Basel Committee on Banking Supervision

Consultative document

Core principles for effective banking supervision

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Dr. Axel Sauer – comments 13th September 2023

Dr. Axel Sauer does permit to publish these comments on the Bank for International Settlements' website.

Introduction

Humans are not capable to make **reliable forecasts,** and it is for humans not possible - **to valid** or to **verify a theory by tests**, **or by observations**. Decision makers approximations, **forecasts** and other prognosis are and will remain guesses - even when highly correlated with decision makers experiences from the past (i.e., déjà vu), and decision makers common sense that these forecasted events did and might again impact - positively or negatively, expected model, theory or concept outcomes.

I am showing, with reference to Mr. Karl R. Popper - "**the need for the falsifiability or testability criterion as a criterion of the empirical character of scientific theories"** (See, Popper, Karl R. 1968. *Conjectures and refutations: the growth of scientific knowledge*. New York, NY: Harper & Row, Chapter 10, p. 249), by comparing **existential statements** which are **formulated in purely empirical terms** (i. e., *on-site work is a tool to obtain independent verification, or the natural rate of interest as a purely notional and unobservable variable)*. That **"empirical evidence can never refute an almost logically true existential statement** (like *on-site work is a tool to obtain independent verification,* or *the natural rate of interest as a purely notional and unobservable variable)*, **but that it** (*on-site work is a tool to obtain independent verification,* or *the natural rate of interest as a purely notional and unobservable variable)* **can** *never reduce its probability.* … **So, the empirical probability or degree of empirical confirmation** (in Carnap's sense) **of our statement about** (i.e., *on-site work is a tool to obtain independent verification,* or about *the natural rate of interest as a purely notional and unobservable variable, ….*) **must forever remain equal to unity, whatever the facts may be."** (See Popper. 1968. Chapter 10, p. 249.)
For the empirical probability or degree of empirical confirmation of i.e., *the natural rate of interest,* I do refer to Mr. John C. Williams, President and Chief Executive Officer of the Federal Reserve Bank of New York, thoughts; "The idea of a natural rate of interest has been around ever since the Swedish economist Knut Wicksell wrote about it in 1898. Early on, it was recognized that it's not something that can be directly observed or measured. As the economist John H. Williams wrote in 1931: "The natural rate is an abstraction; **like faith**, it is seen by its works. One can only say that if the bank policy succeeds in stabilizing prices, the bank rate must have been brought in line with the natural rate, but if it does not, it must not have been." (See John H. Williams. "The Monetary Doctrines of J. M. Keynes," *The Quarterly Journal of Economics* 45, no. 4 (August 1931): 547 – 587.)
And Mr. John C. Williams, continued; "The topic gained renewed relevance in 1993, following John Taylor's famous description of a monetary policy rule that incorporated an assumption of **a natural rate of 2 percent.** (See, John B. Taylor.

"Discretion versus Policy Rules in Practice", *Carnegie-Rochester Conference Series on Public Policy,* Vol. 39 (December 1993), pp. 195 – 214.)

For policymakers, the natural questions—pardon the pun—were: Is 2 percent the right number? Does it change over time? And how would we know? Those were the very questions than then-Federal Reserve Governor Larry Meyer posed to Board staff back in 2000. And that's what brought Thomas and me (Mr. John C. Williams) together. On December 14, 2000, after a few short months of working together, we wrote our ideas and results in a memo to the Board of Governors. The memo started with the bold declaration: "This memo is a first report on a broader project to study alternative definitions and estimates of the equilibrium real rate (R*) and to evaluate their usefulness in the conduct of monetary policy." (See, Thomas Laubach and John C. Williams. Estimates of a Time-varying Equilibrium Real Federal Funds Rate. Memo to the Board of Governors of the Federal Reserve System, December 14, 2000.)

Let me (Mr. John C. Williams) conclude by sharing something I learned from Thomas and hold dear. It's actually hidden in the last line of the abstract from our first published paper. It says: "***Estimates** of the natural rate of interest, however, **are very imprecise** and subject **to real-time measurement error**.*" (See Thomas Laubach and John C. Williams. "Measuring the Natural Rate of Interest," *Review of Economics and Statistics* 85, no.4 (November 2003): 1063-70.)

