

**Belgium: Detailed Assessment of Compliance with the Basel Core Principles for
Effective Banking Supervision**

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DETAILED ASSESSMENT OF OBSERVANCE

BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING
SUPERVISION

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Glossary

AC	Additional Criteria
AML/CTF	Anti-Money Laundering/Combating Terrorist Financing
BCPs	Basel Core Principles
BRGAAP	Belgian Generally Accepted Accounting Principles
CBFA	Commission Bancaire, Financiers et Assurances
CPs	Core Principles
EC	Essential Criteria
ECB	European Central Bank
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FSAP	Financial Sector Assessment Program
FSMA	Financial Services and Markets Authority
GIIPS	Greece, Italy, Ireland, Portugal, and Spain
IAS	International Accounting Standards
ICAAP	Internal Capital Adequacy Assessment Process
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standards
IRB	Internal Rating-based Approach
KYC	Know Your Customer
LCR	Liquidity Coverage Ratio
LGD	Loss Given Default
MiFID	Markets in Financial Instruments Directive
MoU	Memorandum of Understanding
NBB	National Bank of Belgium
NSFR	Net Stable Funding Ratio
PF	Protection Fund for Deposits and Financial Instruments
SPF	Special Protection Fund for Deposits, Life Insurance and Capital of Cooperative Companies
SREP	Supervisory Review and Evaluation Process
VaR-model	Value at Risk Model

SUMMARY, KEY FINDINGS, AND RECOMMENDATIONS

1. Belgium has a high level of compliance with the Basel Core Principles for Effective Banking Supervision (BCPs). This high level of compliance has been achieved in a challenging environment. The financial crisis and subsequent state intervention has transformed the banking system and while acute crisis conditions have abated there is continued elevated stress within the system and vulnerabilities persist. Added to this is the continued pressure on industry to meet forthcoming higher regulatory standards, most notably in capital and liquidity. These conditions put a premium on the quality of risk management practices within the banks themselves and equally on the supervisory oversight conducted by the authorities. In addition to substantial regulatory changes, the supervisory authorities have also had to adjust to the challenges of transition wrought by re-design of the regulatory architecture and the move of prudential supervision to the central bank.

2. The National Bank of Belgium (NBB) deploys high-quality supervisory practices—which it is building upon through well conceived initiatives and reforms—but there are weaknesses in its supervisory process. The NBB has already instituted some enhancements to its risk oversight, such as an annual risk review, and is executing a focused but multi-faceted plan of improvements. These projects will streamline and integrate processes, create greater flexibility in data handling and strengthen and deepen analysis at firm specific and horizontal levels. It is important for the NBB to fully harness these projects in refining its risk based supervisory processes to ensure that it has identified the minimum adequate level of supervisory attention for each institution according to the institution's risk profile. Should crisis conditions re-emerge there will be consequential effects on the entire supervisory process as limited resources will need to be reallocated. The NBB needs to be able to rely on its supervisory processes to guide its decision making in order to manage such reallocation in a fully risk-focused manner. The embedding of this more systematic process would allow the NBB to ensure that the dilution of supervisory activity is dispersed proportionately.

3. An area of weakness in the large exposure regime allows for concessions to smaller banks to exceed the 25 percent limit. Where the amount of €150 million is higher than 25 percent of the own funds, the value of the exposure, after credit risk mitigation, is allowed to exceed the 25 percent limit up to 100 percent of own funds. The concession is not peculiar to Belgium and is derived from Directive 2009/111/EC that has modified Directive 2006/48/EC and a national discretion is however foreseen in order to set a stricter limit (four banks within the EC have done so). While the concession is permitted under the Directive, the concession significantly weakens the regime and exposes smaller banks to concentration risk. In practice, smaller banks don't have access to deep capital markets to quickly raise capital in the event an exposure to an obligor defaults or becomes impaired.

A. Introduction

4. This assessment of the current state of the implementation of the BCPs in Belgium has been completed as part of a Financial Sector Assessment Program (FSAP) undertaken by the International Monetary Fund (IMF) during 2012. It reflects the regulatory and supervisory framework in place as of the date of the completion of the assessment. Importantly, it is not intended to assess the merits of the important policy and implementation issue regarding several aspects of the international regulatory framework that are yet to be decided in international fora, the European Union (EU), and in Belgium, ranging from the finalization of the Basel III liquidity regime to the potential creation of a Single Supervisory Mechanism. An assessment of the effectiveness of banking supervision requires a review of the legal framework, both generally and as specifically related to the financial sector, and detailed examination of the policies and practices of the institutions responsible for banking regulation and supervision. In line with the BCP methodology, the assessment focused on the major banks and banking groups, and their regulation and supervision, given their importance to the system.

B. Information and Methodology Used for Assessment

5. The Belgian authorities agreed to be assessed according to the Core Principles (CP) Methodology issued by the Basel Committee on Banking Supervision (Basel Committee) in October 2006. The current assessment was thus performed according to a revised content and methodological basis as compared with the previous BCP assessment carried out in 2004. The assessment of compliance with each CP is made on a qualitative basis to allow a judgment on whether the criteria are fulfilled in practice. Effective application of relevant laws and regulations is essential to provide indication that the criteria are met.

6. To assess compliance, the BCP Methodology uses a set of essential and additional assessment criteria for each principle. The essential criteria (EC) are the only elements on which to gauge full compliance with a core principle. The additional criteria (AC) are suggested best practices against which the Belgian authorities have agreed to be assessed. Additional criteria are commented on but are not reflected in the grading. The assessment of compliance with each principle is made on a qualitative basis. A four-part grading system is used: compliant; largely compliant; materially noncompliant; and noncompliant. This is explained below in the detailed assessment section.

7. The assessment team reviewed the framework of laws, rules, and guidance and held extensive meetings with officials of the NBB, and additional meetings with the banking sector participants. The team met the industry association representing banks in addition to a number of domestic and non-domestic institutions.

8. The team appreciated the very high quality of cooperation received from the authorities. The team extends its thanks to staff of the authorities who provided excellent cooperation, including extensive provision of documentation, at a time when many other initiatives related to domestic, European and global regulatory initiatives are in progress.

9. The standards were evaluated in the context of the Belgian financial system's sophistication and complexity. It is important to note that Belgium has been assessed against the BCP as revised in 2006. This is significant for two reasons: (i) the revised BCP have a heightened focus on risk management, in comparison to the previous methodology, and its practice by supervised institutions and its assessment by the supervisory authority; and (ii) the standards are evaluated in the context of a financial system's sophistication and complexity.

10. For completeness' sake, it should therefore be noted that the ratings assigned during this assessment are not directly comparable to the ratings assigned in the previous Belgian FSAP, which was performed using the pre-2006 BCP Methodology. Differences may stem not only from the fact that the bar to measure the effectiveness of a supervisory framework was raised by the 2006 update of the BCP Methodology, but by lessons drawn from the financial crisis that may have a bearing on supervisory practices.

11. An assessment of compliance with the BCPs is not, and is not intended to be, an exact science. Reaching conclusions required judgments by the assessment team.¹ Banking systems differ from one country to another, as do their domestic circumstances. Furthermore, banking activities are undergoing rapid change after the crisis, prompting the evolution of thinking on and practices for supervision. Nevertheless, by adhering to a common, agreed methodology, the assessment should provide the Belgian authorities with an internationally consistent measure of the quality of its banking supervision in relation to the revised Core Principles, which are internationally acknowledged as minimum standards.

12. To determine the observation of each principle, the assessment has made use of five categories: compliant; largely compliant, materially noncompliant, noncompliant, and non-applicable. An assessment of "compliant" is given when all essential criteria are met without any significant deficiencies, including instances where the principle has been achieved by other means. A "largely compliant" assessment is given when there are only minor shortcomings, which do not raise serious concerns about the authority's ability to achieve the objective of the principle and there is clear intent to achieve full compliance with the principle within a prescribed period of time. A principle is considered to be "materially noncompliant" in case of severe shortcomings, despite the existence of formal rules and procedures and there is evidence that supervision has clearly not been effective, the practical implementation is weak or that the shortcomings are sufficient to raise doubts about the authority's ability to achieve compliance. A principle is assessed "noncompliant" if it is not substantially implemented, several essential criteria are not complied with, or supervision is manifestly ineffective. Finally, a category of "non applicable" is reserved (though not used) for those cases where the criteria would not relate to the Belgian authorities.

¹ The assessment team comprised Katharine Seal and Christopher Wilson, (both Senior Financial Sector Experts, IMF).

INSTITUTIONAL AND MACROECONOMIC SETTING AND MARKET STRUCTURE OVERVIEW²

13. The Belgian financial system is relatively large, concentrated, and interconnected.

The banking system assets grew rapidly from 384 percent of GDP in 2000 to 470 percent of GDP in 2007, with growth largely driven by an expansion of investment banking activities financed through the surplus of domestic retail deposits and wholesale funding. Post 2008, an initial deleveraging significantly reduced the size of the banking sector to 310 percent of GDP in 2011, with a second wave of deleveraging, at a slower pace, currently underway. The system is concentrated with four dominant banking groups representing almost $\frac{3}{4}$ of consolidated system assets. Assets of foreign-owned banks account for more than half of the sector. The insurance sector is embedded in the predominant bancassurance model and dominated by a few conglomerates.

14. The 2008 global financial crisis had a major impact on the Belgian banking sector.

The rapid deterioration of access to market-based funding sources and declining capital positions forced banks to raise capital, shed assets, and appeal to the state for capital infusions. The Belgian state provided extensive funding and asset relief guarantees to the three largest banks. Since 2008, major banks have shed investment banking and asset management activities and shifted focus to more 'traditional' banking activities at home. Cross-border claims fell from 300 percent of GDP in 2008 to 58 percent of GDP in mid-2012. The largest remaining exposures are to the Czech Republic, France, the United Kingdom, and Ireland.

15. After a short lived recovery, the export-oriented economic growth has slowed significantly since the start of 2012 and is expected to stagnate in 2012–13. In addition to weak external demand in the European Union (main trading partner), domestic demand is also deteriorating, reflecting higher uncertainty, depressed consumer and business sentiment, and the pro-cyclical fiscal consolidation. The general government deficit is expected to fall below 3 percent of GDP in 2012 but given the growth prospects, the dynamics of the debt-to-GDP ratio remain uncertain. The government has initiated labor market and pension reforms in order to boost the employment rate and potential growth, but implementation is challenging and Belgium's competitiveness continues to fall. The deterioration of economic conditions has begun to push the unemployment rate upwards.

16. The links between banks and the Belgian sovereign have intensified due to the crisis.

The total exposure of the banking sector to the federal government has increased substantially since 2008 and stood at 10 percent of banking sector assets in mid-2012, while the contingent fiscal liabilities stemming from the state aid to three banks currently amount to 16 percent of GDP. With exposures to the Belgian government at roughly more than half of all sovereign debt

² In FSAP/FSSA reports, this information will be contained in other parts of the FSAP report. Salient details, however, may be briefly restated for convenience.

holdings of the sector and limited fiscal headroom for further support measures, fiscal consolidation remains critical to avoiding renewed strains on the banking sector, weakening of market confidence and increasing funding costs.

17. Domestic economic challenges and sovereign risk perceptions remain sources of continued uncertainty as the banking sector consolidates. Banks have struggled for profitability since the crisis, and structural costs remain high. A wide and stable deposit base has limited rollover risks and strategic re-orientation of the banking sector towards the domestic markets has prevented a disproportionate decline in credit supply. However, the weak economic environment and higher unemployment are likely to affect debt affordability, accentuated by the deflationary effect of deleveraging by households, banks and the government. Future increases in the interest rates and rising non-performing loan balances amidst weak economic conditions could pose a challenge for banks as they rebuild capital buffers and face implementation of higher regulatory requirements. There are also downside risks to asset quality, especially in banks' foreign subsidiaries, even though the overall level of impairments has remained relatively benign so far.

18. On the positive side, Tier 1 capital for the Belgian banking system has risen from 11.6 percent of risk-weighted assets in 2008 to 14.8 percent in mid 2012, and compares favorably to other major international banking systems. Actions by the authorities, market pressures, and experience from the crisis have led to banks aiming for stronger capital positions and enhanced short-term liquidity. A number of banks have made material progress in longer term programs to reduce their structural liquidity position through less reliance on wholesale funding. Stricter liquidity regulation by the NBB, spearheading future Basel III liquidity framework, has been conducive to greater focus on liquidity risk management, while the measures by the Eurosystem to support liquidity position of Euro area banks eased investors' concerns about their liquidity position.

19. As a direct result of the crisis, the regulatory and supervisory has been re-organized introducing a "twin peaks" model. The new architecture, which entered into force in April 2011, replaced the integrated regulator (the Commission Bancaire, Financiers et Assurances) and allocated the prudential supervision of financial institutions to the NBB and the responsibility for ensuring market conduct and consumer protection to the Financial Services and Markets Authority (FSMA). All bank and insurance supervision staff moved to the NBB.

Crisis management and financial stability coordination

20. The NBB has the formal legal responsibility for coordinating the management of financial crises (NBB Organic Law, Article 36/3, section 1). Furthermore, it has the power to advise the Federal Government and the Federal Parliament on measures that are necessary or useful for financial stability. While the role of the Minister of Finance with respect to crisis management is not explicitly articulated in Belgian legislation, any actions necessary to protect financial stability proposed by the NBB under Article 57bis of the Banking Law require a Royal Decree, which will be deliberated upon by the Council of Ministers. Additionally, the NBB has a legal mandate for

financial stability (Article 12 of the NBB Organic Law of 22 February 1998) including obligations to detect threats to financial stability, to submit recommendations to the government as necessary and to collaborate with the European Systemic Risk Board (ESRB). Furthermore, the NBB has specific powers in respect of systemic risks posed by systemic financial institutions. In particular, these powers include the ability to oppose strategic decisions or to impose specific measures (Article 36/3 section 2 of the Organic Law).

21. A formalized framework for financial stability coordination reflecting the transition to the Twin Peaks model has yet to be put in place. Following the implementation of the Twin Peaks model in Belgium, new arrangements between the NBB and the Ministry of Finance are yet to be agreed. Nevertheless, both the NBB and the Ministry remain bound by MoUs agreed in 2005 and 2008. Progress is being made in respect of agreeing MoUs between the NBB and the FSMA to formalize the modalities of effective exchange of information and cooperation. An agreement on surveillance of financial market infrastructure has been signed (October 2012) and a more general agreement of cooperation is under active discussion.

A. Preconditions for Effective Banking Supervision

22. Belgium has a well developed public infrastructure supporting effective banking supervision. Belgium has a complete system of business laws, consistently enforced. The Belgian legal system is based on civil law. The legislative branch is composed of a parliament with two chambers (Chamber and Senate). Belgium has a constitutional monarchy whereby the King is the head of state and of the executive branch. The judicial branch is independent with a hierarchy of courts, the most senior of which is the Court of Cassation, the supreme judicial court. There are two kinds of ordinary appeal: application to set aside or appeal the decision (Article 21(1) of the Judicial Code) and “special appeals.” The ordinary appeals are dealt with by Court of Appeal, which has five courts whose territorial jurisdiction set out in the Constitution. The Court of Cassation considers “special appeals” the most common of which is whether the decisions referred to it contravene the law. A constitutional court was established in 1980. As a member of the EU, much domestic legislation, including banking regulation, derives from EU regulations, directives and decisions, which are frequently updated to keep pace with international standards.

23. The Belgian accounting framework is established in law, and implemented through Royal Decree. In accordance with EU requirements, Belgium has adopted the IFRS accounting standards for listed companies and other consolidated accounts. Unconsolidated accounts must be prepared in accordance with Belgium Generally Accepted Accounting principles (BGAAP) as set out in the Royal Decree of 23 September 1992. The legal basis for the Belgian accounting framework is the Company law code and the specific supervisory laws applying to insurance and banking. The Commission for Accounting Principles is the statutory body charged with articulating Belgian General Accounting Principles. The NBB takes the Commission’s role for accounting in the specific fields of insurance and banking. The Belgian Institute of Accountants (Institut des Experts-Comptables—IEC) has powers to regulate the profession. The Belgian auditing framework is also established in law and implemented through measures adopted by the Belgian Auditing Institute (Institut des Réviseurs d’Entreprises - IBR/IRE), which is a statutory body. The Institute is part of

the audit oversight system and inspects audit firms in addition to its roles in training and continuous professional education. External auditors are licensed by the IBR/IRE and external auditors auditing a bank must also be accredited by the NBB (Article 50 of the Banking Act). Domestic auditing standards are prepared by the profession, reviewed by the High Council of the Institute and ultimately approved by the competent Minister. Rotation standards are set by the profession requiring a rotation after six years, either of the partner or, in the case of a sole practitioner, a transfer to another external auditor. From 2012 onwards audits of PIE's, have to be performed according to International Standards on Auditing as issued by the IAASB. The Institute is member of international organizations of auditors (FEE at European level and IFAC at the international level).

24. IFRS disclosures apply to all listed companies and all banks are subject to a range of disclosures requirements. Reports that must be issued include annual financial statements, management reports, or annual Risk Report as issued by banks. The NBB is planning to assess the consistency of Pillar 3 disclosures but no assessment has currently been completed beyond the assessment made by EBA, to which the NBB (and previously the CBFA) contributed as Belgian banking groups were included in the EBA assessment. Belgium has a regulated stock exchange (Euronext) and a secondary market that are subject to investor protection and governance rules, information disclosure requirements, and supervision processes to ensure their efficient functioning. Most of the requirements on both investor protection and information disclosure stem from European directives.

Safety nets

25. All credit institutions established in Belgium must take part in a collective deposit guarantee scheme financed by them. Consistent with EU legislation (Directive 94/19/EC) depositors are guaranteed up to a limit of €100,000 per depositor per credit institution. Legislation on the deposit guarantee system entered into force in 1994 and was successively modified in 1999 (establishing a deposit guarantee fund), 2008 (establishing a special guarantee fund), 2009 and 2011. The law provides gateways for the authorities that manage the Belgian deposit guarantee schemes to conclude cooperation agreements with foreign bodies and also creates a legal obligation for the NBB to inform the bodies, which manage the deposit guarantee scheme when it detects any problems likely to give rise to the intervention of these schemes (Article 110 bis2 of the Banking Law).

26. The deposit guarantee scheme is jointly organized by two institutions: (a) the Protection Fund for Deposits and Financial Instruments ("PF") and (b) the Special Protection Fund for Deposits, Life Insurance and capital of cooperative companies ("SPF"). The creation of the SPF in 2008 was to create confidence by giving certainty to depositors that there will be sufficient funds to cover the claims of depositors in event of a failure of a institution. Contributions to the SPF are risk based (solvency, liquidity and asset quality). Prior to 2009 contributions were paid to the PF but are currently suspended in the light of contributions that have had to be paid to the SPF since 2009.

27. While the SPF is an administrative entity falling under the Ministry of Finance, the PF is an autonomous public institution (created under the law of 17 December 1998). The PF is administered by a management committee comprising equal numbers of representatives of the financial sector and the government. The Chairman and five Committee members are appointed by the Minister of Finance, two of whom are drawn from the NBB, with the remaining members being proposed by the banking and stockbroking industry. In case of a conflict of interests a Board member must recuse him or herself (Royal Decree of February 15, 1999).

28. DGS pay-out is triggered when a financial institution has been declared bankrupt by the Court or when the NBB has notified the DGS that a financial institution has failed to reimburse deposits to its clients. The reimbursement period is 20 working days. In the event of a failure, funds are to be drawn first from the PF, then from the SPF and should these funds be insufficient a supplementary advance will be made by the Ministry of Finance and recouped afterwards from contributing members of the deposit guarantee scheme. Following an advance of funds from the Ministry (i.e., government funds), any future contributions by industry participants to the SPF will be evenly distributed between direct repayment to the Ministry and the replenishment of the SPF's reserves. The reserves of the deposit guarantee scheme amounted to €2 billion at end-2012, with an estimated coverage ratio of around 0.6 percent of eligible deposits.

29. The PF may also, within the limits of its financial resources (€241 million at June 30, 2012), take preventive action. The PF may thus assist in the liquidation, the financial reorganization or the resumption of business of a member institution. Such measures can only be taken if the cost of the operation does not exceed the amount of the total payout that would otherwise occur or if the operation is in the public interest of the financial system. Current legislation does not provide scope for preventive action by the SPF.

