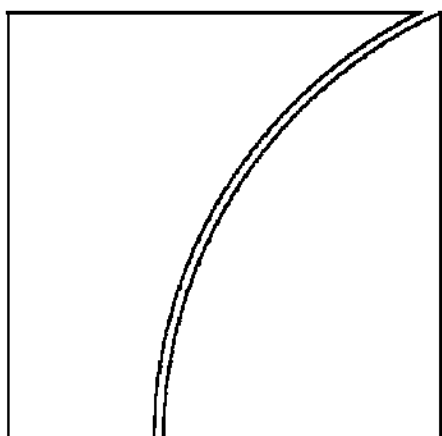


# Basel Committee on Banking Supervision



## **Good practice principles on supervisory colleges**

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## Contents

Introduction.....	1
Principle 1: College objectives.....	2
Principle 2: College structures.....	3
Principle 3: Information sharing.....	6
Principle 4: Communication channels.....	8
Principle 5: Collaborative work.....	9
Principle 6: Interaction with the institution.....	12
Principle 7: Crisis management.....	13
Principle 8: Macroprudential work.....	15
Appendix 1: European Union (EU) colleges.....	17
Appendix 2: Essential elements of a statement of cooperation between banking supervisors.....	18



# Good practice principles on supervisory colleges

## Introduction

Colleges of supervisors<sup>1</sup> are an important component of effective supervisory oversight of an international banking group. This message has been reinforced by the G20 in the wake of the financial crisis. Accordingly, the Basel Committee on Banking Supervision (BCBS) has issued this paper, which builds on previous publications outlining established good practices in colleges and provides some enhanced principles that can be used as a basis for continuing to improve the operation of supervisory colleges. This document does not intend to represent a definitive or exhaustive set of guidance regarding college functioning. These principles are, however, designed to help both home and host supervisors ensure that they work as effectively as possible by clearly outlining expectations in relation to college objectives, governance, communication and information, as well as potential areas for collaborative work.

The BCBS has adopted a principle-based approach so that the good practice principles in this paper are relevant to a wide range of banks across different jurisdictions. Therefore, the principles are designed to allow adequate flexibility in the way that they are implemented by different jurisdictions. To this end, it is reasonable to expect supervisors to discuss and agree on the most appropriate approach for their specific circumstances.

This paper is designed to assist supervisors in running colleges as effectively as possible. It is not meant to suggest that colleges should replace wider bilateral or multilateral cooperation between supervisors, nor impede existing national, bilateral or multilateral arrangements in this respect. Colleges should not be seen as a substitute for effective national supervision nor undermine the legal and prudential responsibilities of respective supervisors. Colleges are not intended to be decision-making bodies but should provide a framework to enhance effective supervision of international banking groups on a consolidated and solo<sup>2</sup> basis, and could inform decision-making in that regard.

While the scope of this paper goes beyond supervisory cooperation issues relating to Basel II implementation, it does not seek to replace broader guidance issued by the BCBS in the past on cooperation and information sharing between home and host supervisors. This set of good practice principles should therefore be interpreted in the context of broader aspects of home-host cooperation covered, for example, in the Committee's 1975 "Report on the supervision of banks' foreign establishments" (the "Concordat") and its 2006 principles on *Home-host information sharing for effective Basel II implementation*.<sup>3</sup> The BCBS intends to

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<sup>1</sup> In general "supervisory colleges" refer to multilateral working groups of relevant supervisors that are formed for the collective purpose of enhancing effective consolidated supervision of an international banking group on an ongoing basis.

<sup>2</sup> Solo supervision in this context refers to the supervision of a single legal entity as opposed to consolidated supervision refers to group oversight.

<sup>3</sup> The following documents have been published since the 1975 publication of the Concordat: *Principles for the supervision of banks' foreign establishments* (1983), *Minimum standards for the supervision of international banking groups and their cross-border establishments* (1992), *The supervision of cross-border banking* (1996), *Essential elements of a statement of cooperation between banking supervisors* (2001), *High-level principles for the cross-border implementation of the New Accord* (2003) and *Home-host information sharing for effective Basel II implementation* (2006).

review these good practice principles on supervisory colleges after approximately two years, in order to take stock of the key lessons learned.

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## **Principle 1: College objectives**

**Supervisory colleges should enhance information exchange and cooperation between supervisors to support the effective supervision of international banking groups. Colleges should enhance the mutual trust and appreciation of needs and responsibilities on which supervisory relationships are built.**

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### **Background**

The overarching objective of a supervisory college is to assist its members in developing a better understanding of the risk profile of the banking group. Moreover, information exchange and cooperation between supervisors can be useful to strengthen the supervision of the individual components of a banking group. Supervisory colleges are, effectively, working groups of supervisors of an international banking group, which have been part of the supervisory framework for some years.<sup>4</sup> Over time, they have become more integrated with supervisory cooperation and coordination. The introduction of Basel II emphasised the need for such supervisory cooperation, as supervisors worked together for model recognition. Supervisory colleges have since played an increasingly important role in sharing information and coordinating supervisory activities related to Basel II implementation, especially for large internationally active banking groups.

Despite not being decision-making bodies, supervisory colleges have developed a key role over time as a forum for broader issues such as discussion and planning of supervisory assessments and sharing information about the overall risk assessment of an international banking group. The role of supervisory colleges in crisis management and macroprudential analysis has also recently come to the fore. Practical experience suggests that college structures are a useful foundation for further collaboration between supervisors and other relevant authorities. For example, in the aftermath of the 2007 crisis some colleges operated as conduits for information sharing in relation to contingency planning and crisis management.

In this context, effective and efficient colleges are important, not only for consolidated supervision at the microprudential level, but also for the promotion of financial stability at the macroprudential level. Colleges can also complement wider peer review processes by promoting a coherent approach across different jurisdictions to the consistent and effective implementation of macroprudential and microprudential policy tools.