To some, that may sound like a negative statement. But it's also what makes **empirical research** so exciting and challenging. There is no one right answer and no single way to view the world. **Empirical research is a process of continuous learning and adaptation—fueled by perseverance**. People come up with different approaches, and we learn from all of them." (See, Williams, John C. 2023. *Measuring the Natural Rate of Interest: Past, Present, and Future,* speech by John C. Williams, President and Chief Executive Officer of the Federal Reserve Bank of New York, at the Thomas Laubach Research Conference, Board of Governors of the Federal Reserve System, Washington, DC, May 19, 2023, page 4.)

However, when according to Mr. John C. Williams - empirical research is a process of continuous learning and adaptation, I want call this process – trial and error. And, if our i.e., banks supervisor and Central Banks employees empirical research does rely on trial and error, there is no need for a process fueled by perseverance. If we i.e., banks supervisor or Central Banks employees, do **fail** on our empirical research by tests, we should not "continue in a course of action". If we do **not fail** on our empirical research by tests we should continue with our tests "in spite of difficulty or little indication of success." (See, Williams, John C. 2023. *Measuring the Natural Rate of Interest: Past, Present, and Future,* speech by John C. Williams, President and Chief Executive Officer of the Federal Reserve Bank of New York, at the Thomas Laubach Research Conference, Board of Governors of the Federal Reserve System, Washington, DC, May 19, 2023.)

This said, the author of this note does take into consideration; "there will be well-testable theories, hardly testable theories, and **non-testable theories**. Those which are non-testable **are of no interest to empirical scientists**. They may be described as metaphysical." (See, Popper, Karl Raimund. 1968. *Conjectures and refutations: the growth of scientific knowledge*. New York, NY: Harper & Row. Chapter 11, p. 257.)

Therefore, we banks supervisor and central bank employees, should take testing results out of well-testable and hardly testable banks business activities or Central Banks forward – looking policymaking and forecasting "*as scientific only if it* (banks business activities and Central Banks forecasting) *makes assertions* (i.e., there is on banks business activities always a fair value or market price (>0) achievable for each human decision maker and financial markets participant) *which may **clash with observations**; and a system* (i.e., banks risks analysis's on business activities, Central Banks scenario analysis on forward – looking policymaking and forecasting) *is, in fact, tested by attempts to produce such clashes, that is to say by attempts to refute it. Thus, **testability is the same as refutability**, and can therefore likewise be taken as a criterion of demarcation. **Only if** a theory* (i.e., about banks testable business activities, Central Banks forward – looking policymaking and forecasting) *successfully **withstands the pressure** of … attempted **refutations can we*** (i. e., banks supervisor or Central Bank employees) ***claim that it*** (i.e., banks business activities, Central Banks forward – looking policymaking and forecasting) ***is confirmed or corroborated by experience** or by **results** which **do reject it.**"* (See, Popper. 1968. Chapter 11, p. 256.)

For cases which are ***confirmed or corroborated by experience** or by **results** which **do reject it***, I am referring to Ms. Christine Lagarde, President of the European Central Bank, speech at the Distinguished Speakers Seminar organized by the European Economics & Financial Center, London, 4 September 2023;
"**An increasingly uncertain world** makes the task of public institutions (*i.e., the European Central Bank*) harder, especially when it comes to forecasting. And we (*the ECB employees*) **need to explain** this better to the wider public – **what we** (*the ECB member*) **can and cannot know**, and what it will take to continue delivering on our mandates in this environment". (See, Lagarde, Christine, 2023. '*Communication and monetary policy*', speech by Lagarde, Christine, President of the European Central Bank, at the Distinguished Speakers Seminar organized by the European Economics & Financial Center, London, 4 September 2023. Page 5.)