30. The Belgian authorities have established a Resolution Fund (RF) vesting it with powers to take preventative measures and to facilitate resolution procedures. The RF is established through the law of 28 December 2011 and implemented by Royal Decree of 23 February 2012. It is managed by the Caisse des dépôts et Consignations / Deposito en Consignatiekas, a special administration within the Ministry of Finance under the direct authority of the Minister of Finance, as is the Special Protection Fund. The RF can be used to finance measures such as preventative action or a bridge bank, total or partial transfer of assets and liabilities, a good/bad bank split. The RF is funded ex ante by annual financial stability contributions, which amount to 0.035 percent of the credit institution's total liabilities net of deposits eligible for deposit guarantee and of regulatory capital. The contributions are paid directly to the Ministry of Finance where they go to general revenue although a resolution reserve has been created using the contributions from the credit institution members of the Fund. Financial Stability Contributions (of €238 million) were paid in 2012 for the first time. No target level of reserves for the resolution fund has been set.

31. The NBB enjoys extensive early intervention and resolution powers. These powers are defined in articles 57 and 57 bis of the law of 22 March 1993 (see CP23). The NBB may appoint a special inspector, suspend the direct or indirect exercise of all or part of a credit institution's

activities or prohibit these activities altogether, require a credit institution to replace a manager or a director, and revoke the authorization. In a resolution phase and when financial stability is threatened, the government, through a Royal Decree, may adopt measures providing for the transfer, sale of contributions relating to the assets, liabilities or one or more fields of activity or all or part of the rights and obligations of a credit institution, as well as securities and shares issued by such an institution.

32. The NBB is the provider of Emergency Liquidity Assistance to credit institutions ("ELA"). ELA is provided for under Article 14.4 of the Statutes of the ESCB. The extension of ELA is subject to consultation with the ECB Governing Council, which can prohibit ELA or subject ELA to conditions to avoid any interference or ELA operations with the ESCB's tasks and objectives. ELA granted by the NBB is automatically guaranteed by the State (Article 9 of the NBB Organic Law).

B. Main Findings

Objectives independence, powers, transparency, and cooperation (CP1)

33. The NBB has a clear legal power to conduct prudential supervision. Similarly the NBB has a legal mandate to detect threats to financial stability. The legal mandate does not, however, clarify the relationship between the discharge of the NBB's supervisory function and of its financial stability function and how the balance of priorities should be achieved should a potential conflict emerge. It is recommended that greater legal clarity be provided, should a revision to the NBB Organic Law be undertaken, and that the NBB should develop and publish a mission statement of its objectives irrespective of legal changes.

34. The NBB has clear lines of accountability, transparency and separate funding when acting in its supervisory capacity. There is no indication in practice that there is any interference with the operational independence of the supervisor. Supervisory resources at the NBB are stretched and this is of concern given the continued stress within the financial system and given the importance of the program of enhancements to supervisory practices and processes that the NBB is urgently seeking to roll out. While there are no standard metrics in relation to adequate resourcing of the supervisory function, the NBB is encouraged to review its project plans very carefully to determine that it has robustly adequate resource required for the successful delivery of the multiple supervisory projects and day-to-day supervisory practice. The NBB should build contingency demands into this planning, not only because there may be demands arising from major EU developments such as the Banking Union, which is understood at the time of the mission to be likely to need to rely, perhaps heavily, on the resources of national authorities, rely but also from the potential for there to be crisis issues emerging in supervised institutions given continued elevated levels of systemic stress.

35. The NBB operates within a clear and balanced legal framework. The NBB Organic Law and Banking Law provide for authorization and ongoing standards of supervision. Additionally, the NBB enjoys a range of remedial measures that allow for an appropriate degree of proportionality in its approach to breaches of laws and regulations. It is noted that the drafting of

Article 57 of the Banking Law usefully takes into consideration that there may be a necessity for swift action in urgent situations. The extensive powers to authorize the disposal of the assets or liabilities of an institution are balanced by the need to obtain ratification of such measures through a Royal Decree. Appropriate legal protections have been put in place in respect of banking supervision and supervisors.

36. The general framework for exchange of information is well articulated but coordination at a domestic level is yet to be fully put in place. The NBB's international relationships are supported by operational agreements and are working fluently. Domestic working level cooperation needs to be underpinned and promoted by an MoU to ensure the modalities of cooperation between the NBB and the FSMA. Amendments to the Twin Peaks Law to rectify drafting oversights in relation to the gateway for the exchange of information between the FSMA and the NBB, currently planned for the end of 2012, are also desirable and should be concluded.

Licensing and structure (CPs 2–5)

37. The legal framework for authorization, on-going standards for supervision and for permissible activities is clearly stated. The law provides that not only the NBB but the FSMA should have regard to the importance of ensuring that the public is not misled into placing deposits with institutions, which are not authorized for this purpose. The NBB is to be commended on its thorough and thoughtful review of fit and proper policies and practices, which ought to provide even greater clarity that fit and proper standards must be met on a continuous basis by relevant individuals and that the NBB can initiate an assessment at any moment. The widening of the formal scope of application of the fit and proper assessment to include key personnel such as the heads of compliance, internal audit and risk management, in cases where these individuals do not form part of the senior management is, similarly, good practice.

38. The change of control of a credit institution and a major acquisition by a credit institution is, broadly, well governed by the laws. There are some gaps that merit attention, however. While the change of control of an authorized institution is largely determined by EU law, it is to the NBB's credit that in its supervisory practice it is increasing its focus on the shareholding and ownership structure above the institution. The authorities are urged to remedy the lack of legal obligation for a credit institution to notify its supervisory authority of a material adverse development that may negatively affect the suitability of a major shareholder. With respect to major acquisition the NBB has comprehensive legal provisions surrounding the governance and scrutiny of major acquisitions by its supervised firms. In particular the powers to pre-approve strategic decisions taken by the systemically relevant institutions provide a great deal of protection. For non-systemic firms, however, it is recommended that the NBB establish either pre-notification or pre-approval thresholds for acquisitions in non-financial entities.

Prudential regulation and requirements (CPs 6–18)

39. Belgium banks have undergone considerable stress over the last several years and, as a result, have increased their capital, importantly the quality of capital in CET1. The major bank Tier 1 capital ratios range between 11.5 percent and 20.6 percent for the larger systemically important banks as at March 2012. The capital ratios across this group of banks demonstrate a high composition of CET1, which has been gradually increasing, albeit with severe stress at stages from the crisis requiring state intervention and support. The quality of the capital base has been improving with a run off of Tier 2 instruments in anticipation of the implementation of Basel III. Nonetheless, increased minimum capital adequacy requirements under BIII will continue to be challenging for some banks in the context of lower internal profit generation.

40. The NBB's approach to Pillar 2 is well developed using a scorecard as the primary tool for risk analysis, taking into account qualitative and quantitative measures. At least on an annual basis, the NBB determines the minimum capital adequacy requirements for all banks on a forward looking basis. The SREP and ICAAP analysis are important inputs into the process and, if available, outputs from banks' economic capital models. Stress testing is also taken into account as to ascertain whether the bank is able to maintain capital buffers under stress conditions.

41. Senior management of the bank is required to submit an annual self assessment of the control environment to the NBB. The external auditor will provide a report, which is a factual evaluation of management's self assessment but is on its own not a positive assurance regarding the design and effectiveness of controls. As a result, the external auditors report will not necessarily identify whether there is hidden build-up of risks or provide a positive assurance as to the quality of risk management. In the absence of an on-site review by the NBB, too much reliance should not be placed on this report as a mechanism to identify the build-up of risks. In practice NBB uses the input from the external auditor in combination with other supervisory activities, such as the ICAAP, on-site reviews and discussions with the Board etc.

42. Annual meetings with the full Board of Directors should form an integral component of the NBB's standard supervision practice. In developing a minimum set of supervisory activities to be performed on a set periodic basis, annual meetings with the full Board (including non-executive independent directors) should be mandatory for all banks. The meeting will help the supervisor assess the role of the Board in overseeing management to ensure that the policies, processes and systems are implemented effectively at all decision levels. Whereas current supervisory practices provide already for frequent meetings between supervisory staff and Board members, there is room for formalizing the minimum set of supervisory activities to be performed on a periodic basis in this respect.

43. The limits regarding large exposures have been strengthened recently. An institution shall not incur an exposure, after taking into account the effect of the eligible credit risk mitigation techniques, to a client (counterparty) or a group of connected clients (counterparties) the value of which exceeds 25 percent of its own funds. Following the European Directive text (*as modified by Directive 2009/111/EC*), where the client is an institution, the value shall not exceed 25 percent of the credit institution's own funds or EUR 150 million, whichever is the higher, provided that the sum of exposure values after taking into account eligible credit risk mitigation

techniques to all connected clients that are not institutions does not exceed 25 percent of the credit institution's own funds. Where the amount of EUR 150 million is higher than 25 percent of the own funds, the value of the exposure, after credit risk mitigation, shall not exceed a reasonable limit in terms of the credit institution's own fund. That limit shall be determined by credit institutions, consistently with the policies and procedures to address and control concentration risk and shall not be higher than 100 percent of the credit institution's own funds. This means concretely that a more lenient large exposure limit may be accepted by authorities for smaller credit institutions (i.e., having own funds below EUR 600 million).

44. Liquidity regime is well embedded. The systemic banks need to report liquidity on a daily basis in addition to meeting a one week and one month liquidity stress test. The objective of the stress test is to ensure the bank is able to meet predefined liquidity buffers or survive a short-dated stress. While the definition of eligible liquids is broader than the Basel LCR definition, the run-off assumptions for liabilities are more stringent. The stress test was introduced at the start of 2009 as an observation ratio with full implementation from 2011. The introduction of a liquidity stress test will help smooth the transition to comply with the LCR for banks when implemented in 2015.

45. Specific guidance has been issued regarding sound management of outsourcing, business continuity management and financial services provided by the internet. The NBB has a dedicated team of eight IT specialists. While all credit institutions are required to perform regular business continuity practices and disaster recovery testing, the NBB will not necessarily receive the detailed results of that testing. The NBB should strengthen the framework for operational risk monitoring by requiring all credit institutions to certify a certain level of resilience on an annual basis, and require immediate reporting of a breach of that level, particularly if bank is systemic.

46. The requirements for managing interest rate risk in the banking book are well established in the regulatory framework. The NBB has made strong efforts to implement new standards and has embedded interest rate risk in its core work. Interest rate risk stress test ratios require banks to hold sufficient capital to cover economic value losses related to adverse structural interest rate changes prescribed by the NBB. While the ratios provide a consistent measure of interest rate risk across banks, the ratios do not always fully capture bank specific risks. When evaluating minimum capital ratios, interest rate risk is taken into account as a Pillar 2 risk.

Methods of ongoing banking supervision (CPs 19–21)

47. The supervisory staff of the NBB are conducting excellent quality risk based supervision both on and off-site. The NBB has put in place a sound analytical process that it is in the process of refreshing and deepening in terms of analytical insight. These revisions will contribute further to the global risk assessments for groups and it will be valuable if the refinements can further emphasize the forward looking elements of the assessments. Relatively

unusually, the NBB shares the detailed risk assessment with the institutions concerned and has found this approach to have a constructive and beneficial effect. The greater power of risk discrimination in the new tools should further support the dialogue between the institutions and the supervisors therefore. Continued incorporation of insurance risk within the global group risk assessments is important and should also be enhanced, as planned. In terms of on-site supervision the NBB has restructured its resources and put in place effective coordination with the off-site teams.

48. The NBB applies a comprehensive supervisory program to the systemic firms but must ensure that “globally balanced supervisory planning” covers all supervised firms. The NBB must put in place a risk based approach to its supervisory process to ensure that each institution systematically receives the appropriate intensity of supervisory attention proportionate to its profile. Such a plan also needs to provide a structured framework to guide decision making in terms of which actions should be postponed or performed less frequently, and which institutions should be affected when new or urgent priorities emerge that demand the reallocation of scarce supervisory resource. Further, the plan should clarify the minimum frequency with which standard (and as necessary) non-standard reporting must be made to the NBB Board for information or decision making. The NBB has already initiated a range of projects, both analytical and IT based, that will be invaluable in delivering this objective. It will be important to ensure the successful completion of such projects, while recognizing that project management is especially challenging in the current environment of elevated systemic risks and the likely introduction of structural changes such as the Banking Union.

Accounting and disclosure (CP 22)

49. In Belgium, the external auditor of a bank is accredited by the NBB. In the Belgium model, the external auditor is seen as a ‘collaborator’ of banking supervision. The external auditor is accredited directly by the NBB after satisfying minimum expectations regarding independence, experience, competence and adequate organization. The external auditor will provide an audit opinion on the financial accounts (six monthly and annually). The auditor will also provide an opinion regarding the self assessment performed by management annually on the internal control environment and on the reliability of prudential returns.

50. Under NBB rules, banks are required to report on a solo and, if part of a group, consolidated basis. Belgium accounting rules (Belgium GAAP) apply on a solo basis and IFRS for consolidated consolidated basis if they have to produce consolidated accounts according to EU directives. Banks submit quarterly prudential returns of key data such as capital adequacy, balance sheet, earnings etc. Liquidity is reported more frequently on a monthly basis. However, concentration risk is only reported annually and interest rate risk data is submitted with a lag of two and half month after the reporting date making an integrated and comprehensive offsite analysis more challenging. Aligning reporting requirements for all key data elements will enhance the quality of offsite supervision. The NBB has a project in place to consider prudential reporting.

Corrective and remedial powers of supervisors (CP 23)

51. The NBB enjoys a broad range of powers for corrective and remedial measures and there is evidence that the NBB is able and ready to use such remedies. Moreover, the strong powers open to the NBB have clearly meant that there are occasions where the supervisory authority has been able to use suasion rather than needing to resort to legal remedies in the first instance. The NBB has indicated it is at present examining the possibility of making its disciplinary powers more graduated and proportionate to the severity of the offence committed by the supervised institution.

Consolidated and cross border banking supervision (CPs 24–25)

52. The NBB has the necessary legal powers and has implemented the necessary regulatory structure to facilitate the practice of consolidated supervision. Given the significance of cross border activities for the systemic groups in Belgium, the NBB has focused on work within the EU supervisory colleges to ensure effective group oversight. The NBB is actively using the college environment to create opportunities to test out the quality of risk focused management within groups by their own management as well as to ensure an adequate distribution of capital within the group. In terms of further developing its practices, the NBB is encouraged to execute plans to enhance governance requirements for groups by stating more explicitly what is expected of the parent company in respect of coordinating and controlling the group in a holistic way. One particular challenge is to ensure that non-banking and, as appropriate, non-financial risks within the group are fully understood, even though these risks may appear to present only a small part of the group. The ability to communicate and cooperate effectively with all domestic regulators as well as international authorities is critical to this task. It is therefore recommended (as also noted in CP 1(6)) that the NBB and the FSMA finalize the MoU setting out the modalities of cooperation as foreseen in the Twin Peaks legislation.

53. The NBB places great value on and is strongly motivated to contribute to and participate in home-host relationships as fully and as effectively as possible. Cooperation arrangements and MoUs are in place with all relevant jurisdictions. Home and host relationships are critical to the successful supervisory oversight of the financial system in Belgium. While EU legislation imposes requirements including joint assessment and decision making processes on EU supervisory colleges, the quality of execution depends on the supervisory authorities. The depth and quality of information sharing, the joint projects undertaken, documentation of exchanges of views between authorities and actions taken attest to a maturing dialogue between supervisors, which should serve the NBB well and for which the NBB's own attitude should be given significant credit. Table 1 below offers a principle-by-principle summary of the assessment results.

Table 1. Summary Compliance with the Basel Core Principles—Detailed Assessments

Core Principle	Grading	Comments
1. Objectives, independence, powers, transparency, and cooperation		
1.1 Responsibilities and objectives	C	Legal mandate to supervise is in place but there could be greater clarity and transparency in terms of the relationship between the supervisory and financial stability goals of the NBB.
1.2 Independence, accountability and transparency	LC	It is not mandatory for the reasons for the dismissal of the Governor of the NBB to be publicly disclosed. Staff resources are over-stretched at a time of elevated stress so capacity to respond to deteriorating conditions may be jeopardized. The limited rule making powers are subject to potential veto by the government.
1.3 Legal framework	C	The NBB operates within a legal framework that provides for authorization and ongoing standards of supervision. See also CP 1.2
1.4 Legal powers	C	A suitable legal framework for banking supervision is in place including a broad range of powers for the supervisor.
1.5 Legal protection	C	Appropriate legal protections have been put in place in respect of banking supervision and supervisors.
1.6 Cooperation	C	The general framework for exchange of information is well articulated and there is evidence, based on the assessors' reviews of files, that it is operational in practice. The modalities of cooperation between the NBB and the FSMA need to be finalized and made fully operational.
2. Permissible activities	C	The laws provide clear definitions and not only the NBB but the FSMA, in their activities, have regard to the importance of ensuring that the public is not misled into placing deposits with institutions, which are not authorized for this purpose.
3. Licensing criteria	C	The NBB has a sound practice in place but has been reviewing its policies and practices around its regime for assessing "fit and proper."
4. Transfer of significant ownership	C	The NBB's application of policies and procedures in this area are comprehensive and there is an increasing focus on looking "upwards" through the shareholding and ownership structure above the institution.

5. Major acquisitions	LC	<p>The requirements of this principle are met in relation to the systemic institutions, due to the NBB's powers to object to strategic decisions made by such firms. Non-systemic firms have the potential to undertake a major acquisition in a non-financial sector without either pre-notification or pre-approval requirements being in place, however.</p>
6. Capital adequacy	LC	<p>The current approach to the deduction for investment in insurance subsidiaries is to deduct 100 percent from Total Capital. While this approach is consistent with the CRD, it is not, consistent with Basel II for a 50:50 deduction from Tier 1 and Tier 2. The application of this deduction from Total Capital is applicable to Belgium's largest domestic consolidated banks. This treatment will be modified to align with the Basel II as of 1 January 2013. It is the intention of the NBB to apply the deduction of participations in insurance companies pursuant to the Basel III framework in the future.</p> <p>An aspect of the Belgium banking sector that was problematic during the crisis involved the practice of banks granting credit to shareholders to subscribe to the capital of the bank where repayment of the loan depended on the proceeds the shareholder received from the capital instrument. The implication of this practice is that capital is not able to absorb losses and cannot be classified as 'paid up' as per the definition of capital. The other dimension of this issue is that published capital adequacy ratios of banks are artificially inflated, which weakens the transparency of the true loss absorbency of capital.</p> <p>We acknowledge that the own funds regulation has been amended to address this issue with a transition period commencing 1 January 2014, although at the time of the mission, the capital base included these amounts.</p>

7. Risk management process	LC	<p>Many of the criteria in CP7 require the supervisor to assess the Board's involvement in the risk management function. Indeed, the Principle focuses on Board oversight of risk management policies and processes. While the regulations require Boards to approve risk management strategies and the ICAAP, the supervisory assessment of the Board's involvement and understanding of risks and risk management will not necessarily involve direct engagement with the full Board (independent non-executive directors), even for larger systemic banks on at least an annual frequency. Without direct engagement with the full Board to challenge their appreciation of the risks, the implementation of risk management and adequacy of capital, it is difficult to see how the supervisor is able to arrive at an accurate, timely and comprehensive view of the Board's oversight of risk management.</p>
8. Credit risk	LC	<p>There is no requirement in the regulations for major credit risk exposures over a certain amount or percentage of the bank's own funds, to be decided by the bank's senior management or Board.</p> <p>Without this requirement, critical credit decisions can, in practical terms, be made by officers of the bank that might not be suitably informed of all risks. An effective delegation structure will strengthen the risk management framework to ensure that credit decisions are only taken at an appropriate level. This will also help to avoid unnecessary conflicts of interest, which might arise in relation to the granting of credit. While a conflicts of interest policy is required by the regulations, it might prove inadequate to mitigate this risk.</p>
9. Problem assets, provisions, and reserves	C	<p>Accounting standards govern the preparation and presentation of general purpose, publicly disclosed financial statements by banks.</p>

10. Large exposure limits	LC	The LE regime provides for concessions for smaller banks to exceed the 25 percent limit up to 100 percent own funds if the exposure is less than 150mn euro. In the event of a default of the counterparty, smaller banks are typically less able to raise additional equity and in some cases, may not have degree of sophistication in reporting and risk management (such as real time exposure reporting) to make timely decisions. CRM can reduce the exposure even at the 100 percent threshold which means in practice, the gross exposure to a single counterparty can exceed 100 percent own funds , which represents significant concentration risk.
11. Exposure to related parties	C	The prudential requirements regarding exposures to related parties is not established in a single regulatory requirement but a number of regulations that act to mitigate this risk. An integrated process for the identification, monitoring and reporting of exposures to related parties approved by the board is not explicitly provided for in the regulations.
12. Country and transfer risks	LC	The NBB has not issued specific guidance on country and transfer risk (other than guidance relating to credit risk and concentration risk in general), and not imposed any more specific reserves against such risks as required by the Principle.
13. Market risks	C	The regulatory framework has been revised to take account of the Basel II.5 enhancements. Since the crisis, the main trading activities of Belgium banks have declined to consist mainly of the management of customer demand. VaR is the main risk management tool used by banks to limit positions.
14. Liquidity risk	C	The regulatory requirements for liquidity risk are relatively well advanced with a quantitative test similar to the Basel LCR in place since 2011. Daily reporting for larger systemic banks is robust. Follow-up of the self assessment process has not been conducted across all banks in the sector.

