Working with Basel Core Principles

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The Core Principles for Effective Banking Supervision (Core Principles) are the de facto minimum standard for sound prudential regulation and supervision of banks and banking systems.

*Basel Committee on Banking Supervision*

2012
What does supervision - and the BCPs - cover?

- Governance
- Coordination
- Relevance
Context to understand BCPs

- Framework
- Proportionality
- No single template for supervision

Comprehensive  Inclusive  Non-Prescriptive
Proportionality matters

BCPs are for EVERYONE

BCPs

- Capable of application to a wide range of jurisdictions whose banking sectors will inevitably include a broad spectrum of banks

- Expectations on supervisors for the discharge of their own functions and in terms of the standards that supervisors impose on banks
The Core Principles are ...

**Not**
- A guarantee that no bank will fail

**Not**
- A rigid set of standards

**Not**
- A remedy for economic mismanagement
Common themes

- Independence, Resources & Mandate
- Corporate Governance
- Corrective Action and Early Intervention
Supervision and data

- Board level responsibility – senior level sign off.
- Fines and sanctions – can focus the bank’s attention.
- Improving data quality – can be a slow process. Don’t give up.
- Have regular process for considering what kind of data you need. Coverage? Granularity?
- Never collect data that you don’t use. It’s a supervisory liability
- Create obligations for banks and auditors/consultants to notify you
- External auditors can be a valuable source of information - but building the relationship can take time. Legal gateways needed.
- Disclosure practices improve over time, so make a start. Supervisor should also disclose
Capital adequacy

- Capital needs to be commensurate to risk
- Quality of capital is critical. IMF supports Basel III definition of regulatory capital
- Supervisor should be able to apply bank specific capital requirements
- BCPs do not require a specific version of Basel (eg II or III)
- It is ok to take a "modular" approach to implementing Basel – implement the parts of Basel that are useful for your jurisdiction
- Advanced approaches not essential
Information gateways are essential. Get them. Use them.

Colleges work better the more they are used and the better they are planned

Trust can take time but it will build

Understand the group. Internally and beyond the consolidated perimeter

Use supervisory relationships to deepen your understanding

Support your fellow supervisors
Corrective actions

Range of powers and willingness to use them, including fines, restriction of business, revocation

Follow through actions to conclusion

Can the supervisor remove senior management or directors?
Emerging issues

Sovereign Exposure

FinTech, TechFin, Cyber
Are BCPs Relevant?
2018 Latvia's central bank chief faces bribery trial

Abdul Qadir Fitrat has fled his job as Afghanistan's central banker, and his country, fearing for his safety.

Integrity of the governance of the supervisor

Legal Protection of the supervisor
Pilatus Bank was granted a license to operate in Malta in January 2014 when its chairman was at that time being investigated for money laundering by US authorities.
We are therefore unable to determine whether or not the delay on the part of the Bank in imposing the 25% limit with regard to Barings’ exposure to OSE was a contributory factor in Barings’ collapse. Nevertheless, we consider that the delay was unacceptable; the Bank was not entitled to assume that the delay would be inconsequential.

Having rules is never enough on its own.

Standards must be implemented
A report by the private international investigation agency Kroll, leaked by the speaker of Moldova's parliament, suggests Ilan Shor was the prime coordinator and beneficiary of a bafflingly complex web of transactions that pushed three leading banks to the verge of collapse.

It says loans worth $1bn were transferred in just two days to a series of UK- and Hong Kong-registered companies — companies whose ultimate owners are unknown.

As a result, the state was forced to step in to bail the banks out — protecting depositors but creating a hole in the public finances equivalent to an eighth of GDP.

The Kroll report describes how the three banks - Unibank, Banca Sociala and Banca de Economii - were taken over, beginning in 2012, by new owners, who appeared to be unconnected.

Some bought their shares using funds from UK limited partnerships, whose ownership is often opaque.

The banks then entered into a series of transactions which Kroll says had "no sound economic rationale". The web of loans emptied them of funds until "they were no longer viable as going concerns".
The Estonian branch generated 11 per cent of Danske’s total profits before tax that year, despite only accounting for 0.5 per cent of the bank’s assets.

Danish regulator asked Danske for information following complaints from its Estonian counterpart about serious anti-money laundering issues.

Danske head office had no person responsible for anti-money laundering (as required by Danish law) all year until November.

Danish financial regulator reprimanded Danske but took no action against its management. (FT 4 October)

CEO is fired. He will receive 12 months’ salary – in 2017 this was $1.8mn
We have considered whether the supervision of UK banks would be improved if the Bank were to undertake, as a matter of course, regular inspection visits to all authorised institutions (or possibly all banking groups) and perform extensive detailed testing; an approach akin to that employed in a number of other countries. This might provide the Bank with more first hand knowledge about each institution (although we note that bank failures resulting from the unauthorised activities of bank personnel have also occurred in inspection based regimes), but we feel there are a number of disadvantages associated with this kind of approach. It would also involve a very significant increase in the cost of supervision which would ultimately be passed on to the customer or taxpayer. From the work which we have undertaken during this inquiry we do not believe that a wholesale change to this style of supervision is justified. We would prefer to see the existing supervisory tools available to the Bank developed further in the manner set out elsewhere in this section.
Working with BCPs
Self Assessment

Objects in the mirror may be closer than they appear...

Pros
- Time
- Resources

Cons
- Benchmarks/peers
- Sense of Perspective
Mirror, Mirror on the wall...who is the fairest of them all?

BCPs are not beauty parades

Advantage

Can offer leverage to the authorities

Can distract from the analysis

Benchmark/Peer

Grades

Intensive

Resources
Making Changes

- **Examine** Recommendations
- **Are legal amendments needed?** Legal Framework
- **Are resources sufficient?** Resources
- **Make a judgment on priorities and changes** Judgment

Examine

Recommendations

Are legal amendments needed?

Legal Framework

Are resources sufficient?

Resources

Make a judgment on priorities and changes

Judgment

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Conclusion

The BCPs record the experiences and, often, failures of the global community of banking supervisors. They are a practical guide borne out of real experience. I commend them to you.
THANK YOU!

Monetary and Capital Markets Department