



**MONETARY AND  
CAPITAL MARKETS**

# Working with the Basel Core Principles

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FR, MCM

# *A reluctant history of supervision*

“A mania prevailed, a bubble burst ... four hundred nobodies were ruined.”

*Nicholas Nickleby, Charles Dickens*

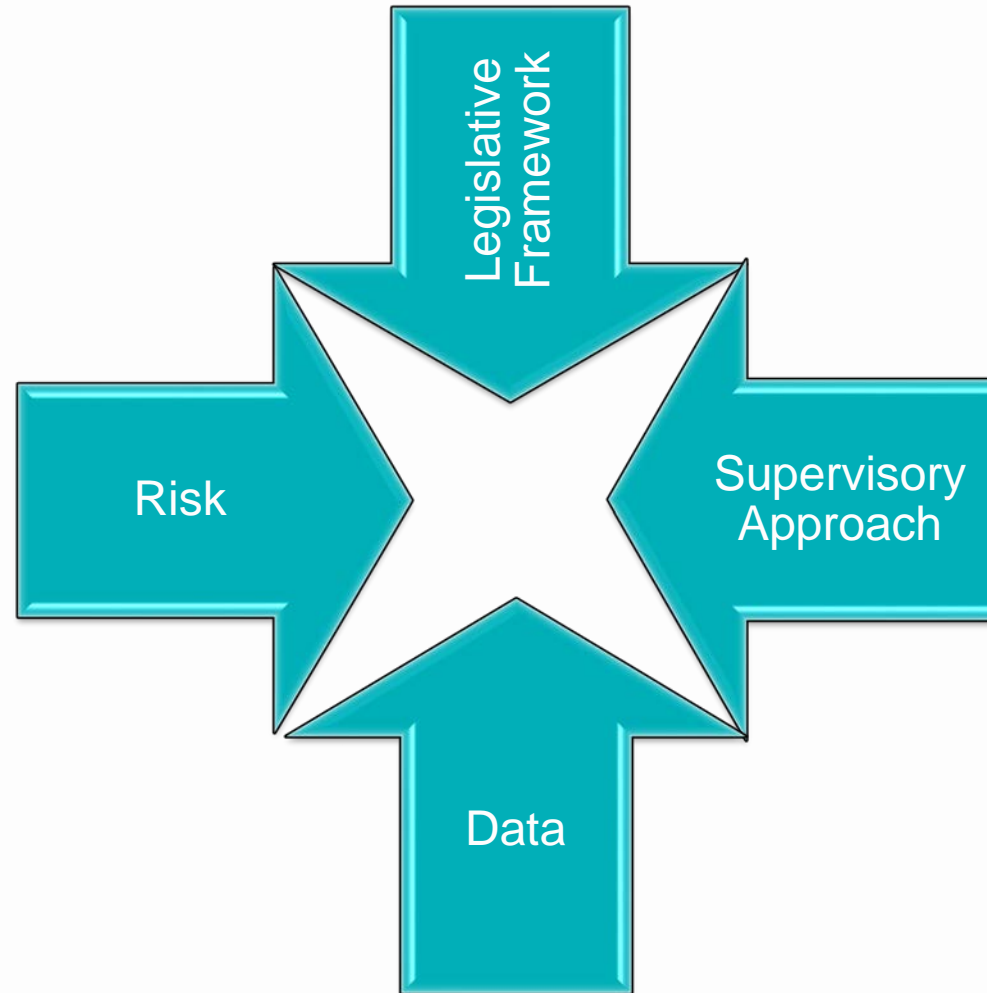
# International standards: The Basel Core Principles

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.

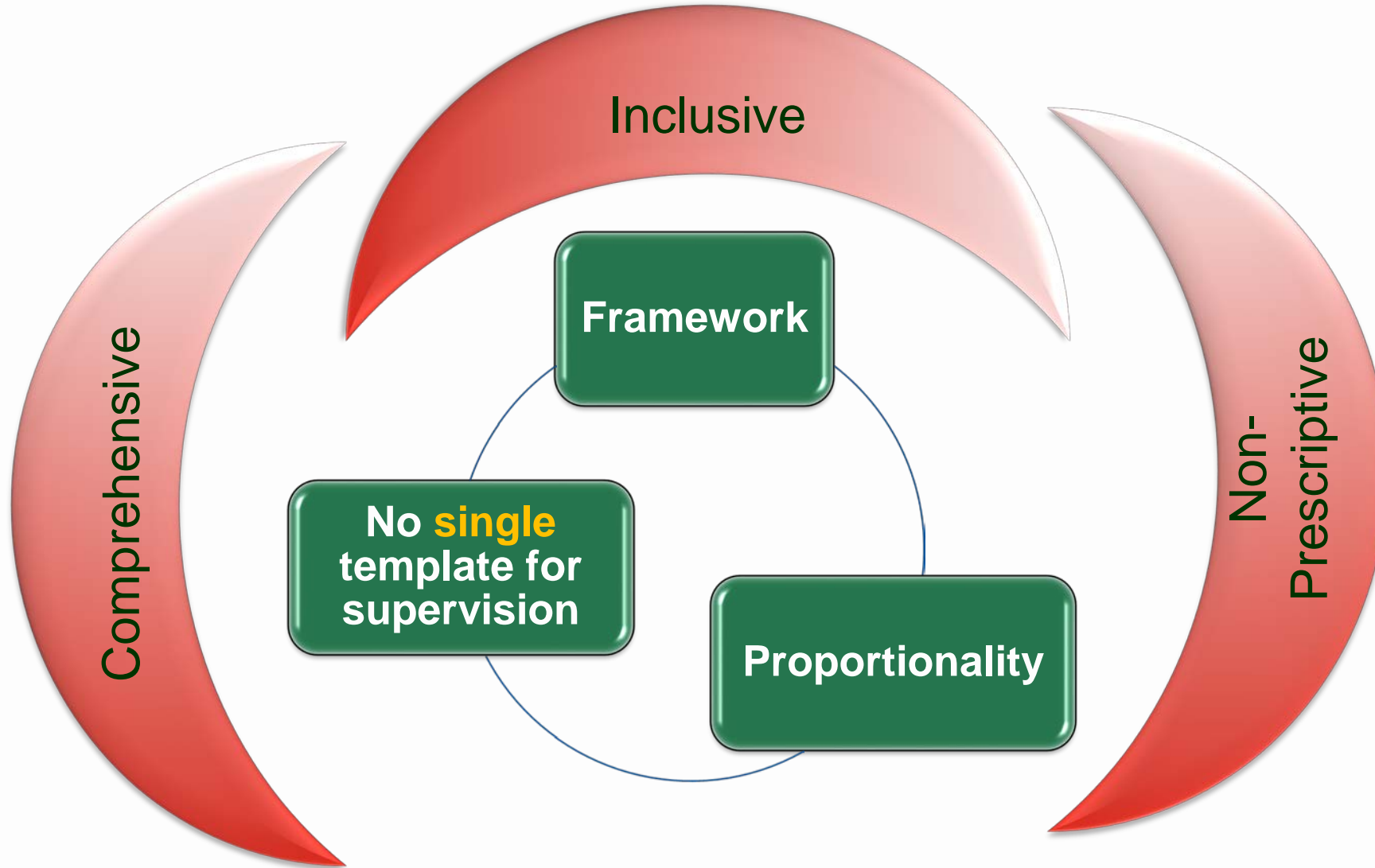
*Basel Committee on Banking Supervision*

