

Implementation of the EU Banking Prudential Standards in Poland

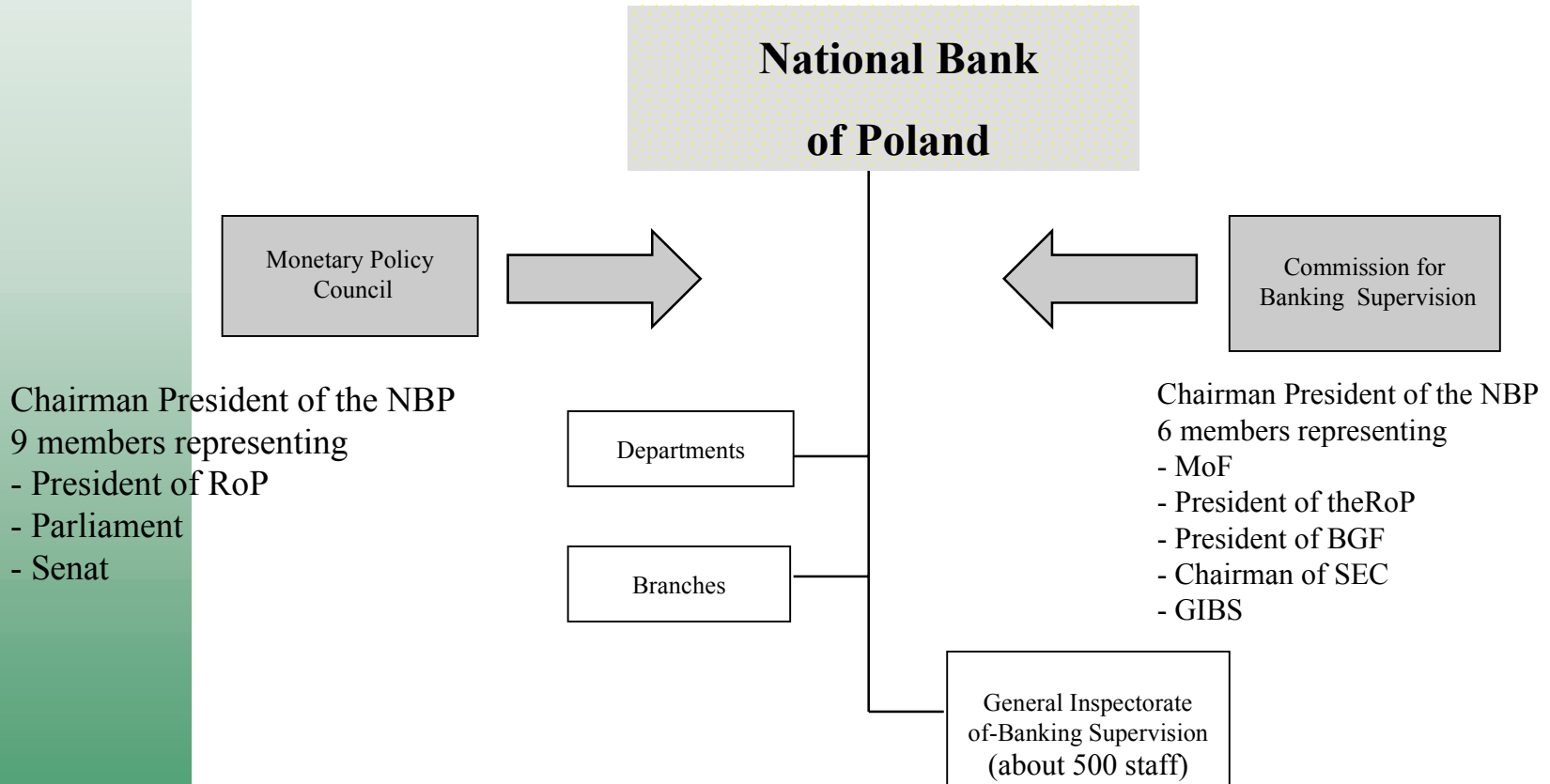
State of Art and Challenges

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Brief history

- ◆ End of 1980's - beginning of two-tier banking system:
 - independent central bank
 - sector of commercial banks
- ◆ 1997 Banking Act establishes
 - Commission for Banking Supervision (CBS)
 - Council for Monetary Policy
- ◆ January 1, 2003 - date for technical readiness for EU accession

Independence of the NBP



Other supervisory bodies

- ◆ 1991 - Securities and exchange Commission
- ◆ 1994 - Banking Guarantee Fund
- ◆ 1996 - State Office for Insurance Supervision

