Basel Committee
on Banking Supervision

High-level principles for the cross-border implementation of the New Accord

August 2003

BANK FOR INTERNATIONAL SETTLEMENTS

Contents

High-level principles for the cross-border implementation of the New Accord

1. The Basel Committee recognises that the New Accord will require more cooperation and coordination between home country and host country supervisors, especially for complex banking groups. The New Accord will accentuate the need for cooperation because the new rules will be applied at each level of the banking group, so that there is a technical requirement on the part of both home country and host country supervisors to provide a Pillar 1 and Pillar 2 assessment. In addition, there may need to be some coordination regarding Pillar 3 requirements. Consequently, the Basel Committee encourages supervisors to elaborate further on the practical implications of the Basel Concordat (see below) for the implementation of the New Accord.

2. Where a banking group has operations in at least one country other than the home country, the implementation of the New Accord may require it to obtain approval for its use of certain approaches from relevant host country supervisors on an individual or sub-consolidated basis, as well as from its home country supervisor in respect of consolidated supervision. The need for approval of more than one supervisor is not a precedent; the 1996 Market Risk Amendment entailed similar requirements. However, the New Accord could significantly extend the scope of such multiple approvals and is therefore likely to create some new implementation challenges.

3. Closer cooperation between supervisors can assist the implementation efforts of both supervisors and banking groups. There are a variety of supervisory responsibilities under the New Accord, including: (1) initial approval and validation of “advanced” approaches (eg IRB, AMA) under Pillar 1; (2) the supervisory review process under Pillar 2; and (3) ongoing assessments to verify that banking groups are applying the New Accord properly and that the conditions for “advanced” approaches continue to be met. The degree and nature of cooperation between supervisors may differ across these different supervisory responsibilities. Whatever arrangements are employed, banks have an important role to play in assisting the effective and efficient cross-border implementation efforts of supervisors.

4. While arrangements for cooperation among supervisors must be practical, the Basel Committee has a clear interest in implementing the New Accord in a way that strengthens the quality of bank supervision across countries. The Committee should also promote the ability of all host supervisors, and especially of those from emerging market economies, to exercise effective host banking supervision over foreign institutions operating in their jurisdictions.

5. The Basel Committee believes that fostering closer practical cooperation between supervisors is essential to implement the New Accord as effectively and efficiently as possible. In particular, the following six principles apply:

Principle 1: The New Accord will not change the legal responsibilities of national supervisors for the regulation of their domestic institutions or the arrangements for consolidated supervision already put in place by the Basel Committee on Banking Supervision.

6. Cross-border responsibilities of supervisors, as set out in 'The Basel Concordat and Minimum Standards'[1] (the Basel Concordat) will continue to apply with the implementation of the New Accord. In essence, home country supervisors are responsible for consolidated supervision and host country supervisors are responsible for supervision on an individual or sub-consolidated basis for entities operating in their country.

7. The implementation of the New Accord should build on the existing framework of the Basel Concordat to achieve effective implementation across jurisdictions without imposing an undue burden on banking groups. The degree of closer practical cooperation between supervisors will be facilitated by certain preconditions for effective exchange of information and practical mutual recognition (eg the degree of equivalence of regulatory and supervisory systems, and acceptable approaches to information sharing and confidentiality).

Principle 2: The home country supervisor is responsible for the oversight of the implementation of the New Accord for a banking group on a consolidated basis.

8. For situations where the home country and host country supervisors adopt different approaches, the home country supervisor will have the final determination on such matters as they relate to the group on a consolidated basis. This does not mean that the home country supervisor will necessarily perform all of the assessment and analysis. In exercising its responsibilities, the home country supervisor may seek input from host country supervisors, particularly where a subsidiary in the host country is material to the group or the subsidiary's business differs significantly from that of the parent bank.

9. Given the nature of Pillar 2, the responsibility for Pillar 2 assessments of a consolidated banking group must rest with the home country supervisor. However, depending on the organisation of the banking group and the importance of activities within the host country, host country supervisors may provide important input into the home country assessment of Pillar 2 for the consolidated banking group. Home country supervisors should seek host country input, where appropriate.

Principle 3: Host country supervisors, particularly where banks operate in subsidiary form, have requirements that need to be understood and recognised.

10. In each country, banks operating in subsidiary form must satisfy the supervisory and legal requirements of the host jurisdiction. Certain jurisdictions may also have relevant requirements in the case of foreign bank branches.