*2012*

# What does supervision - and the BCPs - cover?



# Context to understand BCPs



# The Core Principles are ...

Not

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- **A guarantee that no bank will fail**

Not

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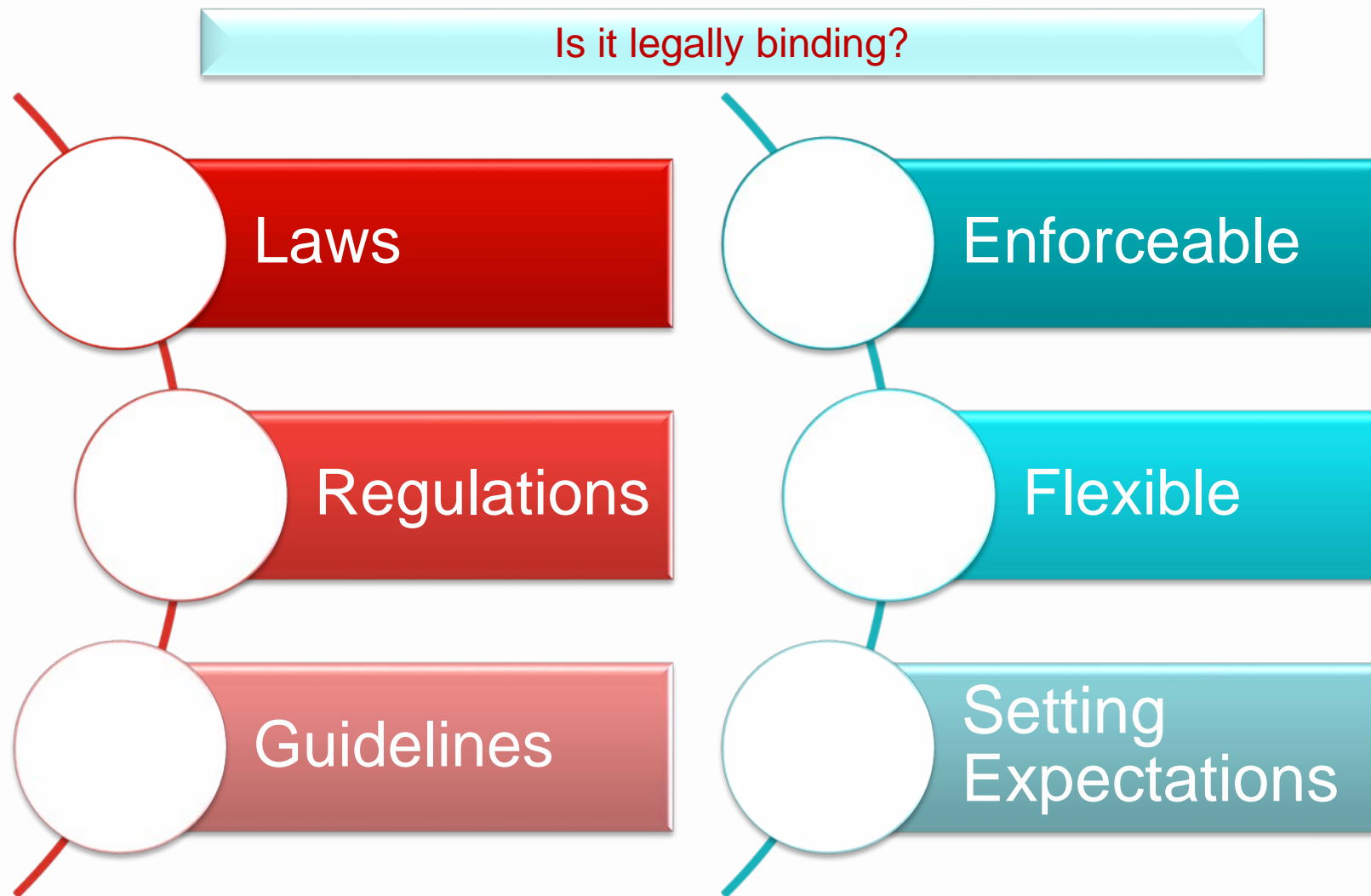
- **A rigid set of standards**

Not

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- **A remedy for economic mismanagement**