### **Implementation guidance**

Clear supervisory understanding and strong levels of mutual trust and confidence between national supervisors through the normal course of supervision are necessary constituents to facilitate the successful implementation of this principle.

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<sup>4</sup> The Basel Committee's Concordat and other documents related to cross-border supervision are accessible at [www.bis.org/list/bcbs/tid\\_24/index.htm](http://www.bis.org/list/bcbs/tid_24/index.htm).



The actual structure and organisation of colleges will vary depending on circumstances to ensure that there is effective information sharing and cooperation between relevant supervisors that does not impede existing national or regional arrangements. However, it is key that the organisation and cooperation processes are clear for all college members.

The delivery of this overarching principle is reliant on supervisors successfully implementing and delivering on the necessary components discussed in Principles 2 to 8.

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## **Principle 2: College structures**

**Supervisory colleges should be structured in a way that enhances effective oversight of international banking groups, taking into account the scale, structure, and complexity of the banking group and the corresponding needs of its supervisors. Whilst a college is a single forum, multiple or variable sub-structures may be used as no single college structure is likely to be suitable for all banks.**

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### **Background**

An international banking group, by definition, has operations in multiple jurisdictions. For the purposes of consolidated supervision, these cross-border operations can take the form of a branch, a subsidiary or other entity such as a joint venture. Two specific categories of supervisors, each with different but mutually reinforcing responsibilities, are important for understanding the relationships that drive the structure of a college: home supervisors and host supervisors.

Home supervisors are responsible for the supervisory oversight of a banking group on a consolidated basis. On the other hand, host supervisors may have different interests in relation to the supervision of the group as a whole depending on whether the group has material risk exposures in the host jurisdiction and whether it poses a systemic risk to the host jurisdiction. Thus, in its broadest sense, members of a college should include host supervisors who have a relevant subsidiary or a significant branch in their jurisdictions and who, therefore, have a shared interest in the effective supervisory oversight of the banking group.

### **Implementation guidance**

A college is a single forum even if it meets in different structures to reflect different supervisory requirements and practices. The structure used to achieve this should reflect supervisors' different roles and information needs. Therefore, it may be the case that different structures will be required for different banking groups, as described in this principle.

The home supervisor should take overall responsibility for designing college arrangements that reflect the nature, scale and complexity of the banking group and the needs of relevant supervisors associated with the group. To meet these objectives, the home supervisor should design the college structures based on the banking group's international operations in discussion, where appropriate, with host supervisors and the banking group. Home supervisors should also strive for consistency of practice between different college structures for an international banking group and effective communication between them. The college's design should be periodically reviewed so that its structures remain appropriate to the banking group as it evolves over time.

### **Enhancing consolidated supervision**

The structure should facilitate effective contribution and appropriate inputs by host supervisors to the home supervisor's overall supervisory assessment of the banking group in order to benefit from host supervisors' specific knowledge of local banking conditions, their ability to communicate directly with entities within their jurisdiction and their ability to take specific supervisory action. It should also allow home supervisors to monitor, assess and address risks faced by the banking group in host jurisdictions more effectively and efficiently. Possible college structures include:

**Unitary college:** This is the simplest college structure. A unitary college is likely to be appropriate where there are just a small number of supervisors, each with a material role in the supervisory oversight of the banking group. However, there may be instances where unitary colleges gather a larger number of supervisors.

**Dual core and universal college structures:** This is a variant of the unitary college combining a 'core' college of a few key supervisors that have responsibility for the primary risk-taking entities within the banking group, with a broader universal college.

**Variable structures:** Additional and variable structures may be appropriate for a college depending on the requirements of the banking group and relevant supervisors. As an example, please see Appendix 1 for arrangements within the European Union. This range of structures or variable geometry – at times with overlapping membership and modus operandi – can be effective in achieving the overarching aims of colleges. For example, there may be specific risk types relevant to the banking group that require more intensive engagement between particular supervisors. In addition, regional issues or business line concerns may merit information sharing between relevant supervisors in order to identify risks to the banking group.

For a given banking group, it is important to ensure that variable college structures are used to facilitate the work of the overall college and do not impede its overall objectives by unnecessary fragmentation. A consistent approach is important at all levels of the college such that, for example, any increase in complexity of a college structure is accompanied by a strengthening in the minimum common practice developed by the home supervisor, taking into account the needs of host supervisors.

#### **Results of BCBS survey on college structures**

In July 2009, the BCBS surveyed a wide range of supervisors involved in supervisory colleges and found that different structures were adopted for different banking groups. In some cases, a single college structure appeared to be suitable where a limited number of supervisors had material responsibility for a banking group's supervisory oversight. In other cases, simple core and universal college structures helped in balancing the high-level needs of home and host supervisors.

However, in some cases, even more flexibility was required to effectively address the needs of both home and host supervisors. For example, additional regional college structures to support effective information sharing and understanding of risk profile between a group of supervisors who are not part of the core college. This type of information sharing is essential for host supervisors as well as serving to inform the supervision of the banking group as a whole.

Additional college structures could also be aligned with key business lines within the banking group to facilitate specific discussion of the risk profile of particular business lines.

### ***Membership criteria***

A home supervisor will have a specific interest in the most material parts of the banking group and should identify supervisors for the core college, with whom it will have ongoing and continuous dialogue. Therefore, the core college, which may include as few as two supervisors, is likely to take on the role of the key forum for sharing information.

The specific criteria for membership of the various college structures will vary on a case-by-case basis, such as the degree to which a supervisor has material supervisory oversight of part of the banking group (eg based on a significant proportion of group risk-weighted assets). In determining appropriate sub-structures the materiality of the banking group in the host jurisdiction(s) should also be considered.

In light of the close relationship between core colleges and crisis management groups and the critical role played by central banks during a crisis, their inclusion in the core college may be considered in those cases where the home supervisor regards the participation of its central bank as appropriate.

