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The universe of supervisory mandates – total eclipse of the core?

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Executive summary

Banking supervisory authorities are vested with multiple mandates, objectives and responsibilities alongside their main role of promoting the safety and soundness (S&S) of banks and the banking system. In certain jurisdictions, these mandates encompass a range of objectives such as supporting the development of the financial sector or fostering competition.

The Great Financial Crisis (GFC) that began in 2007 revealed supervisory failures that may be due in part to unclear and/or conflicting mandates of banking supervisors. The Financial Stability Board and the International Monetary Fund emphasised the importance of a clear S&S mandate in order to encourage supervisors to act early and fulfil their role. The *Core Principles for Effective Banking Supervision* (BCPs), including BCP 1, were revised to clarify that the main objective of banking supervisors is to promote the S&S of banks and the banking system. They also noted that if other tasks are assigned to supervisors, they should be subordinate to, and should not conflict with, this primary objective.

Developments in the post-GFC era have further stretched supervisory mandates. The post-GFC period exposed limitations in the tools for managing financial stability and resolving large banks, and also uncovered a number of misconduct and money laundering scandals. There has also been an increase in the digitalisation of financial services, which presents new opportunities and risks to banks. These developments expanded the remit of some banking supervisors to include other areas such as macroprudential powers and the promotion of fintech and innovation. At the same time, the risks relevant to an S&S remit have expanded to include climate and cyber risks while the prudential implications of banks' misconduct and money laundering scandals have come to the fore.

This paper explores the supervisory mandates of banking authorities in 27 jurisdictions and examines how banking supervisors interpret and navigate their S&S remit in relation to other objectives. The findings are based on responses to a Financial Stability Institute questionnaire from the applicable banking supervisory authority in each surveyed jurisdiction, along with a review of relevant publications. Unless otherwise noted, the terms "mandates", "objectives" and "responsibilities" are used interchangeably to refer to all statutory and non-statutory objectives of the surveyed authorities.

While all surveyed authorities have a statutory S&S remit, the term "safety and soundness" is difficult to define, clouding the powers it confers, including a mandate for early intervention. As the term "S&S" is not clearly defined in legislation, some authorities have attempted to interpret it. In such cases, the definitions provided are high-level, reflecting the ambiguity of S&S terminology. Some focus on the "financial safety" of banks and banking systems to determine the contours of their remit, particularly if other agencies are assigned statutory mandates in areas of potential overlap. Others interpret their mandate broadly to encompass added duties that may impact a firm's overall risk profile, such as consumer protection or anti-money laundering/combating the financing of terrorism (AML/CFT). Importantly, if there is no consensus on what constitutes "safe and sound", it may hinder supervisors' will to take early action.

In addition to S&S, surveyed authorities report having up to 13 other objectives, highlighting the extraordinary pressure placed on supervisors to juggle multiple responsibilities. The majority of surveyed authorities are charged with at least 10 or more objectives and these supervisory authorities are mostly central banks (SA-CBs). Supervisory authorities in emerging market and developing economies have slightly broader mandates than their counterparts in advanced economies, mainly due to

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a greater propensity to promote certain objectives – such as competition, financial inclusion and fintech development – that can collectively expand financial services to un(der)banked consumers.

Despite their numerous objectives, only some of the surveyed banking authorities prioritise between their mandates. Seven authorities prioritise their mandates in law, while two others prioritise via non-legislative means. S&S and financial stability are generally prioritised should there be tensions with other mandates. While prioritisation of mandates is important for all supervisors with objectives beyond S&S, it becomes vital when these additional tasks are statutory. Among 18 surveyed authorities with more than five statutory mandates, only five prioritise their mandates via legislation or other means.

This paper classifies objectives according to a "constellation of supervisory mandates" to determine the relative proximity of these numerous supervisory objectives to the S&S function. The constellation groups objectives into two categories: "surveillance and oversight" (S&O) and "promotional and developmental" (P&D). The S&O category covers five objectives: financial stability, AML/CFT, crisis management, resolution and consumer protection. These tasks are the most common statutory objectives (apart from S&S) among the surveyed authorities, suggesting that they may complement the S&S mandate. The P&D category covers seven objectives that may have less obvious relevance to an S&S remit. The climate risk objective straddles both categories, depending on whether emphasis is placed on promoting green finance or on extending the supervisory framework for climate-related risks.

Some S&O mandates, particularly resolution and consumer protection, present potential conflicts with the S&S mandate. Supervisory and resolution teams could have different views on when to trigger resolution of a bank. In addition, regulatory consumer protection actions such as fines for abusive sales practices could, in theory, jeopardise the S&S of a bank.

Certain P&D objectives can conflict with the S&S mandate and may warrant special scrutiny to ensure that policy trade-offs are well considered. Some P&D goals, such as competition, can accentuate risks in the banking system. Lower barriers to entry could admit players with aggressive strategies that may lead, for example, to an erosion in credit underwriting standards. Other P&D objectives, such as fintech and innovation, may attract non-traditional bank owners and new business models that rely on technology to underwrite and manage risk, introducing new threats to the banking system.

To deliver on their core S&S remit while addressing potential conflicts with other objectives, authorities can consider various initiatives such as:

- providing operational clarity to the term "safety and soundness" that is sufficiently flexible to encompass emerging risks within an S&S remit and granular enough to foster early intervention;
- establishing the prioritisation of the S&S mandate to promote supervisors' independence, which can, in turn, help with balancing their core S&S remit against certain P&D objectives championed by national governments;
- utilising a number of institutional arrangements, such as separate governance structures for different objectives, to minimise potential frictions between competing objectives;
- procuring adequate resources to fulfil the S&S remit and other supervisory mandates, while considering the staffing implications of some P&D objectives – such as competition or fintech development – that may draw resources away from the core S&S function; and
- publishing public statements that specify authorities' interpretation and prioritisation of their mandates, and how potential conflicts are mitigated in order to promote sound accountability.

Above all, the staggering range of objectives imposed on supervisory authorities risks diluting their ability to deliver on the core S&S mandate. For many authorities, multiple layers of objectives are stacked on top of an S&S mandate whose scope and complexity have evolved over time. Therefore, an open question to society and the political class is whether supervisory authorities are being asked to do too much, perhaps at the expense of losing sight of their main S&S mandate.

Section 1 – Introduction

1. **Most banking supervisors' mandates encompass a range of objectives.** These objectives sometimes go beyond the traditional focus on the safety and soundness (S&S) of individual banks and banking systems and may include a number of other activities that could have a bearing on a firm's overall risk profile or an impact on financial stability. Depending on the institutional arrangements in each jurisdiction, these additional areas of responsibility may include, but are not limited to, objectives such as consumer protection, financial sector development, promoting competition, financial inclusion and positioning the domestic market as an international financial centre.

2. **The Great Financial Crisis (GFC) that began in 2007 highlighted weaknesses in supervisory practices, some of which may have been due to unclear and/or conflicting mandates of banking supervisors.** Post-mortem reports by the International Monetary Fund (IMF (2010)) highlighted the importance of establishing a clear S&S mandate to foster a willingness of supervisors to take early actions. Meanwhile, the Financial Stability Board (FSB (2010)) noted that mandates should explicitly incorporate a need for early action, particularly if supervisors are expected to take actions in the absence of any tangible indicators that confirm that early corrective measures are warranted. They also observed that even clear (and multiple) mandates can still conflict with, or take attention away from, fundamental banking supervision objectives. In this context, they recommended that the Basel Committee on Banking Supervision (BCBS) elaborate on what is meant by "clear" when describing a supervisory authority's mandate and objectives.

3. **As part of broader post-crisis reforms, the BCBS revised its *Core Principles for Effective Banking Supervision* (BCPs), enhancing the principle that deals with supervisory mandates.** BCP 1, which focuses on supervisors' objectives and responsibilities, was enhanced to specify that banking supervisory authorities' primary objective is to promote the S&S of banks and the banking system. The BCP requires the primary objective of banking supervisors to be clearly defined in legislation and publicly disclosed. BCP 1 also mentions that if other responsibilities are assigned to banking supervisors, they should be subordinate to, and should not conflict with, this primary objective. In contrast, the 2006 BCPs – which was in place in the run-up to the GFC – stated only that supervisory authorities' objectives and responsibilities should be clearly defined and publicly disclosed.

4. **The post-crisis landscape has triggered a further expansion of supervisory mandates.**[2] One of the limitations exposed by the GFC was the toolkit for managing financial stability and resolving large banks. The post-crisis period also revealed misconduct and money laundering scandals in the banking sector, overlapping with the time frame when some authorities began to consider the financial stability and prudential implications of climate change. Meanwhile, rapid technological innovation offered new opportunities to deliver cost-effective financial services to a broader range of consumers and businesses. Collectively, these developments have further stretched banking supervisors' objectives to encompass new areas of responsibility, most recently including climate risk and the promotion of digital financial services. They also shined a spotlight on the role of prudential supervisors in overseeing consumer protection, conduct risk and AML/CFT activities.

5. **While there are advantages to broadening supervisory responsibilities, it also risks overburdening supervisors with managing and delivering on potentially conflicting objectives.** On the one hand, banking supervisors' involvement in activities that provide input to a firm's overall risk profile can facilitate early intervention and help reinforce their S&S objective. On the other hand, as supervisory mandates multiply, the likelihood of potential conflicts between S&S and other mandates increases, with policy actions that support one objective having a potentially negative impact on the other. Managing these conflicts is challenging in the best of times; it may be particularly difficult if the prioritisation of

[2] See Calvo et al (2018).

multiple objectives is unclear or if the appropriate institutional arrangements for mitigating potential conflicts are not in place.

6. **Generally, all supervisory objectives are ultimately designed to serve the public interest.** A banking supervisor does not aim to preserve the S&S of a bank and the banking system for the sake of the banking industry. Rather, the ultimate goal is for the banking system to be able to continue serving its customers and supporting economic activities. It is understandable that banking supervisors may need to take on new objectives as the financial sector and market environment evolve. In doing so, any new or expanded objectives will need to be predicated on the fundamental objective of serving the public interest. However, at some point, additional objectives will run counter to the core objective, which is why it is important to be careful to avoid over-expansion of supervisory responsibilities.

7. **This study takes stock of supervisory mandates in the post-GFC era and outlines how selected authorities navigate potential conflicts between S&S and other objectives.** The findings are based on a survey of banking supervisors in 27 jurisdictions, comprised of 13 central bank supervisory authorities and 14 standalone supervisory authorities, along with a review of relevant publications by international organisations, central banks and supervisory authorities. While earlier studies discussed the challenges of managing multiple central bank mandates, potential conflicts are almost always analysed through the lens of the monetary policy function.[3] This paper is unique in that the reference point is banking supervisors' S&S mandate, comparing all other mandates of supervisory authorities against this objective. Objectives related to monetary policy, macroprudential policy, and deposit insurance and their potential conflicts with an S&S mandate are beyond the scope of this paper.