# BCPs and the legal framework



# Proportionality matters

BCPs are  
for  
**EVERYONE**

BCPs

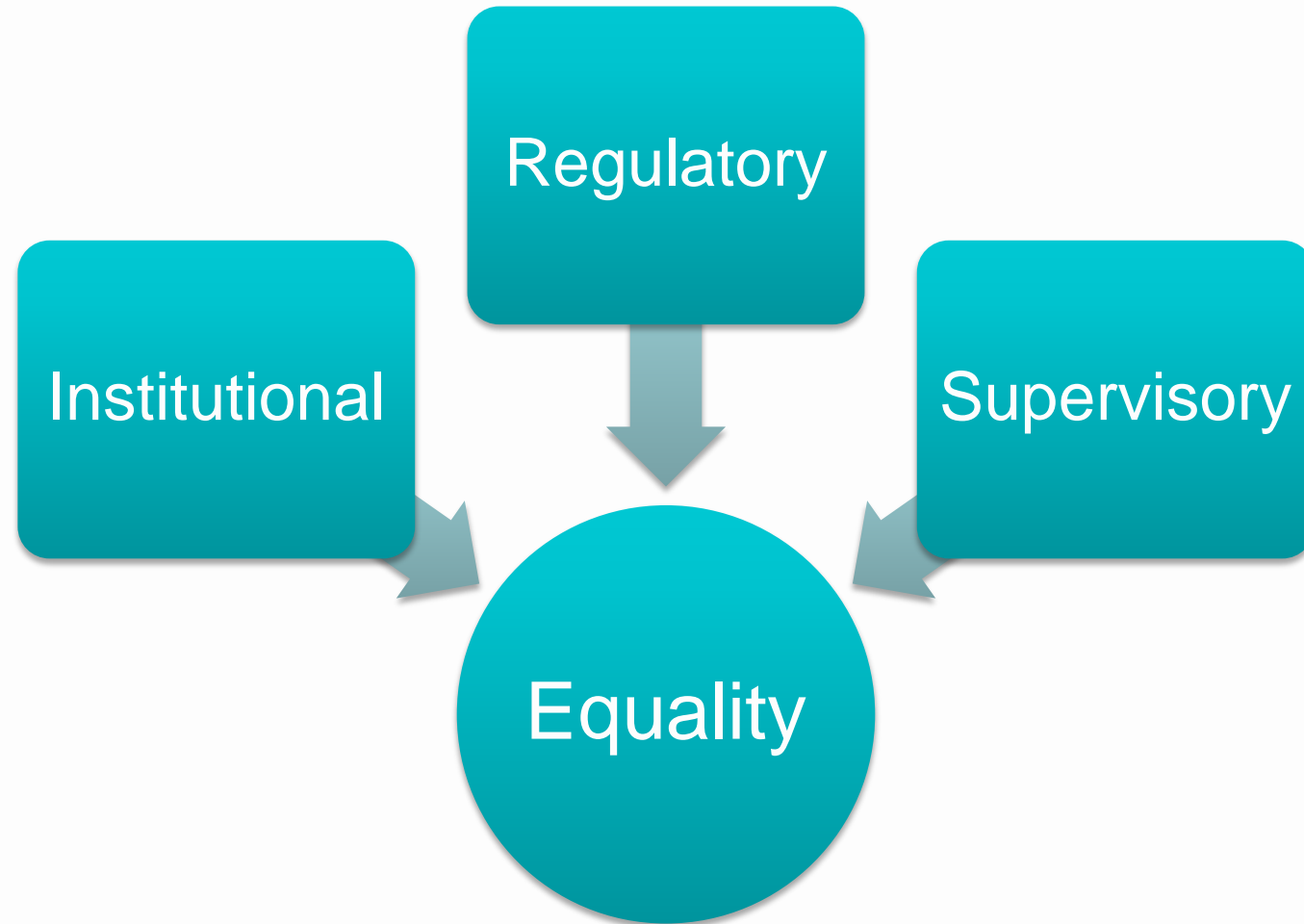
- Capable of application to a wide range of jurisdictions whose banking sectors will inevitably include a broad spectrum of banks

BCPs

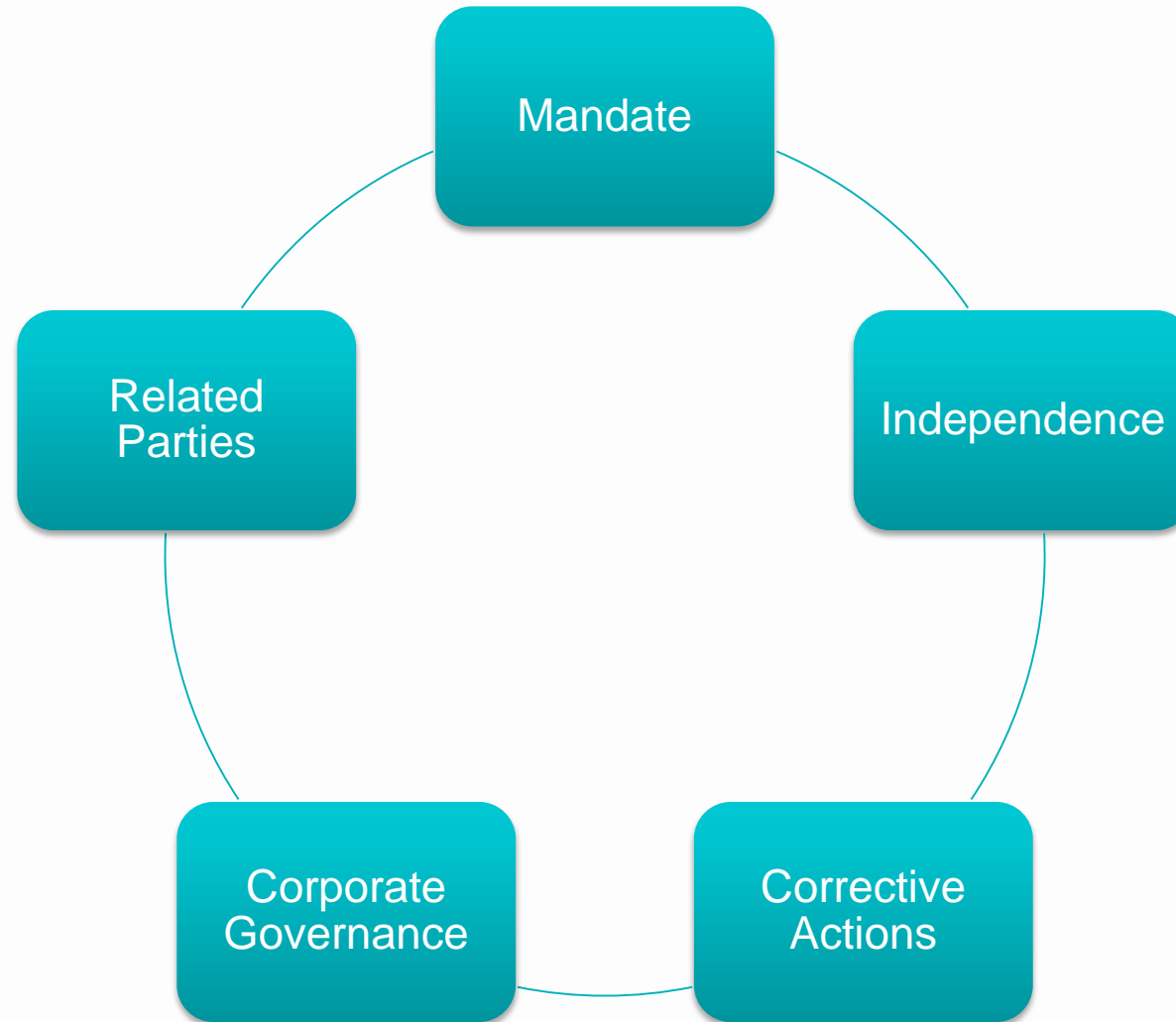
- Expectations on supervisors for the discharge of their own functions and in terms of the standards that supervisors impose on banks