Banking Sector

- ◆ About 65 commercial banks (incl. 2 fully state-owned banks)
- ◆ About 600 co-operative banks (9 associations) - 2% of banking assets
- ◆ About 70% of assets controlled by foreign investors

Responsibilities

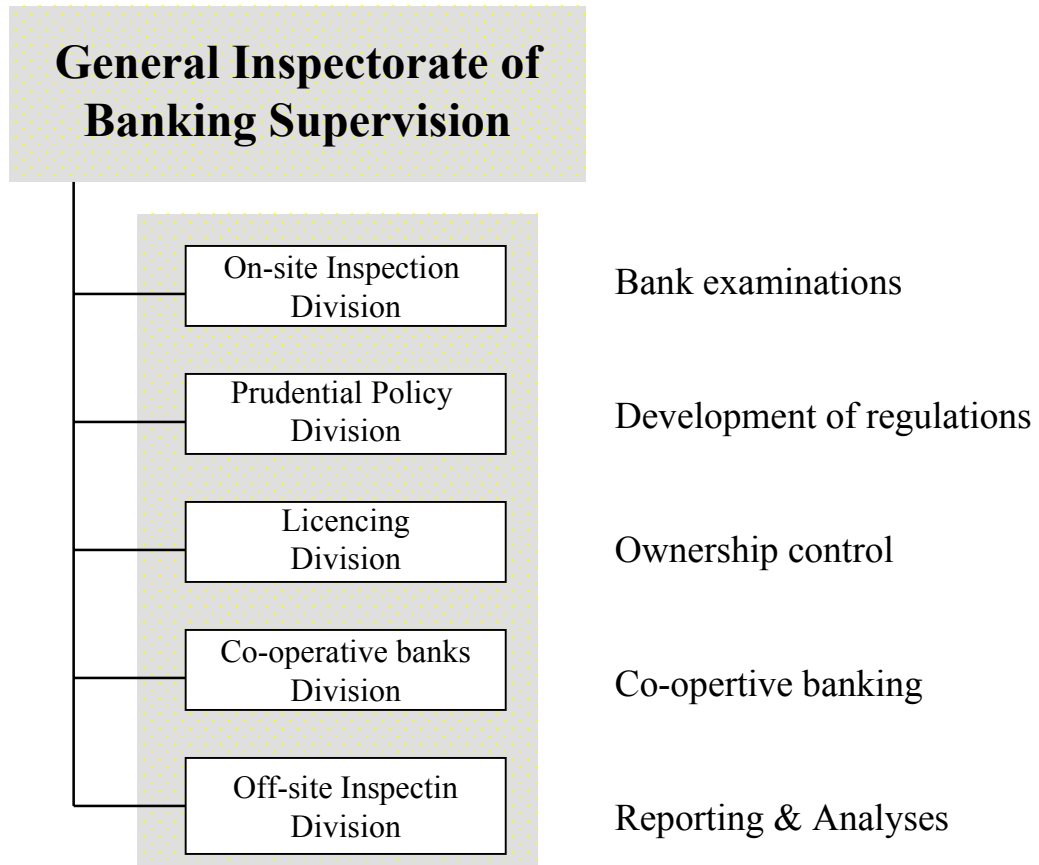
Commission for Banking Supervision

- ensure safety of funds collected by banks
- ensure compliance with law

Monetary Policy Council

- development of monetary policy goals
- NBP's interest rates
- obligatory reserve
- NBP foreign debt

Structure of the General Inspectorate of Bankong Supervision



Structure of the Supervisory Policy Division

- ◆ Legal Interpretations Section,
- ◆ Prudential Regulation Section,
- ◆ Bank Accounting Section,
- ◆ Information Technology Section, and
- ◆ Off-Site Methodology Unit
- ◆ Basle II Unit.

Legal structure

The superior law - **Banking Act**
establishes general rules of banking activities

The Commission for Banking Supervision exercises
its powers through:

- ◆ **resolutions** (quantity rules - binding)
- ◆ **recommendations** (quality rules - recommended).

Trends in regulatory work

In recent 5 years the regulatory work focused on harmonisation of the Polish banking system with European Union requirements and recommendations of Basle Committee for Banking Supervision

- ◆ implementation of international standards (Basle principles, EU Directives)
- ◆ convergence with EU banking system.