8. **This paper is structured as follows.** Section 2 provides an overview of the range of mandates and responsibilities of the surveyed authorities, including how various authorities interpret their core S&S mandate. Section 3 discusses the trade-offs between S&S and other mandates, while Section 4 outlines how specific authorities manage potential conflicts between competing objectives. Section 5 concludes. The Annex provides a list of the jurisdictions and authorities that participated in the survey.

Section 2 – Range of mandates and responsibilities

Overview

9. **Virtually all of the surveyed supervisory authorities have statutory mandates and/or non-statutory[4] responsibilities that extend well beyond their S&S remit.** Among the 27 surveyed authorities, the number of statutory and non-statutory objectives and responsibilities (outside S&S) range from one to 13. Table 1 shows that 25 of the 27 authorities have five or more objectives, while 17 authorities have 10 or more objectives and responsibilities. It is important to note that some of the surveyed authorities may adopt different interpretations of an objective or responsibility, resulting in some cases, in similar functions being classified under different objectives by different authorities.[5]

[3] For examples, see Restoy (2020) and Tucker (2019).

[4] For the purposes of this paper, statutory mandates are objectives and responsibilities that are explicitly specified in legislation and non-statutory responsibilities are those that authorities undertake but that are not explicitly included in legislation. The latter is mentioned in agency's websites, public statements or other forms of official communication.

[5] For example, some supervisory authorities that are also central banks may report having an explicit financial stability mandate, as this is closely related to central bank functions, while some standalone supervisory authorities may also report a responsibility for financial stability via a supporting role or representation in a financial stability committee.

Range of mandates and responsibilities of bank supervisory authorities

Table 1

Jurisdiction	Safety and soundness*	Financial stability	Crisis management	AML/CFT	Resolution**	Consumer protection	Financial inclusion	Financial literacy	Fintech and innovation	Financial sector development	Efficiency	Competition	Climate change	Financial centre
Argentina	●	●	●	●	●	●	●	●		●	x	●		
Australia	●	●	●		●						●	●		
Brazil	●	x	x	●	●		x	x	x	x	x	x	x	
Canada	●	●	●											
China	●	x	●	●	x	●	x	x		x		●		
ECB (SSM)	●	●												
France	●	●	x	●	●	●	x	x	x	x	x	x	x	x
Germany	●	●	●	●	●	●	x	x	x	x	x	x	x	x
Hong Kong SAR	●	●	●	●	●	●	x		x	x			x	●
India	●	●	●	●	●	●	●	●	●	●	●	●	●	●
Indonesia	●	●	●	●	x	●	x	●	x	●	x			
Italy	●	●	●	●	●	●	x	x	x	●	●		x	
Japan	●	●	●	●	●	●	x	x	x	x	x		x	x
Malaysia	●	●	●	●	●	●	●	x	x	●	x		x	●
Mexico	●	●		●	●		●	●	●	●				
Netherlands	●	●	x	●	●		x	x	x		x		x	
Norway	●	x	●	●	●	●								
Poland	●	●	●	●				●	●	●		●		
Russia	●	●	●	●	●	x	●	●	x	●	●	x		
Saudi Arabia	●	●	●	●	●	●	●	●	●	●	●	●		
Singapore	●	●	x	●	●	x	x	x	x	●	x	x	x	●
South Africa	●	●	●	●			●	●			●	●		
Spain	●	●	●	x		●	x	x	●				x	
Switzerland	●	●	●	●	●	●								
Thailand	●	●	●	x	●	●	x	●	x	x	x	x	x	
United Kingdom	●	●	●	x	●		x	x	x		x	●	x	
United States	●	●	●	●	[1]	●	●	x	x				x	

● = Statutory objective/ responsibility (specified in legislation) x = Non-statutory responsibility (including mandate or function that is undertaken but not explicitly included in legislation)

Data based on responses provided by banking supervisory authorities. See Annex 1 for a list of the supervisory authorities that participated in the survey.

* For the purpose of this table, safety and soundness encompasses associated terms such as protecting the interests of depositors and maintaining banking system stability.

** For the purpose of this table, resolution precludes the powers to trigger banks' entry into resolution, and focuses primarily on powers and tools to resolve bank failures.

Switzerland – consumer protection refers to client protection.

United States – based on survey response from the Office of the Comptroller of the Currency (OCC). Its stated objectives may not necessarily be similar to other US Federal banking agencies, such as the Federal Reserve or the Federal Deposit Insurance Corporation. [1]The OCC is the resolution authority for federal branches and agencies of foreign banking organisations in the United States.

Source: FSI survey.

10. **Supervisory authorities that are also central banks (SA-CBs) tend to have broader mandates compared with standalone supervisory authorities.**[6] All 13 SA-CBs report nine or more objectives and responsibilities. Many of these authorities have specific objectives such as development of the financial sector, financial inclusion, promoting efficiency, financial literacy, consumer protection and facilitating fintech development and innovation (see Figure 1). Some of these additional responsibilities may be the result of their perceived implications for central banks' broader objectives, which implicitly target economic prosperity[7] alongside price stability. Arguably, financial inclusion and financial literacy can help maintain economic welfare, reduce poverty, improve monetary policy transmission and improve the functioning of the economy.[8]

Figure 1: Range of mandates – central banks and standalone supervisory authorities

Surveyed authorities comprise 13 SA-CBs and 14 standalone supervisors.

6 In this paper, SA-CB refers to a supervisory authority that is also a central bank, while a standalone supervisory authority is an authority that does not perform central bank functions. From the sample of surveyed authorities, the South African Reserve Bank – Prudential Authority and the French Prudential Supervision and Resolution Authority (ACPR), which are established as entities separate from but attached to central banks, are considered standalone supervisory authorities.

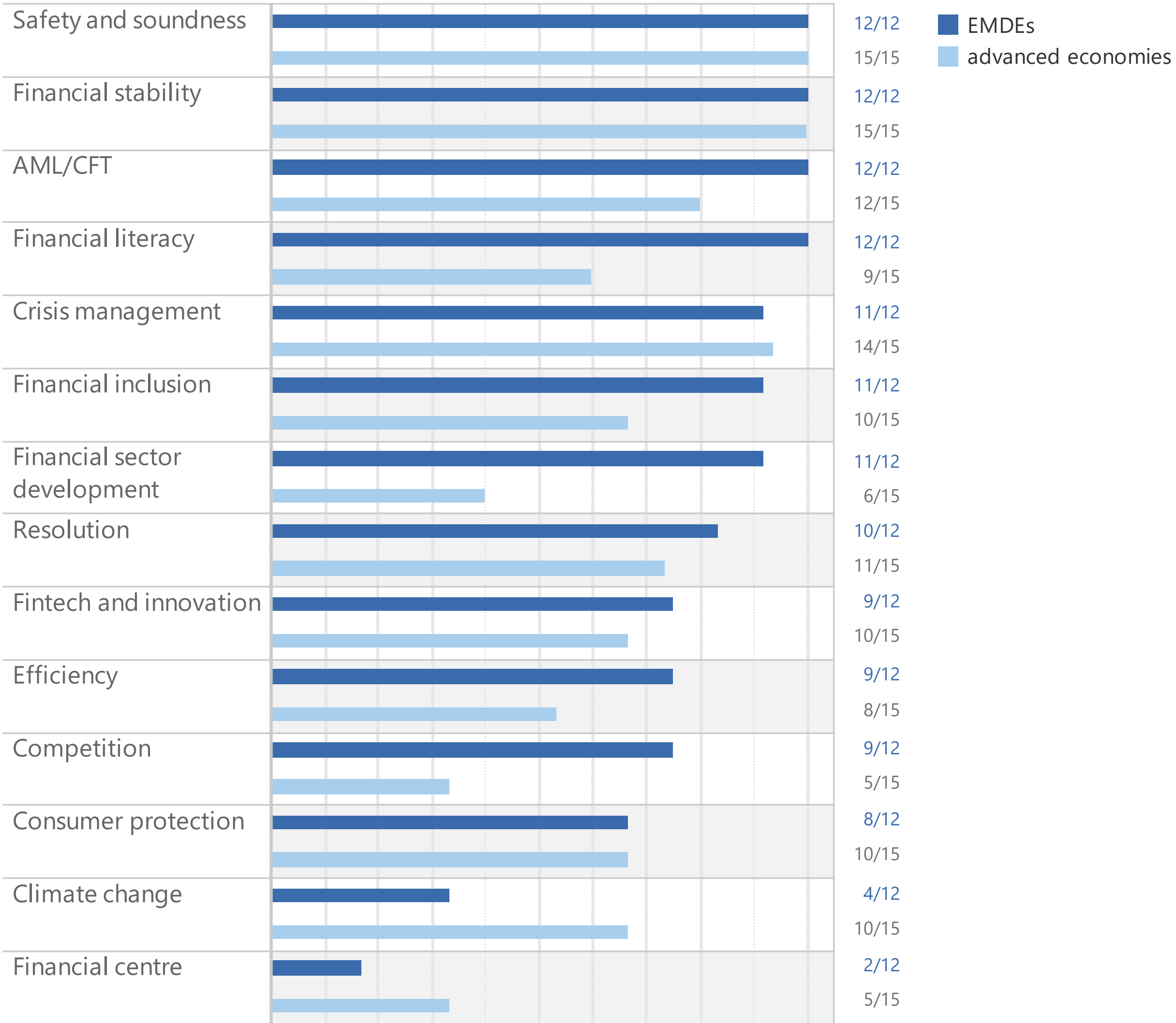
7 For example, the Board of Governors of the Federal Reserve System (the US central bank) has a dual mandate to support price stability and maximum employment. Similarly, the ECB's primary objective is price stability and its secondary objective is supporting the general economic policies of the European Union (which includes "full employment" and "balanced economic growth").

8 See Tissot and Gadanecz (2017).

11. **SA-CBs' broader responsibilities may also explain their greater propensity to take on objectives not specifically included in legislation.** In this context, 11 of the 18 authorities that reported having non-statutory objectives are SA-CBs, while seven out of the nine authorities whose mandates and objectives are limited to just those specified in or derived from legislation are standalone supervisory authorities.

12. **Supervisory authorities in emerging market and developing economies (EMDEs) have slightly broader mandates than their counterparts in advanced economies.** A higher proportion of supervisory authorities in EMDEs is tasked with financial sector development, financial literacy, promoting competition, financial inclusion and facilitating fintech development and innovation. EMDE supervisors' larger role in supporting financial inclusion, with the corresponding supportive roles of fintech development, financial literacy and competition, may be due to the fact that greater portions of their populations are unbanked. In contrast, a higher proportion of advanced economies charge their supervisors with promoting their jurisdiction as a financial centre compared with EMDEs. Figure 2 compares the supervisory mandates of advanced economies and EMDEs.

