

**Comments received on the consultative document "Core principles for effective banking supervision" (print version)**

On 20 December 2011, the Basel Committee released its consultative document [Core principles for effective banking supervision](#). Interested parties were invited to provide written comments by 20 March 2012. These comments, in PDF format, are available below.

The Committee wishes to thank those who have taken the time and effort to express their views.

Abozer Majzoub	30kb
Akio Sashida	573kb
Australian Bankers' Association	59kb
British Bankers' Association	28kb
Bulgarian Institute of Directors	567kb
Canadian Bankers Association	161kb
Central Bank of Barbados	16kb
Child and Youth Finance International	206kb
Chris Barnard	208kb
Consultative Group to Assist the Poor	31kb
David Hawkins	21kb
Dubai Financial Services Authority	73kb
Fit and Proper Consulting	210kb
French Banking Federation	2578kb
Guernsey Financial Services Commission	613kb
Institute of International Finance	361kb
National Research University Higher School of Economics	62kb
Nordic Financial Unions	56kb
Sciteb	478kb
The Bank of Communications	13kb
UniCredit	257kb
World Council of Credit Unions	207kb
WSBI-ESBG	135kb
Zhen Li	244kb

**RESPONSE TO THE BASEL COMMITTEE’S REQUEST FOR COMMENTS ON THE
CONSULTATIVE DOCUMENT “CORE PRINCIPLES FOR EFFECTIVE BANKING
SUPERVISION”**

Buenos Aires, 19 March 2012

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

*Ref.: Consultative Document “Core Principles for Effective
Banking Supervision” – Fit & Proper’s comments*

Dear Committee Members,

I am pleased to submit the following Fit & Proper’s comments and suggestions in response to the Consultative Document *Core Principles for Effective Banking Supervision*, issued by the Basel Committee on Banking Supervision (BCBS) on December 20th, 2011.

Fit & Proper LLC provides advisory and consulting services on issues related to banking supervision and regulation, central banking, financial institutions and financial inclusion and microfinance, among others. On this regard, Fit & Proper provides services to banking supervisors, central banks, deposit insurance agencies, ministries of finance and multilateral organizations, including the Interamerican Development Bank, the International Monetary Fund, and the World Bank. Fit & Proper and its consultants have experience in more than 30 countries. You can find further information in www.fitproper.com.

These comments were prepared by Javier Bolzico, José Rutman, Eugenia Gozzi, and Natalia Teplitz.

I would like to express our appreciation to the BCBS for the opportunity to provide feedback on this Consultative Document.

Furthermore, I would like to take the opportunity to congratulate the BCBS and the staff member of the Secretariat of the Basel Committee on Banking Supervision for the good job that they have done regarding the Core Principles for Effective Banking Supervision. We believe that the new Core Principles will be an important instrument to guide supervisors, contributing to the financial stability.



I would be pleased to provide more information or further discussion on any of these issues. If you have any comments or questions, please feel free to contact us at (54 11) 4719-0704 or info@fitproper.com.

Yours faithfully,

Javier Bolzico
CEO
Fit & Proper LLC

Comments / suggestions on Consultative Document “Core Principles for Effective Banking Supervision”

1. Preconditions for effective banking supervision

Preconditions for effective banking supervision, section III of the Consultative Document, contain two preconditions related to Financial Safety Net:

- “A clear framework for crisis management, recovery and resolution.”
- “An appropriate level of systemic protection (or public safety net)”

The first one states the importance of having a sound institutional framework for crisis management and **resolution** where relevant authorities have a broad range of powers and appropriate tools to resolve a financial institution, while the second emphasizes on the importance of a transparent and carefully designed **deposit insurance** that addresses the risk of contagion and minimizes moral hazard.

On this regard, we suggest:

- a) To include an effective Lender of Last Resort (LOLR) function as a precondition for effective banking supervision, in order to cover the four key elements of Financial Safety Net, which consist on (1) **prudential regulations and supervisory framework**, (2) **lender of last resort**, (3) **bank resolution processes**, and (4) **deposit insurance scheme**. Component (1) -prudential regulations and supervisory framework- is addressed along the 29 principles, while components (2), (3) and (4) of the Financial Safety Net should be part of the preconditions.

Although the LOLR does not replace the need for a sound and robust liquidity management of the bank, it is crucial for preventing a liquidity crisis turning into a solvency one.

- b) To group these preconditions (*clear framework for crisis management, recovery and resolution; appropriate level of systemic protection (or public safety net); and effective LOLR function*) in a single precondition under the title of “An appropriate Financial Safety Net”.

2. Principle 8: Supervisory Approach

“An effective system of banking supervision requires the supervisor to develop and maintain a forward-looking assessment of the risk profile of individual banks and banking groups, proportionate to their systemic importance; identify, assess and address risks emanating from banks and the banking system as a whole; have a

*framework in place for early intervention; and have plans in place, in partnership with other relevant authorities, to take action to resolve banks in an **orderly** manner if they become non-viable.”*

Regarding this principle:

- a) We suggest replacing the word “orderly” with “appropriate”. A resolution process can be conducted in an “orderly manner”, but it does not, necessarily, mean that it is also conducted in an appropriate way. For instance, the resolution process can generate excessive moral hazard (it can be orderly but involve a shareholder bail out, for example).
- b) We recommend specifying, as essential criteria (to assure that the bank resolution scheme is “appropriate”), the need of mechanisms that minimize moral hazard, and reduce time of resolution and fiscal costs.

Furthermore, the following criteria for bank resolution methods could be incorporated¹:

- Minimization of direct financial and economic costs. The chosen resolution scheme should decrease the loss of economic output due to misallocation of public resources (i.e. fiscal or inflationary costs from the resolution process) and the disruption of banking services.
 - Minimization of contagion risk. Bank resolution method should minimize the likelihood of a deposit run on other banks and the financial and economic costs they represent.
 - Ensure a minimum level of protection to “widows and orphans”. Bank resolution process needs to cover small and less-sophisticated depositors, who cannot exert market discipline.
 - No bail out for shareholders. Bank resolution losses must be bear first by shareholders.
 - Adequate transparency. A transparent framework, with clear ex-ante rules and procedures, is needed to avoid hampering the credibility of the authorities during the resolution process and ensure a positive perception of the process by market participants.
 - Timely response and resolution.
 - Available capacity and resources.
- c) We consider that it could be appropriate to include, also as essential criteria, that the supervisor should have a non-public rating system of banks.
 - d) We suggest including the need to have a specific resolution scheme for systemic situations, including the possibility to implement additional

¹ Bolzico J., Mascaró Y., and Granata P. (2007). “Practical Guidelines for Effective Bank Resolution”. World Bank Policy Research Working Paper No. 4389, The World Bank.

alternatives (compared with the non-systemic resolution scheme). This scheme should include the agencies and authorities involved in declaring a systemic situation and implementing the resolution process.

3. Principle 29: Abuse of financial services

“The supervisor determines that banks have adequate policies and processes, including strict customer due diligence (CDD) rules to promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, for criminal activities.”

We suggest including, in the essential criteria, some reference to the recommendations made by Financial Action Task Force (FATF) related to financial inclusion². On this regard, FATF suggests that anti-money laundering and terrorist financing regulations and supervision should take into account the importance of financial inclusion. Countries may use a risk-based approach in order to allow resources to be allocated efficiently and to promote better financial inclusion.

² FATF Guidance. Anti-money laundering and terrorist financing measures and Financial Inclusion. June 2011.