15. Operational risk	C	The supervisor uses a number of tools for identifying and assessing operational risk. The frequency of on-site assessments are risk-based and for the large banking groups, performed on an annual basis. For medium sized and small banks, the frequency of on-site inspections varies between one and four years. Quantitative and qualitative information is included in offsite analysis and used in the scorecarding process.
16. Interest rate risk in the banking book	C	The prudential requirements for managing interest rate risk in the banking book are well established in the regulatory framework. The NBB has made strong efforts to implement new standards and has embedded interest rate risk in its core work.
17. Internal control and audit	LC	The supervisory model places reliance on the credit institution and the external auditor to verify the effectiveness of the control environment. The frequency, depth and comprehensiveness of the supervisors testing of the internal control environment can be enhanced.
18. Abuse of financial services	LC	<p>The last FATFs Mutual Evaluation Report was made in of June 2005, with another scheduled for 2014. In the 2005 report, the level of compliance of the AML/CFT regulation and guidance for the financial sector with the relevant Recommendations appears to be very satisfactory.</p> <p>The NBB use a range of supervisory tools to monitor and supervise this risk. There was overall not a systematic process governing how the compliance requirements fit into the supervisory framework, applied across the population of banks.</p> <p>Several criteria in Principle 18 require the supervisor to confirm that banks have sufficient controls and systems in place for preventing, identifying and reporting potential abuses of financial services, including money laundering etc. It was not sufficiently evidenced that the supervisor had a systematic process to verify adequacy of risk management across the population of banks.</p>

19. Supervisory approach	C	The NBB has put in place a sound analytical process that it is in the process of refreshing and deepening both in terms of analytical insight as well as enhancing the underpinning IT capabilities. The new supervisory tools ought to support a more forward looking analysis and also integrate analysis of insurance risk into the global risk assessment of groups.
20. Supervisory techniques	LC	The NBB applies a comprehensive supervisory program to systemic firms. At present, however, there is no process to identify the level of supervisory intensity that is proportionate for the non-systemic firms. Within the group of non-systemic firms, risk profiles vary and the minimum levels of adequate supervisory attention will also vary. The NBB needs to be certain that it has correctly identified these minimum levels of supervisory activity and is capable of monitoring and updating its plans as circumstances change. The NBB is aware of this dimension and has already embarked on multiple projects that will support a successful outcome.
21. Supervisory reporting	C	Belgium has a well developed system for assessing prudential returns as part of its offsite analysis. Financial analysts within the integrated supervisory teams, assess prudential returns, mainly on a quarterly basis, the results of which feed into the team meetings, which discuss peer comparisons and suggested outcomes for future action.
22. Accounting and disclosure	C	BGAAP applies at a solo level and IFRS for consolidated accounts. There is no concrete plan to harmonize accounting methodologies. The different treatment for valuations might create some lack of consistency in comparing risk profiles.
23. Corrective and remedial powers of supervisors	C	The NBB has wide powers of remedial and corrective action and there is evidence that it is prepared to use such powers, even if moral suasion has been effective upon occasion. Planned legal changes to permit the NBB Board to apply periodic penalty payments will be a potentially useful additional power.

24. Consolidated supervision	C	The NBB has the necessary legal powers and has implemented the necessary regulatory structure to facilitate the practice of consolidated supervision. The NBB has continued to develop its working relationships with key supervisory authorities to ensure the quality of group oversight of the systemic firms in particular.
25. Home-host relationships	C	The NBB places great value on home-host relationships. Cooperation agreements and MoUs have been put in place with all relevant authorities and an increasingly mature dialogue of exchange of information and joint activities is being undertaken.

Aggregate: Compliant (C) – 21³, Largely compliant (LC) – 9, Materially noncompliant (MNC) – zero, Noncompliant (NC) – None (note: CP 1 is divided into six component for this analysis.)

Recommended action plan and authorities' response

Recommended action plan

Table 2 lists the suggested steps for improving compliance. Recommendations are proposed on a prioritized basis.

³ The grading in respect of CP18 (abuse of financial services) is provisional as there was insufficient detail available to make a comprehensive assessment at the time of the review.

Table 2. Recommended Action Plan to Improve Compliance with the Basel Core Principles

Reference Principle	Recommended Action
1.2 Independence, accountability and transparency	The reasons for the dismissal of the Governor of the NBB must be publicly disclosed. Adequacy of staff resources need to be reviewed.
4. Transfer of significant ownership	The authorities are urged to remedy the lack of legal obligation for a credit institution to notify its supervisory authority of a material adverse development that may negatively affect the suitability of a major shareholder.
5. Major acquisitions	Laws or regulations should be amended to ensure that the NBB has the right of pre-approval of a major acquisition by a credit institution in the non-financial sector.
7. Risk Management	<p>Continue with the update of the Circular on Internal Governance. Emphasis on role of Board. Develop a comprehensive risk management standard, which articulates the NBB's minimum expectations for risk management for banks and across a group (leverage off international efforts).</p> <p>Develop a standard supervision program for all banks according to risk profile. Program The baseline supervisory program should include such activities as meetings with the non-executive directors (at least annually), review of Board minutes, onsite review testing controls and risk management and a meeting with the external auditor. Minimum supervision program is linked to the risk scorecard.</p> <p>When updating the Internal Governance Circular consider including a section for the Internal Audit function to formally report to the Audit Committee to ensure functional and operational independence.</p> <p>Suggest the internal Governance Circular requires major policies when approved by the board to be submitted to the NBB. While this might happen in practice, it formalizes the expectation.</p> <p>Establish a formal cycle for all accredited internal models (Pillar 1) to be assessed on a regular basis. The assessment would consider results of annual tests, audit findings etc.</p>

16. Interest rate risk in the banking book	<p>The program could be further enhanced as follows:</p> <ul style="list-style-type: none"> • Write a single regulation to replace multiple rules texts. Include requirements for stress testing, a limit framework that reflects risk appetite. • Strengthen the regulatory framework with a requirement for a functional and operational separation of markets and treasury function. • Consider an Asset Liability Committee for all credit institutions, which will enhance the quality, timeliness and management of this risk. • Extend cross-sectoral analysis to a greater number of banks. Improve the identification of outliers and strengthen the transfer of skills to supervisor.
17. Internal control and audit	<p>Consider obtaining a positive assurance from the external auditor as to the design and effectiveness of controls. This report would extend beyond the scope of the current engagement of the external auditor, which is an assessment of the process and documentation of the self assessment performed by management.</p>
20. Supervisory techniques	<p>The NBB should put in place a systematic supervisory process to ensure that each institution systematically receives the appropriate intensity of supervisory attention proportionate to its profile.</p>
21. Supervisory reporting	<p>Reporting dates for prudential returns, in some instances lag public reporting. Furthermore, some prudential returns are submitted only annually such as concentration risk. Align the reporting dates so that returns are submitted more timely and more consistently to enable integrated and timely financial analysis.</p>

C. Authorities' Response to the Assessment

54. The NBB can subscribe to the general conclusions and the main findings as laid down in this report. The NBB is satisfied with the overall high level of compliance with the 2006 Banking Core Principles and appreciates that recognition has been given to the challenging environment in which the NBB currently performs its supervisory tasks. The challenges stem from the continued crisis conditions and the relatively recent integration of prudential supervision into the NBB, formerly a task performed by the CBFA. During the mission, the NBB had the opportunity to explain the initiatives/reforms underway as a response to these challenges and to indicate how well advanced some of them already are. Discussions with the IMF were thus also a fruitful sounding board for the NBB and we will take into account the advice and recommendations to continue work in this respect.

55. For some of the Banking Core Principles, mainly those for which the NBB received a downgrade, we provide here some more extensive comments to the IMF's assessment or we indicate our future plans to meet the IMF's recommendations.

BCP 1: Objectives, independence, powers, transparency, and cooperation

56. The NBB will reconsider the adequacy of the supervisory resources in order to achieve the appropriate supervisory intensity and effectiveness in the course of 2013.

BCP 4: Transfer of significant ownership

57. The obligation for a credit institution to inform the supervisory authority of any material adverse development (affecting the criteria under which the assessment of the suitability of a major shareholder is made) will be provided soon, on the occasion of the next Banking Law's modification.

BCP 5: Major acquisitions

58. The right of pre-approval by the NBB of a major acquisition by a credit institution in the nonfinancial sector will be provided soon, on the occasion of the next Banking Law's modification.

BCP 6: Capital adequacy

59. We agree with the conclusion relating to the deduction of insurance company but underline that the regulation will be adapted as from 1 January 2013 on.

60. With regard to the deduction of credits to shareholders that have been used to subscribe capital instruments, we underline that the current regulation is fully in line with the Basel 3 framework and notably the eligibility criterion 11 for common equity tier 1 which states that "the instrument is directly issued and paid-in and the bank can not directly or indirectly have funded the purchase of the instrument.

61. This last criterion is new with regard to the conditions that the instrument must be directly issued and the bank can not directly or indirectly have funded the purchase of the instrument. As these conditions are new, the NBB has introduced a transitional measure for the deduction of existing credits at the end of December 2010 in line with the transitional measures of the Basel 3 framework. In the meantime, existing credits that are not deducted from own funds are taken into consideration in the pillar 2 decision relating to capital add-ons set by NBB, meaning that the full amount of these credits must be covered by common equity tier 1. All new credits that have been granted since end 2010 have been deducted from common equity tier 1.

62. With regard to the transparency issue, we will follow the new European regulation transposing the Basel 3 framework that requires each bank to disclose the impact of any transitional measures to the market (see article 470 of the current draft CCR) from the entry into force of this regulation and the guidelines that EBA will issue with regard to disclosure on own funds (see EBA consultation paper EBA/CP2012/04 Consultation paper on draft implementing standards on disclosure for own funds).

63. In addition to the Basel criterion 11, the current Belgian regulation provides also for the deduction of credits to shareholders when they are not granted at market conditions and when there is no evidence that the shareholders have sufficient revenues on an ongoing basis, other than the distributions on the capital instruments held, to support the payment of interest and repayment of the funding.

64. In conclusion, we consider that the issue of credits to shareholders does not constitute a reason for a downgrade and that the NBB is compliant with principle 6 from 1 January 2013 on (when the insurance participations will be deducted from tier 1 and tier 2).

BCP 7: Risk management

65. The NBB plans to review its internal governance framework, including risk management, starting in the autumn of 2013. At that moment, we will take into account the IMF's recommendations regarding the Board's oversight role for risk management and on how to integrate risk management and capital setting better.

BCP 8: Credit risk

66. We largely agree with the assessment but it is unclear whether BCP 8 requires the regulation to prohibit some credit to shareholders because conflicts of interest may arise (and have arisen in the past). The management of conflicts of interest between the bank and the shareholders is already regulated by the provisions of company law and the guidelines of the NBB on internal governance. On the basis of these guidelines, each institution must define a policy relating to conflicts of interest which shall be subject to the scrutiny of the NBB. We agree that these legal provisions and guidelines are not necessary sufficient but NBB has clarified the own funds regulation in order to be able to deduct some transactions made between the bank and its shareholders from the own funds (see above for BCP 6).

BCP 10: Large exposure limits

67. The NBB will examine whether to use the national discretion to set a stricter limit on large exposures within smaller institutions when transposing Capital Requirements Directive, Fourth Iteration (CRD IV).

BCP 12: Country and transfer risks

68. We largely agree with the assessment but underline that the current guidelines of the NBB relating to credit risk management and concentration risk ensure already the compliance with the main principles applicable to the management of country risk (notably obligation to define a policy approved by the board, to set limits, to monitor the evolution of the exposures and the risks, to have an adequate provisioning policy and process). Adding specific guidance on country risk would be mainly a repetition of what is already included in the current guidelines on credit risk and concentration risk.

BCP 16: Interest rate risk in the banking book

69. Interest rate risk has been recognized as one of the priorities in the NBB's Risk Review 2013. As explained to the IMF, the NBB has set up since 2012 an extensive program to further develop its supervision regarding interest rate risk that runs throughout its different supervision departments. When rolling out this program, the NBB will consider how the recommendations in this field can be translated into the NBB's practice.

BCP 17: Internal control and audit

70. It is unclear whether the actual BCP 17 requires that the supervisor should be satisfied as to the effectiveness of the internal controls. The June 2012 BCBS document requires the internal audit function to provide independent assurance on the quality and effectiveness of a bank's internal control.

71. If the supervisor should be satisfied as to the effectiveness of the internal controls, several options could be examined:

- The Bank could require the internal audit function to adhere to the IIA's International Professional Practices Framework (Practice Advisory 2130-1) and to the recently published principles of the BCBS document about the internal audit function in banks;
- The Bank could require the external auditors to give positive assurance on the design and effectiveness of the internal controls. As for internal controls over financial reporting, a reference could be made to PCAOB standard AS 5 (there is no equivalent in the IAASB suite of standards), for the other internal controls reference could be made to ISAE 3000. This standard is under revision and would require the Bank to describe in detail what is expected and what constitutes an acceptable internal control framework;

- It could be envisaged that positive assurance is obtained through on-site inspections performed by the Bank. This could be dealt with in the context of the NOVA project (aiming at a harmonization of and consistency in methods across the supervisory departments). It should however not be expected that such a positive assurance will be obtained on a yearly basis for all supervised institutions and regarding their complete internal control system.

72. We consider that obtaining, in a systematic and sufficiently documented way, comfort as to the design and effectiveness of internal controls is indeed necessary. The report by the external auditor is only one of the building blocks for the control by the NBB and its importance should therefore not be overestimated.

73. To summarize, in our opinion, comfort should be obtained through a pre-defined combination of senior management's self-assessment (as approved by the Board), ICAAP reporting, input from the internal auditors (cf. recent BCBS document about the internal audit function in banks) and from the external auditor, as well as NBB on-site inspections to test these different inputs. This combination is currently the case. We agree however that the process for integrating these different building blocks and for steering the interaction between them could be made somewhat stricter. We will also enhance our own quality assurance on the input of the external auditor. The NBB will include this work when designing baseline supervision (see also BCP 20).

BCP 20: Supervisory techniques

74. We overall agree with the assessment but like to offer some additional inputs to the points contained in the detailed assessment:

- Supervisory action and planning is generally based on priorities and oriented to high risk institutions. We confirm the need to better document choices and to present supervisory planning and realized actions on the basis of a formally agreed and sector wide methodology;
- Pressure is put on team members to strengthen the internal documentation process, to systematically introduce standard presentation, including comparison to peers, in order to make risk assessment more comprehensive and ensure level playing field;
- The ongoing development of an enhanced scorecard system will strengthen the structured dialogue both with the institutions concerned and with their approved commissioners and the competent supervisory authorities, notably via the colleges of supervisors, will drive the decision making process, and will be systematically used and included in periodic reporting to the Board;
- This enhanced scorecarding will facilitate clustering on a more refined and risk-focused basis and will lead to a more balanced and risk based supervisory planning and subsequent appropriate assignment of staff.

75. At the time of closing the FSAP mission, the NBB has already started work to implement a baseline supervision approach. We are in the process of identifying the different clusters and as result of this process, we have to define a baseline supervision even for the low risk institutions.

BCP 21: Supervisory reporting

76. The European Implementing Technical Standards (ITSs) on reporting, currently prepared by the EBA in the context of the future CRD IV, will shorten the remittance dates for prudential returns. These standards will become directly applicable in Belgium.

DETAILED ASSESSMENT

77. **Table 3 below offers the detailed Principle-by-Principle assessment.** It provides a “description” of the system with regard to a particular Principle, a grading or “assessment,” and a “comments.”

Table 3. Detailed Assessment of Compliance with the Basel Core Principles

Principle 1	Objectives, autonomy, powers, and resources. An effective system of banking supervision will have clear responsibilities and objectives for each authority involved in the supervision of banks. Each such authority should possess operational independence, transparent processes, sound governance and adequate resources, and be accountable for the discharge of its duties. A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision; powers to address compliance with laws as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Principle 1(1)	Responsibilities and objectives. An effective system of banking supervision will have clear responsibilities and objectives for each authority involved in the supervision of banks.
Essential criteria	
EC1	Laws are in place for banking, and for the authority (each of the authorities) involved in banking supervision. The responsibilities and objectives of each of the authorities are clearly defined and publicly disclosed.
Description and findings re EC1	<p>The legal framework for banking supervision can be found in the Law of 22 March 1993 (the “Banking Law”) and the Law of 22 February 1998 (the “NBB Organic Law”). Under Articles 12<i>bis</i>, 36/2 and 36/3 of the NBB Organic Law, the NBB is responsible for banking supervision and the Banking Law (Article 1) establishes the legal status and supervision of credit institutions (“the Banking Law”). The Banking Law further establishes (Article 46) that the NBB is responsible for ensuring that banks operate according to the Banking Law and decrees and regulations implementing them.</p> <p>Although the legal framework provides clarity that banks shall be subject to supervision and the NBB is the supervisory authority, neither the Banking Law nor the NBB Organic Law clearly creates publicly stated objectives for NBB in respect of supervision (for example a number of jurisdictions require that supervision is to be undertaken in order to achieve or to support the safety and soundness of the supervised institutions).</p> <p>Belgian regulatory architecture was amended by the law of 2 July 2010, which introduced the “twin peaks” model from April 2011. Both the Organic Law and the Banking Law have been amended so that the banking supervisory responsibility has transferred to the NBB, succeeding the former Banking Finance and Insurance Commission (CBFA).</p> <p>Following the introduction of the Twin-Peaks model the NBB became responsible for the micro- and macro-prudential supervision of banks, insurance and stockbroking investment firms (“sociétés de bourse” - “beursvennootschappen”), and also clearing and settlement institutions. Correspondingly, the FSMA is responsible for market supervision, conduct of business and the supervision of certain institutions (UCITS management companies, asset management companies and investment advisors).</p>

	<p>Cooperation between the NBB and FSMA is governed by Chapter IV/I of the NBB Organic Law and Section 6 of Chapter III of the Law of 2 August 2002 on the supervision of the financial sector and financial services.</p> <p>The Organic Law sets out the objectives of the NBB, including (Article 12) contributing to financial stability and (Art 12bis section 3) establishing that the NBB shall exercise banking supervision and carry out its supervisory tasks exclusively in the general interest.</p> <p>The NBB's mission (established in Art 36/2 and 36/3) is to undertake prudential supervision of <i>inter alia</i> credit institutions and in carrying out its general interest duties must take due account of the potential impact of its decisions on the stability of the financial system in all the other EU Member States concerned. The NBB role in financial stability is foreseen as intervention in detection of threats to the stability of the financial system, in recommending to government and parliament measures that may be necessary to address this risk, to coordinate financial crisis management, and in contributing to the missions of the EU institutions with respect to these issues. In particular the NBB shall determine which institutions are systemically relevant and impose measures upon them when this is deemed necessary.</p> <p>There is no direct or explicit reference to an NBB role in working to promote the safety and soundness of institutions in the legislation. It is noted that Article 1 of the Banking Law provides that the objective of this Law is to regulate the establishment, activities and supervision of credit institutions operating in Belgium, in order to protect savings and ensure the smooth operation of the credit system in Belgium. While this legal provision recognizes implicitly that supervision has a role in protecting savings and ensuring the smooth operation of the credit system, it is conceptually a different point from setting out the role of the NBB. However, the introduction of specific NBB powers in respect of supervision of systemically relevant institutions (and indeed communications of the NBB such as the Financial Stability Review) indicates that the objective of achieving the safety and stability of individual firms is seen as a core component of securing financial stability.</p>
EC 2	The laws and supporting regulations provide a framework of minimum prudential standards that banks must meet.
Description and findings re EC2	The Banking Law is the main legal text, which applies to all credit institutions and is the instrument which implements the requirements of the European Directives in the field of the prudential supervision of banks. The areas covered by the Banking Law include authorization, criteria that must be satisfied on an ongoing basis (including not only requirements relating to risk profile but also management structure and governance and merger and acquisition), supervision by the NBB as well as supervision by the statutory auditor.
EC3	Laws and regulations are updated as necessary to ensure that they remain effective and relevant to changing industry and regulatory practices.
Description and findings re EC3	<p>The Banking Law is kept updated in accordance with changes to the EU Directives relating to banking regulation. Furthermore, the NBB has powers under the Organic Law to issue regulations. Article 12bis, § 2 NBB Organic Law provides that "<i>within the areas of its competence, the NBB may lay down regulations to supplement the relative legal or regulatory provisions in respect of technical aspects.</i>"</p> <p>In addition, there is a specific NBB power and obligation to issue regulations under Article 43 of the Banking Law with regard to requirements relating to, inter alia, solvency, liquidity, and concentration risk.</p>

