

The Benefits and Challenges of Implementation of Basel II in Europe

José María Roldán | 27 Sept 2005

CEBS

Committee of European
Banking Supervisors

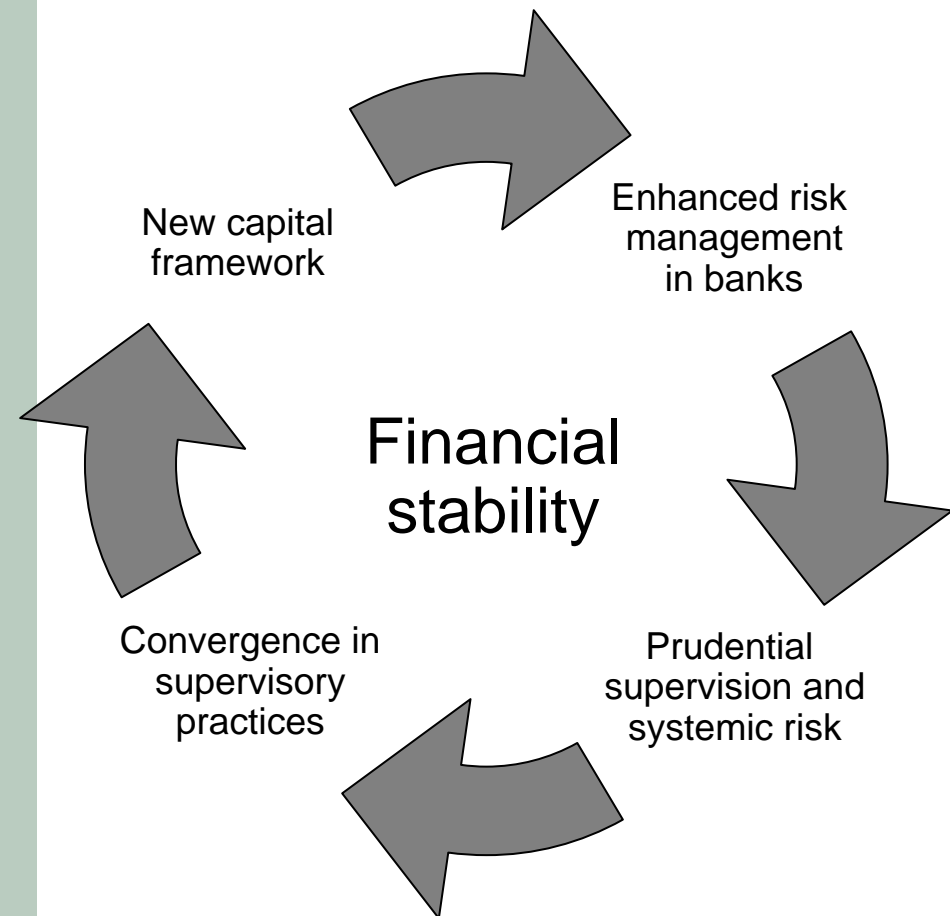
Outline

- Basel II
 - Basel II and financial stability
 - Three Pillars of Basel II = triple protection
 - Enhanced risk management => Incentives
 - Supervisory review process (Pillar 2)
- Implementation in the EU
 - Role of CEBS
 - The challenges and CEBS' response
 - Work programme
 - Publications on CRD