And Ms. Lagarde continues; "**Humility in how we** (*the ECB employees*) **communicate is key to fostering trust.** To rebuild confidence in expert institutions, we (*the ECB employees*) need to do a better job of **conveying the uncertainty we** (*the ECB employees*) **face** and the inherent challenge **in conducting forward-looking policymaking** in this environment. That means being

open about the limits of what we (*the ECB employees*) know, the areas where we (*the ECB employees*) have missed the mark, and what we (*the ECB employees*) are doing about it.
Right now, it is important for us (*the ECB employees*) to acknowledge that, like other central banks, we (*the ECB employees*) underestimated both the dynamics of inflation and its persistence. But we (*the ECB employees*) have been making changes to our forecasting process to address these issues. For example, we (*the ECB employees*) have published sensitivity analysis of key variables (*which … clash with observations?)* like energy prices and wages, and we (*the ECB employees*) used *(a system?)* scenario analysis during the pandemic and after the Russian invasion of Ukraine.
We (*the ECB employees*) are also aiming to be more transparent in accounting for our forecast errors (*as there are "well-testable theories, hardly testable theories, and* ***non-testable theories****?)*. Even if these errors were to deplete trust, we (*the ECB employees*) can mitigate this if we (*the ECB employees*) talk about forecasts in a way that is both more contingent and more accessible, and if we (*the ECB employees*) provide better explanations for those errors." (See, Lagarde, Christine, 2023. '*Communication and monetary policy'*, London, 4 September 2023., p. 5.)
And, as it is for empirical science i.e., on bank risks analyses on business activities, or Central Bank forecasting, "trust wise" helpful - to distinguish by using *a criterion of demarcation,* between *well-testable theories, hardly testable theories, and* ***non-testable theories****"*, particular as "***testability is the same as refutability"****,* empirical science on i.e., risk analysis or forecasting, *should not use or work with "****non-testable theories****. … which* ***are of no interest to empirical scientists****.*" (See, Popper. 1968. Chapter 11, p. 257.).

Comments on consultative document - Core principles for effective banking supervision

Introduction to the Core Principles

Explanation of certain terms used in the Core Principles

10.1 (14) On-site work: ~~is a tool to obtain independent verification~~ (**Delete and replace by** "is applying empirical tests on bank's processes and procedures to obtain that bank's processes and procedures are confirmed or corroborated by experience or by results which do reject") that adequate policies, procedures and controls exist at banks, to determine that information reported by banks is reliable, to obtain additional information on the bank and its related companies that is needed for the assessment of the condition of the bank, to monitor the bank's follow-up on supervisory concerns etc.

Note to 10.1 (14) On-site work; Results out of empirical tests on banks processes and procedures are only confirmed or corroborated by experience, when on-site supervisor does work with i. e. un-rejectable, non-empirical and therefore metaphysical tools or theories. However, as empirical evidence can never refute an almost logically true un-rejectable, non-empirical, metaphysical also called existential statement i. e., there is – a tool applied by On-site supervisor which provides independent verification, this tool "can never reduce its probability. … So, the empirical probability or degree of empirical confirmation (in Carnap's sense)" of our statement about On-site supervision as a tool to obtain independent verification, "must forever remain equal to unity, whatever the facts may be." (See, Popper Chap. 10 p. 249.)
This said, we the market solutions promoting On-site supervisor should take into consideration; "there will be well-testable theories, hardly testable theories, and **non-testable theories**. Those which are non-testable i.e., the tool to obtain independent verification, **are of no interest to empirical scientists**. They may be described as metaphysical." (See, Popper. 1968. Chapter 11, p. 257.)

Therefore, we the On-site supervisor and market solutions promoter aiming to mitigate risk (financial losses) out of banks processes and procedures, should take testing results out of well-testable banks business processes and procedures and hardly testable banks business processes and procedures) "*as scientific only if it* (the testable banks business processes and procedures) *makes assertions* (i.e., there is on banks business activities defined by processes and procedures always i.e., a fair value or market price achievable for each human decision maker and financial markets participant) *which may clash with observations; and a system* (i.e., banks business processes and procedures) *is, in fact, tested by attempts to produce such clashes, that is to say by attempts to refute it. Only if a theory* (i.e., about banks testable business processes and procedures) *successfully withstands the pressure of … attempted refutations can we* (i. e., the banks on-site supervisor) *claim that it* (bank's business processes and procedures) *is confirmed or corroborated by experience* **or** by results which do reject it*."* (See, Popper. 1968. Chapter 11, p. 256.)