11. Host country supervisors have an interest in accepting the methods and approval processes that the bank uses at the consolidated level, in order to reduce the compliance burden and avoid regulatory arbitrage. However, host country supervisors have other legitimate interests which may prevent them from recognising for use at the sub-consolidation level an approach approved at the group level, such as, for example, limitations

[1] Volume Three, Chapter I of the BCBS Compendium.

imposed by their legal obligations, or situations where the home country supervisor does not perform effective comprehensive consolidated supervision.

Principle 4: There will need to be enhanced and pragmatic cooperation among supervisors with legitimate interests. The home country supervisor should lead this coordination effort.

12. The sharing of supervisory results is an evolving practice. Supervisors should look for ways to continue to enhance cooperation and the exchange of information (eg sharing of examination results). Requests by host country supervisors for information on banking groups with operations in the host country should be reasonable in relation to the responsibilities and interests of both the home country and host country supervisors. Whatever arrangements are employed, the emphasis should be on those practical tools and procedures for fostering effective cross-border cooperation.

13. Supervisors should coordinate their respective work plans as far as possible, taking into account legal and other constraints. Over time, greater cooperation between home country and host country supervisors will increase efficiencies for both banks and supervisors.

14. As needed, the home country supervisor would be responsible for measures to organise practical cooperation between supervisors responsible for the material operations of the banking group. This would include holding discussions with the senior management of the group about their implementation plans, communicating these plans as necessary to relevant host country supervisors and agreeing with them the work to be undertaken by each supervisor. The home country supervisor would also develop an appropriate communication strategy with the relevant host country supervisors, supplementing existing cooperative agreements where necessary. As a practical matter, the frequency and scope of communication between supervisors would vary depending on the materiality of operations within the host country.

15. Agreements on cooperation and exchange of information should be recorded on whatever basis best suits individual supervisors. Some supervisors may opt for formal arrangements (like Memoranda of Understanding (MOUs) or other bilateral agreements), while others may prefer less formal communication strategies.

Principle 5: Wherever possible, supervisors should avoid performing redundant and uncoordinated approval and validation work in order to reduce the implementation burden on the banks, and conserve supervisory resources.

16. For initial and on-going validation and approval there is likely to be a particular need for cooperation between home country and host country supervisors because the nature of complex banking group structures increases the likelihood that different techniques will be used in different jurisdictions.

17. The Pillar 1 approval of a credit risk rating system for an IRB capital calculation or an Advanced Measurement Approach for operational risk involves many bank functions. In any given banking group, some of these functions will be carried out at the group level, while others will be performed at the level of the individual entity. It will be highly desirable for supervisors to coordinate their activities, as far as possible, to reflect the organisation and management structure of a banking group, in order to improve efficiency and thereby reduce the implementation burden on both banks and supervisors.

18. The degree of integration in a banking group's risk management, the extent to which a banking group uses a common approach, the availability of data and other factors (such as legal responsibilities), are likely to condition the nature of desirable cross-border arrangements. Where 'mind and management' are centralised in the banking group or where techniques are consistently applied across the group, the home country supervisor will probably be better placed to lead approval work. In such circumstances, the host country supervisor may choose to rely entirely on approval work conducted by the home country supervisor. Conversely, where there is limited integration or where one or more operating companies within the group are using different techniques from the rest of the group, or where, for example, an entity located in the host country manages a global business line, the host country supervisor may be better placed to take the lead for approval work regarding those techniques or those operations. But in this case the home country supervisor will need to maintain a sufficient level of information about the banking group and its operations in the host country, in order to allow it to meet its responsibilities under the New Accord.

Principle 6: In implementing the New Accord, supervisors should communicate the respective roles of home country and host country supervisors as clearly as possible to banking groups with significant cross-border operations in multiple jurisdictions. The home country supervisor would lead this coordination effort in cooperation with the host country supervisors.

19. It is desirable for home country supervisors, in cooperation with the host country supervisors, to develop a plan well in advance of the implementation date, detailing, as far as possible, the practical arrangements between the home country supervisor and relevant host country supervisors to be followed in implementing the New Accord. This will be particularly desirable for those "advanced" complex banking structures with significant cross-border operations because the practical supervisory arrangements will depend on how the banking group operates. This plan should be communicated to the affected banking group. In communicating the supervisory plan, supervisors will take care to clarify that existing supervisory legal responsibilities remain unchanged.

20. The home country supervisor would lead the development and communication of a supervisory plan. The level of detail contained within such a plan should be flexible and tailored to the individual circumstances of a banking group.