Likewise, there may at times be reason to include non-banking and non-prudential supervisors in various structures of the college. This should be considered, on a case-by-case basis, where such inclusion would significantly enhance the ability of members of the college in supervising the banking group and identifying potential risks with systemic implications. For example, the insurance prudential supervisor may be invited to attend some college meetings if the group has a significant insurance entity. Or the college may wish to consider discussing group risk issues with securities supervisors if there is a significant securities arm. The home supervisor should consider the merits of the inclusion of such supervisors in various sub-structures of the college and agree this with the relevant members of the college, bearing in mind legal and confidentiality issues.

### ***Governance by the home supervisor***

The home supervisor is responsible for designing and coordinating the work of the various college structures so that the college focuses on relevant group-level issues. The home supervisor should design the college structure and coordinate the agenda and action plans of all sub-structures so that they enhance consolidated supervision. In this context, promoting appropriate levels of accountability across the college structure should be taken into account as well, particularly regarding follow-up work agreed. The home supervisor should also keep college members sufficiently informed of the different college structures' activities. This should facilitate effective input to discussions from college members, so that even college members not invited to participate in a particular college structure are in a position to provide input to the issues under discussion as appropriate.

### ***Mechanisms to facilitate the college's operational functioning***

To ensure the efficiency and effectiveness of the college, the home supervisor should act as a central point of contact for any matter related to the organisation or operation of its structures. The home supervisor should ensure that the following common functions are performed:

- circulation of meeting agendas and updated contact lists of college members;
- recording of meeting minutes and formal action points;
- ensuring a common approach to information sharing and tasks;
- management of communication channels between supervisors;

- facilitating communication between the banking group, the college structures and other relevant authorities, particularly in emergency situations;
- implementation of outcomes when coordinated supervisory actions are adopted (eg risk assessment of the banking group); and
- consideration of regional outreach meetings to facilitate discussion of regional issues and appropriate access to information for relevant host supervisors.

### ***Transparency in college structures***

The home supervisor should periodically notify host supervisors and the BCBS of the structure of the college and relevant participants, including variable and ad-hoc sub-structures that are used for specific purposes. The home supervisor should also inform the banking group of the overall college structure. The universal college should be notified of changes to the membership of the core college.

### ***Representation***

Host supervisors should inform the home supervisor who their representatives in relevant college structures are. The seniority of representatives should ensure that the information shared at college meetings is relevant to each member's high-level supervisory position. Representation at colleges should be appropriate to facilitate their efficient and effective functioning.

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## **Principle 3: Information sharing**

**College members should make their best efforts to share appropriate information with respect to the principal risks and risk management practices of the banking group. Mutual trust and relationships are key for effective information sharing. Nonetheless, formal confidentiality agreements, such as contained in Memoranda of Understanding (MoUs), among college members facilitate this process.**

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### **Background**

Effective consolidated supervision of an international banking group requires the home supervisor to have sufficient knowledge of the operations of the group, both domestic and foreign, so as to monitor, assess and deal with risks faced by the group. The host supervisor should have corresponding knowledge with respect to the group's operations within its jurisdiction and the impact of those operations on the group. A successful college outcome entails effective information exchange between home supervisors and host supervisors.

Formal information gateways should be underpinned by trust and a network of relationships, particularly where confidential information is concerned. Formal agreements generally should cover the types of information that supervisors would wish to share at any level of the college. However, the lack of such agreements should not impede effective information sharing between members of the college, consistent with applicable law.

### **Implementation guidance**

Best practices for universal and core college structures are outlined below. The range and detail of information will vary between the best practice points of these two structures according to the needs of the particular college structure.

The information shared should reflect the circumstances, risk profile and main risks of the banking group, as well as the information needs of college members based on the principles of proportionality and materiality. In addition, college members should endeavour to encourage the flow of information and contribute to it. The flow of information generally should be continuous and timely, as part of an ongoing college process, rather than a discrete one-off or periodic event.

Information shared at universal colleges is likely to focus on areas of information that are widely relevant (eg risk profiles and supervisory processes). In addition, the information shared at the core college level typically is more detailed, and often quantitative in nature.

The information that is shared by a banking group or its supervisors at a college meeting will vary on a case-by-case basis. However, the following table illustrates recommended and optional information, which the home supervisor should consider providing for universal and core colleges, insofar as it is available and subject to any relevant legal or confidentiality constraints, particularly with regard to market sensitive information. In practice, therefore, it may be that some areas identified below as recommended for universal colleges (eg capital and liquidity plans) may only be appropriate to exchange at the core college level. However, the aspiration for colleges should continue to be greater exchange of information wherever feasible.

### Illustrative example of information exchange in colleges

College Information	Universal	Core
<b>Recommended</b>	<ul style="list-style-type: none"> <li>• High level supervisory risk assessment</li> <li>• A summary of priority risks across business, geographic and key risk dimensions</li> <li>• A summary of the economic environment in relevant/ material jurisdictions/markets, as well as results of stress tests</li> <li>• Supervisory plan</li> <li>• Organisation charts</li> <li>• A summary of relevant financial reports/statements including highlights of financial position and prospects</li> <li>• Capital position/plan</li> <li>• Liquidity position/plan</li> <li>• Key supervisory contact list for both day-to-day supervisory and crisis management purposes</li> </ul>	<ul style="list-style-type: none"> <li>• Detailed supervisory risk assessments and significant findings from relevant risk reports</li> <li>• Extracts from (enterprise-wide) risk reports covering: priority risks across business and geographic lines, as well as credit, market and operational risks</li> <li>• Analysis of the economic environment of material/relevant jurisdictions/markets and results of stress tests</li> <li>• Supervisory plan</li> <li>• Detailed organisation charts</li> <li>• Key financial reports/statements of financial position and prospects</li> <li>• Capital position/plan</li> <li>• Liquidity position/plan</li> <li>• Strategic summary</li> <li>• Crisis management plan</li> <li>• Key supervisory contact list for both day-to-day supervisory and crisis management purposes</li> <li>• Summary of remuneration practices</li> </ul>

College Information	Universal	Core
<b>Optional</b>	<ul style="list-style-type: none"> <li>• Summary of:                             <ul style="list-style-type: none"> <li>– Strategic plans</li> <li>– Credit risk reports</li> <li>– Market risk reports</li> <li>– Operational risk and infrastructure reports</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Group-wide and subsidiary strategic plans</li> <li>• Highlights of relevant material reports from such key sources as:                             <ul style="list-style-type: none"> <li>– Internal audit</li> <li>– Compliance</li> <li>– External audit</li> <li>– External consultants</li> </ul> </li> </ul>

In the case of colleges with variable structures, it is up to the home supervisors to decide the information that should be delivered to each layer of members.