# Every principle matters



# Interconnection and Interdependence



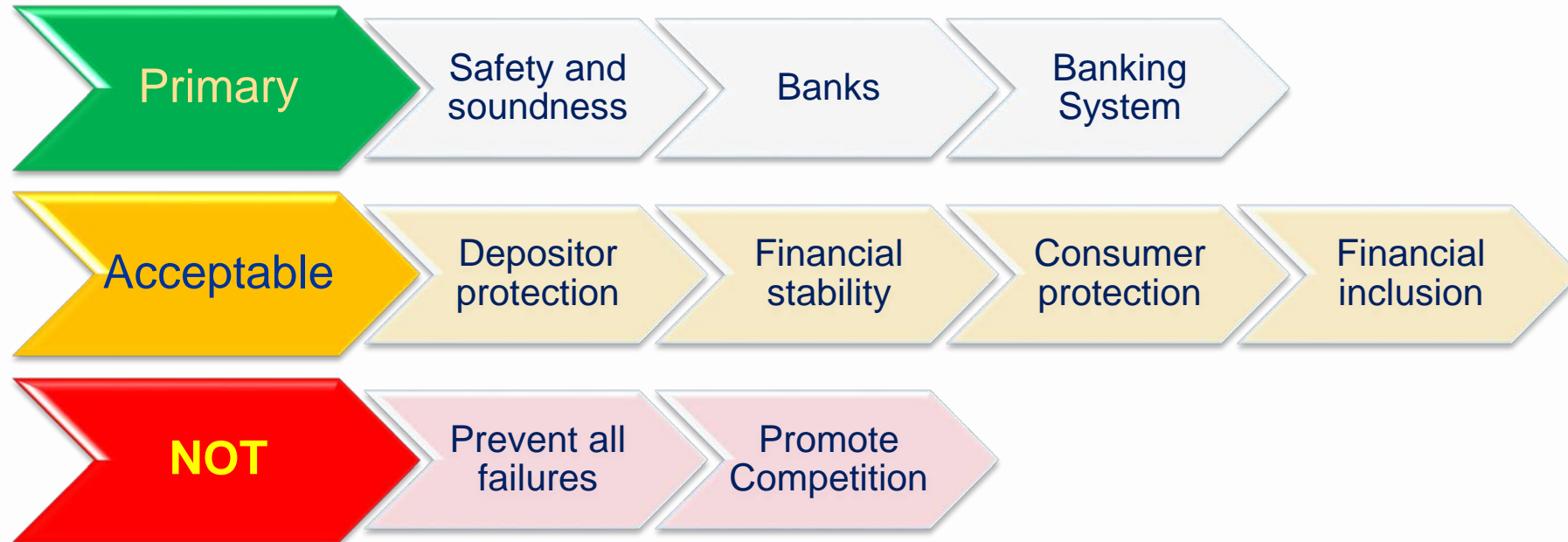
# Common themes

Independence, Resources & Mandate

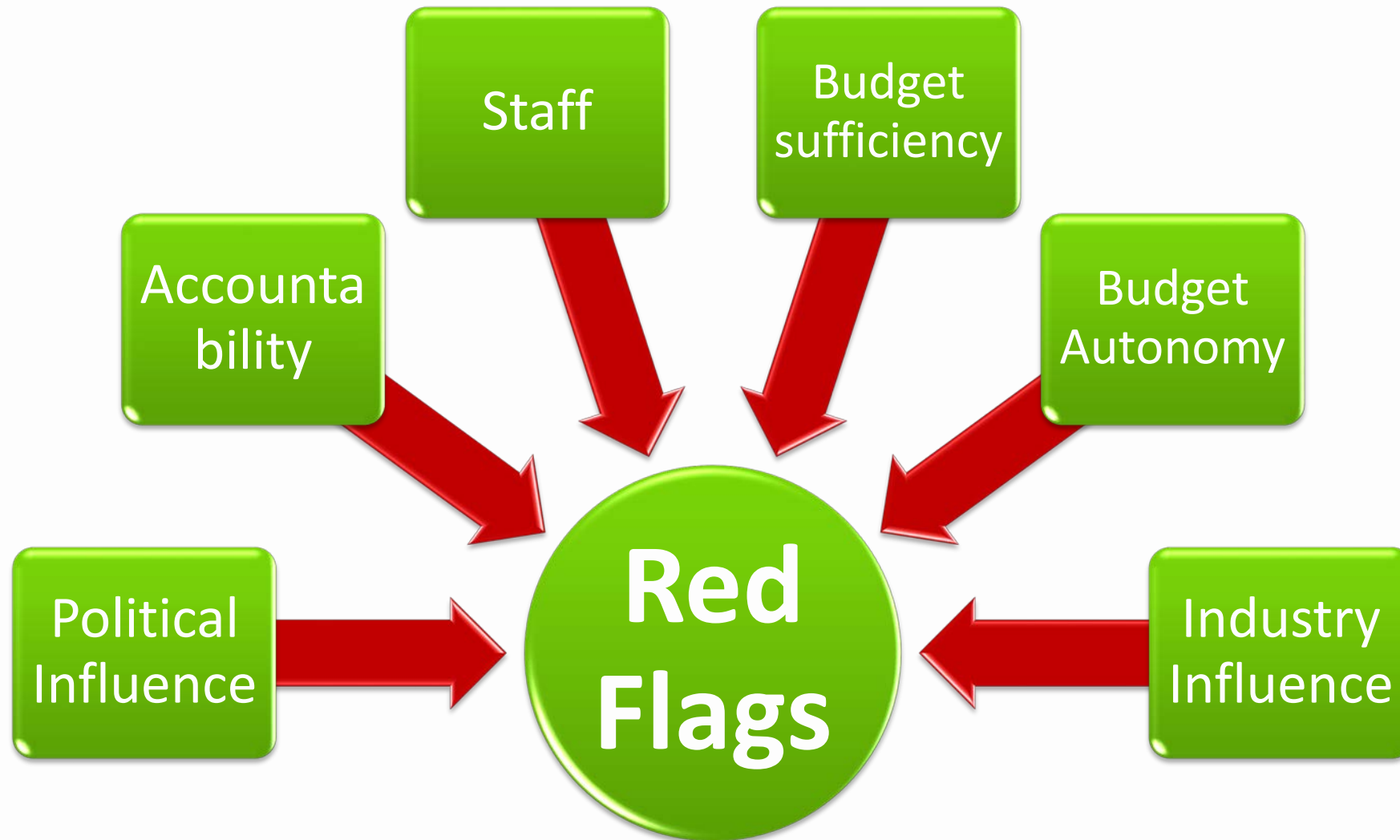
Corporate Governance

Corrective Action and Early Intervention

# Mandates



# Independence – de jure or operational or both?



# Institutional architecture and process

## Governance

Clear internal decision making process

Effective internal communication process