	Finally the NBB can and does issue Circulars to clarify its prudential expectations in respect of some more broadly drafted requirements under the Banking Law where standards are expected to increase over time (e.g., Circulars in relation to Article 20 and Article 20bis). The Circulars do not have the force of regulations and the NBB cannot impose a sanction solely on the basis of failure to comply with a Circular. However, given that the Circular is an elaboration of the supervisor's intentions of the manner in which the law will be applied, sanction could be applied in respect of breach of the underlying law.
EC4	The supervisor confirms that information on the financial strength and performance of the industry under its jurisdiction is publicly available.
Description and findings re EC4	The NBB publishes an annual Financial Stability Review, which provides information on the strength and performance of the financial sector. The NBB is also legally required (Article 28 of the Organic Law) to publish an annual report on its activities , which also provides an overview of financial stability
Additional criteria	
AC1	In determining supervisory programmes and allocating resources, supervisors take into account the risks posed by individual banks and banking groups and the different approaches available to mitigate those risks.
Description and findings re AC1	The NBB applies and is continuing to refine its approach to risk based supervision (please see wider discussion under CPs 19 and 20), which incorporates an approach, which allocates proportionally to identified risks. Recent changes to the legal framework incorporate the concept of a systemically important institution and supervisory planning takes these provisions into account.
Assessment of Principle 1(1)	Compliant
Comments	<p>The laws create an overarching legal framework which is applied to banks and which is amended in a timely manner to take account of national and EU developments.</p> <p>The principle requires there to be clear objectives and responsibilities for each authority for involved in the supervision of banks. As a result of allocating supervisory responsibility to the central bank, the authorities had to amend the Organic Law of the NBB to reflect its new roles. It is a challenging process to amend regulatory architecture to incorporate a significant function such as prudential supervision within an established body that had a pre-existing and very clear mandate such as a central bank.</p> <p>The NBB Organic Law establishes that the NBB will be responsible for supervising credit institutions and also that it has a responsibility to detect threats to financial stability. The legal mandate is thus in place, but the legal mandate does not express the purpose of prudential supervision (e.g. a responsibility for the safety and soundness of individual institutions) and it is not stated how the NBB must balance the priorities and demands of prudential supervision with those of protecting financial stability (e.g., that the safety and soundness of individual institutions is critical to but not necessarily sufficient to achieve a broader goal of financial stability).</p> <p>From the perspective of public policy, the legal mandate therefore lacks full clarity and it</p>

	<p>may not be transparent to the public how the central bank is expected to fulfill its roles. Therefore it would be helpful if the relationship between the two functions could be clearly articulated.</p> <p>It is not essential to amend the NBB Organic Law to address this concern, but it would be opportune to make amendments during the redrafting of the Law that is intended during 2013. The NBB may, in any case, wish to consider articulating a focused mission statement and objective, which they could promulgate on their website in the manner adopted by some other central bank supervisory authorities.</p>
Principle 1(2).	Independence, accountability and transparency. Each such authority should possess operational independence, transparent processes, sound governance and adequate resources, and be accountable for the discharge of its duties.
Essential criteria	
EC1	The operational independence, accountability and governance structures of each supervisory authority are prescribed by law and publicly disclosed. There is, in practice, no evidence of government or industry interference which compromises the operational independence of each authority, or in each authority's ability to obtain and deploy the resources needed to carry out its mandate. The head(s) of the supervisory authority can be removed from office during his (their) term only for reasons specified in law. The reason(s) for removal should be publicly disclosed.
Description and findings re EC1	<p>As noted under CP 1(1), EC1, the supervisory architecture of Belgium was established with the Law of 2 July 2010 (the "Twin Peaks Law"). The Royal Decree of 3 March 2011 implemented the law, thus establishing the Twin Peaks model from 1 April 2011. Under the Twin Peaks model, the NBB is responsible for both the micro- and macro-prudential supervision of—inter alia—credit institutions.</p> <p>The Organic Law (Chapter III) sets out the governance and organization of the NBB. There are five decision-making bodies within the NBB: the Governor, the Board of Directors, the Council of Regency, the Board of Censors and the Sanctions Committee.</p> <p>The Governor directs the NBB and presides over the Board of Directors and the Council of Regency. He is appointed by the King for a renewable term of five years, with no limit to the number of times that his mandate can be renewed. There is however, an age limit of 67.</p> <p>The Governor can only be dismissed during his term for reasons specified by Article 23 of the Organic Law (i.e., due to serious misconduct or if he or she no longer fulfils the conditions required for the performance of his or her duties). It is not mandatory for the reasons for dismissal to be publicly disclosed.</p> <p>In addition, it should be noted that under Belgian administrative rules, a motivation must be provided for all administrative acts. This means that the decision of dismissal must clearly identify the factual and legal elements on which it is based. Hence there is transparency of the decision vis-à-vis the person it concerns (i.e., the Governor).</p> <p>Furthermore, Article 23 grants the Governor the right to challenge a decision of dismissal in accordance with Article 14.2 of the statutes of the Euro System of Central Banks. Hence the decision may be referred to the Court of Justice on grounds of infringement of the Treaties or of any rule of law relating to their application. In such a case, the judgment shall be delivered in open court and the judgment is published in the Official Journal. Hence, in the event that the Governor has challenged a decision to dismiss it is possible that the reasons for the dismissal may become public.</p>

Such arrangements provide for greater legal certainty for the position of the Governor and of the independence of the NBB as an institution without however meeting the requirements of the criterion, which states that the reasons for dismissal should be public, not merely known to the individual dismissed, or have the potential to become public in the context of a legal challenge. While the grounds for dismissal are limited the public cannot know whether the incumbent is being dismissed for misconduct or failure to fulfill the conditions for performance of duty (such as grave ill health). This means that transparency intended by this principle is limited.

The **Board of Directors** is responsible for the administration and management of the NBB and decides on the direction of its policy. Besides the Governor, the Board of Directors consists of at least five and at most seven Directors, appointed by the King upon the recommendation of the Council of Regency. Currently, the Board comprises eight members; in addition there are two special representatives (who are not member of the Board) advising on prudential supervision. This method of nominating the Directors was introduced by law in 1948 to emphasize the public interest character of the NBB's activities. In the preparations for the Law of 28 July 1948 the legislature expressed its desire that the method of appointing the Directors and also the Regents should ensure both the NBB's total independence from individual interests and the technical competence of the candidates.

The Directors are appointed for six years and can only be dismissed for the reasons cited in Article 23 NBB Organic Law. The Governor excepted, the Board is divided equally between Dutch and French speaking members. Currently the Board of Directors consists of seven Directors and the Governor, which totals eight members. In order to avoid any conflict of interests, the Directors may not, under the terms of the Organic Law, except in a limited number of specified instances, perform duties in commercial companies or companies, which are commercial in form, or in public institutions engaged in industrial, commercial or financial activities. They are also prohibited from taking on certain political posts (as members of a parliament, government or ministerial cabinet). Conflict of interest is further managed by the fact that if a member of the Board of Directors has, directly or indirectly, an interest relating to proprietary rights, which conflicts with a decision or transaction of the Board, he must inform the Board and also the auditor and recuse himself from the discussion and decision making, a fact, which must be formally minuted.

The **Council of Regency** discusses monetary policy, the economic state of Belgium and the EU, the supervisory policy applicable to the sectors under NBB supervision, developments with regard to supervision and other issues of general interest to the NBB. The Council approves the budget, the annual accounts and the Annual Report of the NBB as well determining the rules of procedure of the NBB ("*huishoudelijk reglement*" / "*règlement d'ordre intérieur*"). The Council also determines the wages and pensions of the members of the Board of Directors.

The Council is composed of the Governor, the Directors and ten Regents, with an equal number of French and Dutch speaking regents. The regents are elected by the general meeting for a renewable term of three years. Of the ten regents, five are chosen from names submitted by the Minister of Finance and the remainder from names submitted by the most representative labour organizations, industry and commerce, agriculture and from small and medium-sized enterprises and merchants. Regents may not be members of the administrative, management or supervisory bodies of an institution subject to the supervision of the NBB, nor may they perform management duties in such an institution. The procedure for proposing and appointing the Regents was designed to ensure that

the various Belgian socioeconomic interests were fairly represented.

Conflict of interest is managed through the Organic Law prohibition on the Regents being members of the administrative, management or supervisory bodies of an institution subject to the supervision of the NBB (Articles 8, or 12bis), nor may they perform management duties in such an institution or take on certain political posts (as members of a parliament, government or ministerial cabinet).

The **Board of Censors** is responsible for supervising the preparation and implementation of the budget and constitutes the audit committee of the NBB and exercises the tasks laid down by Article 21bis of the Organic Law. Decisions are taken by a majority vote and it meets eight times a year. The Board of Censors reports to the Board of Directors and to the Council of Regency and can make comments and recommendations with regard to the issues that fall within its competence. The Board is composed of ten members including an equal number of French and Dutch speakers. The censors are elected by the general meeting of shareholders of the NBB for a renewable term of three years.

The **Sanctions Committee** pronounces on the imposition by the NBB of administrative fines ("geldboete"/"amende") and penalties ("dwangsom"/"astreinte").

There are six members of the Sanctions Committee, of which two members plus the chairman are required for a valid decision to be reached. The members are appointed by the King: 1) a State counselor or honorary State counselor, proposed by the First President of the Council of State; 2) a counselor or honorary counselor of the Court of Cassation, proposed by the First President of the Court of Cassation; 3) two magistrates who are neither members of the Court of Cassation, nor of the Brussels Court of Appeal; and 4) two other members. Conflict of interest rules are enshrined in the Organic Law so members may not consider a case in which they have a personal interest. For the three years preceding their appointment, the members of the Sanctions Committee may not have been employed by the NBB either in Board capacity or on the staff. Members of the Sanctions Committee have a term of six years, which is renewable. Members may be dismissed by the King (i.e., the federal government) only if they no longer fulfill the conditions for the performance of their duties or if they have been guilty of serious misconduct. At present the Sanctions Committee does not exist as no appointments have been confirmed by Royal Decree.

Restrictions on eligibility of service: There is an age limit of sixty-seven for the members of the Board of Directors, Council of Regency and the Board of Censors, although there are provisions to allow the completion of a term of service, which in the case of the Governor needs to be granted by Royal Decree. In no case may an office-holder remain in position beyond the age of seventy.

NBB's Legal status and oversight

The NBB is an "société anonyme de droit public / naamloze vennootschap van publiek recht," i.e., a public institution, which has adopted the form of a public limited liability company. It was created for the purpose of carrying out tasks of "public service."

The NBB has operational and financial autonomy with respect to its supervisory function. The decisions of the NBB in its capacity as administrative authority are subject to a right of appeal at the Council of State, but the scrutiny applies only to the legal process, i.e., assessing the legality of the decision, but not the substance of the decision. In exercising its supervisory responsibilities, the NBB possesses a measure of "discretionary power" but must explain the grounds (the factual basis and legal grounds) behind its decisions and is also subject to principles of consistency and proportionality in its decision making. The

	<p>NBB's decisions to impose administrative fines or penalties, are subject to appeal lodged only with the Brussels Court of Appeal.</p> <p>Regulations issued by the NBB require enforcement via Royal Decree ("<i>tutelle d'approbation</i>" / "<i>goedkeuringsvoogdij</i>"). The NBB attaches great importance to consultation with firms and their professional associations when preparing regulations and Circulars.</p> <p>NBB has financial independence: its expenses for prudential supervision are met by fees paid by financial institutions. The extent of its authorized expenditures and the manner in which these expenditures are covered, are laid down in detail in the Royal Decree of 17 July 2012.</p>
EC2	The supervisor publishes objectives and is accountable through a transparent framework for the discharge of its duties in relation to those objectives.
Description and findings re EC2	The website of the NBB, its annual report and its annual Financial Stability Review are the means by which the NBB communicates its results, actions and clearly states the missions and activities of the NBB as an organization, including the task of prudential supervision.
EC3	The supervisory authority and its staff have credibility based on their professionalism and integrity.
Description and findings re EC3	<p>The prudential staff of the NBB are a mix of staff brought from the former CBFA and staff of the NBB itself. Staff must abide by the code of ethics laid down by the Council of Regency (in accordance with Article 26, section 3 of the NBB Organic Law). This code of ethics includes various obligations aimed at ensuring the integrity of the NBB including, in particular, a prohibition on trading financial instruments of companies under NBB's supervision.</p> <p>Discussions with the industry and professional bodies within Belgium gave a consistent message that the NBB is seen as accessible, professional and demonstrating technical expertise, which commands the respect of supervised institutions.</p> <p>See also EC1 for conflict of interest restrictions for individuals on the Board of Directors and Council of Regency.</p>
EC4	<p>The supervisor is financed in a manner that does not undermine its autonomy or independence and permits it to conduct effective supervision and oversight. This includes:</p> <ul style="list-style-type: none"> • A budget that provides for staff in sufficient numbers and with skills commensurate with the size and complexity of the institutions supervised. • Salary scales that allow it to attract and retain qualified staff • The ability to commission outside experts with the necessary professional skills and independence and subject to necessary confidentiality restrictions to conduct supervisory tasks • A training budget and programme that provides regular training opportunities for staff • A budget for computers and other equipment sufficient to equip its staff with the tools needed to review the banking industry and assess individual banks and banking groups; and • A travel budget that allows appropriate on-site work.
Description and findings re EC4	The NBB funds its prudential activities through fees levied on the financial institutions

that it supervises (Article 12bis, section 4 NBB Organic Law). This principle of primary legislation is further elaborated by the Royal Decree of 17 July 2012 on covering the operating expenses of the NBB in connection with the supervision on financial institutions. Although the NBB budget is subject to parliamentary scrutiny, because the prudential function is independently funded there has been no experience of, and there is no expectation of, pressure being placed on this budget.

The Royal Decree of 17 July 2012 establishes specifically that:

- the fees should cover the effective cost of supervision;
- there should be stability and predictability in the financing burden imposed on supervised institutions;
- the system is pre-financed with subsequent amendments possible at the year-end (either repayment or additional levies as necessary).

The Royal Decree of 17 July 2012 sets a global amount of resources, which increases each year as follows:

- a) for personnel costs, the increase of resources is linked to increases applied to the NBB staff.
- b) All other expenses are adjusted in line with consumer prices.

Additional amounts added to the levy take account of the real costs driven by coordination and cooperation with other supervisory authorities.

The two sectors the NBB supervises are both levied - the insurance sector on the one hand and the banking and securities sector (investment firms and clearing and settlement institutions) on the other. Each sector is subject to two types of levy. All firms in the sector are subject to a main levy but SIFIs are required to pay a supplementary amount.

There is no ceiling placed on the numbers of staff. When taking over the micro-prudential supervision from CBFA in April 2011, the staff dedicated to prudential regulation and supervision numbered around 200 full time employees (FTE). The NBB Board decided to increase the resources by 40 FTE to benefit both banking and insurance sectors.

In September 2012, the staff dedicated to prudential regulation and supervision amounted to around 230 FTE. This includes staff dedicated to prudential regulation, financial stability, supervision of banking and insurance sector as well as market infrastructure, specific operational support and prudential law. Other support functions, such as secretariat to the Board, IT support, are available to the prudential departments but are not included in these figures.

At least 70 percent of the NBB staff dedicated to prudential regulation and supervision are professional executives. Recent studies (e.g., Hudson Banking Salary Survey) show that the compensation offered at NBB is in the top quartile for commensurate roles.

The NBB have identified a general need for IT personnel. Though supervision does not have dedicated IT or HR, it has enjoyed a major IT budget to deliver a global programme to renew the entire IT architecture and which has absorbed up to 50 percent of the IT staff.

Additional criteria	
AC1	The head(s) of the supervisory authority is (are) appointed for a minimum term.
Description and findings re AC1	The Governor of the NBB is appointed for a minimum, renewable term of five years.
Assessment of Principle 1(2)	Largely Compliant
Comments	<p>Although the supervisory function – which is a department within the central bank – is not protected by laws ensuring the independence of the functions of the Euro System of Central Banks, of which the NBB is a member, there are clear lines of accountability, transparency, separate funding and there is no indication in practice that there is any interference with the operational independence of the NBB acting in its supervisory capacity.</p> <p>Lack of full compliance with this CP derives from the fact it is a requirement of CP1(2) that the reasons for the removal of the head of the supervisory body must be publicly disclosed. This is not the case for the NBB. The assessors accept that there are limited grounds for dismissal and that the motivation for the dismissal must be made known to the incumbent (i.e., the Governor) and that the incumbent has a right of legal challenge , which may ultimately result in a judgement that will be made public and which may disclose the reasons for the dismissal (as discussed under EC1). Nonetheless, and while accepting that these arrangements support the independence of the NBB, the arrangements do not meet the criterion set out and the level of transparency falls short of what is required.</p> <p>Additionally, it was unclear to the assessors at the time of the mission that the supervisory functions had adequate resources to deliver the objective of systematic risk based supervision for all institutions. In mitigation it is acknowledged that there are many complex factors to be taken into account not least including the need for increase in staff to be undertaken at a pace at which they can be effectively absorbed into the organization. It is welcome that the NBB has increased resources in comparison with the former headcount, and also that there is now no formal ceiling on a headcount. In terms of resources, the NBB is well placed to fund its needs (through industry levy). The challenge lies in identifying the scale of future resource needs in the face of current structural uncertainties (in particular discussions around supervision within the Single Supervisory Mechanism) and also ensuring that as increases are identified that they can be appropriately managed and integrated into the supervisory function. Nonetheless, the NBB is strongly encouraged to continue to seek to reassess the numbers and skill set needed to deliver their enhanced risk based supervisory processes in a systematic manner for all their institutions.</p> <p>It is also noted that while the NBB enjoys some limited rule making powers (as required under CP1(3)) the rulemaking requires the issuance of a Royal Decree to take legal effect. As part of the process of obtaining the Royal Decree, the proposed regulation must be open to ministerial scrutiny and possible veto. In practical terms this has had and is likely to have limited or nil effect on the independence of the NBB in this capacity, but it would be preferable for the NBB to have powers to issue binding regulations without this formal constraint. It is, however, recognised that continued regulatory changes within the EU (such as the “single rule book”) may render this particular point redundant.</p> <p>Separately, the assessors noted that under the NBB Organic Law (and as reflected in the Statutes and Corporate Governance Charter) that the Minister of Finance has the right to</p>

	<p>suspend decisions of the NBB. Unlike the functions of the NBB in respect of its duties as part of the Eurosystem of Central Banks (ESCB), there was no legal carve out clarifying that the Minister had no vires in respect of prudential supervision. In discussion with the NBB staff it was understood that the Minister has not exercised this power in practice. Moreover, it appeared that the intention had been to ensure that prudential supervision enjoyed the same carve-out as the ESCB and this loophole would be addressed in a re-writing of the NBB Organic Law planned for 2013. For purposes of good governance and complete clarity it is recommended that the authorities take this opportunity as they already plan to do.</p>
Principle 1(3)	Legal framework. A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision.
Essential criteria	
EC1	The law identifies the authority (or authorities) responsible for granting and withdrawing banking licenses.
Description and findings re EC1	The Banking Law (Section I, Article 7) lays down the exclusive competence of the NBB to authorize a bank and also (Article 57) that the NBB is exclusively authorized to revoke such authorization.
EC2	The law empowers the supervisor to set prudential rules (without changing laws). The supervisor consults publicly and in a timely way on proposed changes, as appropriate.
Description and findings re EC2	<p>In Belgium, in common with all EU member states, many prudential standards are prescribed in EU legislation and transposed into Belgian law. While the NBB cannot change laws, it may issue prudential regulations under the Organic Law Article 12bis, section 2 NBB), which provides that <i>"within the areas of its competence, the NBB may lay down regulations to supplement the relative legal or regulatory provisions in respect of technical aspects."</i> Such regulation only takes legal effect following enforcement by Royal Decree. The NBB has the option of open consultation on any proposed regulation.</p> <p>In addition, there is a specific NBB competence for issuing regulations under Article 43 of the Banking Law, which requires the NBB to issue regulations with regard to requirements relating to, inter alia, solvency, liquidity and concentration risk (e.g., the NBB Own Fund Regulation and the Liquidity Regulation). (See also CP1(1) EC3).</p> <p>Finally, the Banking Law (Articles 20, section 4 and 20bis, section 8) states that the NBB can set out prudential rules with regard to specific topics such as risk management. The NBB has exercised this power.</p>
EC3	The law or regulations empower the supervisor to obtain information from the banks and banking groups in the form and frequency it deems necessary.
Description and findings re EC3	<p>The NBB Organic Law (Article 36/19) provides that the NBB can obtain all necessary information from the institutions under its supervision.</p> <p>The Banking Law (Article 44) requires credit institutions to submit financial reports to the NBB in the manner and frequency prescribed by the NBB.</p> <p>Furthermore, Article 46 provides that the NBB may request information on the financial position, transactions, the organization and operation of credit institutions. The parent of the consolidated group must submit its financial statement to the NBB according to the form and frequency specified by the NBB.</p>