### ***Mechanisms for establishing information gateways***

Information gateways may primarily be established through a MoU, which outlines procedures and provisions for the confidentiality, use and sharing of information. It may be the case that some college members do not have a MoU in place with all attending college supervisors. In these cases, further information gateways may be created through amendments to existing MoUs or college-specific confidentiality agreements. Please see Appendix 2 for the essential elements of a statement of mutual cooperation, such as contained in a MoU.

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## **Principle 4: Communication channels**

**Communication channels within a college should ensure the efficiency, ease of use, integrity and confidentiality of information exchange. The home supervisor should make sound communication channels available to the college and host supervisors should use them appropriately and continuously.**

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### **Background**

Supervisors have found that a range of communication channels are required for effective functioning of colleges. These include physical meetings, video and/or audio conferences, secure online communication tools, e-mail infrastructure and official letters. Some home supervisors have developed secure web-based communication channels (eg secure websites) in order to keep all college members informed of college matters. Communication channels should be sufficiently secure.

### **Implementation guidance**

Supervisory colleges are encouraged to make use of all relevant communication channels to facilitate effective information sharing. The choice of communication channels should be based on improving cooperation between supervisors and should take account of differences in geography and language. Communication channels should make exchange of information easy, fast and reliable whilst maintaining confidentiality. Physical meetings should be held on a regular basis as agreed by members of relevant college structures and for the core colleges of the largest banking groups, at least annually.

In between physical meetings, use of video and/or audio conferences should be considered to facilitate exchange of supervisory assessments and should be arranged on a case-by-case basis when specific items and objectives need to be discussed. Contact lists should be established containing up-to-date names, responsibilities and contact data for all representatives of the supervisory authorities in the college. The list should be used both in the course of regular supervision as well as in crisis management and it should be up-to-date and freely available.

Host supervisors should inform the home supervisor of any specific confidentiality arrangements that will impact the use of the communication channels, so that these can be resolved on a best-efforts basis.

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## **Principle 5: Collaborative work**

**Supervisory colleges should promote collaborative work between members, as appropriate, to improve the effectiveness of the oversight of international banking groups. Collaborative work should be based on agreement between supervisors and should recognise national legal constraints.**

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### **Background**

Home and host supervisors may seek to coordinate and plan supervisory activities or undertake joint work amongst college members in order to increase the efficiency of the college and of the individual supervisors. Supervisory colleges are expected to focus on their key functions of facilitating information exchange and the development and maintenance of a sound network of supervisors whilst promoting specific areas of collaborative work. College members should therefore recognise that there are likely to be specific work streams that could be undertaken in a collaborative fashion in order to improve the effectiveness of consolidated supervision of international banking groups. To this end, college members should ensure they have the ability, where appropriate, to share and allocate work in the pursuit of the college objectives.

Implementation of Basel II has resulted in improvements to supervisory coordination, for example with respect to specific projects such as model approval or validation work that involve the sharing of tasks and the delegation of work between home and host supervisors of international banking groups. Similarly with regard to Pillar 2 (supervisory review process), college members have shared methodologies and, in some cases, undertaken joint on-site inspections of banking groups' economic capital models.

### **Implementation guidance**

When designing the role and functions of a college, the potential for collaborative work should be considered according to the nature, scale and complexity of the banking group.

Collaborative work may be undertaken at various levels of a college. It is likely to occur in a core college but some areas of work may be identified in sub-structures and in the universal college structure. This should not however, necessarily replace existing bilateral arrangements.

### ***Benefits from collaborative work***

College members should be encouraged to coordinate work, as long as doing so does not conflict with any legal requirements and has a specific and identified value in terms of enhancing the consolidated supervision of the international banking group.

Collaboration should improve the quality of the supervisory assessment of the banking group (eg with respect to its risk exposures, capital adequacy and governance). In general, therefore, it leads to a better overview and understanding of the banking group's risk profile.

Collaborative work should also seek to reduce the burden on supervisors and banking groups by avoiding duplication of effort and enhancing the quality of supervision through better information sharing and allocation of expertise. Collaboration may also serve as a conduit to develop supervisory work programmes or improve coordination of supervisory approaches.

### ***Scope of collaborative work***

Collaborative work may focus on one or more group entities (domestic and foreign), the banking group as a whole, or specific aspects of the group's or an entity's functions. Collaboration between supervisors may be more likely in particular areas of work such as model approval, risk assessment and stress testing. Therefore in the future, college members may wish to consider coordinating work in these areas in particular.

### ***Process of collaborative work***

The home supervisor should lead any coordination of work between supervisors generally. College members who agree to undertake collaborative work should be aware of any legal and regulatory restrictions or confidentiality constraints that may impact the extent of collaboration. In addition, they should agree the roles of each supervisor involved in the work and communicate these clearly to the banking group. Supervisors involved in collaborative work should also agree on the extent to which other college members should have access to the results of collaborative work, subject to any legal requirements or confidentiality constraints.

Sharing and allocation of tasks does not absolve supervisors of their obligations. In particular, collaborative work should not imply delegation of an individual supervisor's responsibilities, or of joint decision-making responsibilities.