Basel II and financial stability

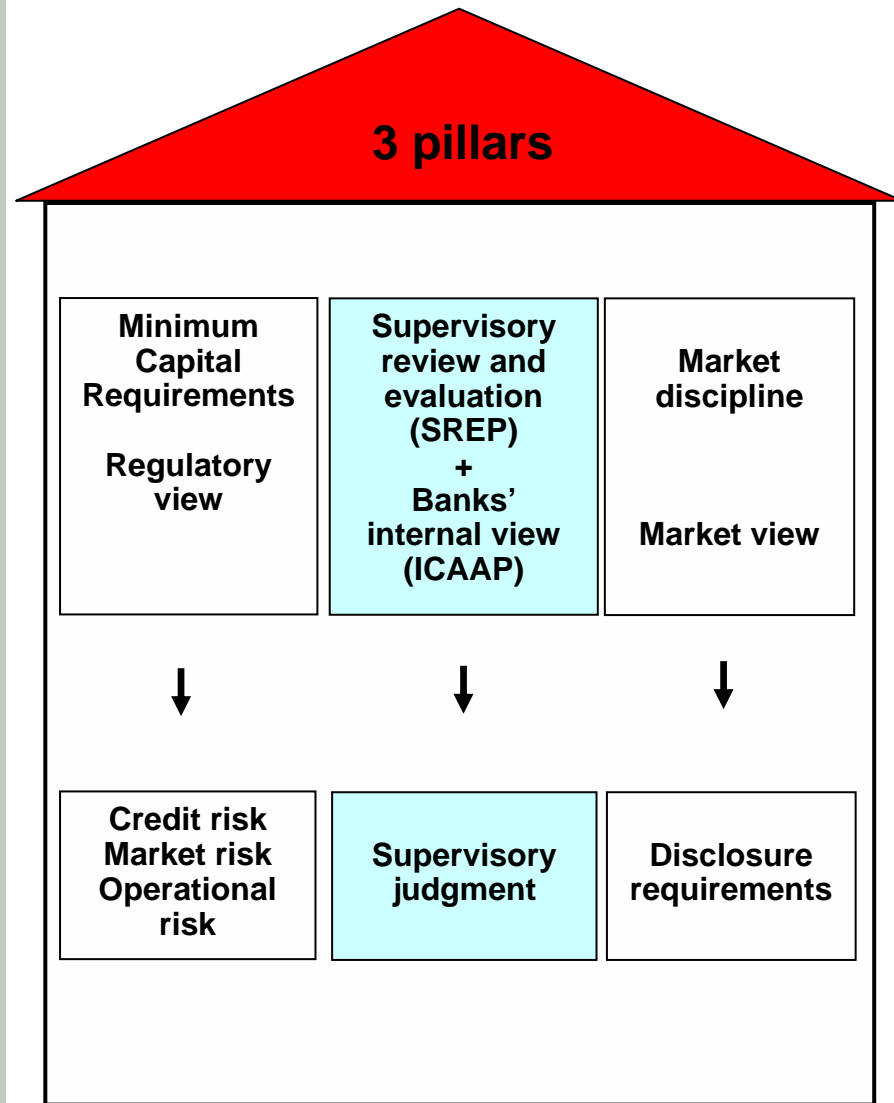
- Basel II: Rules for banks to hold sufficient capital to cover their risks and protect depositors
- Enhanced dialogue between the industry and supervisors
- A window of opportunity in promoting consistency and supervisory convergence

⇒ Level playing field
⇒ Financial stability



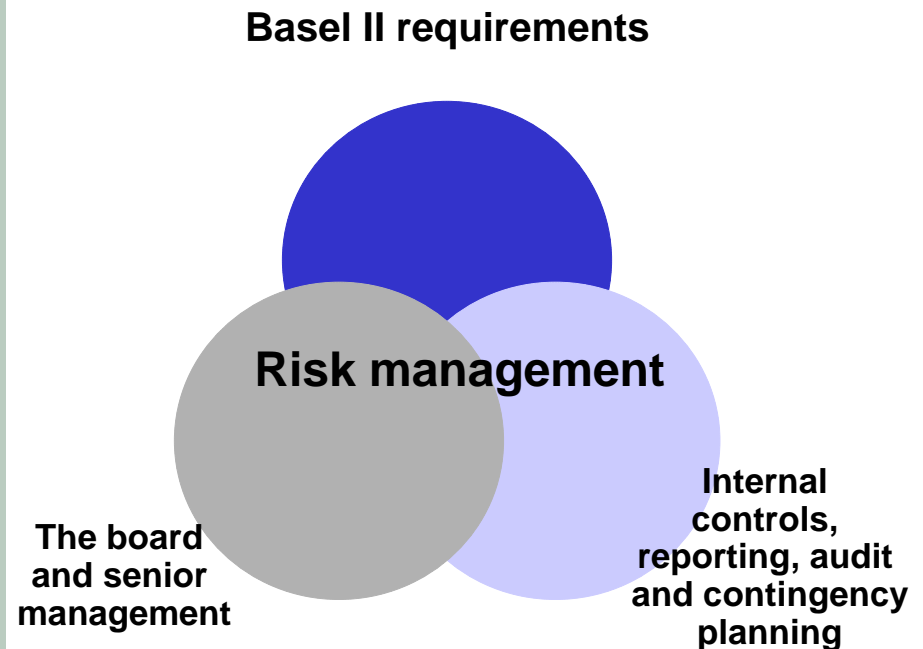
Three pillars of Basel II: triple protection

