The Basel Core Principles – Executive Summary

The *Core principles for effective banking supervision* (CPs) are the minimum global standards for the sound prudential regulation and supervision of banks. Initially published in 1997, and updated in 2006 and 2012, they contain 29 principles. All are universally applicable, partly because the CPs embed the concept of proportionality, thus accommodating a range of banking systems and a broad spectrum of banks (from large internationally active banks to small, deposit-taking institutions).

Prudential authorities use the CPs as a benchmark to assess the quality of their regulatory and supervisory frameworks and to help inform future work priorities. They are also used by the International Monetary Fund and the World Bank to evaluate the effectiveness of countries' systems of banking supervision as part of their Financial Sector Assessment Program. This Executive Summary outlines the preconditions needed for effective supervision and the 29 CPs that are deemed essential to support a sound supervisory system.

Preconditions for effective banking supervision

The CPs identify six preconditions that can have a bearing on the conduct of supervision. While these preconditions are generally outside the control of supervisory authorities, supervisors should work with the government and applicable organisations to address any identified concerns.

Preconditions	Implications for supervision
Sound and sustainable macroeconomic policies	Without sound macroeconomic (mainly fiscal and monetary) policies, imbalances may arise and affect the stability of the financial system.
A well established framework for financial stability policy formulation	An assessment of risks to the financial system as a whole complements the work of microprudential authorities.
A well developed public infrastructure	If the public infrastructure is not well developed, it can contribute to the weakening of financial systems. For example, if the external audit profession is not independent, it can have a bearing on the integrity of banks' published financial statements.
A clear framework for crisis management	Effective crisis management frameworks help to mitigate potential disruptions to financial stability arising from failing or troubled banks.
An effective level of systemic protection	An effective level of systemic protection (eg deposit insurance) promotes confidence in the banking system and limits any contagion from banks in distress.
Effective market discipline	Market participants' assessment of a bank's risk profile supplements the work of prudential supervisors. Effective market discipline depends on the timely, accurate and meaningful flow of information to market participants.

Powers, responsibilities and functions of supervisors (CPs 1–13)

Principles 1–13 focus on what supervisors themselves do, covering their powers, responsibilities and functions. Within this group, CPs 1–7 deal with the legal and regulatory powers and institutional setup needed to properly licence, oversee and intervene against banks. Meanwhile, CPs 8–13 address various aspects of on- and off-site supervision.

Core Principles	Key elements	Rationale
1–3 **Powers, independence and cooperation**	• Supervisory authority has powers to license banks, set and enforce rules, conduct supervision and take action. • The operational independence and legal protection of the supervisor are prescribed in law. • Laws, regulations or other arrangements provide a framework for cooperation with relevant domestic and foreign authorities.	• Insufficient legal powers inhibit the conduct of effective supervision. • The lack of independence, resources or sufficient legal protection can undermine effective supervision. • Cooperation agreements are critical to supervising banks that operate in different domestic financial sectors or across borders.
4 **Permissible activities**	• The permissible activities of institutions that are licensed as banks are defined.	• Lack of defined activities may enable banks to engage in high-risk activities that are incompatible with a banking licence.
5 **Licensing criteria**	• The licensing authority has power to set licensing criteria and reject applications that do not meet the criteria.	• Allows the authority to control the quality of banks that enter the banking system.
6–7 **Transfer of significant ownership and major acquisitions of banks**	• Supervisor has power to review and reject proposals to transfer significant ownership or controlling interests in banks to other parties. • Supervisor has power to approve or reject major acquisitions or investments by a bank, against prescribed criteria.	• Allows the supervisor to control significant changes in bank shareholders based on prudential considerations. • Allows the supervisor to prohibit major bank acquisitions based on prudential grounds.
8–10 **Supervisory approach, techniques and reporting**	• Supervisor develops and maintains a forward-looking assessment – using a range of techniques – based on the risk profile and systemic importance of banks. • Supervisor collects and analyses prudential returns from banks.	• Supervisory framework and the techniques used set the context for day-to-day supervision. • Prudential reports are essential for off-site surveillance and for calculating key prudential ratios.
11 **Corrective actions**	• Supervisor acts early – with an adequate range of tools – to address activities/weaknesses that could pose risks to banks or to the banking system.	• Early intervention requires the ability (powers and toolkit) and will of supervisors to act and can help to rehabilitate weak banks.
12–13 **Consolidated supervision and home-host relationships**	• Banking groups are adequately monitored and supervised on a consolidated basis. • Home and host supervisors of cross-border banking groups share information.	• Consolidated supervision is fundamental to understanding a banking group's overall risk profile. • Home and host protocols are critical to enable consolidated supervision.

Prudential regulations and requirements for banks (CPs 14–29)

Principles 14–29 cover supervisory expectations for banks, emphasising the importance of good corporate governance and risk management, as well as compliance with various supervisory standards. One way to think about this set of principles is to consider that sound corporate governance, risk management and internal controls (CPs 14, 15, 26) underpin the safety and soundness of banks and banking systems. These need to be augmented with robust capital requirements (CP 16) and standards on how banks identify, measure and control their material risks (CPs 17–25, 29). In aggregate, the quality of corporate governance, capital adequacy and the management of material risks determine a bank's overall risk profile, which, in turn, is ultimately reflected in its published financial statements (CPs 27 and 28).

Core Principles	Key elements	Rationale
14–15 **Corporate governance and risk management process**	• Supervisors determine that banks have robust corporate governance and risk management practices that are commensurate with the risk profile and systemic importance of the bank.	• Quality of banks' corporate governance and risk management is arguably the most important indicator of a bank's future risk profile.
16 **Capital adequacy**	• Supervisor sets capital requirements that reflect the risks undertaken.	• Capital ensures a bank's viability and promotes confidence.
17–18 **Credit risk, problem assets and provisions**	• Supervisor determines that banks have an adequate credit risk management and problem loan identification process. • Supervisor ensures that banks maintain adequate provisions and reserves.	• Credit risk is a major source of risk for all banks. • Inadequate provisions can lead to overstated earnings and regulatory capital.
19–20 **Concentration risk and related-party transactions**	• Supervisor determines that banks adequately manage concentration risk and sets limits for bank exposures to single or connected counterparties. • Supervisor requires "arm's length" transactions with all related parties.	• Loan concentrations to a single or group of connected parties can increase credit risk. • Related-party transactions can be a source of abuse by bank shareholders and executives.
21 **Country and transfer risks**	• Supervisor determines that banks have adequate policies to manage country risk and transfer risk.	• International lending exposures are a source of, and bring an added dimension to, credit risk.
22–25 **Market, interest rate risk in the banking book (IRRBB), liquidity and operational risks**	• Supervisor determines that banks have an adequate process to manage market, IRRBB, liquidity and operational risks. • Supervisor sets liquidity requirements for banks.	• Banks with material trading book exposures are exposed to significant market risk. • IRRBB, liquidity and operational risks are material sources of risk for most banks.
26–28 **Internal control, financial reporting and disclosure**	• Supervisor determines that banks have adequate internal control processes. • Supervisor determines that banks prepare and publish financial statements – subject to external audits – that reflect their financial condition.	• A robust internal control process enhances the integrity of banks' risk management. • Published and reliable financial statements provide confidence to bank stakeholders.
29 **Abuse of financial services**	• Supervisor determines that banks have adequate oversight over the due diligence process to prevent the bank from being used for criminal activities.	• Money laundering and terrorist financing are sources of risk that may have reputational and financial consequences for banks.

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