Collaborative work should only occur where there is agreement between the supervisors involved, as with on-site inspections, which are generally subject to the relevant supervisors' prior consent. Collaboration should be consistent with individual jurisdictions' legal requirements and the responsibilities of national supervisors.

### **Examples of collaborative work**

#### ***Risk assessment and stress testing***

One of the objectives of supervisory colleges is to enable college participants to develop a common understanding of the banking group's risk profile, as a starting point for effective supervision at the consolidated level. Evaluation of the main risks in banking groups is an important stage of the supervisory review and evaluation process (Pillar 2). The high-level issues colleges should consider are:



- For large, complex and internationally active banking groups, the home supervisor should take account of local supervisory risk assessments when performing assessment at the consolidated level. Likewise, where local supervisory review and evaluation processes rely on central inputs, host supervisors should consider consolidated analysis and insight on group-wide processes.
- As a result of the risk assessment process, the members of a supervisory college should be satisfied that the banking group has an adequate risk management framework in place aligned with the size and complexity of the banking group's operations and governed by policies and procedures that identify, assess, monitor and mitigate relevant risks.
- The scope of a risk assessment may vary with the size, business lines, products and systemic importance of the banking group and its individual entities. The home supervisor should determine timescales for the contributions of college members to the risk assessment on a case-by-case basis. The home supervisor has a responsibility to take account of local risk assessments in performing its assessment at the consolidated level and accordingly to adjust its judgment on the overall capital requirement for the banking group as necessary. Similarly host supervisors should draw on all relevant risk assessments to inform their own assessment and associated outcomes.
- The stress test results of the group and material entities may be considered as part of the college's risk assessment. Colleges may consider whether to coordinate a stress testing exercise across the banking group.
- The college should discuss the bank's forward-looking capital plans under stressed conditions in the context of relevant and credible management actions to ensure solvency in a stress event.

### ***Model validation***

In connection with model approval, the home and host supervisors may work together in the college to reach a view on use of internal models. The high-level issues they would consider are:

- The allocation of tasks taking into account the organisation of the group as well as the type and characteristics of the models, to avoid duplication of work and unnecessary supervisory burden;
- The structure of the application form and the details of the review and validation plan;
- Coordination and review of the supervisory action plan. The college may discuss the draft assessment prepared by the home supervisor; and
- Coordination and ongoing review of the model's compliance with requirements. College members may discuss the consequences of non-compliance with the requirements.

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## Principle 6: Interaction with the institution

**Interaction between the college members and the banking group should complement the interaction that individual supervisors (both home and host) have with the specific entity they supervise.**

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### Background

In the context of multiple supervisors and banking operations in different jurisdictions, normal interaction between relevant supervisors, the banking group and its international operations will remain in place but the college structure may assist in enhancing the coordination of information requests and other work.

### Implementation guidance

#### **(i) Information to be communicated to the banking group**

The college should agree the type of information related to the college that should be communicated to the banking group (eg sharing/delegation of tasks agreed, supervisory plans for on-site inspections, supervisory risk assessment findings etc). In addition, colleges may choose to consider providing additional feedback from the college to management of the group, reporting on key outcomes of college meetings.

The home supervisor should take responsibility for communication with the banking group and the host supervisors should take responsibility for communication with the banking group's operations in their local jurisdictions. However for specific issues, the college may agree on other methods of communication.

Sharing information with the banking group should be consistent with individual jurisdictions' legal requirements regarding confidentiality.

#### **(ii) Information to be requested from the banking group**

Information requests from the banking group in connection with the college should be coordinated by the home supervisor (eg a list of information should be established covering strategy, future business plans, etc).

It is likely that host supervisors will request information from the banking group's operations in the host jurisdictions<sup>5</sup> and that the home supervisor will request information from the parent. In addition, it is recognised that host supervisors may require relevant information on the banking group as a whole that may have a significant impact on the banking operations in their jurisdiction. In the unlikely event that host supervisors are unable to obtain relevant information from local management they should address group information requests to the home supervisor. Home supervisors will endeavor to accommodate information requests from host supervisors in a prompt manner, subject to the general principles of relevance, materiality and proportionality.<sup>6</sup>

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<sup>5</sup> Banking groups should empower local management to accommodate information requests from local supervisors.

<sup>6</sup> *Home-host information sharing for effective Basel II implementation* (2006).

**(iii) Participation of the banking group in college meetings**

The banking group may be invited to attend some universal college meetings to provide information on its plans and strategy, so that college members are informed of the high-level outlook for the banking group. It is also expected that more in-depth and focused discussions with senior management of the group will take place in other college structures (core, business line, bilateral).

Discussions between the banking group and the college may take place at different levels of seniority depending on the topics being discussed.

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## **Principle 7: Crisis management**

**Supervisory colleges and crisis management structures are distinct but complementary. The work of a banking group's supervisory college should serve as one of the building blocks for crisis management planning.**

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### **Background**

The Financial Stability Forum (now the Financial Stability Board - FSB) published *Enhancing Market and Institutional Resilience* in April 2008 recommending that a supervisory college be established for each of the largest global financial institutions as a means to improve information exchange and cooperation between authorities. Similarly, the G20 Action Plan in November 2008 supported the creation of supervisory colleges for all major cross-border financial institutions.

In April 2009, the *FSB Principles for Cross-border Cooperation on Crisis Management* were endorsed by G20 Leaders at the London Summit. The principles recommended that relevant supervisory and non-supervisory authorities meet on an annual basis to discuss contingency planning and consider any constraints to coordinated action in times of severe stress. In general, crisis management planning arrangements should build on the work of colleges and, as such, the annual crisis management group meeting should probably take place in conjunction with a meeting of the core college (or other relevant college sub-structure). Supervisory colleges will work to ensure smooth functioning with other developments in crisis management structures as they emerge.

### **Implementation guidance**

Colleges should facilitate effective crisis management for the banking group concerned, by assisting in planning the crisis management meeting, encouraging the banking group to produce appropriate information for crisis management and serving as a conduit for information sharing.

