the CEO	**PRA SS24/15, Paragraph 3.4**: Specifies ALCO and C-level governance in Treasury's liquidity management	**MaRisk AT 5**: Governance Structure for Risk Control **CRR Art. 76**: Governance arrangements **EBA Guidelines on Internal Governance (GL44)**: Governance requirements for ALCO oversight and C-level involvement	Federal Law No. 14 of 2018 (Banking Law), Chapter 3: Governance in risk management
Independent Risk Assessment and Reporting	Risk management should independently set and monitor liquidity risk limits, ensuring Treasury reports its liquidity exposures without influence.	Liquidity Risk Control (Risk Management); Treasury Operations (for reporting)	Risk Control function reports to CRO; Treasury Operations reports daily liquidity data to CFO	**PRA SS24/15, Paragraph 4.2**: Mandates independent limit-setting and monitoring of liquidity risk exposures	**MaRisk AT 4.3.3**: Independent Monitoring & Reporting **CRR Art. 98**: Liquidity risk management **EBA Guidelines on Liquidity and Funding Risk Management (GL31)**: Requires clear independent reporting lines and limits in liquidity risk	CBUAE Liquidity Risk Regulations 2019, Section 7: Independent monitoring of liquidity risk
Oversight of Front-Office and Treasury Operations	Implement controls to ensure front-office Treasury activities align with the firm's risk management framework and oversight standards.	Front Office Treasury; Internal Audit (for periodic oversight); Risk & Controls assessment (SLOD)	Treasury oversight from CFO; Internal Audit reports directly to Board Audit Committee	**PRA SS24/15, Paragraph 4.5**: Requires oversight controls for front-office Treasury activities	**MaRisk AT 4.4**: Front-Office Oversight Controls **CRR Art. 85**: Measures on liquidity and leverage **EBA Guidelines on Internal Governance (GL44)**: Front-office control and oversight within liquidity risk management (SLOD)	Central Bank of UAE Standards, Art. 19: Oversight and control of front-office activities
Tailoring for Proportionality	Smaller or simpler firms may adopt streamlined structures, as long as key Treasury functions maintain independent reporting and control.	Small Treasury Team (single role managing liquidity, reporting to CFO); Independent Compliance oversight in SLOD	Treasury reports to CEO or CFO. Controlling remains in CRO	**PRA SS24/15, Paragraph 1.2**: Proportional requirements based on firm size and risk profile	**MaRisk AT 3**: Proportionality Principle **CRR Art. 108**: Application of proportionality in risk management frameworks **EBA Guidelines on Proportionality**: Proportional application of governance requirements based on firm size and complexity	CBUAE Liquidity Risk Guidelines 2019, Section 3: Proportionality in governance

About the Author

Neo Kathitziotis is a PhD student at the University of Hamburg. He has 15 years of experience in Treasury and Risk at European banking institutions, including at NatWest Bank's European subsidiary.

Appendix: Operationalizing regulatory considerations for a Newly Established Bank's Treasury Organisation

1. Segregation of Duties and Independence

Example: In a newly established bank, the Treasury team responsible for liquidity management (e.g., managing cash flows and funding) should be operationally separate from the team handling risk control. For instance, the front-office Treasury function managing cash positions would be structurally separated from the risk management team that monitors compliance with liquidity limits. This could mean housing Treasury within its own department and a separate reporting line into senior management i.e. the CFO, with risk control and compliance located in a different department that reports directly to senior management i.e. the CRO. In practice a small Treasury team may consist of only 2 individuals, a Front Office manager executing deals and a balance sheet manager which may perform not only liquidity planning but also operational monitoring of limits working together with the front office desk to ensure meeting liquidity requirements. A risk manager in the SLOD will perform the mandatory oversight of limits as mandated by the regulatory requirements.

Reference: PRA SS24/15, Paragraph 3.1 – "The PRA expects firms to ensure that the management of liquidity and funding risk is operationally independent from risk control functions to maintain an objective oversight of these activities."

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2. Governance Framework

Example: It advisable that the newly formed bank establishes an Asset and Liability Committee (ALCO), responsible for overseeing Treasury's activities, particularly those related to funding and liquidity management. The ALCO should include senior management from various departments (e.g., Treasury, Risk, and Finance) and meet regularly (at least once per month) to ensure compliance with regulatory expectations and internal governance standards. Treasury activities would be reviewed by ALCO, which has the authority to set risk appetite limits and make adjustments as needed. Given the start-up nature of the newly established Bank it is not uncommon for ad-hoc ALCO's to be arranged or offline decisions by ALCO members to take place in order for governance matters to be expedited i.e. signing off capital increases or funding deals exceeding certain regulatory limits.

Reference: PRA SS24/15, Paragraph 3.4 – "Senior management should establish a governance framework that includes oversight committees to review and approve the firm's liquidity risk management practices."

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3. Independent Risk Assessment and Reporting

Example: In practice, this means the Treasury team would not be allowed to set or adjust its own risk limits. Instead, the risk management function would independently set limits on liquidity exposures, with Treasury or a dedicated Risk Reporting team required to report daily on its liquidity position to the SLOD. This separation ensures that Treasury has no direct influence over its own risk limits, promoting objectivity in risk assessment. In practice Treasury will propose a Risk Appetite Limit, SLOD will review and provide a separate assessment with ALCO approving the same if in aggreement.

Reference: PRA SS24/15, Paragraph 4.2 – "Firms should have an independent risk management function responsible for setting limits, monitoring exposures, and reporting on liquidity risk positions."

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4. Oversight of Front-Office and Treasury Operations

Example: In a practical setup, the Treasury team's cash management activities (e.g., intra-day funding and overnight placements) would be continuously monitored by the risk team with a dual focus on limit management and conduct. Treasury's operational activities would be reviewed by an internal audit function, and any deviations from policy would be reported to senior management. This approach ensures accountability and control, with Treasury operations subject to independent oversight by the risk team and compliance departments. In fact periodic risk and controls assessments will be carried by the SLOD and it is not uncommon for Audit and External Auditors to scrutinize the Treasury function in particular within the first 12 months of operations given it's mandate to manage Capital and Liquidity Risk for the Bank.

Reference: PRA SS24/15, Paragraph 4.5 – "The PRA requires firms to implement controls to ensure front-office operations adhere to the firm's risk management framework and reporting standards."

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5. Tailoring for Proportionality

Example: For a newly established bank, the PRA's proportionality principle may allow it to maintain a simpler Treasury structure initially. For instance, if the bank's size is small and its funding profile low-risk, a single person could oversee liquidity management, with another individual in risk management. However, these roles would remain functionally separate and still report independently to senior management, meeting the PRA's expectation for segregation while acknowledging the entity's small scale. A similar expectation can be derived through the EBA's Small and non-complex institutions regulation in Europe.

Reference: PRA SS24/15, Paragraph 1.2 – "The PRA acknowledges that the application of its expectations may vary depending on the size, scale, and complexity of the firm, with proportionality applied where appropriate."

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