Prudential Areas:

Most of regulatory adaptations concerned

- ◆ own funds
- ◆ capital adequacy
- ◆ large exposures
- ◆ classification of assets and provisioning

Other:

- ◆ money laundering
- ◆ electronic banking
- ◆ MoUs

Own Funds

Full implementation of Directive 2000/12 (own funds) - Resolution No. 6/2001 of the CBS of Dec. 12, 2001 on banks' own funds

- ◆ deduction of intangibles according to time schedule - up to 2004

Capital Adequacy

- ◆ Until 2001 Solvency Ratio Directive implemented with some position limits for FX risk (converted into capital requirements for credit risk and FX risk in 2001)
- ◆ Internal models for FX risk allowed but lead to disadvantageous effects

2002 - Capital Adequacy Directive fully implemented (capital requirements for credit risk and full range of market risks) - Resolution No. 5/2001 of the CBS of Dec. 12, 2001, on capital adequacy of banks (fine-tuned in June, 2003)

Capital Adequacy

- ◆ Banks operate under CAD or non-Cad regime based on the scale of trading activities
- ◆ higher capital requirements to account for higher market volatility (to be reduced during 2003-2004)
- ◆ several option pricing models approved by the CBS
- ◆ internal modelling of market risk allowed - no applications by now

Large exposures

Implementation of Directive 2002/12 (large exposures) - Resolution No. 7/2001 of the CBS of Dec. 12, 2001 on banks' exposure concentration

- ◆ Exposures defined in a narrower sense - only credit exposures included (capital exposures to be included under current amendment of Banking Act)
- ◆ Measurement problems - accounting for specific reserves, purchased debt

Risk Reserves and Provisions

Reserve for general risk

- ◆ **General risk fund** - created from after-tax profit, included in own funds
- ◆ **General risk provision** - created against tax deductible costs (level restricted), not included in own funds

Provisions for specific risk

- ◆ **Specific provisions** - created against costs (partially tax deductible) for specified exposures

Specific provisions

Classification of assets based on simultaneous double criterion:

- timeliness of payment - ex post
- borrower standing - forward looking

Collateral not accounted for in classification

About 21% receivables classified as irregular

Provisioning base - eligible collateral deducted

Specific provisions - 20%, 50%, 100% of provisioning base

Specific treatment of consumer & Small Business (retail receivables) - no financial-standing criterion

CBS Recommendations

- ◆ on the system of financial liquidity monitoring (1996),
- ◆ on management of risks connected with derivative operations by banks (1997),
- ◆ on the limitation of bank's capital investment risk (1997),
- ◆ C on the management of risks connected with large exposures (1997),
- ◆ on the management of risks involved in information technology used by banks (1997),

CBS Recommendations

- ◆ on the preparation of IT systems for operation in the Year 2000 (1997),
- ◆ on the internal audit in banks (1999),
- ◆ on the management of foreign exchange risk in banks and rules connected with foreign exchange operations.
- ◆ operational risk (planned)
- ◆ electronic banking (planned)

Supervisory co-operation issues

GIBS, supported by the Legal Department of the NBP, develops:

- ◆ agreements of co-operation
- ◆ memoranda of understanding

with foreign banking supervision agencies and domestic bodies and institutions supervising functioning of financial institutions other than banks,

Accounting

The GIBS develops accounting procedures for the banking sector:

- ◆ model chart of accounts
- ◆ valuation rules
- ◆ implementation of international standards

Accounting principles introduced through CBS Resolutions (until 2001)

Accounting regulations

- ◆ Since the beginning of 2002 the secondary legislation related to the Act on Accountancy is issued by the MoF
- ◆ The drafts, if requested by the MoF, are prepared by the Division and approved by the CBS
- ◆ According to the Law on Accountancy the final drafts are submitted by the MoF to the CBS for formal opinion

Secondary legislation issued by the MoF

- ◆ Procedures for provisioning against the risk of banking operations (specific provisions)
- ◆ Detailed accounting principles of banks
- ◆ Definition of the model chart of accounts for banks
- ◆ Principles concerning consolidated financial statements of financial holdings

Analytical Tools

- ◆ Banking supervisor has to identify existing and future risks and threats in a particular bank and in the banking sector.
- ◆ GIBS developed some analytical tools

The Tools

- ◆ BIS Database (Bank Statistical Information)
- ◆ UBPR (Uniform Bank Performance Report)
- ◆ Supervisory Profile (including Executive Summary)
- ◆ CAMEL and CAEL supervisory rating systems
- ◆ Large Exposures database

Consolidated Supervision

- ◆ Banking Law - general rules
- ◆ Law on accountancy - cons. financial stat.
- ◆ CBS regulations - cons. prudential limits
- ◆ reporting system - cons. reports

Future tasks

Implementation of Basle II (CAD III)

- ◆ new Basle II unit established
- ◆ participation in consultation process
- ◆ co-operation with the sector and the Polish Bankers Association

Further MoUs to be signed

Status of foreign banks subsidiaries in Poland after accession

See You!

- ◆ The Polish banking supervisors do not expect their life will be easier in the EU environment
- ◆ Nevertheless,
See you in Europe on May 1st, 2004!