**(i) Crisis management meeting**

The home supervisor, assisted by core college members, should identify the relevant supervisory and non-supervisory authorities involved in a banking group's crisis management.

Building on the information sharing protocols developed for the college, supervisors should determine if additional/different protocols are required for crisis management purposes. This may involve identifying the types of information that can/should be shared with non-

supervisory authorities and ensuring that confidentiality arrangements are in place with the authorities involved as appropriate.

The home supervisor should set the time and agenda for the annual crisis management planning meeting.

**(ii) Banking group information**

The core college should regularly review and discuss a banking group's contingency planning with a view to ensuring that it is reasonable and that the group can meet ongoing supervisory needs as well as crisis management needs. Specific areas of review should include:

- robustness and timeliness of the contingency planning process; and
- severity of stress scenarios for capital and liquidity planning.

Group-wide management information systems that meet supervisory and crisis management needs (eg group structure, assets, exposures, revenues, etc) should be identified. In addition:

- core college members, led by the home supervisor, should explore whether, to the extent practicable, data items and report formats could be standardised to avoid creation of multiple reports across jurisdictions that provide the same information; and
- management information systems should be kept up to date and should be amended as necessary for supervisory and crisis management purposes.

The core college should identify any host country reports that are critical for crisis management.

**(iii) Information sharing**

Where there are non-supervisory authorities involved in a banking group's crisis management, core college members should, as appropriate, consider:

- identifying points of contact;
- establishing relationships with non-supervisory authorities in their home jurisdictions; and
- working with non-supervisory authorities to ensure that members have sufficient knowledge of the banking group.

During the resolution of an institution, core college members should, consistent with applicable law, provide current, relevant information on the institution to non-supervisory authorities involved in crisis management as appropriate.

Subject to legal and confidentiality constraints, the crisis management group generally should be provided with presentations or other information on the banking group (eg structure, risks, interconnected businesses, etc) that is provided to the supervisory college.

In general, home country authorities have primary responsibility for sharing information in times of crisis. However, the supervisory college can facilitate this process by:

- maintaining information on key points of contact for the banking group as well as relevant authorities;

- identifying key sources of information in host jurisdictions; and
- identifying vulnerabilities that may affect crisis management.

In times of crisis, the home supervisor may rely on host supervisors to disseminate information to authorities in their countries that are involved in the banking group's crisis management.

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## **Principle 8: Macroprudential work**

**Supervisory colleges can help ensure that the intensity of supervision of large, complex, internationally active banking groups is tailored to their systemic importance. Supervisory colleges should facilitate the process of identification and dissemination of information relevant to macroprudential analysis.**

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### **Background**

There are clear links between the role of the supervisory college and macroprudential supervision. Even though colleges are structured around individual banking groups, financial stability requires that the supervisory approach for the largest, most internationally active banking groups is related to the systemic impact that an idiosyncratic problem can have on the financial system and potentially the real economy. Colleges are well positioned to help identify emerging systemic problems because they bring supervisors together on a global basis.

At present, risk assessments are typically conducted using a “bottom-up” approach, which seeks to combine assessments of individual risks, associated controls and risk management processes in order to obtain an overall risk assessment for market, credit, operational, legal and liquidity risks. Going forward, risk assessments may also include a “top-down” macroprudential perspective that could identify issues such as position concentrations, correlations, and problematic asset class pricing levels.

Colleges may also serve as a mechanism for collecting information for macroprudential analyses that identify market-wide and firm-specific vulnerabilities.

### **Implementation guidance**

As the international debate about macroprudential supervision develops, there may be more that colleges can do to help to achieve the objectives of this principle. However, supervisory colleges can help to ensure that supervisory programmes for systemically important banks cover the potential systemic impact of stress events, and colleges should start to incorporate this objective.

One area of defining a clearer link between supervisory colleges and relevant macroprudential oversight structures is for colleges to promote consistent and effective implementation of macroprudential tools. National supervisors may choose different combinations of policy tools to tackle the too-big-to-fail problem associated with systemically important banks to reflect their individual circumstances. This implies that internationally active banks could be subject to different sets of rules depending on the jurisdictions in which they operate. Supervisory colleges could usefully exchange information on different supervisory approaches, assess their consistency, and consider ways to enhance their effectiveness. Colleges should also play an important role in peer review processes to ensure consistent and effective implementation.

In identifying and disseminating information relevant to macroprudential analysis, members of supervisory colleges should consider both institutional data and supervisory assessments, for example Pillar 2 risk assessments, and how they support the analysis of systemic risk.

## Appendix 1

### European Union (EU) colleges

EU competent authorities have developed a framework of cooperation which is legally binding for all supervisory authorities from the European Economic Area (EEA) (in particular the Capital Requirement Directive-CRD n° 2006/48/EC<sup>7</sup>). This legal framework also address colleges and requires the Committee of European Banking Supervisors (CEBS) to develop guidelines for their operational functioning (the most recent work being *CEBS' Guidelines for the Operational Functioning of Colleges* – published June 2010). CEBS also developed a MoU template on the basis of the practical experience of EU colleges, which all EEA supervisors will have signed by the end of 2010.

The EU has long and solid experience of multilateral cooperation and coordination in the supervision of EU cross-border banking groups and therefore EU colleges do not simply reflect local legal arrangements in one jurisdiction. However, EU cross-border banks are increasingly developing their businesses in significant non-EU jurisdictions, particularly in North America and Asia. Consequently, the EU framework has been designed to link non-EEA supervisors to EU colleges.

