



Core Principles: Next Steps

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Introduction

- Significant progress in establishing the Core Principles
 - As high level principles, they can guide thinking about design.
- The next challenge
 - How to ensure broad acceptance of the Core Principles?
 - How to use Core Principles to guide deposit insurance design?
 - How to use Core Principles for financial stability?
- Critical element: a broadly accepted assessment methodology



Financial Stability Assessment Programs

FSAPs: Objectives And Design

- Fund's main instrument for financial sector surveillance
- Twin objectives
 - Financial stability
 - Financial sector development
- Main design features
 - Stability assessment
 - Stress testing
 - Assessment of compliance with standards and codes

Standards and Codes

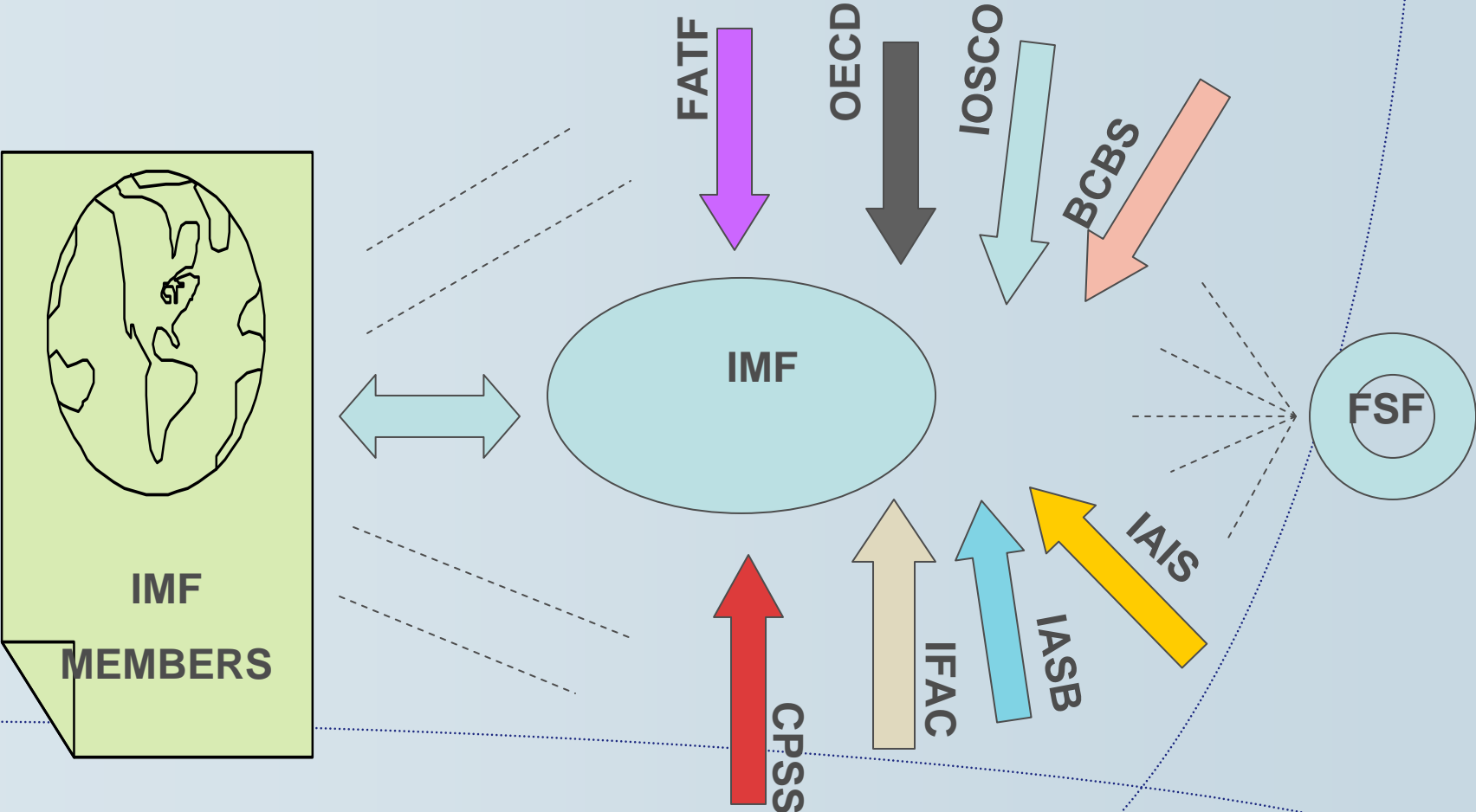
Core principles

- Developed by standard setters
- High level principles
- Guides establishment and assessments of systems

Methodologies for assessment

- Gives greater specify to high level principles
- Broad consensus on approach
- Outreach to ensure buy-in

Sources of Standards and Codes





Establishing a Methodology: Case of the BCP

Organization

- In June 2004, the Basel Committee of Banking Supervisors (BCBS) established a small Steering Committee (8 persons) to identify approaches and policy issues.
- In December 2004, the Steering Committee submitted their report to BCBS with proposed responses to a list of policy issues on the scope of the BCP and proposals for methodology.
- Three drafting teams were established with a regional balance and a fair distribution between BCBS and non-BCBS members.