Principle 10 – Supervisory reporting

40.23 Principle 10:[17] "The supervisor collects, reviews and analyses prudential reports and statistical returns [18] from banks on both a solo and a consolidated basis, and independently ~~verifies~~ (**Replace by**, "is applying empirical tests on banks reports and statistical returns to obtain that it (bank's reports and statistical returns) is confirmed or corroborated by experience or by results which do reject") these reports through either on-site examinations or use of external experts".

40.24 Essential criteria: (3) "The supervisor requires banks to have sound governance structures and control processes for methodologies that produce valuations. The measurement of fair values maximizes the use of relevant and reliable inputs which are consistently applied for risk management and reporting purposes. (**Delete;** ~~The valuation framework and control procedures are subject to adequate independent validation and verification either internally or by an external expert.)~~ The supervisor assesses whether the valuation used for regulatory purposes is reliable and prudent. Where the supervisor determines that valuations are not sufficiently prudent, the supervisor requires the bank to adjust its reporting for capital adequacy or regulatory reporting purposes".

Note to 40.24 (3); Delete; ~~The valuation framework and control procedures are subject to adequate independent validation and verification either internally or by an external expert.~~ Regardless of the underlying i.e., valuation framework and control procedures, by assuming to be in the mind of supervisor an item or subject to adequate independent validation and verification either internally or by an external expert, this assumption will not and cannot prevent that supervisor do examine "whether the valuation used for regulatory purposes is reliable and prudent", by untestable, non-empirical and therefore metaphysical theories which should be "**of no interest to empirical scientists**." (See, Popper. 1968. Chapter 11, p. 257.)

However, as banks supervisor might identify themselves as empirical scientists they should claim – "*only if a theory* (i.e., about a bank's testable valuation framework and control procedures) *successfully withstands the pressure of … attempted refutations can we* (i. e., the banks supervisor) *claim that it* (bank's testable valuation framework and control procedures) *is confirmed or corroborated by experience* (to be reliable and prudent) ***or*** *by results which do reject it."* (See, Popper. 1968. Chapter 11, p. 256.)

A bank's supervisor is not capable to make reliable validation and verification i.e., on bank's testable valuation framework and control procedures, as bank's supervisor is always facing the risk that there might be a test result which does reject i.e., a bank's valuation framework or control procedure. And therefore, is it, i.e., for supervisor, not possible - **to valid** or **to verify** a testable valuation framework and control procedure by tests, or by observations.

40.24 Essential criteria: (8) "The supervisor utilizes policies and procedures to determine ~~the validity~~ (**Replace by;** "bank's testable valuation framework and testable control procedures") and integrity of supervisory information. This includes a Programme for ~~the periodic verification~~ (**Replace by**, "periodically tests of banks valuation framework and control procedures aiming to attempt refutation") of supervisory returns by either the supervisor's own staff or by external experts.

Note to 40.24 (8); "*Only if a theory* (i.e., a Programme for bank's testable valuation framework and testable control procedures) *successfully withstands the pressure of … attempted refutations can we* (i. e., the banks supervisor) *claim that it* (the bank's testable valuation framework and testable control procedure) *is confirmed or corroborated by experience* (to be reliable and prudent) ***or*** *by results which do reject it."* (See, Popper. 1968. Chapter 11, p. 256.)

Principle 15 – Risk management process

40.34 Essential criteria: (6) "Where banks use models to measure components of risk, the supervisor determines that the following conditions are met:
(a) banks comply with supervisory standards on the use of models;
(b) the banks' boards and senior management understand the limitations and uncertainties relating to the output of the models and the risk inherent in their

use; and
(c) banks perform regular and independent ~~validation and testing of the~~ (**Replace by**, "through empirical testing of their") models.

In addition, the supervisor assesses (**Amend;** "and has to make a decision") whether the model outputs appear reasonable as a reflection of the risks assumed."

