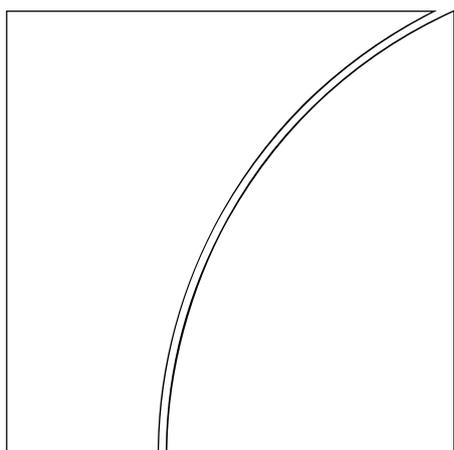


Basel Committee on Banking Supervision



Essential elements of a statement of cooperation between banking supervisors

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BANK FOR INTERNATIONAL SETTLEMENTS

Essential elements of a statement of cooperation between banking supervisors

In the course of recent discussions under the auspices of the Financial Stability Institute at the Bank for International Settlements, a number of countries have suggested that there is a need for a statement setting out the essential elements of a Memorandum of Understanding (MOU) or similar document that can be used as a reference for establishing bilateral relationships between banking supervisory authorities in different countries (and, where appropriate, between banking supervisors and other financial regulators).

The attached document presents the essential elements of a statement of mutual cooperation between supervisors. It is intended to provide a framework for an agreement between supervisors, leaving sufficient discretion and flexibility to supervisors to add additional details and responsibilities, if they so wish and upon mutual agreement, when entering into bilateral relationships. The Basel Committee encourages convergence towards this common modality and standard, particularly for countries that are seeking to develop an institutional framework for supervisory cooperation or are in the process of doing so.

The document has been prepared by the Working Group on Cross-border Banking, a working group of the Basel Committee which includes selected members of the Offshore Group of Banking Supervisors. It has also benefitted from comments made by a number of other bank supervisors on an earlier draft circulated in December 2000. In its development, the Working Group started from the proposition established in many Basel Committee documents, going back to the 1975 Basel Concordat, that supervisory authorities need to have a good working relationship with their counterparts in other countries with which they have a cross-border relationship. While communication does not necessarily need to be frequent, there must be a basis of mutual trust and a willingness to share information when the circumstances justify it. 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 two countries concerned. The essential elements of a statement of mutual cooperation, as attached, 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.

National laws, for example laws designed to protect the legitimate interest of bank customers, may limit the transmission of information between supervisory authorities. Any statement of mutual cooperation along the lines of the attached document 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 both sides 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 necessary for risk management on a global basis, and for compiling consolidated reports to the home supervisor. Any significant impediments will mean that the parent institution will not be able to conduct effective oversight of its own operations abroad, and should not be operating in that foreign jurisdiction.

The working group also discussed mutual assistance in criminal matters. This is an important area that supervisors must consider. However as it involves obligations arising from non-supervisory legislation, falls within the responsibility of law enforcement agencies, and is

often the subject of existing separate bilateral mutual legal assistance treaties or agreements, it is not thought appropriate that this matter should be covered in the attached document.

It is recognised that in certain circumstances, there will be significant costs associated with the provision of assistance, e.g. 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 information¹ between the supervisors of country² A and country B to facilitate the performance of their respective duties and to promote the safe and sound functioning of financial institutions³ with cross-border establishments in their respective countries. The statement should demonstrate the commitment of the supervisors in country A and country B to the principles of effective consolidated supervision and cooperation between banking supervisors, and to their respective responsibilities, as laid down in the Basel Committee's Concordat and Core Principles for Effective Banking Supervision.

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 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. 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

The statement should recognise that information should 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. Information-sharing should include contact during the authorisation and licensing process, in the supervision of the on-going activities of such entities and in the handling of problem institutions.

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

¹ In this document, information refers to both supervisory and enforcement information.

² In this document, country refers also to autonomous regions, dependent territories, etc that have their own supervisory authorities.

³ Financial institutions may include only banks, or banks and other classes of financial institutions such as securities firms. Institutions to be covered by this statement, to be agreed mutually, should be stated clearly.

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, the home and host supervisors should share information on the fitness and properness of prospective directors, managers and relevant shareholders of a cross-border establishment⁴.

In connection with the ongoing supervision of their cross-border establishments, 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) inform their counterpart of material administrative penalties imposed, or other formal enforcement action taken, against a cross-border establishment. Prior notification shall be made, as far as 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.

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 inspections⁵ 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 examination on its behalf, and to indicate the purposes and scope of the visit. 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, examinations may be carried

⁴ It is recognised that, in some countries, procedures to exchange information may be constrained by legislation.

⁵ The words "inspection" and "examination" are used here interchangeably.

out by the home supervisor alone, or accompanied by the host supervisor. Following the inspection, an exchange of views should take place between the examination team and the host supervisor.

Protection of information

The statement should recognise that mutual trust between supervisory authorities can only be achieved if exchanges of information can flow with confidence in both directions. The supervisor receiving the information must provide the 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 pursue areas where 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 that maintain cross-border establishments in the respective countries.