# Governance and control

## Poor governance

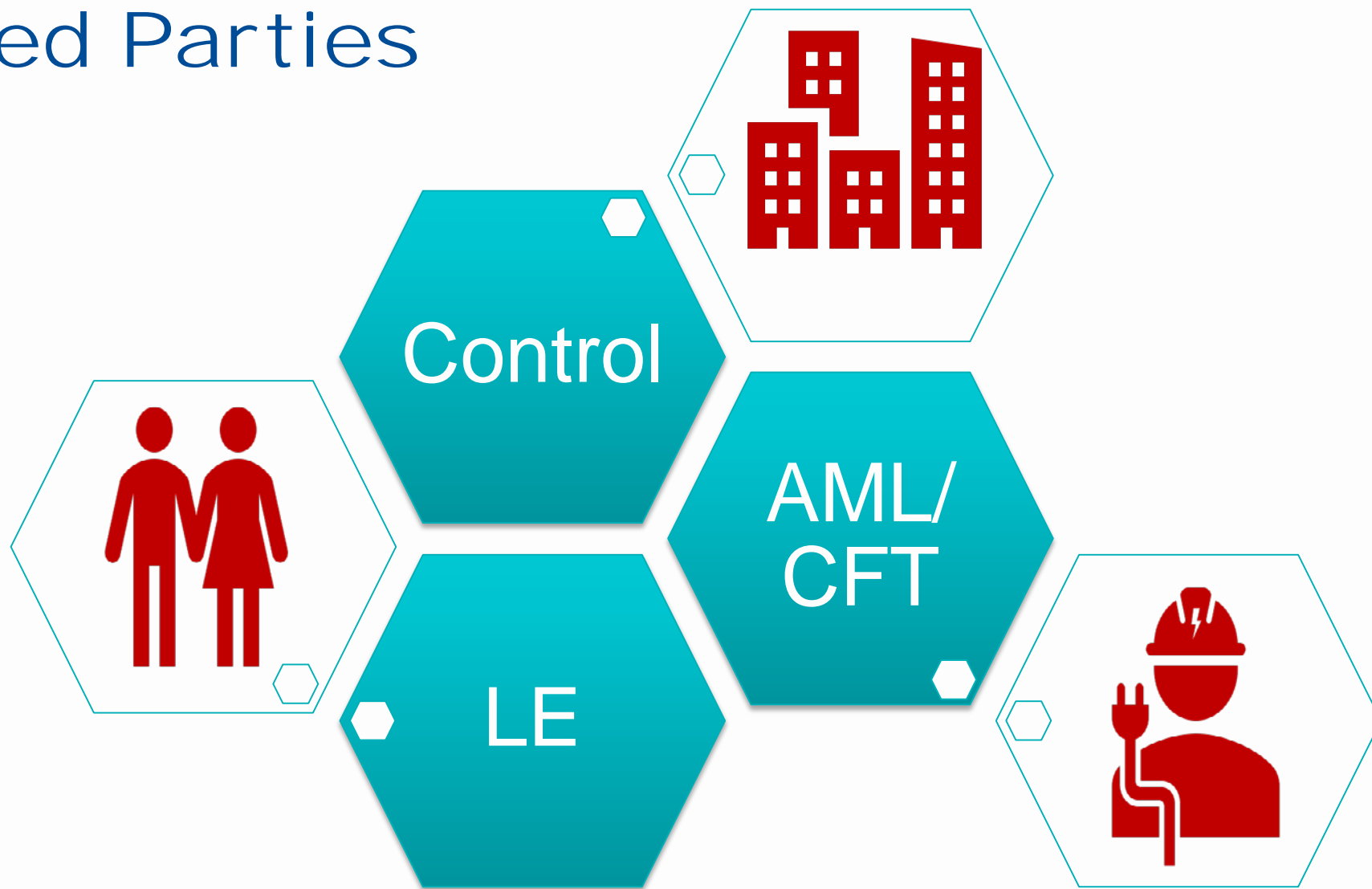
We're very pleased. It's the first time our Russian sub has sent the report we asked for. (CFO)

How big is our exposure to MBS?  
(Co-President,  
Morgan Stanley)

All our profits are from derivatives. I don't understand them but the Board is very happy.  
(Chairman)

We want to open an arbitrage desk. I can't explain it but the traders say everyone is doing it. (CEO)