Figure 2: Range of mandates – advanced economies and EMDEs



Surveyed jurisdictions comprise 15 advanced economies and 12 EMDEs.

13. **All supervisory authorities have published some form of guidance – varying in scope and specificity – that elaborates on how they implement their various mandates.** The most common approach that authorities take, aside from the usual information included in the "About us" pages on their

respective websites, is to publish their strategic plans or to outline in their annual reports different activities undertaken to support their mandates and objectives and their associated outcomes.

14. **Some authorities have published more comprehensive documents that provide useful insights on how their statutory mandates are operationalised.** These public statements share a number of common features[9] such as a description of objectives and/or desired outcomes linked to governing legislation; functions they perform to achieve these objectives; the prioritisation of these objectives; and how potential conflicts between competing objectives are managed. Collectively, these more in-depth publications provide the general public with greater clarity on how a supervisory authority plans to deliver on its mandates and allow for its performance to be evaluated.

15. **The degree to which supervisory authorities are responsible for discharging certain mandates varies, due in part to differences in their institutional arrangements and the functions assigned to them and their interpretations of what those functions imply.** This appears to be determined by the extent to which supervisory mandates are shared with other domestic authorities,[10] as joint responsibilities may require fewer resources – but greater coordination efforts – than mandates that are the sole or primary domain of a supervisory authority.

The constellation of supervisory mandates

16. **For analytical purposes, we classify different responsibilities according to a "constellation of supervisory mandates" in order to help visualise the relative proximity of these numerous supervisory objectives to the core S&S function.** The constellation divides the universe of supervisory mandates into two categories: "surveillance and oversight" (S&O) and "promotional and developmental" (P&D) objectives, with the former perceived to be more closely related to the S&S remit than the latter. Of the surveyed authorities' 13 non-S&S objectives, five fall under the S&O category, while seven are categorised as P&D objectives. Figure 3 provides an illustration of the constellation of supervisory mandates grouped into the two respective categories.

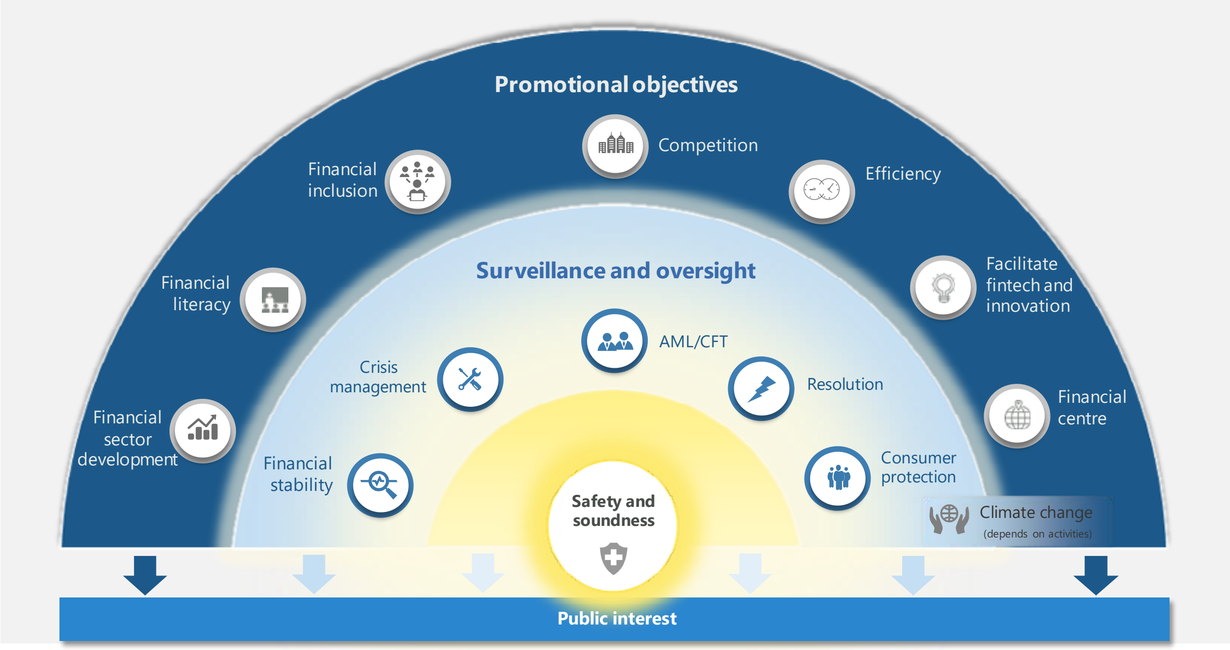
17. **Certain supervisory mandates, however, may not necessarily be limited to a single category.** Climate risk is an objective that straddles both categories depending on whether the supervisory authority focuses efforts on integrating climate risk into its supervisory framework or emphasises the promotion of green finance. Consumer protection is another mandate that encompasses a range of activities, some of which fall under S&O (such as assessing the fair treatment of consumers), while other tasks (for example, reviewing whether consumer disclosures are provided) may divert scarce supervisory resources away from the core S&S remit.[11] For the purposes of our paper, however, we have classified consumer protection as an S&O objective due to the significance of assessing conduct risk under most consumer protection mandates, which in turn helps inform prudential risk assessments of banks.

[9] For examples, see APRA (2019), BoE (2018) and MAS (2004, revised 2015).

[10] Based on our survey, the mandates most commonly shared with other domestic authorities include financial stability, consumer protection, financial sector development, financial inclusion and financial literacy.

[11] A consumer protection mandate may encompass a range of activities such as assessing firms' fair treatment of consumers (in other words, their market conduct). Such activities are closely aligned with the S&O function; other elements, such as reviewing whether disclosures to consumers comply with applicable laws and regulations or evaluating how quickly banks respond to consumer complaints, may not necessarily have significant bearing on a firm's S&S.

Figure 3: Constellation of supervisory mandates



Box 1

Climate risks – two sides of the same coin?

In 1988, the Basel Committee on Banking Supervision issued the first global capital standard for internationally active banks, focusing on credit risk. Eight years later, the standard was expanded to cover market risk, and eventually, operational risk, after another eight years. Risks assessed under Pillar 2 have also expanded over time. This evolution illustrates how safeguarding the S&S of banks and the banking system needs to keep up with time.

Climate change from a risk perspective

Almost three decades after the inception of the Basel Framework, the international supervisory community is at a critical juncture in confronting risks arising from climate change. It is increasingly accepted that financial risks arising from climate change through physical and transition risks (see Cleary et al (2019)) should be considered alongside the more "traditional" risk categories or as manifestation in existing risk categories. Such assessments should therefore constitute either an integral part of S&S or, at the very least, an additional S&O objective that complements banking supervisors' core S&S mandate.

Climate change from a developmental perspective

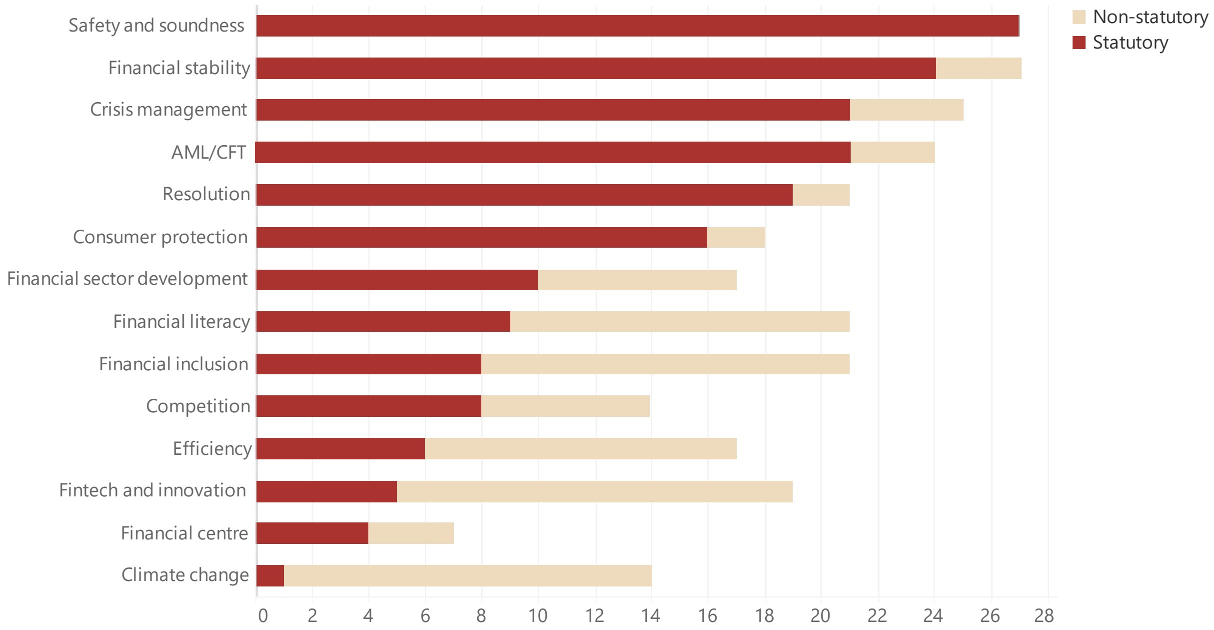
Another perspective, with arguably less consensus, is supervisors' role in promoting initiatives to combat climate change, which falls under the "P&D" grouping of mandates in this paper. Initiatives such as promoting green finance through regulatory incentives could facilitate the transition to a more sustainable economy, which ultimately should contribute to the stability of the banking system. Nevertheless, care needs to be taken to stay true to the fundamental principles of banking supervision, in terms of "risk neutrality", by treating each risk category equally. In this sense, supervisory frameworks should identify underlying risks and avoid the build-up of a green bubble with potentially systemic implications in the future.

As the supervisory landscape continues to evolve, the constellation of supervisory mandates will no doubt need to adapt. Beyond climate risks, there are initial discussions to consider other environmental risks such as the loss of biodiversity and its financial impact. Ultimately, public accountability and expectations will shed light on the right path to take at this important juncture, as the raison d'être of banking supervision is to serve the public interest.

18. **Apart from S&S, the surveyed authorities' five most common statutory mandates and responsibilities are all S&O objectives.** Almost all of the surveyed authorities have a role in maintaining

financial stability. Crisis management, AML/CFT, resolution and consumer protection are also recurring responsibilities among the surveyed authorities, as depicted in Figure 4.