Note to 40.34 (6); A bank's supervisor is not capable to make reliable validation or verification i.e., on bank's testable models, as bank's supervisor is always facing the risk that there might be a test result which does reject i.e., a bank's model output as a not reasonable result of the risks assumed. And, it is, i.e., for supervisor, not possible - **to valid** or **to verify** risks assumed by the model, by comparing these risks with model test results or observations as reasonable, or justifiable result of the risks assumed by the model.

The supervisor has **to make a decision** whether the model outputs appear reasonable or justifiable as a reflection of the risks assumed.

Principle 18 – Problem exposures, provisions and reserves

40.42 Essential criteria: (4) "The supervisor determines that banks have adequate and appropriate policies, processes, methodologies and organizational resources for establishing provisions and write-offs. The supervisor determines that policies, processes and methodologies for the measurement of provisions are appropriate defined (**Delete;** ~~to ensure~~) that provisions and write-offs are timely and reflect ~~realistic~~ (**Replace** by "testable") repayment and recovery expectations and, where relevant, include ~~appropriate~~ (**Replace** by "testable") expectations about future credit losses based on ~~reasonable~~ (**Replace** by "testable") appropriate (**Delete;** ~~and supportable~~) information. (**Delete;** "~~The supervisor determines that banks' credit loss provisions and write-off methodologies and levels are subject to an **effective** review and **validation** process conducted by **a function** independent of the relevant risk-taking function".)~~

Note to 40.42 Essential criteria: (4); The **effective** review and **validation** process does become a metaphysically statement if supervisors have to **assume** or have to make it to "**a matter of faith**" there is on the **validation** process, conducted by supervisor or banks risk manager or compliance officer, **a function**, a system, a concept, **independent of the** relevant **risk-taking function**.

Principle 23 – Interest rate risk in the banking book

40.53 Essential criteria: (3) "The supervisor determines that banks' policies and processes establish an appropriate and properly controlled interest rate risk environment, including:

(a) comprehensive and appropriate interest rate risk measurement systems;

(b) a regular review and ~~independent~~ (**Replace by**, "independently") (internal or external) ~~**validation**~~ (**Replace by**, "applied tests") of any models used by the functions tasked with managing interest rate risk (including a review of key model assumptions, e.g., regarding optional elements embedded in a bank's assets, liabilities and (**Delete**;~~/or,~~ and **insert**; "all") off-balance sheet items, in which the bank or its customer can alter the level and timing of their cash flows);

(c) appropriate limits, approved by the banks' boards and senior management, that reflect the banks' risk appetite, risk profile and capital strength and that are understood by and regularly communicated to relevant staff;

(d) effective exception tracking and reporting processes which ensure prompt action at the appropriate level of the banks' senior management or boards, where necessary; and

(e) effective information systems for the accurate and timely identification, aggregation, monitoring and reporting of interest rate risk exposure to the banks' boards and senior management."

Note to 40.43 Essential criteria: (3); A bank's supervisor is not capable to make reliable independent (internal or external) **validation** by tests of any model used by the banks senior manager and staff to manage interest rate risk. Bank's supervisor cannot - **valid** or **verify** a model by tests, or by observations. However, *"only if a theory* (i.e., on banks testable models to manage interest rate risks out of business activities) *successfully withstands the pressure of … attempted refutations can we* (i. e., banks supervisor, or banks senior manager and staff) *claim that it* (i.e., banks model to manage interest rate risk) *is confirmed or corroborated by experience or by results which do reject it."* (See, Popper. 1968. Chapter 11, p. 256.)

Principle 24 – Liquidity risk

40.55 Essential criteria: (4) "The supervisor determines that banks' liquidity strategy, policies and processes establish an appropriate and properly controlled liquidity risk environment, including:

(a) clear articulation of an overall liquidity ~~risk appetite~~ (**Replace by;** “planning in banks relevant currencies”) that is appropriate for the banks’ business and their role in the financial system, and that is approved by the banks’ boards;

(b) sound ~~day-to-day~~ (**Replace by**; “hour-to-hour”) intraday liquidity risk management practices;

(c) effective information systems to enable active identification, aggregation, monitoring and control of liquidity risk exposures and funding needs (including active management of collateral positions) bank-wide;

(d) adequate oversight by the banks’ boards to ensure that management effectively implements policies and processes for the management of liquidity risk (**Delete;** ~~in a manner consistent with the banks’ liquidity risk appetite~~); and

(e) regular review by the banks’ boards (at least annually) and appropriate adjustment of the banks’ strategy, policies and processes for the management of liquidity risk in the light of the banks’ changing risk profile and external developments in the markets and macroeconomic conditions in which they operate.