# Related Parties





# Corrective actions

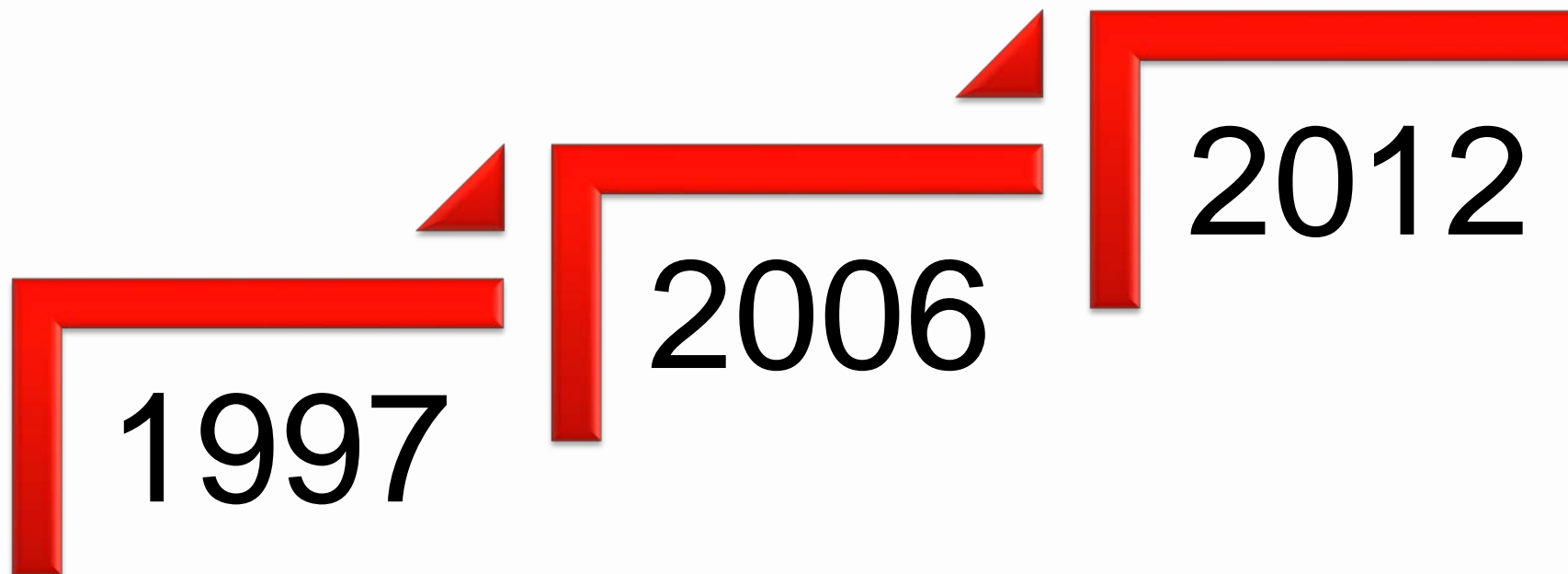


Supervisors  
need a full set  
of **GRADUATED  
POWERS**

They must be  
**WILLING** and **ABLE**  
to use these  
powers

Legislative  
framework and  
supervisory  
**INDEPENDENCE**  
vital

# BCP Evolution – where next? When next?



# Emerging issues

Sovereign Exposure

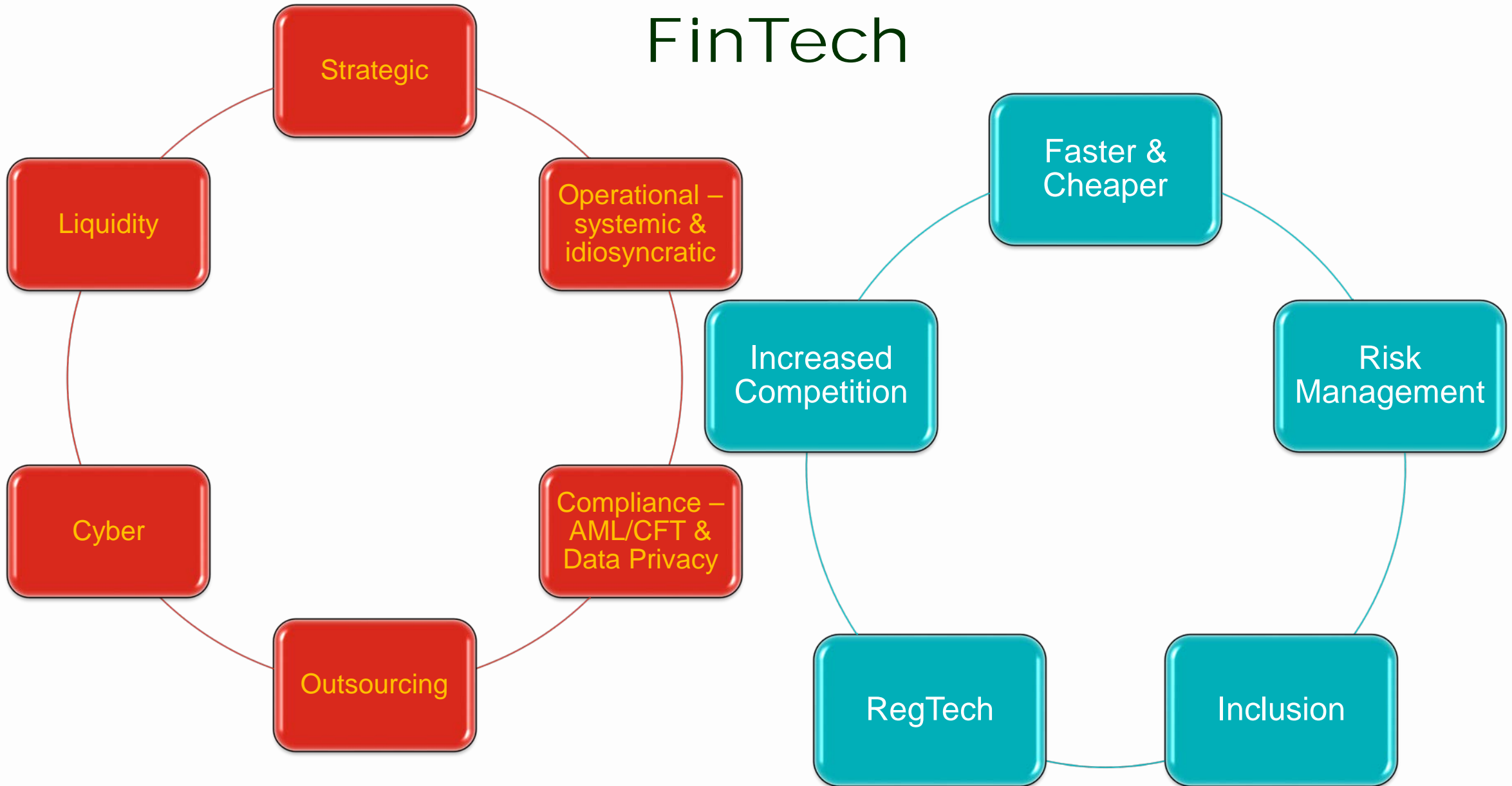
FinTech, TechFin,  
Cyber

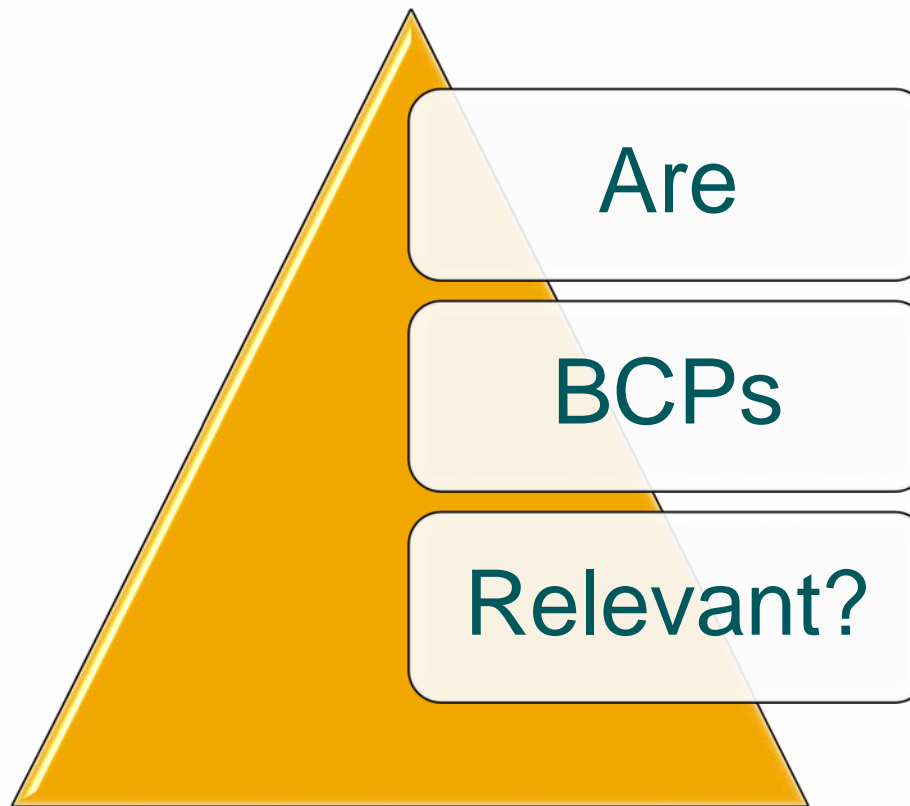
# Emerging issues

Sovereign Exposure

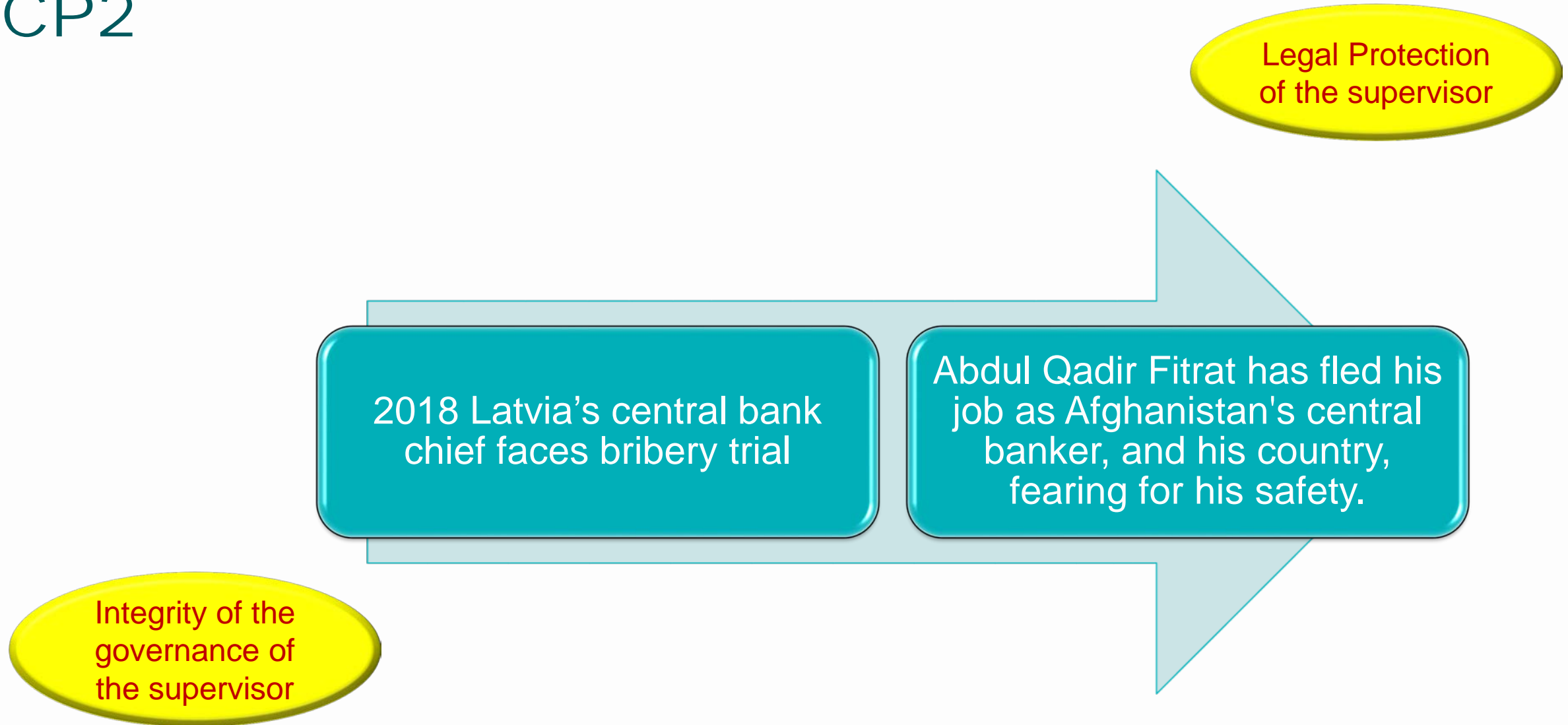
FinTech, TechFin,  
Cyber

# FinTech





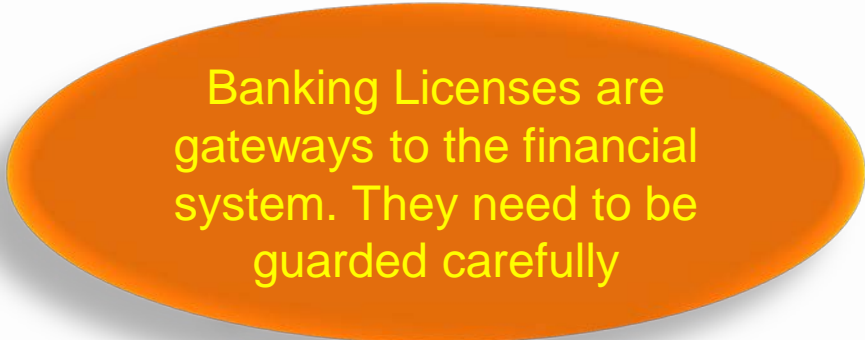
# CP2





CP5

- 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.



Banking Licenses are gateways to the financial system. They need to be guarded carefully



# CP19...or is it?

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