Figure 4: Range of mandates – statutory and non-statutory



19. **These five S&O objectives may complement the S&S remit.** A financial stability[12] mandate has the closest relationship to S&S, as the S&S mandate includes stability of the banking system. AML/CFT risks – outside of their impact on the integrity of the banking system – may affect the S&S of banks by heightening their exposure to reputational, operational, compliance and concentration risks.[13] Similarly, a consumer protection mandate requires, among other issues, efforts to promote fair treatment of consumers and to protect them against misconduct risk (eg the mis-selling of financial products).[14] A bank that conducts its business fairly should be less exposed to operational and reputational risks, thus contributing to a sound business model and its S&S.[15] Misconduct issues may also be signs of broader prudential concerns regarding banks' governance and internal controls, while widespread misconduct abuses could jeopardise trust in the banking system as a whole.[16] Lastly, both supervision and resolution aim to reduce the impact of bank failures. As a bank's financial condition deteriorates, supervisory monitoring and actions can help inform subsequent crisis management and resolution decisions.

20. **The seven mandates and responsibilities that we classify as P&D have less obvious links to an S&S mandate, regardless of their potential merits in advancing the public interest.** These mandates and responsibilities include a range of objectives where the supervisory authority is asked to

[12] For the purposes of this paper, an implicit or explicit financial stability mandate means that the supervisory authority has some role in financial stability oversight – either solely or through its participation in domestic interagency committees. It should not necessarily be taken to mean that the supervisory authority also has powers related to macroprudential policies.

[13] See BCBS (2014, revised 2020) and FATF (2015).

[14] See OECD (2011).

[15] For example, ACPR (2017) views consumer protection as a central concern alongside prudential risks. It sees customer protection as playing a part in boosting confidence in banking institutions as well as in the transparency and effectiveness of the financial system. This makes consumer protection a significant factor in financial stability.

[16] ESRB (2015) describes how banks' misconduct could impair proper functioning of the financial system by eroding public confidence and how fines for misconduct could themselves give rise to systemic risks.

put on its "promotional hat", such as developing the financial sector; facilitating fintech innovations; enhancing the attractiveness of the local market as an international financial centre;[17] fostering competition and efficiency; or promoting financial inclusion and financial literacy. Unless these P&D objectives are carefully managed, they can potentially detract from, or conflict with, supervisors' overarching S&S remit.

21. **In many jurisdictions, a number of these P&D objectives are assigned together to the same authority.** This suggests that these objectives complement each other. Often times, facilitating innovation is not seen as an end in itself, but rather viewed through a broader lens as a means of promoting efficiency and competition, thus supporting the overall economy. This, in turn, may benefit society by building a more inclusive financial system and increasing growth opportunities for the financial sector. Financial education goes hand in hand with financial inclusion and helps minimise the risks posed to consumers from innovative financial products. This provides a foundation for financial sector development.

22. **Certain P&D objectives are also championed by national governments.** Some authorities have been charged with specific objectives – such as promoting the local market as an international financial centre, supporting fintech and innovation, and fostering competition – that are part of broader government-led initiatives. This may place added pressure on supervisors to prioritise these objectives over other responsibilities. In this context, supervisory authorities need sufficient independence to balance governmental expectations against their core S&S remit.

The parameters of the safety and soundness mandate

23. **While all of the surveyed supervisory authorities have a statutory mandate to promote the S&S of banks and the banking system, the term "safety and soundness" is inherently difficult to define.** As a result, different terms such as "protection of depositor interests" and "maintaining banking system stability" are used by the surveyed authorities in close connection with their S&S mandate. Figure 5 provides examples of different terms used by the surveyed authorities in reference to the S&S objectives specified in applicable legislation.

[17] A mandate to promote the local jurisdiction as an international financial centre is not the same as a mandate to develop the financial sector, though there may, at times, be some overlaps. The former is focused on attracting international institutions to operate in the domestic jurisdiction by highlighting a range of perceived benefits. The latter involves various initiatives to promote economic growth; provide greater credit access to consumers and small and medium-sized enterprises at a lower cost; and reduce poverty. A developmental mandate may also include programmes to enhance banking industry skill sets.

Figure 5: Terms associated with safety and soundness

24. **The lack of clarity on what S&S means allows considerable scope for interpretation, including powers this objective implies.** This is particularly relevant in jurisdictions where prudential authorities do not have explicit mandates to oversee various S&O objectives that may complement supervisors' traditional focus on the S&S of individual banks. In this context, some authorities are guided by their statutory mandates and do not use their S&S remit as a basis for expanding their responsibilities to other S&O objectives where they have no legal authority. Others interpret their S&S mandate more broadly, to also include powers for overseeing consumer protection, AML/CFT and financial stability. The Reserve Bank of India (RBI) uses its monetary policy remit to support financial stability in India. It takes a broad interpretation of its statutory monetary policy mandate as justification for an S&S remit, which in turn provides a mandate to oversee a number of other S&O and P&D objectives. The RBI considers the term "safety and soundness" to be read into the provisions of relevant legislation even if it is not specifically referred to.

25. **The ambiguity of S&S terminology also makes it difficult to measure how well supervisors are delivering on their core mandate, including taking timely corrective measures.** Unlike the monetary policy function, where the inflation rate is relatively easy to quantify and compare against a central bank's stated objectives, the primary objectives of prudential supervision are less clear. Although the BCBS mentions that the aim of supervision is to reduce the probability and impact of a bank failure,[18] some jurisdictions may not necessarily tolerate either any bank failures or the failure of a large, systemically important bank. Several authorities have attempted to expand their definition of "safety and soundness", going beyond what is specified in applicable legislation (Table 2). While these explanatory elements provide more context, they also highlight the inherent difficulties in creating measurable objectives for the S&S mandate.

18 See BCBS (2012).

Safety and soundness explanation — Table 2

Jurisdiction	Explanation relating to "safety and soundness"
Australia	Core to the Australian Prudential Regulation Authority's (APRA) financial safety objective is ensuring that institutions are soundly managed. APRA seeks to achieve this outcome by establishing and enforcing prudential standards that are designed to ensure the prudent governance, risk management and (where relevant) financial capacity of each regulated institution. This, in turn, ensures that depositors, policyholders and superannuation fund members can have confidence that there is a high probability their claims on APRA-regulated institutions will be able to be met. *(Information paper on APRA's objectives)*
Canada	Office of the Superintendent of Financial Institutions (OSFI) is a prudential regulator focused on controlling risks that can threaten a financial institution or pension plan's solvency. In short, it is about ensuring the "safety and soundness" of regulated entities. *(Discussion paper* Developing financial sector resilience in a digital world – Our mandate*)*
Hong Kong SAR	The Hong Kong Monetary Authority (HKMA) has a general objective to promote the safety and stability of the banking system. Achieving this objective is contingent upon the financial system being highly resilient and capable of providing the critical financial services the Hong Kong economy needs. *(HKMA annual report 2019)*
Switzerland	FINMA undertakes prudential supervision to ascertain whether supervised financial institutions are prepared for potential risks and thus in a stable position now and in the future, so that their customers are adequately protected. *(FINMA annual report 2019)*
United Kingdom	"Safety and soundness" involves firms having resilience against failure, now and in the future, and avoiding harm resulting from disruption to the continuity of financial services. *(PRA's approach to banking supervision)*
United States	The OCC does not define safety and soundness but utilises a definition of "unsafe and unsound banking practice"* to mean "any action, or lack of action, contrary to generally accepted standards of prudent operation, the possible consequences of which, if continued, would be abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds".

* See Financial Supervisory Act of 1966: Hearings on S. 3158 Before the House Comm. On Banking and Currency, 89th Congress, 2d. Sess. 49 (1966) Statement of John E. Horne, Chairman of Federal Home Loan Bank Board, 112 CONG. REC. 26, 474 (1966).

Source: Various public documents.

26. **Regardless of the complexities in defining "safety and soundness", the range of risks that have a bearing on a bank's risk profile is continuously expanding, making it more difficult than ever for supervisory authorities to meet societal expectations of their primary S&S mandate.** Various authorities are now considering a number of prudential risks, such as climate and cyber risks, more explicitly as part of their S&S assessment of banks and banking systems. Even where prudential authorities do not have statutory responsibilities in certain areas, they are expected to ascertain the extent to which those areas have a bearing on prudential risk assessments. For example, APRA's capability review[19] noted that even though APRA is not a conduct regulator, governance and culture risk assessments fall under APRA's domain; in this context, aspects of conduct oversight fall under APRA's S&S remit since egregious misconduct may undermine an institution's financial safety.[20] In Canada, while OSFI does not identify AML/CFT as one of its mandates, the risk of non-compliance and its impact on reputation and/or S&S are considered part of OSFI's supervisory framework.

[19] On 11 February 2019, the Australian Government announced a review to consider APRA's capabilities of responding to an environment of growing complexity and emerging risks for sectors regulated by APRA. The report makes 24 recommendations which seek to ensure that APRA is best placed to deal with the future environment and its challenges.

[20] See Australian Treasury (2019) for further information.

27. **As supervisory resources are being stretched to meet authorities' primary S&S mandate and related S&O objectives, many authorities are also increasingly asked to take on a range of P&D objectives.** At least 20 of the 27 surveyed authorities have four or more P&D objectives. In trying to deliver on these various objectives, a key challenge for all prudential authorities is not only to manage the potential conflicts that may arise, but to also ensure that sufficient capacity exists to fulfil their core S&S mandate.

Section 3 – Potential trade-offs between mandates

28. **Certain supervisory mandates could conflict with the core objective of banking supervision, that is, to preserve the S&S of banks and the banking system.** Past Financial Sector Assessment Programs (FSAPs)[21] of the IMF emphasised that consumer protection, market development, fintech innovation, competition, financial centre positioning, macroprudential and financial stability mandates can conflict with banking supervisors' core S&S responsibilities. The reports emphasised that conflicts could arise between mandates in cases where legislation does not explicitly provide primacy to S&S objectives. Understanding perceived or real conflicts between objectives is a necessary first step in identifying effective ways to mitigate such risks or to make informed trade-offs when discharging a banking supervisor's main responsibility. Conflicting mandates can draw limited supervisory resources away from the S&S mandate or, in extreme cases, lead to supervisory actions and policy measures that go against this core mandate.

29. **Around half of the surveyed authorities acknowledged that potential conflicts could arise between their mandates.** The other half make up a diverse set of authorities ranging from standalone supervisory authorities with a small number of mandates to SA-CBs with wide-ranging responsibilities. It is noteworthy that different authorities with the same sets of mandates take different views as to whether those mandates may conflict. This section first describes potential conflicting mandates based on the survey responses, followed by a conceptual description of how other conflicts could arise.

30. **Resolution, conduct of business and competition are the three mandates cited most by the surveyed authorities as potentially conflicting with the core S&S mandate.** Examples of the ways in which conflicts could arise include:

a. Resolution: differences in views between supervisory and resolution teams on when to trigger resolution[22] of a banking institution.

b. Conduct of business: regulatory actions aimed at protecting fair treatment of consumers (for example, the imposition of fines for abusive sales practices) could jeopardise the financial soundness of a banking institution.

c. Competition: lowering regulatory barriers to entry could end up admitting banking institutions with unsustainable business models (eg lower margin business strategy, more aggressive risk appetite), which could give rise to solvency problems in the future.