- Basel II: three pillars with checks and balances
- Each pillar has value on its own, but together they are even more potent
- Complex in detail but clear purpose and architecture
- Based on the best practices of the industry => efficient regulation from an economic perspective
- Flexible framework for small and big banks
- Suitable for emerging and developing markets



Enhanced risk management: Incentives

- Recognises and encourages developments in risk management and supervisory practices
- Incentives to adopt more sophisticated approaches
- A good business tool with business value (not just costs!)
- More than 100 countries plan to adopt Basel II



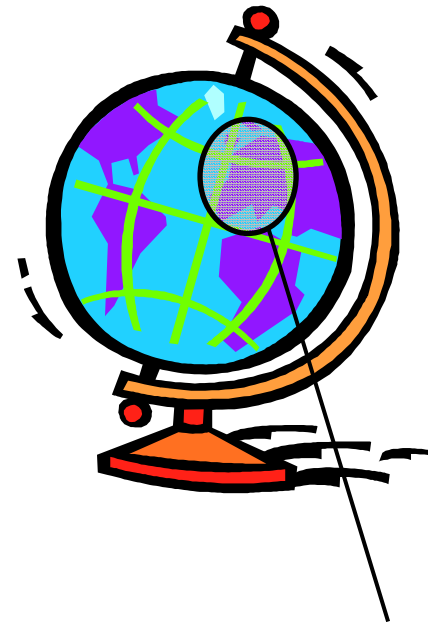
Enhanced risk management: Pillar 2

- **Supervisory review process (Pillar 2)**
- **Critical and integral part of the new capital framework**
- **Objectives of Pillar 2 are to:**
 - Ensure institutions have adequate capital to support all risks in their business
 - Encourage institutions to manage risk
 - Foster an active dialogue between institutions and supervisors

Implementation in the EU

- Legal instrument to transpose Basel II to European legislation: proposed Capital Requirements Directive (CRD).
- Legislation to implement Basel II as common framework across all 25 EU countries (and 3 EEA countries).
- Importance of the scope: The directive will apply to all **credit institutions** and **investment firms**.
- CEBS guidelines

Basel II – a global agreement



The CRD – European legislation

Implementation in the EU: Role of CEBS

- **CEBS – Committee of European Banking Supervisors**
 - Gives technical advice to the European Commission
 - Promotes consistent implementation of Community legislation and convergence in supervisory practices
 - Enhances supervisory co-operation and exchange of information
- **CEBS members have a powerful voice**
 - High level representatives of supervisory authorities and central banks
- **CEBS is a part of the legal framework in the EU**
 - Fleshing out the technical details in banking regulations
- **CEBS work affects the banking business**
 - Main tools: standards and guidelines
 - Members commit to implement on national level

The Challenges

CEBS response

Consistent implementation



Supervisory Disclosure

Convergence in supervisory practices



Common reporting requirements
Model validation
Supervisory review process

Streamlining the supervisory process for cross-border groups



Guidelines to enhance co-operation and exchange of information between authorities

Effective consultations



Dialogue and interaction with market participants and end-users, Consultative Panel

Accountability



Transparency, Annual Report, dialogue with the Parliament

CEBS' Work Programme

Priority areas of work

Regulatory advice to the Commission

- Cross-border mergers in banking
- Deposit guarantee schemes
- Own funds
- E-money

Convergence of supervisory practice

- Supervisory Review Process (Pillar 2)
- Validation of IRB and AMA systems
- External Credit Assessment Institutions (ECAIs)
- Harmonisation of reporting requirements
- Supervisory disclosure

Co-operation and information exchange

- Supervision of cross-border groups (home-host)
- Crisis management (joint with the BSC)
- Information exchange

Other areas of work

- Risks to banking stability
- Outsourcing
- Internal governance
- Impact of IFRS on prudential requirements
- The role of the audit function for prudential supervision

Cross-sectoral issues:

- Supervision of financial conglomerates
- Off-shore financial centres

Delivered products

- Advice: national discretions (work continues), prudential filters, cross-border mergers, e-money
- Consultation papers: consultation practices, outsourcing, supervisory review process, common reporting, supervisory disclosure, financial reporting, validation, ECAIs, home host

CEBS' publications on CRD

Consultation papers on:

- **Supervisory review (pillar 2)**
- **Validation (pillar 1)**
- **Common reporting**
- **Recognition of ECAs**
- **Home-host**
- **Supervisory disclosure**

All available at www.c-eps.org



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