	<p>Article 49 provides that the NBB can obtain necessary information from entities, which control a credit institution, or which may be non-consolidated subsidiaries of a credit institution provided that such entities are not already part of the consolidation or the financial group (conglomerate), which is subject to supplementary supervision.</p> <p>These articles grant the NBB the right to conduct on-site verification of information it has received, or to require verification by accredited auditors or foreign experts.</p> <p>It is a criminal offence under the Banking Law (Article 104, section 1, point 12) to refuse to give the required information, or wrongful or incomplete information or to prevent the NBB from carrying out inspection and verification procedures. (See Core Principle 1(4) below).</p>
Assessment of Principle 1(3)	Compliant
Comments	The NBB operates within a legal framework that provides for authorization and ongoing standards of supervision.
Principle 1(4)	Legal powers. A suitable legal framework for banking supervision is also necessary, including powers to address compliance with laws as well as safety and soundness concerns.
Essential criteria	
EC1	The law and regulations enable the supervisor to address compliance with laws and the safety and soundness of the banks under its supervision. The law and regulations permit the supervisor to apply qualitative judgement in safeguarding the safety and soundness of the banks within its jurisdiction.
Description and findings re EC1	<p>Under Article 46 of the Banking Law the NBB is required to ensure that every credit institution operates in conformity with the Banking Law and its implementing decrees and regulations.</p> <p>The law demands that the NBB pay specific attention to qualitative aspects of credit institutions such as suitability of its risk management, its administrative and accounting organization and internal control systems; in addition to the quantitative elements such as the adequacy of its capital.</p>
EC2	The supervisor has full access to banks' board, management, staff and records in order to review compliance with internal rules and limits as well as external laws and regulations.
Description and findings re EC2	The NBB has the right to meet the board of a credit institution, its executive management, its staff and have right to all records. Notably, the Banking Law (Article 46) gives NBB broad powers to carry out on-site inspections on the firm's premises and read and copy information in relation to compliance with banking regulations, the accuracy of information provided by the institution as well as in relation to the adequacy of management, administration, internal controls, governance and accounting of the institution.
EC3	<p>When, in a supervisor's judgment, a bank is not complying with laws or regulations or it is or is likely to be engaged in unsafe and unsound practices, the supervisor has the power to:</p> <ul style="list-style-type: none"> • take (and/or require a bank to take) prompt remedial action; and • Impose a range of sanctions (including the revocation of the banking license).

Description and findings re EC3	<p>The Banking Law (Article 57) grants the NBB a range of remedial measures that it may apply. These measures extend from the appointment of a special commissioner, requirements with regard to solvency, liquidity, risk concentration, to the revocation of the banking license. (See also CP23).</p> <p>Remedial measures should be distinguished from the administrative sanctions as described in Articles 102 and 103 of the Banking Law and the criminal sanctions as referred to in Articles 104 et seq. of the Banking Law</p> <p>Remedial measures</p> <p>In the event that the NBB uncovers deficiencies or lack of compliance with the laws and regulations it shall determine the timeframe within which the credit institution must rectify the situation (Article 57 Banking Law). Should the deadline not be met, the NBB may impose a number of measures:</p> <ul style="list-style-type: none"> • it may appoint a special commissioner, whose approval is required for all or part of the acts and decisions of the credit institution; • it may impose additional requirements with regard to solvency, liquidity, and risk concentration; • it may impose restrictions on the variable elements of remuneration; • it may suspend for a certain period all or part of the credit institution's activities and can require an institution to transfer the shares it holds in accordance with Articles 32, §§ 4 and 5 Banking Law; • it may order the institution's directors to be replaced or, failing compliance with the order, appoint one or more temporary directors; and finally, • it may revoke the credit institution's authorization. <p>It must also be noted that in applying measures under Article 57, the NBB must act according to the principle of proportionality. This means that the measures imposed cannot exceed what it is necessary to remedy the credit institution's situation.</p> <p>In the case of systemic institutions (where there could be an impact on the stability of the Belgian or international financial system) disposal of the assets or liabilities of the credit institution can be required under Article 57bis through the application of a Royal Decree. The NBB may initiate procedures for such a process, though this competence is shared with the government, which (in such an instance) is obliged to consult with the NBB. To date the powers under Article 57bis have not yet been exercised, although the NBB has reached the stage of initiating the process of disposal.</p> <p>Administrative sanctions</p> <p>The Banking Law provides for two types of administrative sanctions, namely fines and also publication of failure to comply with orders made to adhere to the provisions of the law (or implementing decrees).</p> <p>Fines are imposed under Article 103, which allows the NBB to require compliance with the laws and regulations and to set a timetable for compliance. The infringement of the laws and regulations themselves can lead to a fine and the failure to comply with an order to rectify non-compliance within the specified timetable leads to a fine.</p> <p>Thus, if the institution fails to comply with the requirements in the specified period the NBB may impose a fine of up to EUR 2,500,000 per infringement or a maximum of EUR 50,000 euros per each day's delay.</p>
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	<p>In addition, the NBB has the right to impose an administrative fine for the infringement of the regulations (i.e., the same offence or same totality of offences for which a deadline for remedial action was set), which shall be between €2,500 and 2,500,000.</p> <p>The fine is payable to the Ministry of Finance.</p> <p>Publication of failure to comply with injunctions ordering it to comply with the provisions of this Law or its implementing decrees is governed by Article 102. In the event that publication might inflict significant damage upon the institution, the notice can be published without names being disclosed.</p> <p>It should be noted that administrative sanctions would have to be decided upon by the Sanctions Committee and that at present a Sanctions Committee has not yet been convened at the NBB. Appointments to the Sanctions Committee must be ratified by the government and at the time of the mission names had not been confirmed.</p> <p>Criminal sanctions</p> <p>Article 104 Banking Law imposes a range of criminal sanctions for specific breaches of the Banking Law This is outside of the range of the NBB , which may not to impose these sanctions as this is the prerogative of the criminal courts.</p> <p>Any criminal investigation, or action following such investigation, with regard to the potential breach of the Banking Law and other related regulations by administrators, directors, managers, statutory auditors of financial institutions should be notified to the NBB under the terms of the Banking Law</p> <p>Potential amendments</p> <p>At the time of the mission, the authorities were discussing potential legal changes that would allow for a more administratively efficient approach to imposing periodic penalty payments upon firms as one dimension of corrective and remedial measures. When the legal framework relating to the power of imposing administrative sanctions was imported into the Organic law of the NBB by the Twin Peaks Royal Decree it was provided that the Sanctions Committee was competent to impose fines ("geldboete"/"amende") and periodic penalty payments ("dwangsom"/"astreinte") to the supervised institutions. These two measures are seen as fundamentally different. Periodic penalty payments ("dwangsom"/ "astreinte") are intended to create an incentive to respect a requirement, while the purpose of fines is to punish an illicit behavior on ex post basis⁴. In the legal framework governing the FSMA (the Law of August 2nd 2002 as modified by the Law of 2 July 2010), however, the imposition of fines was in the competence of the Sanctions Committee and the imposition of periodic penalty payments was the sole competence of the Board of directors. The NBB would like to mirror this is division of responsibility and it is now intended to adopt a new law removing the qualification of "administrative sanction" from the periodic penalty payments ("dwangsom"/ "astreinte"). This would thus allow the adoption of such measures by the Board of Directors without the more elaborate and extensive procedures required at present (Articles 36/9 and seq. of the Organic Law of the NBB).</p>
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⁴ Preparatory Documents, Parliament (Chambre des Représentants), 2001-2002, n°50-1842/1, p. 288.

Assessment of Principle 1(4)	Compliant
Comments	The NBB enjoys a range of remedial measures that allow for an appropriate degree of proportionality in its approach to breaches of laws and regulations. It is noted that the drafting of Article 57 of the Banking Law usefully takes into consideration that there may be a necessity for swift action in urgent situations.
Principle 1(5)	Legal protection. A suitable legal framework for banking supervision is also necessary, including legal protection for supervisors.
Essential criteria	
EC1	The law provides protection to the supervisory authority and its staff against lawsuits for actions taken and/or omissions made while discharging their duties in good faith.
Description and findings re EC1	Liability protection for the NBB and its staff is provided under the Organic Law (Article 12 <i>bis</i> , section 3): “the NBB, the members of its bodies and the members of its staff shall not bear civil liability for their decisions, acts and conduct in the exercise of the legal tasks of the NBB, save in the event of fraud or gross negligence.” Additionally, civil liability is limited to fraud or gross negligence in cases where persons have carried out the remedial measures outlined in Article 57 <i>bis</i> of the Banking Law (see CP1(4) EC 3).
EC2	The supervisory authority and its staff are adequately protected against the costs of defending their actions and/or omissions made while discharging their duties in good faith.
Description and findings re EC2	In 2008 an insurance agreement covering the costs of defending actions was concluded for the NBB staff. This insurance agreement was amended in 2011 to also cover the NBB staff working in relation to its prudential supervision tasks.
Assessment of Principle 1(5)	Compliant
Comments	Appropriate legal protections have been put in place in respect of banking supervision and supervisors.
Principle 1(6)	Cooperation. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Essential criteria	
EC1	Arrangements, formal or informal, are in place for cooperation and information sharing between all domestic authorities with responsibility for the soundness of the financial system, and there is evidence that these arrangements work in practice, where necessary.
Description and findings re EC1	EU legislation provides the over-arching legal gateways for exchange of confidential information between domestic authorities. At present, and following the introduction of the “Twin Peaks” law there is a deficiency in the domestic legal provision for the exchange of information between the FSMA and the NBB when acting in its supervisory capacity. Such information is covered by professional secrecy constraints and requires a specific exemption, which was omitted, in error, from the law and an amending instrument is needed. It is hoped that this technical remedy can be achieved shortly, possibly by the end of 2012. In practical terms exchange of information and cooperation continue at a working level – a fact confirmed to the assessors by a range of NBB staff – and work has also taken place on drafting a protocol (MoU) for formalizing the arrangements. At the time of the mission discussions were continuing between the NBB and the FSMA on whether the protocol could be agreed or whether refinements would be needed.

EC2	Arrangements, formal or informal, are in place, where relevant, for cooperation and information sharing with foreign financial sector supervisors of banks and banking groups of material interest to the home or host supervisor, and there is evidence that these arrangements work in practice, where necessary.
Description and findings re EC2	<p>Under the provisions of Section 4 of the Organic Law, the NBB may also communicate information to other (foreign or national) authorities involved in the financial sector in compliance with the conditions provided for by law (see Articles 36/13 et seq. NBB Organic Law).</p> <p>Specifically, to promote cooperation with foreign authorities, the Organic Law (Article 36/16,) allows the NBB to conclude agreements with competent authorities, so that terms and conditions and procedures of cooperation may be established, including any distribution of supervisory tasks, the designation of a competent authority as a supervision co-ordinator and the method of supervision (on-the-spot inspections or otherwise). The terms and conditions governing the collection and exchange of information are also covered.</p> <p>Ten cooperation agreements have been concluded since 2005 – with a number of these agreements having been made by the NBB’s predecessor authority the CBFA. Agreements are in place with the supervisory authorities of: Hong Kong (2005), Poland (2005), Malta (2006), Switzerland (2006), Canada (2007), Serbia (2008), Dubai (2008), China (2008), U.S. (2011) and Turkey (2011). As a rule, though, MoUs are no longer drawn up with other EU authorities as cooperation arrangements are covered by the EU directives (notably 2006/48/EC and its amending directives).</p> <p>On top of these bilateral cooperation agreements the NBB has also agreed on several (five) multilateral cooperation agreements for the supervision of specific cross-border financial groups.</p> <p>Some non-institution related cooperation agreements have also been concluded such as an MoU between the financial supervisory authorities, central banks and finance ministries of the European Union (2008).</p> <p>There is also an MoU on Cooperation between the Financial Supervisory Authorities, Central Banks and Finance Ministries of the European Union on cross-border Financial Stability , which provides the common practical guidelines for crisis management provide detailed operational guidance and reflect a common understanding between the Parties of their respective role as well as of the steps and procedures to be taken in relation to a cross-border systemic financial crisis situation.</p> <p>The financial crisis of the past few years has clearly tested cooperation arrangements and agreements between all financial authorities. The NBB noted that in emergency conditions, formal arrangements that are envisaged in MoUs and which can be time consuming, are typically not possible. However, the NBB has enjoyed good working relationships with its counterparts in other jurisdictions (see notably the discussion in CP25). The assessors saw files which demonstrated that high quality, and often extensive, information sharing is taking place on a regular and frequent basis.</p>

EC3	The supervisor may provide confidential information to another domestic or foreign financial sector supervisor. The supervisor must take reasonable steps to ensure that any confidential information released to another supervisor will be used only for supervisory purposes and will be treated as confidential by the receiving party. The supervisor receiving confidential information from other supervisors is also required to take reasonable steps to ensure that the confidential information will be used only for supervisory purposes and will be treated as confidential.
Description and findings re EC3	Again, under the provisions and conditions of Section 4 of the Organic Law, (Articles 36/13 et seq) in accordance with Article 44(2) of Directive 2006/48/EC provides gateways for the exchange of confidential information with non-domestic banking supervisory authorities or other financial sector supervisors. The recipients must be subject to an equivalent obligation of professional secrecy.
EC4	The supervisor is able to deny any demand (other than a court order or mandate from a legislative body) for confidential information in its possession.
Description and findings re EC4	The relevant articles in the NBB Organic Law clearly stipulate that the NBB "may" share confidential information. As such there is no legal obligation to do so. This is confirmed in the explanatory documents, which clarify that the communication of confidential information is an exception to the professional secrecy and is only a possibility, never an obligation.
Assessment of principle 1(6)	Compliant
Comments	<p>The general framework for exchange of information is well articulated and there is evidence, based on the assessors' reviews of files, that it is operational in practice.</p> <p>It is important for the authorities to ensure that the drafting oversight in the Twin Peaks law, which does not provide the formal exemption for the FSMA to exchange confidential information with the NBB when the latter is acting in its capacity of supervisor, is remedied at the earliest opportunity. The authorities aim to have the amendment in place before the end of 2012. It is particularly desirable for the NBB and the FSMA to conclude their protocol governing their working arrangements and exchanges of information to ensure that each authority has access to full, relevant information that it needs in the discharge of its own responsibility. The assessors noted that the de facto working level relationships exist and that exchanges of information have continued to take place, notwithstanding the current technical legal anomaly. Were, however, the current situation to persist over time without an MoU there is a clear risk that supervisory relationships might degrade to the detriment of effective supervision and oversight of groups.</p>
Principle 2	Permissible activities. The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined and the use of the word "bank" in names should be controlled as far as possible.

Essential criteria	
EC1	The term “bank” is clearly defined in laws or regulations.
Description and findings re EC1	<p>The term “credit institution” is defined in Article 1 of the Banking Act. Deposit taking is prohibited for any institution that is not authorized as a credit institution by the NBB under Article 4 of the Banking Law.</p> <p>The term “credit institution” is drawn from EU legislation (i.e., an institution that extends credit and also takes deposits) , which demands that all credit institutions must be regulated under EU law. Article 1 of the Banking Law defines credit institutions as Belgian or foreign companies whose activities—currently—consist in: 1) receiving deposits or other repayable funds from the general public and offering credit for their own account; 2) issue payment instruments under the form of electronic money. It may be noted that the Electronic Money Law is expected to be amended and will then exclude this electronic money issuance from the Banking Law and include it in legislation in payment institutions.</p>
EC2	The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined either by supervisors, or in laws or regulations.
Description and findings re EC2	<p>A credit institution requires a license for the taking of deposits from the general public and the offering of credit for their own account. At the point of application for a license, the institution must submit a business plan outlining the planned activities to the NBB who will permit or refuse authorization to conduct these activities. In principle a banking license in Belgium provides comprehensive authorization for all activities listed. However, when an institution wishes to embark on new activities post-licensing and where these new activities would constitute a change in the basis for granting the license, it must also notify the NBB who will assess the application typically via Article 20 of the Banking Law.</p> <p>The main potential banking activities (a non-exhaustive list) are listed into the law to facilitate the operation of the EU passport, which permits these activities to be carried out in the single market if the credit institution has a license to perform these activities from its home state authority. These activities are:</p> <ul style="list-style-type: none"> - Acceptance of deposits and other repayable funds - Lending including, <i>inter alia</i>: consumer credit, mortgage credit, factoring, with or without recourse, financing of commercial transactions - Financial leasing - Money transmission services - Issuing and administering means of payment (e.g., credit cards, travellers' cheques and bankers' drafts) - Guarantees and commitments - Trading for own account or for account of customers in: <ul style="list-style-type: none"> (a) money market instruments (cheques, bills, certificates of deposit, etc.); (b) foreign exchange; (c) financial futures and options; (d) exchange and interest rate instruments; or (e) transferable securities.