Note to 40.55 Essential criteria: (4) Banks liquidity has to be monitored hourly by banks treasury staff, operating in regard to outgoing payments (incoming payments are not manageable) within board approved and predefined liquidity, limits and buffers in all relevant currencies for outgoing payments. And therefore, is for banks treasury staff - managing outgoing payments, no space for any liquidity risk appetite, without entering into a liquidity risk scenario what can jeopardize banks liquidity reputation, and might be capable to trigger a “bank run”.

40.55 Essential criteria: (7) “The supervisor requires banks to include a variety of short-term and protracted bank specific and market-wide liquidity stress scenarios (individually and in combination), using conservative and regularly reviewed assumptions, into their stress-testing programmes for risk management purposes. The supervisor determines that the results of the stress tests are used by the bank to adjust its liquidity risk management strategies, policies and positions and to develop (**Delete;** ~~effective~~) contingency funding plans.”

Note to 40.55 Essential criteria: (7) There is **or** is not - sufficient liquidity for outgoing payments, as incoming payments are not manageable by banks treasury staff. There is **no symmetry** between incoming and outgoing payments, what has to be reflected by banks treasury staff **liquidity planning** in all relevant currencies, and by banks treasury staff applied **liquidity stress scenarios** in each relevant currency, and by banks treasury staff applied (board approved) **liquidity buffer** (i.e., securities sellable at markets or pledged at the Central Bank) in each for the bank relevant currency. These, by banks treasury staff applied (board approved) measures **liquidity planning, liquidity stress scenarios** and **liquidity buffer** should make it for banks supervisor very clear - there is **no space for any liquidity risk appetite**.

Principle 25 – Operational risk and operational resilience

40.56 Principle 25:[64] "The supervisor determines that banks have an adequate operational risk [65] management framework and operational resilience [66] approach that considers their risk profile, risk appetite, business environment, tolerance for disruption to their critical operations,[67] and emerging risks. This includes prudent policies and processes to: (i) identify, assess, evaluate, monitor, report and control or mitigate operational risk on a timely basis; and (ii) identify and protect themselves from threats and potential failures, respond and adapt to, as well as recover and learn from, disruptive events to minimise their impact (Should be **endorsed** by supervisor;) on delivering critical operations through disruption".

40.57 Essential criteria: (4) "The supervisor determines that banks develop and implement (**Insert;** "an empirically testable") response and (**Insert;** "empirically testable") recovery plans to manage incidents that could disrupt the delivery of critical operations in line with the bank's risk appetite and tolerance for disruption and that they continuously improve their (**Insert;** "empirically testable")incident response and (**Insert;** "empirically testable") recovery plans (**Delete;** ~~by incorporating the lessons learnt from previous incidents~~".

Note to 40.57 Essential criteria: (4) Incorporating "lessons learnt from previous incidents" by, at banks for operational risk responsible staff, will be only possible when banks staff is working with empirically testable recovery plans, or empirically testable prudent policies and processes which, on testing "*successfully withstands the pressure of … attempted refutations can we* (i. e., the banks supervisor) *claim that it* (bank's testable recovery plan, or bank's empirically testable prudent policies and processes) *is confirmed or corroborated*

by experience (trial and error or lessons learnt) ***or*** *by results which do reject it."*
(See, Popper. 1968. Chapter 11, p. 256.)