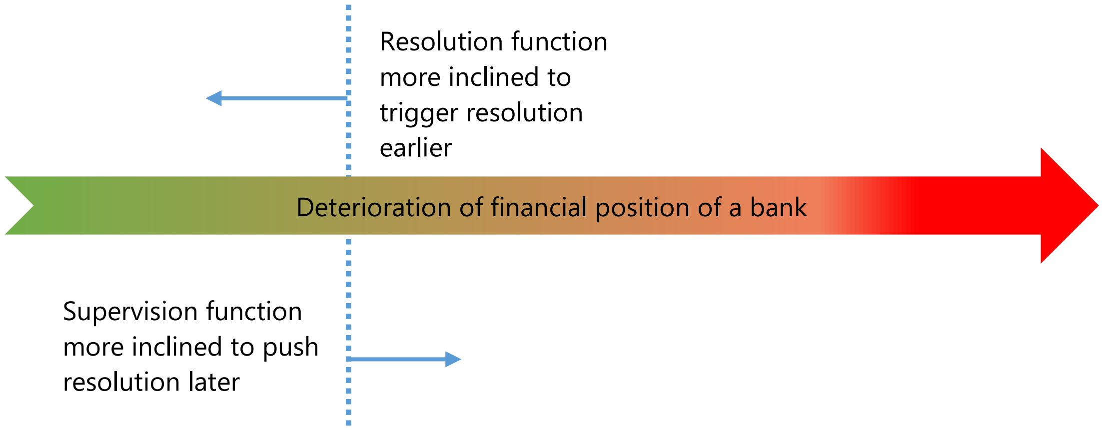
[21] The FSAP is a joint programme of the IMF and the World Bank, whereby relevant authorities in participating jurisdictions are assessed against internationally recognised standards and codes as a way to measure compliance with accepted practices. For further details, see the IMF website (www.imf.org/external/np/fsap/fssa.aspx).

[22] Because supervisory authorities typically have the power to declare a bank non-viable as part of their S&S remit, there is a risk of potential delays in triggering resolution even if a separate resolution authority exists. However, such risks could be even more evident if the resolution and supervision functions fall under the same authority.

We consider each of these objectives in greater detail.

31. **Resolution aims to manage banks' failures without the need for taxpayer bailouts.** The FSB *Key Attributes* state that the objective of resolution is to resolve financial institutions without severe systemic disruption and without exposing taxpayers to loss, while protecting vital economic functions.[23] It is conceivable that, in a financial crisis, a bank or several banks may need to be resolved in an orderly manner, which may involve going against the interests of certain depositors (eg losses borne by uninsured depositors) for the greater good. Such conflicts could translate into concrete supervisory dilemmas. For example, a supervision team may be inclined to delay resolution actions against a bank in order to preserve consumer interests as long as possible or due to fears of broader, systemic contagion. Beyond this, supervisors could also be hesitant to "pull the trigger" due to the perception that a bank failure equates to a supervisory failure.[24] On the other hand, a resolution team would be inclined to exercise resolution actions as early as possible in order to preserve the value of the bank. This tension is depicted in Figure 6, which shows how resolution and S&S objectives could pull a banking authority in opposite directions.

Figure 6: Illustration of the opposing interests of supervision and resolution teams



32. **At a broader level, the time horizons of supervisory and resolution perspectives could differ – a supervisory view typically places more emphasis on going-concern whereas resolution takes a gone-concern perspective.** While a bank remains a going-concern, actions could be taken to make it more resolvable in a gone-concern scenario by removing obstacles to the effective application of the preferred resolution strategy. These actions may involve changes to legal and business structures and activities, funding arrangements or divestment of certain assets. In most cases, supervisory and resolution actions should align.

33. **As regards conduct of business, regulatory actions that seek to correct unfair treatment of financial consumers can sometimes be taken at the expense of a bank's S&S.** An obvious example is the imposition of fines[25] on a bank for mistreating its customers, which could adversely impact its earnings and capital positions. In an extreme situation, a banking supervisor having both conduct and S&S responsibilities could find itself in a difficult position if faced with a financially deteriorating bank that has significantly violated consumers' interests. Would the supervisor impose financial penalties to compensate mistreated consumers, risking the viability of the bank, or would it prioritise the S&S of the bank over consumers' interests? Another example of how poor conduct could adversely affect the S&S of banks

[23] See FSB (2014).

[24] A banking authority's funding structure that relies on fees levied from the banking industry could also disincentivise the removal of a large, failing bank's licence.

[25] More generally, the imposition of fines to fulfil other supervisory objectives such as AML/CFT could also impair a bank's financial position, which is an example of how competing mandates could conflict with the S&S objective. Banks that are deemed in violation of AML/CFT rules could also erode public confidence, which could also undermine their S&S.

relates to redress or compensations to unfairly treated or mis-sold consumers. Given that banking is a business that relies heavily on consumer trust, the potential impact of an adverse public reaction to banks' poor conduct should not be underestimated, because it could ultimately hinder the viability and sustainable development of the industry.

34. **While a competitive banking system should lead to better outcomes for financial consumers in terms of more choices and cost efficiency, an overemphasis on competition objectives could jeopardise the S&S of the banking system in the longer term.** In the United Kingdom, the Prudential Regulation Authority's (PRA)[26] secondary objective is "to act, so far as reasonably possible, in a way that facilitates effective competition in the markets for PRA-authorised firms carrying out regulated activities". The PRA sees this secondary competition objective as complementary to its primary objective of promoting the S&S of PRA-authorised firms. Looking at prudential regulation through the lens of competition also allows for an assessment of whether prudential interventions are being applied proportionately. Nevertheless, there could be a potential conflict between maintaining S&S and lowering barriers to entry and growth, to the extent that new entrants adopt an unsustainable business model or excessive competition erodes industry-wide credit underwriting standards.[27]

35. **Although few of the surveyed authorities cited developmental and financial inclusion objectives as potentially conflicting with S&S objectives, such mandates are not always compatible with an S&S remit.** S&S and promotional objectives are inherently in conflict whereas the former is concerned with monitoring and mitigating risks, the latter – facilitating business enterprise and innovation – involves taking risks.[28] Past FSAPs emphasised that developmental objectives could impinge on the core S&S mandate, for example, if supervisors delay corrective or preventive supervisory actions against banking institutions. Potential conflicts could also arise if the authority accepts lower loan underwriting standards in order to promote financial inclusion or market development. A concrete manifestation of this conflict was the subprime mortgage crisis[29] that contributed to the GFC.

36. **Other supervisory mandates, though not specifically mentioned by any of the surveyed authorities, could also conflict with the core S&S objective.** Such examples are listed in Table 3.

[26] See Dickinson et al (2015).

[27] For further details on potential trade-offs between competition and financial stability, see Vives (2016).

[28] See MAS (2004, revised 2015).

[29] See BIS (2008).

Conceptual description of how certain mandates could conflict with safety and soundness

Potential conflicting mandates — Table 3

Mandate	Description of potential conflict with safety and soundness
Climate change	Promoting green finance through favourable capital treatment without considering downside risks could go against the fundamental principle of risk-based capital rules, ie higher risk requiring higher capital.
Financial centre	Regulatory incentives to attract banking players, in the form of lower regulatory requirements or lighter supervisory oversight, could weaken their financial resilience.
Fintech and innovation	Promoting fintech and innovation may accentuate risks in the banking system, eg increased credit risk due to new credit underwriting methodologies based on non-traditional data such as social media;* heightened cyber risk and elevated liquidity risk due to a limited core deposit funding base.
	Newly licensed digital banks may include non-traditional bank owners, such as technology firms and other non-financial entities that may introduce new risks.**

* Nonetheless, Gambacorta et al (2019) shows that a model based on machine learning and non-traditional data used by a fintech company outperforms traditional credit scoring models.

** Conflicts may also arise when promotion of fintech and authorisation of digital banks fall under the same authority. For example, a fintech facilitation unit within a banking authority could facilitate the entry of a new player through the licensing process, but a separate licensing unit within the same authority may reject its licensing application; alternatively, the fintech facilitation unit of a banking authority may facilitate the entry of a new player, placing added pressure on the separate licensing unit to approve the new bank licence.

37. **In addition to considering potential conflicts that could arise from each individual objective, it is important to assess the combined impact of all of these objectives.** Operational conflicts could arise in allocating finite supervisory resources to other objectives beyond the S&S objective. Diverting supervisory resources away from core activities could weaken the supervisory oversight of banking institutions, thus exposing the authority to the risk of missing early warning signs from banks with deteriorating financial conditions and the build-up of risks that may jeopardise the stability of the banking system. A key governance question for banking authorities centres on the extent to which they can take on other responsibilities before their resources are completely stretched, compromising their ability to fulfil their S&S mandate.

Section 4 – Common approaches to mitigating potential conflicts and balancing trade-offs

Overview

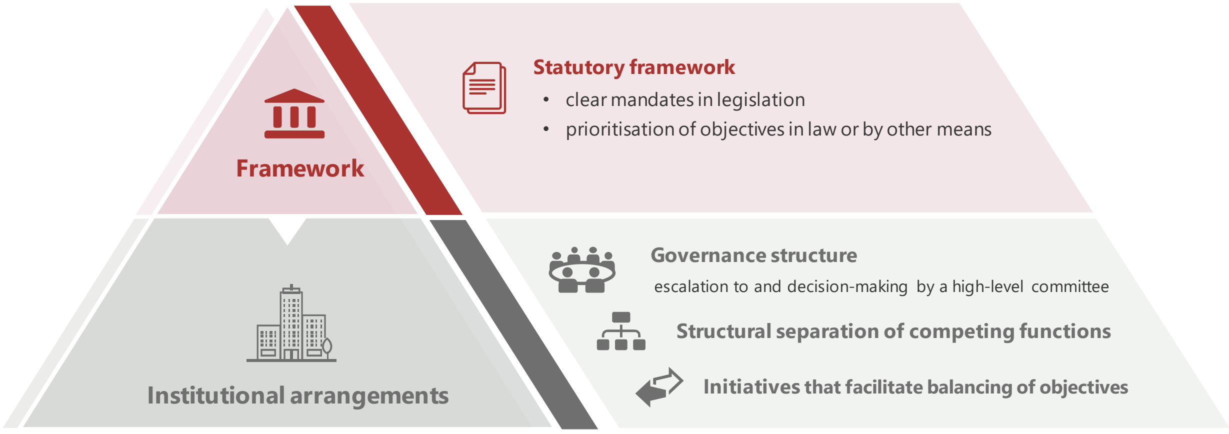
38. **Surveyed authorities have adopted several approaches to mitigate potential conflicts between S&S and other mandates.** These approaches can be divided into two broad categories:

- Statutory frameworks with supervisory mandates set out and prioritised in legislation; and
- Institutional arrangements such as the structural separation of competing functions within an authority or procedures for escalation to a high-level body in order to resolve potential conflicts (Figure 7).