	<ul style="list-style-type: none"> - Participation in securities issues and the provision of services related to such issues - Advice to undertakings on capital structure, industrial strategy and related questions and advice as well as services relating to mergers and the purchase of undertakings - Money broking - Portfolio management and advice - Safekeeping and administration of securities - Credit reference services - Safe custody services
EC3	The use of the word "bank" and any derivations such as "banking" in a name is limited to licensed and supervised institutions in all circumstances where the general public might otherwise be misled.
Description and findings re EC3	<p>Only entities that possess a banking license may make use the word "bank," as protected by Article 6 of the Banking Law.</p> <p>Under the terms of the Banking Law the terms "credit institution," "bank," and any derivations thereof may - in principle - only be used by a limited number of institutions and namely by:</p> <ul style="list-style-type: none"> - Belgian credit institutions; - foreign credit institutions that perform tasks under the free provision of services or via the establishment of a branch office; - representative offices. <p>Some exceptions to that rule exist, for instance: the NBB, the ECB, other international public banking organizations, and also financial holding companies.</p> <p>In practice, if the NBB becomes aware of a wrongful use of the term "bank" it will inform the Office of the Public Prosecutor and the FSMA. In addition, in order to enable the NBB to verify whether a transaction or an activity falls within the scope of the laws and regulations it supervises, the NBB can formally require all necessary information from institutions executing the transaction or performing the activity and any third party that facilitates such transaction or activity on the basis of Article 36/19 of its organic law. This information request is subject to penalties in case of non-compliance. There are no recent examples of this power needing to be used in this context.</p> <p>The FSMA also plays a role in the detection and prevention of illegal deposit taking firms or activities. In accordance with the Law of 2 August 2002, (Article 45, section 1), the FSMA is mandated "to contribute towards compliance with the rules aimed at protecting savers and investors against the illegal offer or supply of financial products or services." The FSMA, in its market surveillance, seeks to identify any solicitation of deposits or any offering of investment services by unauthorized persons or companies. In addition to acting promptly to close down the unlicensed activities, the FSMA will typically also issue a warning to the general public (via press release and announcement on its website), although there are no recent examples of the NBB or the FSMA having identified illegal deposit taking.</p>

EC4	The taking of deposits from the public is generally reserved for institutions that are licensed and subject to supervision as banks.
Description and findings re EC4	The Banking Law requires credit institutions that take deposits from the public to be licensed and subject to supervision.
EC5	The supervisory or licensing authority publishes, and keeps current, a list of licensed banks and branches of foreign banks operating within its jurisdiction.
Description and findings re EC5	Article 13 of the Banking Law requires the NBB to establish a list of all licensed credit institutions. The updated list is published on the NBB's website and is notified to the European Commission. It is subdivided into sections (banks, saving banks, public banks, investment banks). An annex to the list covers the Belgian financial holding companies.
Assessment of Principle 2	Compliant
Comments	The legal framework provides clear definitions and not only the NBB but the FSMA, in their activities, have regard to the importance of ensuring that the public is not misled into placing deposits with institutions, which are not authorized for this purpose.
Principle 3	Licensing criteria. The licensing authority must have the power to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the ownership structure and governance of the bank and its wider group, including the fitness and propriety of Board members and senior management, its strategic and operating plan, internal controls and risk management, and its projected financial condition, including its capital base. Where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.
Essential criteria	
EC1	The licensing authority could be the banking supervisor or another competent authority. If the licensing authority and the supervisory authority are not the same, the supervisor has the right to have its views considered on each specific application. In addition, the licensing authority provides the supervisor with any information that may be material to the supervision of the licensed institution.
Description and findings re EC1	In Belgium the supervisory authority and the licensing authority are the same.
EC2	The licensing authority has the power to set criteria for licensing banks. These may be based on criteria set in laws or regulations.
Description and findings re EC2	<p>The conditions that have to be fulfilled in order to obtain a banking license from the NBB are set out in the Banking Law in particular in the Articles 15 to 22. These conditions relate to the legal form of a credit institution, initial capital, shareholders, the management of the credit institution, organizational requirements, the location of the head office and the membership to a deposit guarantee system.</p> <ul style="list-style-type: none"> - <i>Legal form:</i> Article 15 of the Banking Law requires that credit institutions are established as commercial companies. - <i>Minimum initial capital:</i> Article 16 of the Banking Law requires a fully deposited minimum capital of 6.2 million euro. - <i>Shareholders:</i> The NBB will only grant an banking license after being informed of the identities of the shareholders or members, whether direct or indirect, natural or legal persons, that have qualifying holdings, and of the amounts of those holdings (Article 17). - <i>Leaders of the credit institution:</i> The effective management of a credit institution must

	<p>consist of at least two natural persons who need to possess the necessary professional reliability and suitable experience. They may not have prior convictions for activities set out in Article 19.</p> <ul style="list-style-type: none"> - <i>Organizational requirements:</i> Every credit institution has to possess a suitable management structure, an adequate administrative and accounting structure, and has to have in place control and IT-security measures and a suitable internal control. If a credit institution also conducts investment services or activities it must meet the terms of Article 20<i>bis</i> relating to internal organization. - <i>Location of the head office:</i> The head office of a Belgian credit institution should be located in Belgium. - <i>Membership of a deposit guarantee system:</i> Every Belgian credit institution wishing to acquire a banking license is required to participate in a deposit guarantee scheme. <p>Power of the NBB to set more detailed criteria</p> <p>The King, on recommendation from the NBB and the FSMA, can further specify rules and obligations in relation to investment services and activities (see the organizational requirements of Article 20<i>bis</i> Banking Law)—i.e., recommendations from the authorities are confirmed through Royal Decree to take legal effect.</p> <p>The NBB can also further specify certain requirements (e.g., Article 20, sections 4 and 5; Article 20<i>bis</i>, sections 4 and 8; and Article 20<i>ter</i>) and may thus define more clearly what is meant by suitable internal organization of an institution (e.g., including internal control, risk management function, compliance function, internal audit function, including the requirements for the audit committee of a credit institution).</p>
EC3	The criteria for issuing licenses are consistent with those applied in ongoing supervision.
Description and findings re EC3	The conditions for authorization are set out in the Banking Law (Articles 15-22) and must be met on a continuing basis by the credit institution.
EC4	The licensing authority has the power to reject an application if the criteria are not fulfilled or if the information provided is inadequate.
Description and findings re EC4	<p>NBB has the discretionary power to assess the fulfillment of the criteria set out in the Banking Law It must demonstrate its grounds for having made a decision in the case of a refusal to grant a license.</p> <p>The NBB has a Licensing Memorandum, which proposes a two phase procedure for authorization as a credit institution incorporated in Belgium. The first phase is essentially a screening phase and is not obligatory but firms are encouraged to use both phases as it is likely to enhance the chances of a successful application. Similarly, candidates are encouraged to discuss possible applications with the NBB even prior to embarking on Phase one.</p> <p>The first phase is a consideration of the conceptual proposal. Details which must be included in this submission are listed in the memorandum. On the basis of its analysis, which will include consultation with any other supervisory authorities who may be relevant (for example if the credit institution were to be the subsidiary of another credit institution) the NBB advises the applicant on whether there are issues that have been identified that would stand in the way of a successful formal application or to invite the candidate to submit a detailed, formal application which is phase two of the process. The conditions and formalities that must be met in phase two are also set out in the memorandum.</p>

	<p>At the end of phase two, an accredited auditor or firm of auditors selected by the applicants in consultation with the NBB but paid for by the candidate is required to prepare a report to confirm that the conditions for obtaining an authorization have been satisfied and that an appropriate organization has been developed. Additionally, the NBB may perform its own on-site visits before making the final authorization decision.</p> <p>Provided the institution satisfies the conditions laid down in Articles 15 to 22 of the Banking Law the NBB will grant the authorization. When granting authorization, the NBB may, in the interest of sound and prudent management, impose certain conditions/limits on the exercise of certain of the activities proposed (Article 11 of the Banking Law).</p> <p>A false declaration or the concealment of relevant details may give rise to administrative sanctions against the enterprise or against the person or persons responsible for providing the details.</p>
EC5	The licensing authority determines that the proposed legal, managerial, operational and ownership structures of the bank and its wider group will not hinder effective supervision on both a solo and a consolidated basis.
Description and findings re EC5	<p>The Banking Law provides that, as part of the licensing criteria, the governance structure and organization of a credit institution must be appropriate to the activities and services proposed. Article 20 is the legal provision on which the NBB bases its governance policy for credit institutions (and for financial institutions in general). Section 7 of Article 20 provides that if the credit institution has close links with legal or natural persons these links must not be an impediment to the prudential supervision of the credit institution on an individual or solo basis.</p> <p>A credit institution's governance structure must be tailored to the nature, size, complexity and risk profile (Article 20 sections 1-2).</p> <p>A credit institution has to establish a governance structure at both solo and group level.</p> <p>Supervision of a firm's governance is based on a combination of legally binding minimum requirements as laid down in the Banking Law and further detailed supervisory guidance as laid down in circulars. In 2007, the former CBFA published a cross-sectoral so-called "Internal Governance Circular" (PPB-2007-6-CPB-CPA on the CBFA's prudential expectations on financial institutions' sound governance, March 2007). This Circular is still in force and expresses the supervisor's prudential expectations (based again on the principle of proportionality) for an institution's governance structure and organization.</p> <p>The credit institution must (under Article 20 and as elaborated in the Circular) submit a governance memorandum to the NBB and in the memorandum describe its governance structure including a discussion of the choices it has made. The NBB does not formally "approve" a governance memorandum, but gives its "nihil obstat," often combined with further recommendations to improve the governance structure and organization. The assessors were able to review several governance memorandum as well as a "scorecarding" assessment (see CP19) of governance within an institution.</p>
EC6	The licensing authority identifies and determines the suitability of major shareholders, including the ultimate beneficial owners, and others that may exert significant influence. It also assesses the transparency of the ownership structure and the sources of initial capital.

Description and findings re EC6	<p>Article 17 of the Banking Law requires the NBB to assess the suitability of direct and indirect (solo or jointly) qualifying shareholders of an institution upon authorization. Authorization shall be refused if the NBB has any reason to believe that the shareholders are not able to offer guarantees with regard to the sound and prudent management of the credit institution.</p> <p>The NBB checks the ultimate beneficial owners as well as the sources of initial capital.</p>
EC7	A minimum initial capital amount is stipulated for all banks.
Description and findings re EC7	Articles 16 and 23 specify a minimum level of capital of EUR6.2mn. Grandfathering of institutions with lower capital than the minimum threshold is permitted legally but no such institutions remain in Belgium.
EC8	The licensing authority, at authorization, evaluates proposed directors and senior management as to expertise and integrity (fit and proper test), and any potential for conflicts of interest. The fit and proper criteria include: (i) skills and experience in relevant financial operations commensurate with the intended activities of the bank; and (ii) no record of criminal activities or adverse regulatory judgments that make a person unfit to uphold important positions in a bank.
Description and findings re EC8	<p>The Banking Law provides that the NBB shall verify whether the persons in charge of the bank's "senior management" (<i>de facto</i> often the equivalent of "members of the management committee") are fit and proper and have the adequate experience to carry out their functions. The assessment of the qualities required, in particular as regards the necessary expertise and the adequate experience, are also applied to "persons taking part in the direction or management without participating in the senior management" (<i>de facto</i> the non-executive directors) (Article 18 of the Banking Law). Furthermore, the Banking Law (Article 19) states that the directors and managers of the credit institution must not have convictions or have been prohibited from carrying out their profession.</p> <p>Banks are required to notify the NBB in advance of any proposal for the appointment, renewal (or non-renewal) or dismissal of directors and senior managers in the institution's company officers; of any information and documents necessary to assess the qualities required of them; and, where applicable, of the distribution of tasks within the governing bodies (Article 26bis of the Banking Law).</p> <p>The Circular on the exercise of external functions by directors and managers (PPB-2006-13-CPB-CPA) provides a definition of senior management, which, broadly, includes the directors of a board and members of a management committee of a board (if this committee is established) and any persons who are identified by that management committee as senior management.</p> <p>The Circular also includes the concept of "Key staff," which is defined as any person, other than a senior manager, who fulfills a key function (secretary general, legal affairs, human resources, communication) or is in charge of independent control functions (such as internal audit, compliance and risk management). This group of individuals are currently not formally subject to fit and proper assessment but in practice are often informally screened. In particular the CFO or CRO of an institution would be subject to assessment if the CFO/CRO position does not fall within the definition of senior management for that bank.</p>

	<p>Conflicts of interests, their prevention and management, must be subject to an internal policy of the bank - see principle VIII of the Internal Governance Circular (see EC5 above).</p> <p>Individuals subject to fit and proper assessments must submit forms to the NBB at the initial appointment to their role and at any subsequent renewal of their mandate. The forms seek to identify information regarding experience and skill as well as integrity and reputation.</p> <ul style="list-style-type: none"> • Regarding experience and competence, required details include: education, professional experience in and outside the financial sector, reasons why previous professional posts have ended, the tasks and duties of the new position and so on. • Regarding integrity/reputation, required details include: any convictions and continuing inquiries that are relevant for supervisory purposes, previous prudential assessments, administrative and disciplinary sanctions and so on. <p>The assessment is intended as in-depth exercise of judgment and can involve extensive deliberations. At present an interview can be requested by the NBB and in the future interviews are likely to become standard practice for a limited group of persons i.e., members of the management committee, chairperson of the board and chairpersons of specialized committees within the board. It is proposed that these interviews will be held by the Governor or another member of the NBB's Board of Directors.</p> <p>The fit and proper regime at the NBB was under review at the time of the mission. The NBB had been giving considerable thought to revising the regulation and practices of assessing fit and proper for individuals in credit institutions including clarifying the understanding that individuals must meet such standards on a continuing basis and that the NBB might initiate more frequent checks in the future. A draft Circular had already been prepared for the Board to consider prior to an open consultation with the industry. The key changes in regulation and practice are likely to be:</p> <ul style="list-style-type: none"> • A widened scope of application of the fit and proper assessment to include persons responsible for independent control functions (i.e., risk management, internal control and compliance); • Confirming the obligation of the credit institution to inform the NBB of any material issue that might negatively affect the consideration of a person who is required to be 'fit and proper'. • More consistent use of interviews with senior NBB staff. <p>To prepare the new Circular, a major stock-taking exercise of all significant fit & proper during the last five years was undertaken, in addition to international standards and practices of some other jurisdictions to obtain a deeper understanding of what is intended by "adequate competence & experience" (= "fit") and "good reputation" ("proper").</p> <p>In discussion with NBB staff it was clear that much reflection has been given to how skills might be assessed effectively and consistency and the challenges of establishing a view on integrity. The new approach would provide more structure to assess potentially difficult situations. The NBB emphasized that the primary responsibility for appointing suitable persons rests with the institution.</p>
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	<p>Internally the NBB has already undertaken some restructuring to create a centralized function that can systematise the assessment of fit and proper. The changes are intended to support enhanced efficiency, consistency and depth of analysis. The NBB Board of Directors must make the final decision on "fit and proper" and now receives advice from the central unit, which is supplemented by the advice of the relevant supervisory team for the institution in question. The dual approach is intended to apply a "four eyes" principle and also to ensure that firm specific expertise is used in cases where more detailed follow up may be necessary. In view of the likely broadening of the application of fit and proper testing, the increased efficiency of the centralized function will be valuable. The NBB is also revising the forms that individuals must complete.</p>
EC9	<p>The licensing authority reviews the proposed strategic and operating plans of the bank. This includes determining that an appropriate system of corporate governance, risk management and internal controls, including those related to the detection and prevention of criminal activities, as well as the oversight of proposed outsourced functions, will be in place. The operational structure is required to reflect the scope and degree of sophistication of the proposed activities of the bank</p>
Description and findings re EC9	<p>Pursuant to Article 8 of the Banking Law authorization is granted on the basis of the assessment of a business plan, which includes a description of the future activities of the institution and pro forma financial statements and projections.(See also EC10).</p> <p>As mentioned under EC5, governance arrangements are also scrutinized. Proportionality is key when setting up and supervising governance arrangements. The institution must always take into account its size, nature and complexity of its activities (see Article 20, section 1, second paragraph).</p> <p>Internal control functions (audit, risk management, compliance) must be part of the governance arrangements a bank must set up; the bank must describe them in its governance memorandum. (See also CP 17).</p> <p>Outsourcing arrangements must be in line with the guidelines set out in the "Outsourcing Circular" (PPB 2004/5).</p>
EC10	<p>The licensing authority reviews pro forma financial statements and projections for the proposed bank. This includes an assessment of the adequacy of the financial strength to support the proposed strategic plan as well as financial information on the principal shareholder of the bank.</p>
Description and findings re EC10	<p>As noted under EC9 above, Article 8 of the Banking Law requires that authorization is contingent upon a suitable business plan, which includes a description of the future activities, and pro forma financial statements and projections. The NBB requires pro forma data including projections and sensitivity analysis (covering 2-3 years) to assist its evaluation of whether the institution may be viable and have sufficient capital to support the proposed plan on a stand-alone basis. If that is not the case, the license will not be granted.</p> <p>The fit and proper character of main shareholders is also evaluated during the licensing process (and on an ongoing basis). This includes the ability of shareholders to support the bank if needed (see Article 24 of the Banking Law).</p> <p>The assessors discussed a case with NBB staff in which an authorization had been refused due to the funding arrangements and financial strength of a proposed shareholder.</p>

EC11	In the case of foreign banks establishing a branch or subsidiary, before issuing a license, the host supervisor establishes that no objection (or a statement of no objection) from the home supervisor has been received. For purposes of the licensing process, as well as ongoing supervision of cross-border banking operations in its country, the host supervisor assesses whether the home supervisor practices global consolidated supervision.
Description and findings re EC11	<p>During authorization, the NBB assesses whether the home country supervisor practices consolidated global supervision and ascertains whether approval (or no objection) from the home supervisor has been received. Adequate information exchange with the home supervisor is also required.</p> <p>The relevant (legal) provisions are:</p> <ul style="list-style-type: none"> ➤ <u>EU/EEA subsidiary</u>: Article 9, 2nd para of the Banking Law of 22 March 1993 ➤ <u>non-EU subsidiary</u>: page 4 of the Memorandum on the procurement of an authorization by a credit institution governed by Belgian law: reference to the principles laid down by the Basel Committee ('Minimum Standards for the Supervision of International Banking Groups and their Cross-border Establishments' – June 1992; and 'The Supervision of Cross-border Banking' – October 1996) ➤ <u>EU/EEA branch</u>: Article 65 of the Banking Law of 22 March 1993 ➤ <u>non-EU branch</u>: Article 79, §1, 1°, of the Banking Law of 22 March 1993 <p>Furthermore, regarding branches the NBB applies the CEBS (now EBA) Guidelines for Passport Notifications (17 December 2010). These Guidelines are currently under revision by EBA.</p>
EC12	If the licensing, or supervisory, authority determines that the license was based on false information, the license can be revoked.
Description and findings re EC12	False declaration or the concealment of relevant details can give rise to administrative and penal sanctions against the enterprise or against the person or persons responsible for providing the details. The NBB noted that in such circumstances close consideration would be given to whether direct revocation was the most appropriate course of action or whether one of the NBB's other remedial powers might be suitable. For example, in a situation where it were uncovered that the shareholder(s) was not fit and proper, the NBB might consider using powers under Article 25 of the Banking Law to divest the shareholder of its holding in the credit institution.
EC13	The board, collectively, must have a sound knowledge of each of the types of activities the bank intends to pursue and the associated risks.
Description and findings re EC13	Besides the "fitness" of individuals the NBB can also assess collective "fitness," i.e., whether the board as a whole possesses sufficient relevant knowledge and experience, and whether tasks within the board are appropriately divided. Such screening most often happens in the course of more general governance inspections. This collective aspect will be more explicitly expressed through the future fit and proper policy, but is already reflected in supervisory circulars. For example, at present, the Internal Governance Circular (paragraph 52), explains that the criteria envisaged by the supervisory authority for assessing the qualities required of non-executive directors will be applied both collectively and on an individual basis. The NBB discussed with the assessors the need for there to be a continuous assessment of the suitable composition of the board of the institution. This should not necessitate a full formal review every time a board appointment was made, but the NBB would always review the appointment. For example, failure to ensure a key skill

	was covered at the board would trigger follow up. It was noted that the composition of the board was primarily the responsibility of the institution. It was essential to ensure that the firms were undertaking their own assessment and not relying on supervisory scrutiny and approval, even though this was necessary and important function of the supervisors.
Additional criteria	
AC1	The assessment of the application includes the ability of the shareholder to supply additional financial support, if needed.
Description and findings re AC1	<p>The NBB may evaluate, on this basis of its assessment under Article 8 of the Banking Law whether the institution is viable and has sufficient capital to support the proposed plan on a stand-alone basis. If this is not the case, the license will not be granted. The ability of the shareholder to supply additional financial support is part of this evaluation.</p> <p>The fit and proper character of main shareholders is also evaluated during the licensing process (and on an ongoing basis). This includes the ability of shareholders to support the bank if needed (see article 24 of the Banking Law).</p> <p>As noted above in EC10 the assessors discussed a case with NBB staff in which an authorization had been refused due to the funding arrangements and financial strength of a proposed shareholder.</p>
AC2	The licensing or supervisory authority has policies and processes in place to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met.
Description and findings re AC2	There are no specific policies in respect of supervisory practice relating to a new credit institution. The intensity of the supervisory process will be assessed as part of the normal risk based supervisory planning cycle. The assessors discussed a case in which it had been decided that quarterly updates had to be provided to the Board in part to monitor progress in relation to a number of conditions that had been placed on the credit institution as a condition of its authorization.
Assessment of Principle 3	Compliant
Comments	The NBB are to be commended on their rational and thoughtful review of fit and proper policies and practices. Despite planned changes to the regulatory architecture of the EU (details of which were not confirmed at the time of the mission) it is hoped that the NBB will be able to institute further changes, following internal and external consultation, and benefit from a deeper and more meaningful (as well as consistent) approach in this field.
Principle 4	Transfer of significant ownership. The supervisor has the power to review and reject any proposals to transfer significant ownership or controlling interests held directly or indirectly in existing banks to other parties.
Essential criteria	
EC1	Laws or regulations contain clear definitions of "significant" ownership and "controlling interest."
Description and findings re EC1	<p>While the Banking Law does not itself contain definitions of "control," "participation," "parent company," or "subsidiary" but instead refers to other instruments, including the Royal Decree of 23 September 1993 and the Company Law Code in which these definitions may be found (Article 3, section 1, point 2 and Article 44).</p> <p>The definition of control is set out in the Company Law Code, articles 5 to 12. Moreover, the NBB extends its scrutiny of the concept of control to any entity, which exercises a dominant influence.</p>