The potential input from non-EEA host supervisors to the consolidated supervision of international banking groups has to be considered carefully, particularly because centralised risk processes and procedures of international banking groups may implicitly cover both EEA and non-EEA jurisdictions. Also, non-EEA operations could be significant to the financial soundness of some EU cross-border banking groups. Consequently the EU home supervisor, subject to agreed upon confidentiality requirements, is required to:

- include non-EEA host supervisors of significant operations of an EU cross-border banking group in relevant activities of the college when a single college with multiple structures has been established; and
- consult non-EEA host supervisors of significant operations of an EU cross-border banking group to agree their individual contributions to other activities of the college (including model validation and Pillar 2 supervisory review) taking into account their own prudential standards. This is the case even if non-EEA host supervisors are not bound by the joint decision processes on model validation and the levels of own funds under Pillar 2.

The EU home supervisor has to ensure that non-EEA supervisors contribute to the assessment of major risks within the banking group. It consults with non-EEA supervisors to determine whether a risk assessment of their relevant entities can be shared within the college as additional input to the EU-coordinated risk assessment of the group.

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<sup>7</sup> From end 2010, EU competent authorities will be bound by the provisions on colleges of supervisors set out in Directive 2009/111/EC of 16 September which amended Directive 2006/48/EC.

## Appendix 2

### Essential elements of a statement of cooperation between banking supervisors

Following the recent development of principles on the effective functioning of supervisory colleges (*Good practice principles on supervisory colleges*, October 2010), the Basel Committee agreed that it would be useful to update a May 2001 statement of cooperation between banking supervisors (*Essential elements of a statement of cooperation between banking supervisors*).

Similar to the 2001 paper, this paper sets out the essential elements of a statement of mutual cooperation, such as contained in a Memorandum of Understanding (MoU) or similar arrangement, that can be used as a reference for establishing bilateral or multilateral relationships between banking supervisory authorities in different countries (and, where appropriate, between banking supervisors and other financial regulators). This paper is intended to provide a framework for mutual cooperation between supervisors, leaving sufficient discretion and flexibility for supervisors to add additional details and responsibilities, if they so wish and upon mutual agreement, when entering into bilateral or multilateral relationships. The Basel Committee encourages convergence towards this common framework, particularly for countries that are seeking to develop an institutional framework for supervisory cooperation or are in the process of doing so.

There are different ways in which the relationship between the two sets of supervisors can gain expression. Some prefer something akin to a legal document which is drafted by lawyers to provide protection to both parties, while others prefer a simpler and more flexible understanding that can be set out in an informal exchange of letters. The manner in which the understanding is framed will be a matter for the countries concerned. The essential elements of a statement of mutual cooperation, as set out below, can be included in either approach, but experience has shown that supervisors should take care that any statement does not become too prescriptive or they may find themselves constrained in their ability to communicate.

Basel Committee policy statements in recent years have encouraged countries to update privacy laws to facilitate consolidated supervision by home country supervisors, including the assessment of “know-your-customer” (KYC) principles.<sup>8</sup> Nevertheless, national laws in some countries, for example laws designed to protect the privacy interests of bank customers, may limit the transmission of information between supervisory authorities. Any statement of mutual cooperation along the lines proposed here cannot override such laws. In agreeing to a statement, each supervisor should inform the other of the existence of any legislative or administrative restrictions on information exchange, and if all relevant parties so wish, these caveats could be detailed in the statement.

It is important that there are no impediments to the flow of information from a cross-border establishment to its parent institution as necessary for risk management on a global basis, and for compiling consolidated reports to the home supervisor. Any significant impediments

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<sup>8</sup> 2006 Core Principles Methodology (CP25, EC7); October 2004 Consolidated KYC Risk Management (see paragraphs 21 and 25).



will mean that the parent institution is not able to conduct effective oversight of its consolidated operations or its own operations abroad, and should not be operating in that foreign jurisdiction.

The Committee recognises that in certain circumstances, there will be significant costs associated with the provision of assistance, eg when a home supervisor requests a host supervisor to carry out specific investigatory and/or enforcement action. Parties to a statement of mutual cooperation may therefore wish to refer in the statement to the circumstances when cost sharing arrangements might be applicable.

## Essential elements of a statement of mutual cooperation

This note sets out the essential elements of a statement of mutual cooperation designed to establish arrangements for the sharing of information<sup>9</sup> between the supervisors of country<sup>10</sup> A and country B<sup>11</sup>, in order to facilitate the performance of their respective duties and to promote the safe and sound functioning of financial institutions<sup>12</sup> with cross-border establishments in their respective countries.

The supervisors in country A and country B should express, through these arrangements, their willingness to cooperate with each other on the basis of mutual trust and understanding in the supervision of cross-border establishments within their respective jurisdictions. A cross-border establishment is defined to include a branch, a subsidiary<sup>13</sup> or any other entity within the jurisdictions which gives rise to the need for consolidated supervision.

The supervisors in country A and country B should recognise the complementary character of their supervision of a cross-border establishment. Their statement should demonstrate their commitment to the principles of effective consolidated supervision and cooperation between banking supervisors, and to their respective responsibilities, as set out in the Basel Committee's Concordat and Core Principles for Effective Banking Supervision. In accordance with the Core Principles, each supervisor should assess the nature and extent of the supervision conducted by the other party, so as to determine the extent of reliance that can be placed on that supervision.

### Sharing of information

Formal statements of mutual cooperation, such as contained in MoUs, outline procedures and provisions for the confidentiality, use and sharing of information. But these must be underpinned by trust and a network of relationships that are required for effective information sharing, particularly where confidential information is concerned.

The statement of mutual cooperation should recognise that information needs to be shared between the relevant authorities in country A and country B in order to facilitate effective consolidated supervision of financial institutions operating across their national borders and solo supervision of group entities in the host jurisdiction. Information sharing should include contact during the authorisation and licensing process, during supervision of ongoing activities and during the handling of problem institutions.

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<sup>9</sup> In this document, information refers to both supervisory and enforcement information.

<sup>10</sup> In this document, country refers also to autonomous regions, dependent territories, etc that have their own supervisory authorities.

<sup>11</sup> While the essential elements refer to the bilateral relationship of supervisors in country A and country B, it is evident that they may respectively apply to a multilateral relationship between a larger number of supervisors (such as in a universal college).