Report to the House of Commons on the Inquiry into the Collapse of Barings  
Bank 1995

## CP20 - Related Parties matter and can be difficult to control

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".

# Den Danske

CP8

Did Business Model Analysis identify this discrepancy?

**2011** 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.

Nearly a year without an AML official?

**2012** Danish regulator asked Danske for information following complaints from its Estonian counterpart about serious anti-money laundering issues.

CP29

**2013** Danske head office had no person responsible for anti-money laundering (as required by Danish law) all year until November.

**May 2018** Danish financial regulator reprimanded Danske *but took no action against its management*. [FT 4 October)

**October 2018.** CEO is fired. He will receive 12 months' salary – in 2017 this was \$1.8mn

CP11

Did the supervisor have sufficient powers?

CP14

Why did the Board not act and ask questions



# Making Changes?

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.

Decisions on what to change, how to change and when to change are never easy and may be political.

Report to the House of Commons on the Inquiry into the Collapse of Barings Bank 1995

# Working with BCPs



# Self Assessment

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



Pros

Cons

Time

Resources

Benchmarks/  
peers

Sense of  
Perspective



# External Assessment

BCPs are *not* beauty parades



*Mirror, Mirror on the wall...who is the fairest of them all?*

Advantage

Benchmark/  
Peer

Can offer  
leverage to the  
authorities

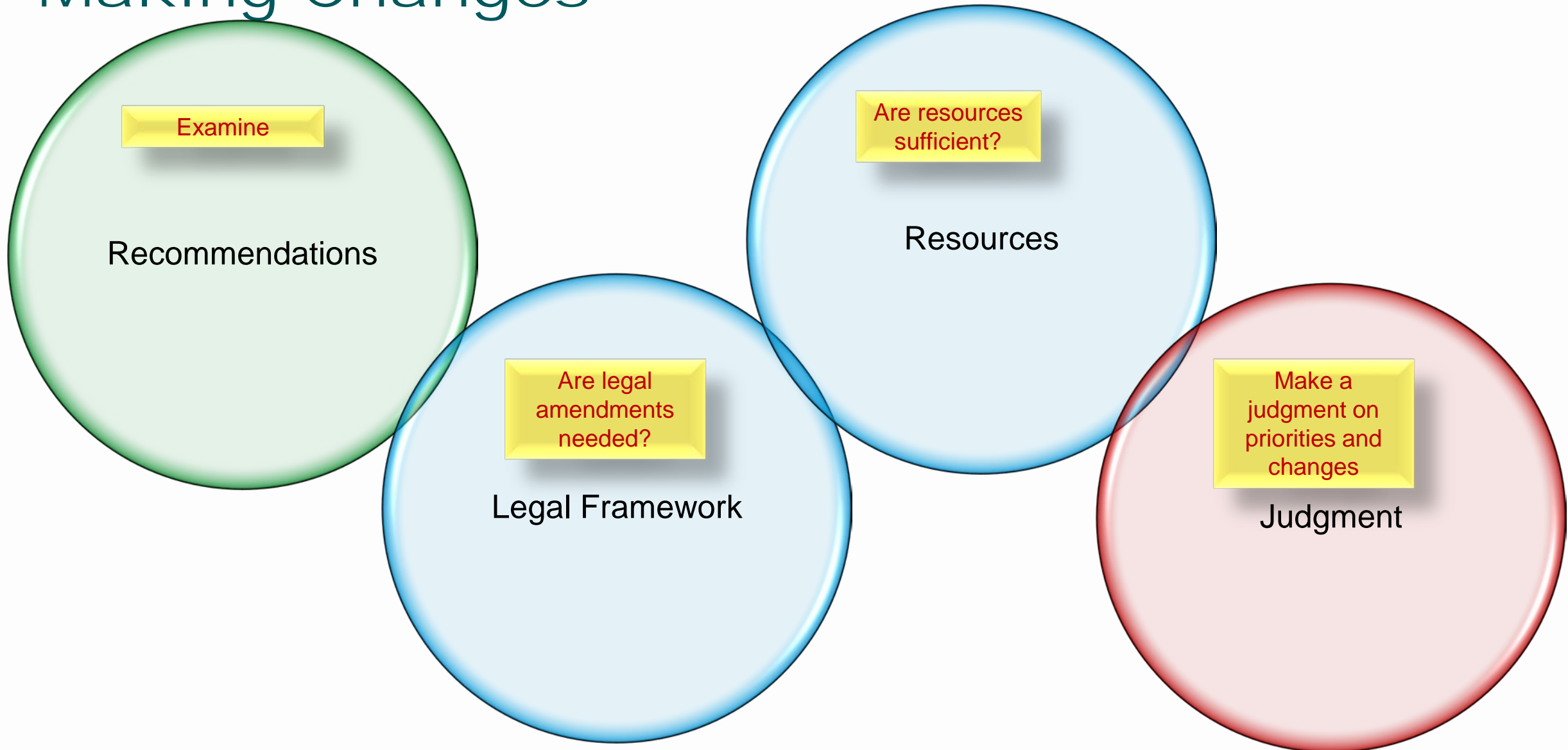
Grades

Can distract from  
the analysis

Intensive


Resources

# Making Changes





# 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***