Drafting Process

- December 2004, the drafting work starts. Each team (composed of 10 people each) assigned principles to elaborate and write assessment methodology. The Steering Group oversaw the drafting process.
- April 2005: BCBS Meeting discuss the first comprehensive draft. Comments go back to Steering Committee
- September-2005: BCBS Meetings discussed a second draft. Regional groups of banking supervisors consulted in parallel.
- QI-2006: Final draft to be presented to the BCBS.
- QII-2006: The final proposal to adopt the amended BCP submitted for endorsement and public release.



Examples of Methodologies

IOSCO Principles

Principle 2:

The regulator should be operationally independent and accountable in the exercise of its powers and functions.

Independence

- Does the securities regulator have the ability to operate on a day-to-day basis without political or commercial interference?
- Where particular matters of regulatory policy require consultation:
 - Is the consultation process established by law?
 - Is consultation not required for day-to-day technical matters?
 - Are the circumstances requiring consultation clear and transparent?
- Does the securities regulator have a stable source of funding?
- Are the regulatory authority, accorded adequate legal protection?
- Are the head and governing board of the regulator subject to mechanisms intended to protect independence?

Accountability

- Is the regulator accountable to the legislature or another government body on an ongoing basis?
- Is the regulator required to be transparent in its way of operating and use of resources and to make public its actions?
- Is the regulator's receipt and use of funds subject to review or audit?
- Are there means for natural or legal persons adversely affected by a regulator's decisions to seek review in a court
- Is confidential and commercially sensitive information subject to appropriate safeguards to prevent inappropriate use or disclosure?

IOSCO Evaluation

- ***Fully Implemented***
 - Requires affirmative responses to all applicable Questions.
- ***Broadly Implemented***
 - Requires affirmative responses to all applicable Questions except to Question 6(b).
- ***Partly Implemented***
 - Requires affirmative responses to all applicable Questions except to either Question 2(b) or 2(c), and to Questions 4, 5, 6(b) and 7(c).
- ***Not Implemented***
 - Inability to respond affirmatively to one or more of Questions 1(a), 1(b), 2(a), both 2(b) and 2(c), 3, 6(a), 6(c), 7(a), 7(b), 7(d) or 8.

Basel Core Principles

Principle 23: Corrective and remedial powers of supervisors

Supervisors must have at their disposal an adequate range of supervisory tools to bring about timely corrective actions.

Essential Criteria

- The supervisor raises supervisory concerns with management at an early stage, and requires that these concerns are addressed in a timely manner.
- The supervisor participates in deciding when and how to effect the orderly resolution of a problem bank situation.
- The supervisor has an appropriate range of supervisory tools for use when a bank is not complying with regulations or is engaged in unsafe or unsound practices.
- The supervisor has available a broad range of possible supervisory measures, which may include ...
- The supervisor has the authority to take measures should a bank fall below the minimum capital ratio, and seeks to intervene at an early stage.
- The supervisor applies penalties and sanctions not only to the bank but, when and if necessary, also to management and/or the Board.

Additional Criteria

- Laws or regulations guard against the supervisor unduly delaying appropriate corrective actions.
- The supervisor has the power to take remedial actions, including ring-fencing of the bank f, parallel-owned banking structures and other related companies in matters that could impair the safety and soundness of the bank.
- When taking formal remedial action in relation to a bank, the supervisor ensures that the regulators of non-bank related financial entities are aware of its actions and, where appropriate, coordinates its actions with them.

BCP Evaluation

Fully Compliant

When all essential criteria applicable for this country are met without any significant deficiencies.

Largely compliant

Whenever only minor shortcomings are observed and the authority's ability to achieve full compliance within a prescribed period of time.

Materially non-compliant

Whenever there are severe shortcomings, and there is evidence that supervision has not been effective,.

Non-compliant

Whenever there has been no substantive implementation of the Principle.

Issues

- How to assess—specific questions or intentions?
 - Rating scale
 - What kind of criteria--essential or also additional criteria?
- How encompassing do you want “full compliance”?
 - If easy, less adequate
 - If difficult, less acceptable
- What level of global acceptance is desired?
 - How to achieve consensus
 - How broadly do you want consensus—IADI, EFDI, all countries?
- What to do with the assessment
 - If inclusion in FSAP, methodology needs Bank/Fund approval
 - If inclusion in FSAP, early participation is helpful.



Conclusions

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- Important progress has been achieved by establishing the Core Principles
- But considerable work remains to embed these principles in global financial stability analysis
 - Methodology refining Principles is needed.
 - The methodology will have to be developed with wide participation if it is to be accepted.
 - The methodology will have to be tested and refined following trials.



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