39. **While statutory frameworks can provide clarity and high-level guidance, in practice, institutional arrangements are crucial to address potential conflicts between objectives.** When objectives are clear and prioritised in legislation, corresponding governance and organisational structures

provide support to supervisors managing multiple statutory objectives. Without well laid-out objectives and directions in statute, institutional arrangements become even more vital in managing trade-offs.

Figure 7: Overview of approaches to mitigating potential conflicts and balancing trade-offs



Statutory framework

40. **Well defined supervisory mandates and prioritisation via legislation or other means provide clarity on what supervisors should aim to achieve and which objectives will prevail should conflicts arise.** Clear objectives serve as a guide for supervisors as they exercise their powers to achieve desired outcomes and can be used to hold the supervisory authority accountable for its performance.

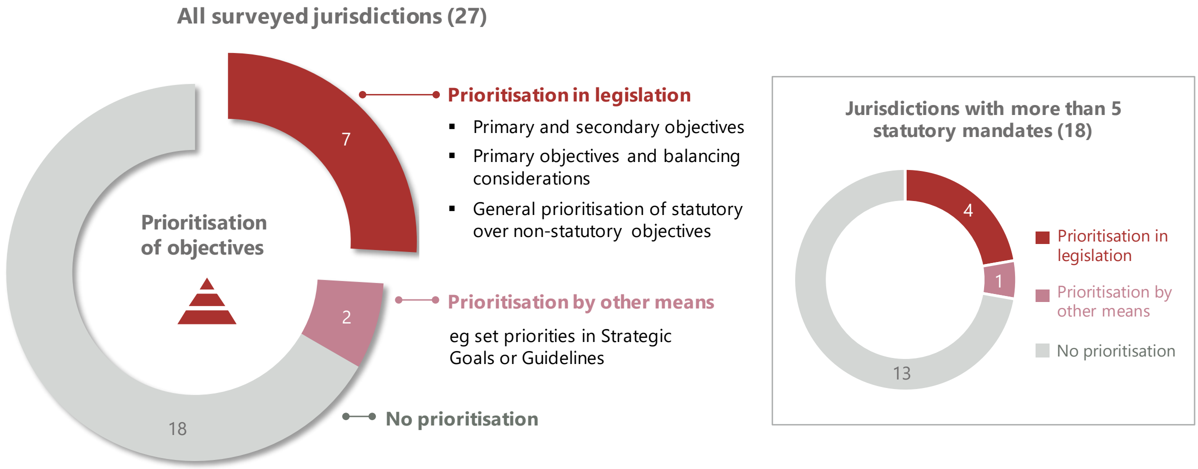
41. **Prioritisation creates a hierarchy of objectives and thus provides clear guidance for supervisors by attaching weights to their different functions.** The BCPs require primacy of the S&S objective where the supervisor is assigned broader responsibilities.[30] Embedding such prioritisation in statutory frameworks or public documents makes it clear that supervisors' decisions will appropriately balance potentially competing objectives. However, the primacy of a mandate does not mean that supervisors cannot pursue other objectives. Rather, it provides a guidepost for supervisors when differentiating between core and ancillary objectives, with the former requiring greater attention and resources than the latter.

42. **Overall, only nine of the 27 surveyed authorities set priorities for their (statutory and non-statutory) mandates, seven of whom set this prioritisation into applicable law.** The other two authorities set priorities via other, non-legislative, means. S&S and financial stability are generally primary objectives and are prioritised should conflicts with other mandates arise. The relatively low number of authorities that prioritise multiple objectives is noteworthy given that 25 of the 27 surveyed supervisors have six or more statutory and non-statutory objectives and responsibilities (including S&S).

43. **While prioritisation of supervisory mandates is relevant for all supervisors assigned objectives beyond S&S, it is particularly helpful when these additional tasks are statutory requirements.** Among the 18 surveyed authorities with more than five statutory mandates, only four authorities prioritise their mandates in legislation. The more objectives statutorily assigned to a supervisor, the higher the risk of potential conflicts arising between different statutory mandates. Ideally, prioritisation of statutory mandates should be done through legislation to ensure certainty and enforceability. It may also be useful to consider the potential benefits of prioritising between non-statutory responsibilities going forward. Figure 8 shows the number of surveyed authorities that prioritise multiple objectives and how these objectives are prioritised in legislation and via other means.

[30] See BCBS (2012), BCP 1 Essential criteria 2 for further details.

Figure 8: Prioritisation of objectives



44. **Some jurisdictions explicitly rank their mandates as primary and secondary, or subordinate one objective to the other.** One of the PRA's primary objectives is to promote the S&S of the firms it regulates.[31] The PRA also has a secondary competition objective to act, so far as is reasonably possible, in a way that facilitates effective competition.[32] In practice, this means that the PRA also actively considers its approach from a competition perspective when discharging its general functions to advance its objectives. In Singapore, the Monetary Authority of Singapore (MAS) Act states that the objective of fostering a sound and reputable financial centre and promoting financial stability prevails over developmental objectives.[33]

45. **Another prioritisation approach is setting out primary objectives and associated balancing considerations.** According to APRA's legislation, in performing and exercising its functions and powers, APRA is to balance the objectives of financial safety, efficiency, competition, contestability and competitive neutrality, and, in doing so, promote financial system stability in Australia.[34] APRA does not introduce or impose requirements regarding its "balancing considerations" (efficiency, competition, contestability and competitive neutrality), but it does take them into account in prudential policy development and implementation.[35] In practice, APRA assesses the impact of each proposed policy on its primary objectives of financial safety and financial system stability and on its balancing considerations. Such assessments are included in its published discussion paper on the proposed policy in question.[36]

46. **Some surveyed authorities view statutory mandates as overarching and generally overriding non-statutory ones.** Malaysia's Central Bank Act stipulates that the Central Bank of Malaysia's (BNM) principal objectives are "to promote monetary stability and financial stability conducive to the sustainable growth of the Malaysian economy".[37] The Bank of Thailand (BoT)'s

[31] Financial Services and Markets Act 2000 (FSMA), Section 2B. Another primary objective of the PRA specific to the regulation of insurers is to help secure an appropriate degree of protection for those who are or may become policyholders.

[32] FSMA, Section 2H.

[33] Monetary Authority of Singapore Act (MAS Act), Section 4.

[34] Australian Prudential Regulation Authority Act 1998, Article 8.

[35] Byres (2017).

[36] For examples, see APRA (2017, 2018a).

[37] Central Bank of Malaysia Act 2009, Section 5.

non-statutory responsibilities, such as financial inclusion and promoting competition, are subordinate to its statutory primary objective of maintaining financial institution system stability.[38]

47. **Some jurisdictions prioritise their mandates via other means.** The Central Bank of Brazil (BCB) sets out its main priorities in the Strategic Guidelines that are incorporated in the federal government's Multiyear Plan.[39] This prioritisation minimises potential conflicts between mandates. Similarly, the Financial Supervisory Authority of Norway assigns priority through its strategic goals, which also provide direction for its activities.

48. **The lack of clarity on and the need for prioritisation of supervisory mandates are recurring recommendations in FSAP reports.** Our survey confirms that this remains an ongoing challenge, as 18 of 27 authorities with multiple statutory and non-statutory objectives – including 14 authorities with more than five statutory mandates – do not prioritise between their objectives in applicable legislation. In certain FSAPs, the IMF had recommended that, short of a statutory framework, there should be a formal document clarifying a supervisory authority's objectives and responsibilities, emphasising that the main objective of supervision is to promote S&S, and other objectives are secondary.[40]

Institutional arrangements

Overview

49. **Institutional arrangements are used to manage potential conflicts between S&S and S&O mandates as well as between S&S and P&D mandates.** These arrangements involve governance frameworks with procedures for escalation to senior management and/or the structural separation of competing activities. Resolution and conduct supervision (including consumer protection and AML/CFT) are examples of S&O objectives that some surveyed authorities structurally separate from prudential supervision. Certain P&D objectives, including financial sector development; promoting the jurisdiction as an international financial centre; facilitating fintech development; and fostering competition, are balanced against S&S considerations via a variety of institutional arrangements. Examples of such arrangements include establishing separate reporting lines, creating centralised teams to coordinate across functions or applying the proportionality principle.

50. **An appropriate governance framework, such as a management committee that oversees different functions and clear escalation processes, enables an authority to consider the necessary trade-offs in decision-making.** When conflicts arise between objectives, some authorities have governance processes and escalation procedures in place to bring such issues to the attention of senior management or a management committee for decision-making. High-level committees are often in charge of the institution's overall objectives. Senior management or a high-level committee may have support from an advisory committee or a working group comprised of representatives from different departments to identify possible conflicts and propose solutions. An alternative institutional design involves establishing a specialised high-level committee that is set up for a specific function, for example, financial stability and resolution, in order to maintain independence from other functions in decision-making.

51. **An internal organisational structure that separates reporting lines and resources can facilitate the independent operation of competing functions.** Structurally separating potentially conflicting functions can minimise undue influence from competing objectives. Additionally, as a result of separate reporting lines, any potential conflicts or trade-offs can be resolved at a higher management

[38] Bank of Thailand Act B.E. 2485, Section 7 and IMF (2019b).

[39] See the Central Bank of Brazil website (www.bcb.gov.br/en/about/strategicplanning).

[40] For further details, see the IMF website (www.imf.org/external/np/fsap/fssa.aspx).

level. Differences in authorities' organisational structures may be due in part to differences in the desired degree of separation and the necessity of coordinating between functions.

Institutional arrangements: "surveillance and oversight" objectives

52. **The need for operational independence of resolution functions is highlighted in the FSB's *Key Attributes*.**[41] The *Key Attributes assessment methodology for the banking sector* further explains that an authority may perform resolution functions as well as other functions, such as supervision, provided there are adequate governance arrangements to manage any potential conflicts of interest.[42]

53. **To facilitate the discharge of resolution responsibilities independently from supervision, many authorities structurally separate the resolution function, with a separate reporting line to a designated senior management and a dedicated staff.**[43] Some authorities set up a separate Resolution Office that reports directly to the Chief Executive (eg HKMA) or a separate department for resolution that reports to a different Deputy Governor from the supervisory function (eg Bank of England (BoE)).[44] The Resolution Office or department has its own staff separate from that of supervisors. In some cases, the resolution function is not established as a separate department, but rather incorporated into an existing department that is separate from that of supervision.[45]

54. **In addition to separate reporting lines, some authorities have established a specific resolution committee or assigned more votes on resolution decisions to a senior management official who is not involved in supervision.** In the French Prudential Supervision and Resolution Authority (ACPR), a separate Resolution Directorate reports directly to the Resolution College which is tasked with overseeing the preparation and implementation of measures to resolve banking and insurance crises, separate from the Supervisory College. The Resolution College is chaired by the Governor of the Bank of France and is composed of a designated Deputy Governor and representatives from related authorities.[46] In the Netherlands Bank, resolution tasks are assigned to an Executive Director who does not have banking supervision as a primary responsibility.[47] The Executive Director's vote on most resolution matters in the Executive Board carries as much weight as the combined votes of other Executive Directors, and has a deciding vote in a stalemate.