Principle 26 – Internal control and audit

40.60 Essential criteria: (1) "Laws, regulations or the supervisor require banks to have internal control frameworks that are adequate to establish a properly controlled operating environment for the conduct of their business, considering their risk profile with a forward-looking view".**[74]**

Footnotes
[74] "The time horizon for establishing a forward-looking view should ***(Delete;*** *~~appropriately~~* ***(and replace by;*** *"distinguish between well-testable theories, hardly testable theories, and* ***non-testable theories*** *to") reflect climate-related financial risks and emerging risks as needed".*

Note to footnote (74). The footnote will be classified by i.e., banks risk manager as un-rejectable, not empirically testable, and un applicable statement about *a forward-looking view on banks climate-related financial risks and emerging risks.* Therefore, the *forward-looking view on climate-related financial risks and emerging risks* has to be reviewed and reformulated. On the reviewing process will it for empirical scientists be helpful - to distinguish *on climate-related financial risks and particular on emerging risks,* between - *well-testable theories, hardly testable theories, and* ***non-testable theories.*** Empirical science should **not** work on *climate-related financial risks and emerging risks analysis or forecasting* with *"**non-testable theories**. … which **are of no interest to empirical scientists**.*"
(See, Popper. 1968. Chapter 11, p. 257.).

Principle 27: Financial reporting and external audit

40.62 Essential criteria: (3) "The supervisor determines that banks use valuation practices consistent with accounting standards widely accepted internationally. The supervisor also determines that the framework, structure and processes for fair value estimation are subject to independent ***(Delete;*** ~~verification and validation~~ ***(and replace by;*** "empirical tests"), and that banks document any significant differences between the valuations used for financial reporting purposes and for regulatory purposes".

Principle 28 – Disclosure and transparency

40.65 Essential criteria: (2) "The supervisor determines that the required disclosures include both qualitative and quantitative information on a bank's financial performance, financial position, risk management strategies and practices, risk exposures, aggregate exposures to related parties, transactions with related parties, accounting policies, business models, management, governance and remuneration. The scope and content of the information provided and the level of disaggregation and detail are ***(Delete;*** ~~commensurate~~ ***(and replace by;*** "corresponding in size and degree") with the risk profile and systemic importance of the bank. At least for internationally active banks, disclosure requirements are not less stringent than the applicable Basel standards.

Principle 29 – Abuse of financial services

40.67 Essential criteria: (5) "The supervisor determines that banks establish CDD policies and processes that are well documented and communicated to all relevant staff. The supervisor also determines that such policies and processes are integrated into the bank's overall risk management and includes appropriate steps to identify, assess, monitor, manage and mitigate the risks of money laundering, terrorist financing and proliferation financing with respect to customers, countries and regions, as well as to products, services, transactions and delivery channels on an ongoing basis. The CDD management programme, on a groupwide basis, has as its essential elements:

(a) a customer acceptance policy that identifies business relationships that the bank will not accept (or will be terminated) based on identified risks;

(b) an ongoing customer identification, ~~verification~~ (**Delete;** verification) and due diligence programme, which ~~encompasses verification~~ (**Replace by;** "include comprehensively"; **delete;** ~~of~~) beneficial ownership, understanding the purpose and nature of the business relationship, and risk-based reviews to ensure that CDD information is updated and relevant;"

Structure and guidance for assessment reports prepared by the International Monetary Fund and the World Bank

99.15 "Assessors may also include "comments" where they find particularly good practices or rules in some field that might serve as examples and best practice to other countries. Planned initiatives aimed at amending existing or adopting new regulations and practices but which are not yet in effect can receive favourable mentions in this section. Recent legislative, regulatory or supervisory initiatives for which implementation could not be ***(Delete;*** ~~verified~~ ***(and replace by;*** "identified"*)* should be mentioned in this section as well."

99.20 "The seventh section comprises a "recommended actions" table providing principle-by-principle recommendations for actions and measures to improve the regulatory and supervisory framework and practices. This section should list the suggested steps for improving the compliance and overall effectiveness of the supervisory framework. Recommendations should be proposed on a prioritised basis in each case where deficiencies are identified. The recommended actions should be specific (**Delete;** ~~in nature~~). An explanation could also be provided as to how the recommended action would assist in improving the level of compliance and strengthening the supervisory framework. The institutional responsibility for each suggested action should also be clearly indicated to prevent overlaps or confusion. Recommendations can also be made regarding deficiencies in compliance with the additional criteria and to principles which are fully compliant but where supervisory practice can still be improved. The table should indicate only those principles for which specific recommendations are being made. The template for the recommended actions is as follows."

References

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