	<p>For prudential purposes participation is presumed to exist in case of a direct or indirect holding of 20 percent.</p> <p>The Banking Law does define the term “qualified holding” (Article 3, section 1, point 3). A qualifying holding means a direct or indirect holding in an undertaking, which represents 10 percent or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of that undertaking. This is consistent with the definition of a qualifying holding under the European Capital Requirements Directive (CRD).</p>
EC2	<p>There are requirements to obtain supervisory approval or provide immediate notification of proposed changes that would result in a change in ownership, including beneficial ownership, or the exercise of voting rights over a particular threshold or change in controlling interest.</p>
Description and findings re EC2	<p>Any acquisition or disposal whereby the person or entity acquiring or disposing of crosses a notification threshold as defined by Article 24 of the Banking Law must notify the NBB in advance of the acquisition or disposal. The notification triggers a timetable set out in law during which the NBB must assess the proposal, which is a maximum of sixty days. The timetable is taken from the EU directive on mergers and acquisitions (Directive 2007/44/EC) and may not be extended due to the provisions of “maximum harmonization” of that directive although suspension of the timetable (to a maximum of thirty days) is permitted so that the institution can provide additional information.</p> <p>The notification thresholds (which trigger assessments by the NBB as required under the EU directives) are: 20, 30 or 50 percent of the voting rights or share capital. Furthermore, a proposed acquirer wishing to become the parent undertaking of the credit institution needs to inform the NBB in writing of its intention to acquire shares in accordance with Article 24. Notification obligations are also placed on the credit institution itself by virtue of Article 24 (section 8).</p> <p>Additionally, the Banking Law (Article 24, section 7) requires any person acquiring shares above a threshold of 5 percent of the voting rights to notify the NBB within 10 days of the acquisition. The same notification applies for a transfer of shares, which causes a shareholder to fall under the 5 percent threshold. Hence the NBB is able to maintain a fully accurate record of the shareholder structure of the credit institution and to conduct any necessary follow up and assessment.</p> <p>The assessment addresses both <i>direct</i> and <i>indirect</i> equity interests in credit institutions and <i>joint</i> equity interests. In addition the definition of control also includes the <i>de facto</i> control i.e., the (factual) power to exert a decisive influence over the designation of the majority of the management or over the orientation of the management.</p> <p>These legal requirements have been further elaborated in Circular CBFA_2009_32, which is addressed to credit institutions and clarifies that if the institution becomes aware of a potential change in ownership structure it must notify the NBB and Communication CBFA_2009_31 of 18 November 2009, which is addressed to proposed acquirers and shareholders.</p>

EC3	The supervisor has the power to reject any proposal for a change in significant ownership, including beneficial ownership, or controlling interest, or prevent the exercise of voting rights in respect of such investments, if they do not meet criteria comparable to those used for approving new banks.
Description and findings re EC3	The Banking Law grants the NBB powers (Article 24, section 3) to assess candidates who propose to acquire a qualifying holding. If the NBB has not made a decision by the end of the assessment period it shall be deemed not to have objected. However, the NBB can object to the proposal on the grounds of incomplete information. The Banking Law similarly grants the NBB the power of objection. In the event that the application is refused, an appropriate statement of the grounds for the decision may be made public at the request of the proposed purchaser.
EC4	The supervisor obtains from banks, through periodic reporting or on-site examinations, the names and holdings of all significant shareholders or those that exert controlling influence, including the identities of beneficial owners of shares being held by nominees, custodians and through vehicles which might be used to disguise ownership.
Description and findings re EC4	<p>The threshold of notification to the NBB for any changes in shareholding is 5 percent (Article 24, section 8 of the Banking Law). The notification must be made within 10 days of the change. Under the same legal provision, an institution must also provide an annual notification to the NBB of the shareholders who have directly or indirectly (and individually or collectively) have a qualifying holding. The annual submission must also cover acquisitions and disposals of shares that were not required to have been notified at the time of the transaction.</p> <p>A standard reporting format for this information is issued by the NBB a qualifying holding. The chairman of the board of directors of the institution must countersign the submission of information on shareholders (provision of false or incomplete information can result in penalty sanction).</p> <p>The NBB has recently informed firms that it is adopting a more vigorous “look through” approach in its assessment of shareholders. The NBB indicated that it would seek to look through corporate and trust structures.</p> <p>Additionally, the FSMA is responsible, as the market supervisor, for applying transparency requirements set out in the Law of 2 May 2007 (Title II) regarding the disclosure of major holdings issuers whose shares are listed in a regulated market. The law transposes the EU transparency directive.</p>
EC5	The supervisor has the power to take appropriate action to modify, reverse or otherwise address a change of control that has taken place without the necessary notification to or approval from the supervisor.
Description and findings re EC5	<p>In the event that the legal notification has not been made for a change of control, Article 24, section 6 of the Banking Law provides that that on submission of notification from the NBB, the President of the Commercial Court, can annul all or part of the decisions taken by the general assembly of shareholders (in accordance with Article 516, section 3 of the Companies Code).</p> <p>The NBB has not had any experience of this situation arising, however, if the NBB has reasonable grounds to consider that a person possessing a qualified holding could hamper the sound and prudent management of the credit institution, Article 25 of the Banking Law gives the NBB the right to impose certain measures, such as divesting the shareholder of his shares or suspending his voting rights.</p>

	In accordance with the Banking Law (Article 104, section 1), any person who deliberately omits to notify the NBB as required by Article 24 or ignores the objection of the NBB in this respect or the suspension of the voting rights as foreseen via Article 25, may be subject to criminal sanctions, although the NBB is not the authority that exercises these specific powers.
Additional criteria	
AC1	Laws and regulations provide, or the supervisor ensures, that banks must notify the supervisor as soon as they become aware of any material information , which may negatively affect the suitability of a major shareholder.
Description and findings re AC1	Primary legislation currently does not require a bank to inform the NBB if it would become aware of any material information , which may negatively affect the suitability of one of its major shareholders, namely with regard to (i) reputation; (ii) financial soundness; (iii) the bank's ability to meet its prudential requirements; and (iv) suspicion of money laundering or financing of terrorism.
Assessment of Principle 4	Compliant
Comments	The change of control of an authorized institution is largely governed by EU law, however not all elements of this principle are captured in EU directives. Broadly, however, the NBB's application of policies and procedures in this area are comprehensive and it is noticeable that there is an increasing focus on looking "upwards" through the shareholding and ownership structure above the institution. Nevertheless the authorities are urged to remedy the lack of legal obligation for a credit institution to notify its supervisory authority of a material adverse development that may negatively affect the suitability of a major shareholder. The assessors welcomed the authorities' indication that appropriate changes could be put in place on the occasion of the next Banking Law's modification , which was expected to be soon.
Principle 5	Major acquisitions. The supervisor has the power to review major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and confirming that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Essential criteria	
EC1	Laws or regulations clearly define what types and amounts (absolute and/or in relation to a bank's capital) of acquisitions and investments need prior supervisory approval.
Description and findings re EC1	<p>The legal framework in Belgium distinguishes between institutions, which are deemed to be systemically relevant and those which are not. In brief, there are clear thresholds and powers for the NBB to be pre-notified and approve acquisitions by systemic institutions. These are subject to some pre-notification and pre-approval requirements but the regime is more complex and is not complete.</p> <p>With respect to systemically relevant institutions:</p> <p>The NBB is obliged under the NBB Organic Law (Article 36/3, section 2) to determine, which institutions are systemically relevant. These institutions are, in turn, required to submit any strategic decision to the NBB for approval. The NBB must specify (and publish) , which decisions are to be deemed as strategic, though it should be noted that the legal provision itself states that strategic decisions should be understood to mean:</p>

	<p>“notably decisions to acquire or establish another institutions, to set up a joint venture established in another state, to conclude cooperation agreements or agreements on capital investment or acquisition of a branch of activity, merger or demerger”</p> <p>The Circular (CREFS_2010_01) provides the guidance forseen under the NBB Organic Law, and establishes that decisions , which have an impact exceeding the following thresholds shall be deemed systemic: of investment of at least10 percent of the total consolidated balance sheet or income and revenue or 5 percent of capital and reserves.</p> <p>For non-systemic institutions:</p> <p>Article 33bis of the Banking Law provides that any credit institution which plans to acquire or create a non-domestic subsidiary must provide advance notification to the NBB. The period of notice is not specified in the legislation.</p> <p>Further, Article 30 states that mergers or transfers of assets between domestic credit institutions or between credit institutions and financial institutions are subject to prior approval by the NBB. If the supervisory authority fails to act within a 3 month period its approval will be deemed to have been given.</p> <p>Additionally, there are certain limits in place on shareholdings and participations which would, de facto, impose some constraint on the nature and magnitude of possible acquisitions. Shareholding and participations held by credit institutions are regulated via Article 32 (in particular section 5) of the Banking Law , which defines the conditions and limits for such shareholdings and participations. Section 5 provided that no single shareholding may exceed 10 percent and that the total amount of all shareholdings may not exceed 35 percent of its own funds. A credit institution may never own qualifying holdings exceeding 15 percent of its own funds and the total amount of all shareholdings may never exceed 60 percent of these own funds. Article 32 also provides a trading book exemption so that shares in trading portfolios would not be regarded as an acquisition.</p>
EC2	Laws or regulations provide criteria by which to judge individual proposals.
Description and findings re EC2	<p>Article 30 of the Banking Law provides that the NBB can refuse authorization of merger or transfer of activities on the grounds of concerns relating to sound and prudent management in the case of mergers between credit institutions or the transfer of activities between credit institutions or credit institutions and other financial institutions.</p> <p>For the systemically relevant institutions there are broad criteria stated in the NBB Organic Law (Article 36/3, section 2), namely whether the proposals would “go against sound and prudent management of the system-relevant financial institution or are liable to have a significant effect on the stability of the financial system.”</p> <p>As touched on in EC1, mergers and acquisitions involving credit institutions and non-financial institutions do not require regulatory pre-approval (unless the credit institution in question was a systemic institution). However, once the NBB is aware of such an acquisition and were the authority to have concerns, the acquisition may be considered <i>ex post</i> by the NBB and assessed against the general conditions of the Banking Law (Article 20 which sets out minimum requirements for credit institutions).</p>

	Also as noted above (EC1), Article 32 of the Banking Law sets out the conditions and limits under which a credit institution may own shareholdings (directly or indirectly) in other undertakings, although these are restrictions on the credit institutions rather than criteria with which to judge the suitability of a specific proposal.
EC3	Consistent with licensing requirements, among the objective criteria that the supervisor uses is that any new acquisitions and investments do not expose the bank to undue risks or hinder effective supervision. The supervisor can prohibit banks from making major acquisitions / investments (including the establishment of foreign branches or subsidiaries) in countries with secrecy laws or other regulations prohibiting information flows deemed necessary for adequate consolidated supervision
Description and findings re EC3	<p>The extent to which the NBB has legal powers to prohibit major acquisitions or investments made by credit institutions is discussed under EC1 above.</p> <p>As discussed above (EC1) systemically relevant institutions must submit strategic decisions to the NBB and may be opposed if considered to have the potential to undermine the soundness of the institution or of financial stability in general.</p> <p>Further, and in respect of all credit institutions, Article 30 of the Banking Law provides that the NBB can refuse authorization of merger or transfer of activities on the grounds of concerns relating to sound and prudent management in the case of mergers between credit institutions or the transfer of activities between credit institutions or credit institutions and other financial institutions.</p> <p>The NBB can object to the establishment of a non-domestic branch of an institution under Article 34 of the Banking Law The grounds for objection include an adverse impact on the organization, financial position or supervision of the credit institution. When establishing a foreign subsidiary, the credit institution must pre-notify the NBB (pursuant to Article 33bis of the Banking Law). Pre-notification allows the NBB the opportunity to investigate whether the non-domestic subsidiary might have an adverse impact on the credit institution and the NBB enjoys wide powers, if necessary, to prevent a credit institution's activities. In deciding whether to invoke such powers, the NBB would consider whether the establishment of the non-domestic subsidiary was compatible with the requirements of Article 20, which sets out a range of organizational requirements. Finally, the "close links" requirement (Article 20, section 7 of the Banking Law) provides a further legal power to the NBB to object if the "close links" of the credit institution were to hinder the individual or consolidated supervision on the said institution.</p>
EC4	The supervisor determines that the bank has, from the outset, adequate financial and organizational resources to handle the acquisition/investment.
Description and findings re EC4	<p>On a legal basis, Article 30 of the Banking Law provides the NBB with the power to deny a merger or acquisition involving other financial institutions on grounds related to the sound and prudent management of a credit institution, (providing that the objection is made within three months of having been notified).</p> <p>The NBB can object to an acquisition or investment on the grounds set out in Article 20 of the Banking Law regarding organizational requirements for example if the establishment of foreign subsidiaries or branches would compromise a suitable management structure, administrative and accountancy organization, control and security measures with regard to electronic data-processing or internal control of the concerned credit institution.</p>

	The NBB confirmed that its Board undertakes scrutiny of financial and organizational arrangements when considering an acquisition or investment and discussed examples indicating how the global assessments of the proposals had been carried out.
EC5	Laws and regulations clearly define for which cases notification after the acquisition or investment is sufficient. Such cases should primarily refer to activities closely related to banking and the investment being small relative to the bank's capital.
Description and findings re EC5	<p>There are no formal ex-post notification requirements associated with acquisitions or investments. However, the governance memorandum which the institution must submit to the NBB on an annual basis would provide relevant information.</p> <p>The range of acquisitions or investments which are permitted but which are not subject to pre-notification or pre-approval is relatively limited given the following constraints:</p> <ul style="list-style-type: none"> • All acquisitions made by a systemically relevant institution are subject to pre-approval. • All mergers and transfers between credit institutions and either credit institutions or financial institutions are subject to pre-approval • Any acquisition or establishment of a non-domestic subsidiary is subject to pre-notification • Shareholdings that do not fall within the description of Article 32 are not permitted. <p>Therefore, and also as noted under EC2 above, mergers and acquisitions involving credit institutions and non-financial institutions do not require regulatory pre-approval, but limits and thresholds (as described in EC2) are in place. It should, though, be noted that when calculating these limits, shares issued by companies which are regarded as constituting a single risk are aggregated and considered as a single shareholding. Affiliated enterprises shall be regarded as constituting a single risk unless evidence to the contrary can be provided.</p>
EC6	The supervisor is aware of the risks that non-banking activities can pose to a banking group, and has the means to take action to mitigate those risks.
Description and findings re EC6	<p>The acquisition of an institution active in non-banking activities does not require prior approval from the NBB, although (as noted above) the Banking Law sets limits on the holding of shares and participations in non-financial institutions.</p> <p>The Organic Law (Article 36/3, section 2) places an obligation on SIFIs to notify the NBB of all its strategic decisions and empowers the NBB to object to such decisions should the NBB consider the strategy is inconsistent with sound and prudent policies or would jeopardize financial stability. Hence, the NBB has the requisite powers to mitigate risks posed by non-banking activities in SIFIs.</p> <p>Article 20 of the Banking Law provides the NBB with the grounds to object to acquisition or investment in non-banking activities if the establishment of foreign subsidiaries or branches were deemed likely to jeopardize the organizational soundness (e.g., risk management) of the credit institution.</p>
Additional criteria	
AC1	When a bank wishes to acquire a significant holding in a financial institution in another country, the supervisor should take into consideration the quality of supervision in that country and its own ability to exercise supervision on a consolidated basis.

Description and findings re AC1	Although there is no explicit law or regulation requiring this, the NBB confirmed that it would take the quality of supervision of a host jurisdiction into account when assessing a major acquisition. The NBB further indicated that its practice was to establish relationships and MoUs as necessary with relevant host jurisdictions to facilitate supervision (noting that the MoU itself could not be signed with a jurisdiction that was non-compliant with key elements such as professional secrecy requirements).
Assessment re Principle 5	Largely Compliant.
Comments	The requirements of this principle are met in relation to the systemically relevant institutions, largely due to the NBB's extensive powers to scrutinize and, if necessary, object to strategic decisions made by systemically relevant institutions. For the much smaller non-systemically relevant sector of the market, the principle is largely but not wholly met. The degree of non-compliance is not extensive and relates to the potential to undertake a major acquisition in a non-financial sector without either pre-notification or pre-approval requirements being in place. It is recognized that there are a range of mitigating factors already in place, including extensive powers of <i>ex poste</i> intervention by the NBB if deemed necessary, a baseline of reporting to the NBB provided by the governance memorandum and also the fact that there are clear limits placed on investments that may be made in non-financial sectors. Furthermore, a credit institution obtains its authorization on the basis of its program of operations, which in the case of a major acquisition in a non-financial sector could be considered to occur. While notification requirements are not imposed on firms, a departure from their approved program of operations is likely to promote disclosure of intention by the firm to the supervisor before the acquisition takes place. Nonetheless, it is recommended that at minimum pre-notification procedures are put in place. In the interests of completeness and over-arching regulatory clarity and transparency, it is recommended that the NBB be given powers of pre-approval for any acquisition or investment that exceeds a defined benchmark. The 5 percent threshold, which is a commonly used standard to denote significant shareholdings might be a suitable benchmark to consider.
Principle 6	Capital adequacy. Supervisors must set prudent and appropriate minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. At least for internationally active banks, these requirements must not be less than those established in the applicable Basel requirement.
Essential criteria	
EC1	Laws and regulations require all banks to calculate and consistently maintain a minimum capital adequacy ratio. Laws, regulations or the supervisor define the components of capital, ensuring that emphasis is given to those elements of capital available to absorb losses.

Description and findings re EC1	<p>Capital regulations follow standards set by the European CRD. NBB regulation, confirmed by a Royal Decree, both dated November 2011 and issued by force of Article 43 of the Banking Law, set out the own funds requirement for all credit institutions. The Banking Law states that the NBB “shall determine the following on monetary grounds, by means of a regulation and in accordance with the provisions of European Law: the standards on solvency, liquidity and concentration risks, and other restrictions to be adhered to by credit institutions or by categories of credit institutions.”</p> <p>Credit institutions are required to calculate minimum capital ratios using the Basel measurements and definitions with the minimum capital set at 4 percent Tier 1 and TC 8 percent. The NBB Regulation is the transposition under Belgian Law of the terms and requirements of the Basel 2 and Basel 2.5 framework, and the specific rules applicable in the EU (notably retention rules relating to securitization transactions).</p> <p>Currently the major bank Tier 1 capital ratios range between 11.5 percent and 20.6 percent for the larger systemically important banks as at March 2012. Within this group, capital ratios have a high composition of CET1 which has been gradually increasing, albeit with periods of severe stress from the crisis requiring state intervention and support. The quality of the capital base has been improving with a run off of Tier 2 instruments in anticipation of the implementation of Basel III.</p> <p>Capital floors are in place for banks accredited to use internal models for the calculation of regulatory capital at 80 percent of B1.</p> <p>The Regulation distinguishes between the different categories of capital – Tier 1 and Tier 2 as well as deductions. The definitions are consistent with those of the Basel Committee. Hybrid instruments within tier 1 are authorized up to 25 percent of Tier 1 with the possibility to exceed this limit (up to 33 percent) for mandatory convertible instruments. Tier 2 may not exceed the amount of Tier 1.</p> <p>All Tier 1 capital instruments included in the calculation of the regulatory capital base are subject to prior approval by the NBB. Capital redemptions (other than redemption at maturity date of Tier 2 dated instrument) are subject to prior approval of the NBB.</p> <p>The own funds regulation is applicable to all banks at any time on a solo and consolidated basis. Under the own funds regulation, banks are subject to 3 minimum capital rules: the first is the minimum TC requirement of 8 percent of risk weighted assets as per Basel as mentioned above. The second is a gearing ratio and the third is a coverage ratio measured against fixed assets.</p> <p>Under the NBB’s gearing ratio requirements, the minimum own funds (Tier 1 + Tier 2 minus regulatory deductions) must be higher than the following percentage of the liabilities:</p> <ul style="list-style-type: none"> - first slice; between 0 and 25.000.000 € of liabilities 6 percent - second slice; between 25.000.000 € and 125.000.000 € of liabilities; 4 percent - third slice; between 125.000.000 € and 250.000.000 € of liabilities; 3 percent - fourth slice; between 250.000.000 € and 1.250.000.000 € of liabilities; 2.5 percent - fifth slice; more than 1.250.000.000 of liabilities; 2 percent
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	<p>Under the coverage ratio, own funds (Tier 1 + Tier 2 - deductions) must be higher than fixed assets that are not already deducted from own funds.</p> <p>The own funds reporting requirements for credit institutions described in the Banking Law requires each credit institution to provide the NBB on a regular basis with a detailed and comprehensive calculation of its regulatory capital requirement in respect of its specific risk profile.</p> <p>Capital requirements cover credit, market and operational risk as Pillar 1 risks. The methodology to calculate risk weighted assets is consistent with the Basel 2 and Basel 2.5 framework. The NBB will consider besides the Pillar 1 risks also Pillar 2 risks as part of its annual SREP and assessment of banks' ICAAP.</p> <p>The NBB receives quarterly reports on capital adequacy as well as six monthly and annual accounts audited by the external auditor. Included in the annual accounts is the bank's analysis of its specific risk profile; inputs for such analysis are both quantitative and qualitative and are drawn from prudential reporting, external audit reports and assessments by NBB-inspectors. The result of the analysis is reflected in the RAS (Scorecarding tool) and is used to set, if necessary, additional capital requirements (Pillar 2 process) to individual banks.</p> <p>Prudential filters applied by the NBB include: unrealized gains and losses on AFS bonds portfolio are neutralized; unrealized gains on AFS equity portfolio are recognized in Tier 2 (unrealized losses are deducted from Tier 1); and Deferred tax assets are deducted when they exceed 10 percent of tier 1 (with the exception of DTA relating to unrealized losses on AFS bond portfolio that are neutralized).</p> <p>At present, the NBB-services are preparing a revision of the CAD-requirements in view of the new EU-proposals relating to the transposition of the Basel III framework.</p> <p>A feature of the Belgium banking sector that was problematic during the crisis involved the practice of banks granting credit to shareholders to subscribe to the capital of the bank where repayment of the loan depended on the proceeds the shareholder received from the capital instrument. The implication of this practice is the effective absorption capacity of capital.</p> <p>Article II.1 of the own funds regulation was amended in 2010 to clarify the requirements relating to the deduction of credits to shareholders. Article II.1 states that if the institution provides funding directly or indirectly to the shareholder to subscribe to acquire a capital instrument of the bank, the corresponding amount of capital is not recognized in equity. While capital will be deducted for instances of this practice after 31 December 2010, those capital instruments continue to be included and will commence being deducted from 1 January 2014 at a rate of 20 percent per year until fully deducted by 1 January 2018. The result being that at the time of the review, the amounts that had been accrued prior to December 2010 continued to be counted in the capital base of banks that are published.</p> <p>While the own funds regulation has been amended, at the time of the mission, these amounts are still being included in the published capital ratios for systemically important banks. This weakens the transparency of the true loss absorbency of capital.</p>
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	<p>While the investment is deducted when Pillar 2 capital ratios are assessed, published capital ratios are artificially inflated.</p> <p>Paragraph 49(i) of the Basel II capital framework states that “the key element of capital on which the main emphasis should be placed is equity capital and disclosed reserves. This key element of capital is the only element common to all countries' banking systems; it is wholly visible in the published accounts and is the basis on which most market judgments of capital adequacy are made; and it has a crucial bearing on profit margins and a bank's ability to compete. This emphasis on equity capital and disclosed reserves reflects the importance the Committee attaches to securing an appropriate quality, and the level, of the total capital resources maintained by major banks.”</p> <p>EC1 explicitly refers to the need for the regulations to emphasize those elements of capital that absorb losses. The NBB was clearly aware of this risk and had adjusted the risk assessment process when setting minimum capital adequacy ratios.</p>
EC2	<p>At least for internationally active bank, the definition of capital, the method of calculation and the ratio required are not lower than those established in the applicable Basel requirement.</p>
Description and findings re EC2	<p>The definition of capital, the method of calculation and required minimum ratios are the same for all credit institutions and are based on the European Capital Requirements Directive (CRD). The Basel II.5 requirements implemented in CRD3 are in effect in Europe and implemented in Belgium.</p> <p>In terms of Basel III, banks are implementing transition plans to comply with the definitions, and higher ratios.</p> <p>In calculating risk weighted assets, banks are authorized to use a standardized method or an internal model (IRB approach) with the prior approval of the NBB. Under the standardized approach, the risk weight is a function of the external rating of the counterparty. Under the internal approach the risk weight is a function of the internal rating of the counterparty and the loss given default. Banks may also use a model to estimate the loss given default.</p> <p>For market risk, banks may use a standardized or an internal model (VaR) to calculate risk weighted assets. Under the internal model approach, banks may estimate the capital requirements relating to the general and the specific market risk of their trading positions subject to the prior authorization of the NBB.</p> <p>For operational risk, banks have the option of using a basic indicator approach, the standardized approach or an internal model approach (AMA). Under the standardized approach the operational risk requirement is a percentage of the average revenues of the institution (the percentage is set in function of the activities). The use of the AMA approach is subject to the prior authorization of the NBB.</p> <p>Revaluation gains, when related to equities or real estates may be accounted as part of Tier 2. Tier 2 may not represent more than 100 percent of Tier 1. In terms of prudential filters, the main deductions are:</p>