55. **Another approach is to set up a specific resolution committee and a resolution unit composed of representatives from various departments, but without a dedicated staff.** The MAS's Resolution Unit (RSU) leads resolution policies and execution. The RSU is chaired by an Assistant Managing Director who does not have supervisory responsibilities over banking or insurance entities, and consists of representatives from various departments. Supervisory teams are responsible for recommending

[41] See FSB (2014).

[42] See FSB (2016).

[43] Eg ACPR, APRA, BoE, Bank of Spain (preventive resolution), BoT, HKMA and Netherlands Bank. For further details on institutional arrangements for bank resolution, see Baudino et al (2021, forthcoming).

[44] For example, in the BoE, decision-making authority on resolution issues lies with the Deputy Governor for Markets and Banking and the Executive Director for Resolution, while critical decisions are reserved for or may be escalated to the Governor. There are separate supervisory functions that report to the Deputy Governor for Prudential Regulation, and decision-making for microprudential functions falls to the Prudential Regulation Committee. See Bank of England (2021) for further details.

[45] For instance, in the BoT, a resolution unit is set up within the Regulatory Policy Department, reporting to different Assistant Governors from those of the supervision departments. Decision-making on resolution matters is escalated through inter-department committees to the Crisis Management Committee and the Financial Institutions Policy Committee, chaired by the Governor.

[46] For further details, see ACPR's website (https://acpr.banque-france.fr/en/acpr/colleges-and-committees/resolution-college).

[47] See IMF (2017).

resolution actions to the appropriate management forum. To alleviate the risks of supervisory forbearance, the RSU would comment and provide its independent views to the management forum.[48]

56. **Practices of and motivations for separating conduct supervision from prudential supervision are varied.** Reporting lines join at different management levels depending on internal organisation. Some authorities make the separation in order to increase the functions' independence from one another,[49] while others may be driven by the need to increase regulatory focus on conduct issues and build specialised skills. In 2019, the BCB transferred conduct and AML/CFT supervision to a different Deputy Governor separate from the Deputy Governor for prudential supervision in order to enhance governance and independence. This gives each of the functions their own representatives on the Board of Governors.[50] The HKMA established separate departments for conduct, AML/CFT and prudential supervision, but all three report to the same Deputy Chief Executive. The HKMA's rationale for this separation is that it steps up supervision of conduct and AML/CFT issues and centralises resources into a specialised department, which requires different expertise than that of prudential supervision.

57. **When authorities choose to structurally separate prudential supervision and other S&O functions, effective internal coordination mechanisms are needed.** Some of the surveyed authorities emphasise the importance of coordination mechanisms and a smooth flow of information between supervision and resolution functions.[51] Such coordination is crucial in taking appropriate resolution actions that preserve the continuity and consistency of recovery and resolution plans. Conduct and AML/CFT issues may also have prudential implications, so cooperation between these functions and prudential supervision is desirable.

Institutional arrangements: "promotional and developmental" objectives

58. **Structural separation between supervision and certain P&D objectives has been adopted by several authorities in order to minimise potential conflicts with the S&S objective.** Supervisory functions report to different senior management than do functions that are responsible for developmental objectives,[52] such as promoting a jurisdiction as an international financial centre or fostering fintech innovation.[53] Reporting lines are not crossed between supervision and development groups. The intention is to resolve potential conflicts and trade-offs at the senior management level. For some

[48] See IMF (2019) and FSB (2018). The Management Resolution Committee, chaired by the Deputy Managing Director (Financial Supervision) and comprising the General Counsel and senior management across Financial Supervision Group, can approve the triggering of resolution or winding up of a non-systemic financial institution. For resolution of financial institutions that may have a systemic impact or require resolution funding, decisions are escalated to the Crisis Management Team, chaired by the Managing Director and comprising senior management across MAS.

[49] Surveyed authorities that identify separation of conduct supervision as an approach to addressing potential conflicts with prudential supervision include, but are not limited to, ACPR, BCB, Bank of Italy and Bank of Spain.

[50] To allow for more focus on conduct and AML/CFT risks, the BCB also implemented a separate matrix, or rating system, for evaluating such risks, and excluded them from its prudential risk rating system. However, if prudential implications arise, findings related to AML/CFT and clients' relationship risks may be considered when assessing reputational risk, operational risk, strategy and governance.

[51] Eg ACPR, BoE and HKMA.

[52] Eg BNM, HKMA and MAS. See the BNM website (www.bnm.gov.my/index.php?rp=org_structure_en), the HKMA website (www.hkma.gov.hk/eng/about-us/the-hkma/organisation-chart/) and the MAS website (www.mas.gov.sg/who-we-are/Organisation-Structure).

[53] For example, at MAS, groups that report to the Deputy Managing Director for Markets & Development include the Development and International Group, which supports Singapore's growth as an international financial centre and promotes vibrant financial markets, and the Fintech and Innovation Group, which is responsible for policies and development strategies for technology and innovation to better manage risks, enhance efficiency and strengthen competitiveness in the financial sector. These are separate from supervisory functions, which report to the Deputy Managing Director for Financial Supervision.

authorities, functions related to licensing and competition also have their own reporting lines separate from those of supervisory functions.[54]

59. **Some of the surveyed authorities established a centralised team to facilitate engagement with different stakeholders representing competing objectives and to develop specialised capabilities.** Such a team is used as a point of contact for the industry on specific issues and is separate from prudential supervision. This approach has been adopted to promote fintech innovation and competition objectives. One example is the ACPR's Fintech Innovation Unit, directly attached to the Secretary General and aimed at developing expertise on innovation issues and assisting with the completion of new fintech entrants' licensing applications, while the power to approve bank licences lies in another department.[55] It coordinates with other ACPR directorates and, when necessary, with other authorities; it also seeks to enhance dialogue between authorities and fintech players. The authority views this initiative as supporting fintech growth by balancing the flexibility that the move towards innovation requires with necessary prudential security.[56]

60. **A centralised team may enable competing functions to work together in support of P&D objectives while allowing for the management of related risks.** As regards competition, APRA established a centralised licensing team to manage new licence applications, partnering with frontline supervisors and risk specialists and acting as a central point of contact.[57] This approach aims to enhance the licensing process and facilitate competitive dynamics, while maintaining a balance with the promotion of financial safety and stability. Another argument for establishing such a dedicated team is the development of expertise, including with regard to new, non-traditional business models.

61. **Apart from institutional arrangements, authorities also apply the principle of proportionality to balance trade-offs between S&S and promotional objectives.** A regulatory sandbox has been implemented in many jurisdictions with the goal of keeping a balance between promoting fintech innovations and maintaining S&S.[58] By balancing competition with S&S, APRA's Restricted License Framework allows new entrants to conduct limited banking business while developing their capabilities and resources, facilitating entry into the banking sector without substantially lowering entry standards.[59] A similar rationale and consideration of proportionality is reflected in Singapore's phased entry of digital banks.[60]

54 For example, at BCB, licensing and competition functions report to different Deputy Governors than do supervisory functions. At ACPR, there is a Directorate of Authorisation, separate from Bank Supervision Directorates. See the BCB website (www.bcb.gov.br/en/about/orgchart) and ACPR (2020).

55 See the ACPR website (https://acpr.banque-france.fr/en/acpr/organisation/fintech-innovation-unit). Another example regarding innovation is the HKMA's Fintech Facilitation Office (FFO), which is intended to facilitate the healthy development of the fintech ecosystem and promotes Hong Kong SAR as a fintech hub in Asia. Among other tasks, the FFO acts as an interface between market participants and regulators. The FFO has reporting lines separate from those of the banking departments that oversee prudential, conduct and AML/CFT risks. Another example of a dedicated licensing team is the UK's New Bank Start Up Unit, which is a joint initiative by the PRA and Financial Conduct Authority.

56 See ACPR (2017).

57 See APRA (2017). The centralised licensing team was established in 2017 within the Regulatory Affairs and Licensing unit under the Executive Director for Policy and Advice, separate from Banking Supervision under the Executive Director for Banking.

58 Eg in Hong Kong SAR and Singapore.

59 APRA (2018b).

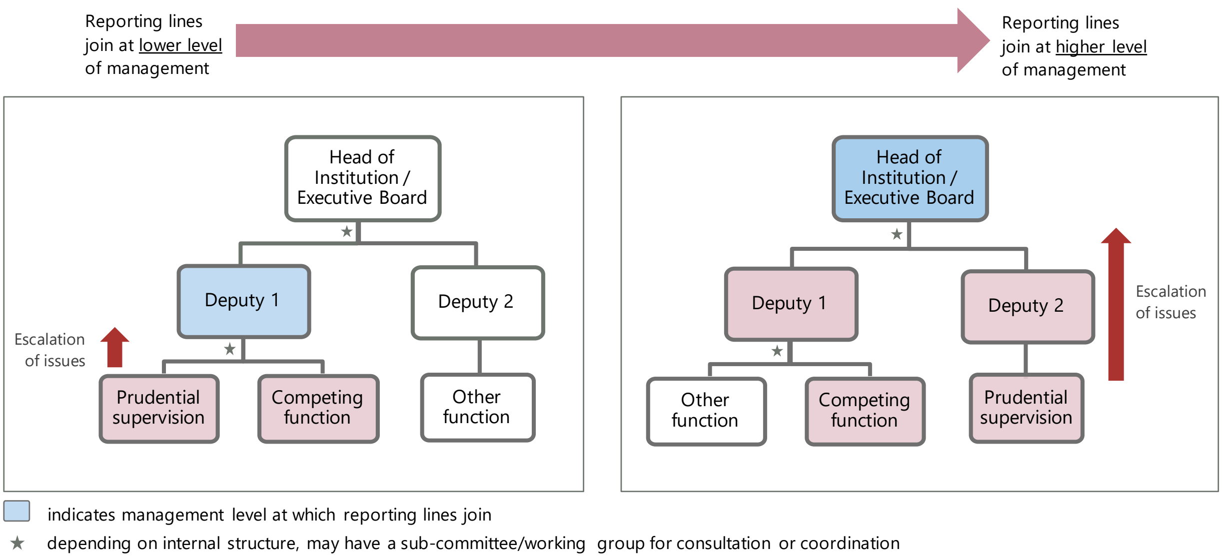
60 See MAS (2019). MAS has adopted a phase-in approach for digital banks' minimum paid-up capital and business scope. Digital banks are nonetheless subject to the same prudential requirements (such as risk-based capital) as incumbent banks.