<sup>12</sup> Financial institutions may include only banks, or banks and other classes of financial institutions such as securities firms. The institutions to be covered by this statement should be agreed mutually, and stated clearly.

<sup>13</sup> However, it should be taken into account the characteristics and differences that may exist in the case of branches.

In connection with the authorisation process, and in accordance with the Core Principles:

- (a) the host supervisor should notify the home supervisor, without delay, of applications for approval to establish offices or make acquisitions in the host jurisdiction;
- (b) upon request, the home supervisor should inform the host supervisor whether the applicant bank is in substantial compliance with banking laws and regulations and whether the bank may be expected, given its administrative structure and internal controls, to manage the cross-border establishment in an orderly manner. The home supervisor should also, upon request, assist the host supervisor by verifying or supplementing any information submitted by the applicant bank;
- (c) the home supervisor should inform the host supervisor about the nature of its regulatory system and the extent to which it will conduct consolidated supervision over the applicant bank. Similarly, the host supervisor should indicate the scope of its supervision and indicate any specific features that might give rise to the need for special arrangements; and
- (d) to the extent permitted by law or relevant supervisory responsibility, the home and host supervisors should share information on the fitness and properness of prospective directors, managers and relevant shareholders of a cross-border establishment.

In connection with the ongoing supervision of cross-border establishments under their respective jurisdictions, the two supervisors should:

- (a) provide relevant information to their counterpart regarding material developments or supervisory concerns in respect of the operations of a cross-border establishment;
- (b) respond to requests for information on their respective national regulatory systems and inform each other about major changes, in particular those which have a significant bearing on the activities of cross-border establishments;
- (c) notify their counterpart of material administrative penalties imposed, or other formal enforcement action taken, against a cross-border establishment, with such notification to be made in advance of the enforcement action insofar as is practicable and subject to applicable laws; and
- (d) facilitate the transmission of any other relevant information that might be required to assist with the supervisory process.

Supervisors should, to the extent permissible under national laws or relevant supervisory responsibility, consider how to exchange information regarding money laundering, terrorist financing, unauthorized banking business, and other criminal financial activities.

Requests for information should normally be made in writing. However, where the supervisory authorities perceive a need for expedited action, requests may be initiated in any form but should be confirmed subsequently in writing.

## **On-site inspections**

The statement should recognise that cooperation is particularly useful to the supervisors of country A and country B in assisting each other in carrying out on-site inspections of cross-border establishments in the host country. Prior to deciding whether an on-site inspection is necessary, the home supervisor should review any relevant examination or other supervisory reports prepared by host supervisors. The home supervisor should notify the host supervisor of plans to examine a cross-border establishment or to appoint a third party to conduct an

inspection on its behalf, and should indicate the purposes and scope of the inspection. The host supervisor should allow the home supervisor or its delegated agent to conduct on-site inspections. As may be mutually agreed between the parties, inspections may be carried out by the home supervisor alone, or accompanied by the host supervisor. Following the inspection, an exchange of views should take place between the team involved in the inspection and the host supervisor.

## **Confidentiality of information**

The statement should recognise that mutual trust between supervisory authorities can only be achieved if information can flow with confidence in both directions. The supervisor receiving information must provide assurance that all possible steps will be taken to preserve the confidentiality of the information received. In this regard, employees of supervisory authorities should be bound to hold confidential all information obtained in the course of their duties. Any confidential information received from the other supervisor should be used exclusively for lawful supervisory purposes.

A supervisor in one jurisdiction that has received confidential information from a supervisor in another jurisdiction may subsequently receive a request for that information from a third party, including a third party supervisory authority, who has a legitimate common interest in the matter. Prior to passing information to the third party, the recipient should consult with and seek agreement from the supervisor that originated the information, who may attach conditions to the release of information, including whether the intended additional recipient is or can be bound to hold the information confidential.

In the event that a supervisor is legally compelled to disclose to a third party, including a third party supervisory authority, information that has been provided in accordance with a statement of mutual cooperation, this supervisor should promptly notify the supervisor that originated the information, indicating what information it is compelled to release and the circumstances surrounding its release. If so required by the originating supervisor, the supervisor will use its best endeavours to preserve the confidentiality of the information to the extent permitted by law. Supervisors should inform their counterparts of the circumstances in which they may be subject to legal compulsion to release information obtained.

## **Ongoing coordination**

The statement should recognise that visits for information purposes and exchanges of staff may promote cooperation between supervisors in country A and country B. In addition, the supervisors in the two countries should consider whether the training of staff at either agency would benefit from input and support by the other agency in order to reinforce sound banking supervisory practices in both countries.

The supervisors of country A and country B should conduct meetings as often as appropriate to discuss issues concerning banks with cross-border establishments in the respective countries. Such information sharing can be part of wider bilateral or multilateral arrangements between supervisors, such as an ongoing college process, which has evolved to become an important component of effective supervisory oversight of a cross-border establishment.

## Annex

### **Principles for establishing statements of cooperation for the sharing of confidential supervisory information**

- Statements of cooperation are not necessarily legally binding but act as a promise of intent.
- Statements of cooperation represent a shared understanding of a process by which information flows can be enabled and cross-border supervisory cooperation can be facilitated.
- Statements of cooperation can be specifically tailored to detail, for example, actions to be taken in crises or with respect to supervision arrangements for specific firms.
- Supervisory statements of cooperation must meet appropriate criteria for maintaining standards, protecting confidential information and using supervisory resources efficiently. These criteria include:
  - Materiality: Refers to the existence or expectation of reasonable and/or sufficient cross-border business;
  - Equivalence: Refers to one counterparty's legal treatment of information meeting confidentiality requirements equivalent to those imposed in the other counterpart jurisdiction; and
  - Reliability: Refers to an assessment of the counterparty's ability in practice to protect and share information, such as judicial and political credibility and regulatory track record.