Key elements for institutional arrangements

62. **Authorities' use of sound institutional arrangements to address potential conflicts suggests three key elements**: **independent decision-making structures, different reporting lines and separation of resources.** Decision-making on conflicting issues is typically escalated to and resolved by senior management or a management committee. Another general practice is to separate the reporting lines and staff of competing functions in order to preserve operational independence. While examples of arrangements drawn from the surveyed authorities are related to certain mandates, these approaches to conflict mitigation may be applicable to other potentially competing mandates. Specific arrangements must be designed to suit each authority's context and internal structure.

63. **In designing institutional frameworks, authorities may consider the degree of separation necessary to mitigate conflicts while maintaining sufficient coordination.** The higher the management level at which reporting lines join, the further removed the competing functions are from each other and the higher conflicting issues need to be escalated (Figure 9). On the other hand, the greater the degree of separation, the more pressing the need for effective coordination mechanisms. In this context, given the close links between S&S and S&O mandates, authorities can establish internal coordination protocols while maintaining independence between functions to mitigate potential conflicts.[61] As for P&D mandates, a higher degree of separation may be desirable since the risks of potential conflicts with the S&S mandate are greater. At the same time, the fulfilment of some P&D objectives – such as meeting a competition or fintech innovation remit by issuing new bank licences – requires close coordination with supervisors so that prudential considerations are factored into the licence approval process.

Figure 9: Degree of separation – where reporting lines join



64. **Adequacy of staff capacity is crucial in all institutional structures.** Ensuring sufficient staff capacity, in terms of headcount and skill sets, can better equip supervisors to take on additional mandates without diverting focus away from S&S. The array of risks that fall within an S&S mandate has become more complex and has continued to expand. Certain P&D objectives – such as fostering competition or promoting fintech innovation – have led to an increase in newly licensed banks and financial institutions with innovative business models. These developments underscore the challenge faced by supervisory

[61] Similarly, where S&O mandates are assigned to other authorities, mechanisms for coordination between such authorities and prudential supervisors are important in order to effectively fulfil S&S objectives.

authorities to maintain sufficient resources to effectively deliver on their S&S mandate,[62] let alone their capacity to carry out other supervisory mandates.

65. **Staff training on potentially conflicting supervisory mandates may enhance an authority's ability to balance different considerations, provided appropriate safeguards are in place.** The PRA introduced mandatory training on their secondary competition objective in order to help staff identify potential competition issues in the policy-making process and consider alternatives that can mitigate competition concerns without undermining S&S. This arrangement complements its statutory framework, which sets out a hierarchy of objectives. That said, without a clear prioritisation of objectives in the legal framework, staff training that focuses on other mandates may dilute supervisors' attention on S&S.

[62] APRA increased its staff headcount to accommodate the increased workload expected as a result of the restricted licence framework; the HKMA's banking supervision staff has increased by over 10% since the HKMA granted eight virtual banking licences between March and May of 2019.

Section 5 – Conclusion

66. **Despite general consensus (as reflected in the BCPs) that the primary objective of banking supervisory authorities is to promote the S&S of banks and the banking system, many authorities lack the necessary legal framework to this effect.** The mandates of banking supervisors, especially those of central banks or from EMDEs, seem to be expanding to include objectives that not only present potential conflicts with the core S&S mandate, but may also divert scarce supervisory resources away from this core objective. Not only have statutory mandates expanded without a clear prioritisation of the core S&S mandate; some banking supervisors are also broadening their non-statutory remits for a variety of reasons.

67. **Our survey revealed a number of institutional approaches, ranging from authorities that focus mainly on the S&S of banks to those that have broader promotional or surveillance mandates.** The expansion of supervisory mandates beyond S&S objectives is prompted by a combination of factors. These include lessons learned from the GFC, technological changes that are rapidly transforming the banking landscape, and broader economic and developmental goals, such as financial inclusion, to meet public expectations. Certain supervisors have also interpreted their S&S mandate to include emerging risks such as climate and cyber risks in addition to traditional risks that may have implications for prudential risk assessments, such as consumer protection and AML/CFT.

68. **The constellation of supervisory mandates can be broadly categorised into S&O and P&D mandates.** S&O mandates such as climate risk, AML/CFT, consumer protection and resolution show some complementarity with S&S mandates. In contrast, P&D mandates, such as facilitating fintech and innovation, promoting competition or financial inclusion are further removed from the S&S remit.

69. **The absence of a common understanding of what S&S means makes it difficult to identify the exact scope of this mandate and measure its fulfilment.** Supervisors need to have a well defined understanding of their S&S mandate. Without a clear understanding, authorities may not be compelled to take timely supervisory actions, particularly in the absence of any tangible indicators confirming that early action is warranted. Moreover, without a clear grasp of S&S, it is difficult to measure supervisory performance. Further work to define this mandate at a global level could contribute to a common understanding of what it entails. In doing so, a fine balance must be struck to enable supervisors to adapt their S&S responsibilities to address future risks.

70. **Some other supervisory objectives may potentially generate conflicts with core supervisory responsibilities.** Conflicts could arise when different objectives lead in opposing policy and supervisory directions. Moreover, multiple responsibilities may create operational constraints by drawing scarce resources away from the core S&S mandate. Resolution, competition and conduct of business objectives could potentially conflict with the S&S mandate. Yet, from the constellation of supervisory mandates, P&D objectives are the most likely to conflict with the S&S mandate. Careful consideration is warranted before expanding supervisory responsibilities to take on such mandates.

71. **Potential conflicts between mandates seem to be minimised or mitigated through two broad measures: statutory frameworks and institutional arrangements.** For most certainty, prioritisation of the S&S mandate should ideally be explicitly enshrined in the relevant legislation or regulation. Nevertheless, legislative prioritisation of an S&S mandate is necessary but not sufficient. It must be implemented in practice. Our survey found that the most common approach to minimising potential conflicts is through the structural separation of competing functions and a governance framework that empowers senior management to balance competing priorities. While the degree of structural separation between S&S and other competing objectives is context driven, there are merits in separating various P&D objectives furthest away from core supervision in order to minimise potential conflicts. In jurisdictions where legislation or other mechanisms do not explicitly prioritise the S&S mandate, it is particularly important that sound institutional arrangements be implemented.

72. **To deliver on their core S&S remit while addressing potential conflicts with other objectives, supervisors can consider initiatives such as**:

- *Establishing a clear S&S mandate and developing guidance to operationalise the term "safety and soundness"*: As required by the BCPs, legal frameworks should provide for a clear S&S mandate. The definition of S&S should be sufficiently broad so that the S&S remit is fit for purpose and provides supervisors with sufficient powers to assess various emerging prudential risks; at the same time, it should be granular enough to support the expectation that supervisors should intervene at an early stage.
- *Prioritising the S&S mandate to promote supervisors' independence*: Independence of supervisors from undue political influence is essential to enable effective discharge of S&S responsibilities. Explicitly stating that S&S is a priority mandate can help supervisors balance their core S&S remit against P&D objectives (such as fostering competition or facilitating fintech and innovation) championed by national governments. Expanding too much beyond the S&S mandate could risk losing institutional independence that is crucial to avoiding undue external pressures to act against this core mandate.
- *Utilising institutional arrangements to minimise potential frictions between competing objectives*: The effectiveness of practical measures to minimise conflicts – such as sound governance frameworks – hinges on whether potential conflicts are identified, elevated and adequately addressed by the relevant decision-making bodies.
- *Procuring adequate resources to deliver on supervisory mandates*: Supervisors need to regularly evaluate if their staffing and skill sets are commensurate with their mandates. Some authorities with a competition or fintech and innovation remit have licensed a number of new banks. These newly chartered banks, some of which are digital only, may require more staff with the requisite skills to supervise the new business models and their underlying technologies.
- *Publishing public statements on authorities' interpretations of their mandates to promote accountability*: Authorities can consider publishing a description of their objectives and/or target outcomes; the prioritisation of these objectives; and how potential conflicts between competing objectives are managed and mitigated, including via institutional arrangements and adequate resources. Such publications allow for an assessment of how well supervisors are delivering on their mandate.

73. **The core S&S mandate should stand the test of time even though banking supervisory practices will need to evolve with the financial landscape.** The fundamental objective and raison d'être of banking supervisors is ultimately to protect the interests of the general public. The banking supervision function was created to protect depositor interests and, more broadly, to regulate an industry that may otherwise not meet the needs of society. While supervisors will continue to have competing demands to take on new responsibilities, they will need to keep their eyes on the core S&S prize.

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Annex 1 – Jurisdictions covered in this study

Regional classification — Table A.1

Region	Banking supervisory authority	Jurisdiction
Africa	South African Reserve Bank – Prudential Authority	South Africa**
Americas	Central Bank of Argentina	Argentina**
Americas	Central Bank of Brazil	Brazil**
Americas	Office of the Superintendent of Financial Institutions	Canada*
Americas	National Banking and Securities Commission	Mexico**
Americas	Office of the Comptroller of the Currency	United States*
Asia-Pacific	Australian Prudential Regulation Authority	Australia*
Asia-Pacific	China Banking and Insurance Regulatory Commission	People's Republic of China**
Asia-Pacific	Hong Kong Monetary Authority	Hong Kong SAR*
Asia-Pacific	Reserve Bank of India	India**
Asia-Pacific	Indonesian Financial Services Authority	Indonesia**
Asia-Pacific	Japan Financial Services Authority	Japan*
Asia-Pacific	Central Bank of Malaysia	Malaysia**
Asia-Pacific	Central Bank of the Russian Federation	Russia**
Asia-Pacific	Monetary Authority of Singapore	Singapore*
Asia-Pacific	Bank of Thailand	Thailand**
Europe	European Central Bank	Euro area*
Europe	French Prudential Supervision and Resolution Authority	France*
Europe	Federal Financial Supervisory Authority	Germany*
Europe	Bank of Italy	Italy*
Europe	Netherlands Bank	Netherlands*
Europe	Financial Supervisory Authority of Norway	Norway*
Europe	Polish Financial Supervision Authority	Poland**
Europe	Bank of Spain	Spain*
Europe	Swiss Financial Market Supervisory Authority	Switzerland*
Europe	Bank of England	United Kingdom*
Middle East	Saudi Central Bank	Saudi Arabia**

* Advanced economies

** Emerging markets and developing economies