	<ul style="list-style-type: none"> • own shares • intangible and goodwill • significant participation in financial and insurance companies • non significant participations in financial and insurance companies if the aggregate amount exceed 10 percent of own funds before deductions. Only the excess amount is deducted • significant participations in non financial companies exceeding 15 percent of own funds before deduction or, on aggregate basis, 60 percent of own funds before deductions. Only the excess amount is deducted. <p>The CRD allows countries to exercise some elements of national discretion in implementing Basel II. In addition, there are some differences between the CRD and Basel II requirements. There is one area relevant to Belgium where the CRD on risk weighting is lower than the applicable Basel rules such as for certain real estate and equity investments. For the definition of capital in Belgium, the issue relates to the deduction of participation in an insurance subsidiary. It is recognized that Basel II has some flexibility in the treatment of banks' investment in insurance companies. To avoid double counting the Basel rules text express a preference for deduction of the investment in investment subsidiaries from the capital of the bank, but does not require it. However, they indicate that, if the deduction is used, half should be from T1 and half from T2.</p> <p>As currently applied for major banking groups in Belgium, investments in insurance subsidiaries are deducted 100 percent from Total Capital rather than 50:50 from T1 and T2. The result is that T1 capital ratios can appear larger than it would be under Basel II if applied. The NBB own funds regulation (Art II.6) provides that at the end of 2012, the deduction of investments in insurance subsidiaries will be 50:50 from T1 and T2 in line with Basel II. Furthermore, the intention is to apply the deduction of participation in insurance companies pursuant to the Basel III framework in the future.</p>
EC3	The supervisor has the power to impose a specific capital charge and/or limits on all material risk exposures.
Description and findings re EC3	<p>Specific capital charges and limits may be imposed on the basis of Article 43 and 57 of the Banking Law. Under the organic law of the National Bank (see article 2-36/3, § 3), the NBB may impose to the Domestic SIFIs additional capital requirements or requirements relating to liquidity position and concentration risks in order to take into account their systemic importance.</p> <p>Allocation of capital is assessed under Pillar 2. Conclusions of this assessment are shared within the college of supervisors of each banking group (where applicable). The joint college of supervisors decide, on basis of the risk assessment of each supervisory authority, on the minimum capital that must be available at the level of each banks of a banking group. The joint college process for determining capital appeared to be a mature and effective process.</p> <p>Belgian banks are also subject to the own funds regulation on a solo basis. Meaning that each banks should have own funds that are available to cover its own risk weighted assets. For the solvency test on solo basis, the participations in consolidated subsidiaries are not deducted but subject to a risk weight of 400 percent.</p>

EC4	The required capital ratio reflects the risk profile of individual banks. Both on-balance sheet and off-balance sheet risks are included.
Description and findings re EC4	<p>The minimum capital ratios are calculated based on the Basel II methodology for Pillar 1 and cover credit, market and operational risks. The methodology takes into account the amount of the exposures and the risks of these exposures. All exposures (on and off balance, derivatives) are taken into account for the calculation of minimum capital requirements.</p> <p>The specific risk profile of the institution is assessed by the NBB and, on basis of this assessment, NBB sets capital add-ons above the minimum capital requirements in order to take into account the risks not captured by the minimum capital requirements (Pillar 2 approach). The main objective of the capital assessment by the NBB is to determine whether "an institution has sufficient capital/own funds, as well as an adequate policy/process on the matter, to face its current and future risks." An important feature of the capital assessment is that it is forward looking.</p>
EC5	Capital adequacy requirements take into account the conditions under which the banking system operates. Consequently, laws and regulations in a particular jurisdiction may set higher capital adequacy standards than the applicable Basel requirements.
Description and findings re EC5	<p>The NBB may set higher capital requirements on basis of its Pillar 2 assessment. The Pillar 2 assessment is a well defined process within the NBB's supervisory framework.</p> <p>All banks will be assessed through the risk scorecarding tool which is at the centre of the risk assessment process. The scorecard captures both quantitative and qualitative metrics across a range of categories. The scorecard will take into account both bank specific but also environmental factors into the assessment.</p> <p>In addition to the output from the risk scorecard, the supervisor will assess the ICAAP. The ICAAP assessment will potentially involve an offsite inspection or onsite review, an assessment of the Pillar 1 estimates from the bank (and economic capital numbers if available) and an evaluation of approaches to the calculation of Pillar 1 capital such as risk diversification, model risk etc. In addition to the ICAAP assessment, the results of stress testing are taken into consideration and so is the capital needs under the SREP. Interest rate risk in the banking book is a Pillar 2 risk. In general, the worse result of the three tests will be used as the capital add-on. Through this process, the capital decision takes into consideration a full range of risks.</p>
EC6	Laws or regulations clearly give the supervisor authority to take measures should a bank fall below the minimum capital ratio.

Description and findings re EC6	Article 43 s3 states that "If the Bank deems that a credit institution's policy on its own funds requirement is not appropriate to the institution's risk profile, it may, without prejudice to the provisions of Article 57, with regard to the goals mentioned in Article 1 of this Law, lay down requirements on solvency, liquidity, concentration risks and risk positions in addition to those mentioned in s1." Art 57 stipulates that "if the NBB finds that a credit institution is not operating in accordance with the provisions of this Law.....or does not have sufficient guarantees of its solvency.....it shall determine the deadline within which the situation must be rectified." The law gives the NBB broad powers to remedy if a bank falls below minimum capital ratios.
EC7	Where the supervisor permits banks to use internal assessments of risk as inputs to the calculation of regulatory capital, such assessments must adhere to rigorous qualifying standards and be subject to the approval of the supervisor. If banks do not continue to meet these qualifying standards on an ongoing basis, the supervisor may revoke its approval of the internal assessments.
Description and findings re EC7	<p>The use of internal models to calculate regulatory capital is subject to the prior approval of the NBB. The qualifying standards are defined in the own funds regulations and are in line with the Basel II and II.5 frameworks.</p> <p>The requirements are identical to those proposed by the Basel Committee. Each internal model must be approved formally by the NBB before using it for the capital calculations. With regard to internationally active banking groups, the decision to approve a model is made after consultation with relevant supervisors as was evidenced through the documentation (within the college of supervisors).</p> <p>The approval is only granted if the banks meet all the criteria of the regulation. These criteria relate to the use test, governance and risk management framework, independence of risk management and development of internal models, the adequacy of the rating system, the internal validation process, the documentation, the data collection, the conservatism of the different estimates. Belgium has 8 banks approved to use internal models for credit risk, 3 for operational risk and 4 banks approved for market risk. At the time of approving an internal model to calculate regulatory capital, the NBB will attach conditions to the approval to allow for periodic monitoring of the model and assess results of implementation.</p>
Additional criteria	
AC1	For non-internationally active banks, the definition of capital, the method of calculation and the capital required are broadly consistent with the principles of applicable Basel requirements relevant to internationally active banks.
Description and findings re AC1	There is no difference between the minimum capital requirements rules for internationally or non-internationally active banks. As discussed in EC2, the own funds regulation differs from Basel II in relation to the deduction of investments in insurance subsidiaries, however the NBB has taken steps to align regulations with BII and BIII.
AC2	For non-internationally active banks and their holding companies, capital adequacy ratios are calculated and applied in a manner generally consistent with the applicable Basel requirement, as set forth in the footnote to the Principle.

Description and findings re AC2	The own funds regulation is the same for internationally or non internationally Belgian banks.
AC3	The supervisor has the power to require banks to adopt a forward-looking approach to capital management and set capital levels in anticipation of possible events or changes in market conditions that could have an adverse effect.
Description and findings re AC3	The Banking Law of 22 March 1993 (article 43) requires the bank to assess the amount of capital necessary to cover the risk of losses on a forward looking manner and expressed in the ICAAP (detailed in title XII of the own funds regulation).
AC4	The supervisor requires adequate distribution of capital within different entities of the banking group according to the allocation of risks.
Description and findings re AC4	The minimum capital ratios are applied at a solo and consolidated basis and assessed by the SREP process.
AC5	The supervisor may require an individual bank or banking group to maintain capital above the minimum to ensure that individual banks or banking groups are operating with the appropriate level of capital.
Description and findings re AC5	The supervisor has the power to set minimum capital ratios at both the solo and consolidated basis.
Assessment re principle 6	Largely Compliant
Comments	<p>At the time of the assessment, the capital rules did not align with Basel II in respect of the treatment of investments in insurance subsidiaries. It is acknowledged that this aspect of the regulation will be remedied by 31 December 2012, however, at the time of the review the definition of capital did not strictly meet that of BII.</p> <p>An aspect of the Belgium banking sector that was problematic during the crisis involved the practice of banks granting credit to shareholders to subscribe to the capital of the bank where repayment of the loan depended on the proceeds the shareholder received from the capital instrument. The implication of this practice is that capital is not able to absorb losses and cannot be classified as 'paid up' as per the definition of capital. The other dimension of this issue is that published capital adequacy ratios of banks are artificially inflated which weakens the transparency of the true loss absorbency of capital.</p> <p>We acknowledge that the own funds regulation has been amended to address this issue with a transition period commencing 1 January 2014. At the time of the mission, the capital base included these amounts.</p>
Principle 7	Risk management process. Supervisors must be satisfied that banks and banking groups have in place a comprehensive risk management process (including Board and senior management oversight) to identify, evaluate, monitor and control or mitigate all material risks and to assess their overall capital adequacy in relation to their risk profile. These processes should be commensurate with the size and complexity of the institution.

EC1	Individual banks and banking groups are required to have in place comprehensive risk management policies and processes to identify, evaluate, monitor and control or mitigate material risks. The supervisor determines that these processes are adequate for the size and nature of the activities of the bank and the banking group and are periodically adjusted in the light of the changing risk profile of the bank or banking group and external market developments. If the supervisor determines that the risk management processes are inadequate, it has the power to require a bank or banking group to strengthen them.
Description and findings re EC1	<p>Art. 20 § 3 of the Banking Law describes the basic requirements for credit institutions to maintain an independent risk management function which applies on both a solo and consolidated level. Art 43 and 20 form the legal basis for risk management in the Banking Law. Details are provided through Regulation dated 5 June 2007 on the organizational requirement for institutions that provide investment services (more specifically articles 11 to 13 of this Regulation).</p> <p>While the Banking Law obliges credit institutions to have an independent risk management function, there is no comprehensive Circular devoted to risk management (e.g., on the role of the CRO, on how to set up the risk management function etc.). Risk management principles are instead contained within the Circulars for specific risk types such as credit risk, operational risk, market risk etc. and refer to the relevant Basel documents as minimum expectations.</p> <p>The NBB uses the EBA Internal governance guidelines (GL 44 dated September 2011) as a reference for its expectations regarding the overall risk management framework within the credit institution and, as part of that overall framework, for the independent “risk management function.” The European principles are aligned in large part with the BCBS “Principles for enhancing corporate governance,” October 2010. In line with all other governance requirements, the risk management function must be set up taking into account the size, nature and complexity of the activities of the bank and the banking group. The NBB is in the process of planning to revise its guidance regarding risk management in the Internal Governance Circular to further enhance the expectations of risk management.</p> <p>An important component of the governance of risk management for banks is the requirement to develop and approve an Internal Capital Adequacy Assessment Plan (ICAAP). The ICAAP assesses the risk profile of the bank to assess whether capital is sufficient to support the risk profile of the bank. The ICAAP is drafted by senior management and approved by the whole board.</p> <p>The Internal Governance Circular describes the NBB’s expectations that governance is central to the concept of risk management. The role of senior management to identify and assess all material risks and identify controls to mitigate risks is set out in the ICAAP and measured against the adequacy of capital. The NBB’s risk scorecard approach takes into account the ICAAP as a central input into the assessment.</p> <p>Taking the various Circulars together, the NBB articulates its expectations for banks to maintain a comprehensive risk management function for all material risks. An overarching document clarifying the NBB’s minimum expectations for risk management would be optimal and potentially enhance the level of consistency of risk management standards across the sector. The planned future work by the NBB on the Internal Governance Circular should enhance the existing regulatory requirements.</p>

	<p>A key component of this criterion is for the supervisor to have powers to require a bank and banking group to strengthen the risk management framework. In terms of the NBB's supervision, ideally the risk management framework would be regularly tested by the supervisor through onsite reviews, testing the design of policies, design of controls across the various group at each level (here lines of defense) i.e., business (line 1), independent risk management (line 2), and IA, EA, Board (line 3).</p> <p>The NBB arrives at its risk assessment through a variety of supervisory activities at its disposal, such as onsite inspections, discussions with the internal and external auditors and bank management etc. Frequent meetings with the full Board of directors (which includes executive and non-executive independent directors) is not a normal dimension of the risk assessment process and there is no minimum frequency of direct engagement with the full Board mandated by the supervisory framework.</p> <p>The supervision cycle does not mandate annual on-site inspections aligned with specific assessments of risk. While the NBB is actively engaged with the larger more systemic banks, the control environment will not necessarily be tested and assessed across the entire population of banks via an annual onsite review. In the absence of an onsite review performed by the NBB, reliance will be placed on the external auditors report of Internal Controls, which is performed annually.</p> <p>The external auditor's report does not give a positive assurance of the design and effectiveness of controls. It is based on a factual review of the self assessment performed by management, complete with documentation. The external auditors report will not necessarily identify whether a control is failing or whether there is a hidden build-up of risks. Nor will the report attest to the quality of risk management or extent of risk taking.</p> <p>The structure of bank supervision rests on four layers (concentric circles of supervision) beginning with internal control, then internal audit, the external accredited auditor and lastly the NBB. The external auditor layer creates some weakness if an onsite review by the NBB is not performed to test the effectiveness of controls: in order for the supervisor to be satisfied that banks and banking groups have in place comprehensive risk management to mitigate or control all material risks, the external auditor must be engaged to provide a positive opinion of the design and effectiveness of internal controls.</p> <p>Supervisors should also conduct meetings with bank Boards, at least on an annual frequency, to assess their understanding of the risks of the bank and that appropriate oversight is being discharged. This would significantly enhance the NBB's ability to make a comprehensive, accurate and timely risk assessment of a bank.</p>
EC2	The supervisor confirms that banks and banking groups have appropriate risk management strategies that have been approved by the board. The supervisor also confirms that the board ensures that policies and processes for risk-taking are developed, appropriate limits are established, and senior management takes steps necessary to monitor and control all material risks consistent with the approved strategies.
Description and findings re EC2	The Internal Governance Circular requires the Board of Directors to regularly assess and approve the financial institution's general policy and strategy guidelines, which will include risk management.

	<p>The Circular does not, however, require updates to previously approved policies to be resubmitted to the NBB. The policy framework will therefore be assessed on an exceptional basis by the supervisor. In the absence of an onsite activity, the supervisor would not be aware of the changes to the policy framework.</p> <p>One of the requirements for EC2 is for supervisors to confirm that banks and banking groups have risk management strategies that are approved by the Board. The supervisory framework does not have in place regular engagement with the Board that would determine whether risk management strategies are appropriate.</p> <p>The regulatory framework does not require risk management policies to be submitted to the supervisor on a specified cycle. Policies would be reviewed as part of an onsite for example, but in the absence of an onsite review, a desk review of policies is not a minimum feature of the supervisory cycle. Not all banks are subject to a minimum assessment of policies. The larger banks that are subject to more intense supervision will have policies reviewed and evaluated. However this activity is not performed across all banks.</p> <p>Ideally a requirement would be in place in the regulations requiring credit institutions to forward to the supervisor all salient policies on an annual basis that have been approved by the Board. The supervisor would then review the policies against better practice (peer benchmarked internally) and assessment against the understanding of the banking sector its risks and emerging issues.</p> <p>Through this reporting and review, the supervisor would also gain periodic assurances from the risk management function that controls are in place and working. The external auditors role would be certify this is the case via testing. Periodically the supervisor would complement with its own testing via a deep dive into certain high risk issues. While these practices might occur, it is not mandated by the Circular.</p> <p>EC2 specifically requires Board involvement and by inference Board accountability for the risk management policies and practices. Ideally, Board involvement would be tested via a Board paper review, review of minutes, and meeting with the Board, however, meeting with the Board of directors is not a feature of the supervisory framework for all banks. The role of the Board is fundamental in establishing an appropriate risk management function. Supervisor should regularly engage with the Board to assess how it is discharging its oversight responsibilities. Review of the governance of the Board seemed deficient in terms of regular minimum supervisory activities for all banks.</p> <p>The other supervisory activity which would enable supervisors to arrive at an assessment of Board involvement in the risk management framework is a review of Board minutes and reports. This activity was performed across a number of banks but was not mandatory prior the annual assessment of the risk scorecard. Without direct engagement with the Board and a review of Board minutes, an accurate and comprehensive assessment of the Board's involvement in the risk management framework is doubtful.</p>
EC3	<p>The supervisor determines that risk management strategies, policies, processes and limits are properly documented, reviewed and updated, communicated within the bank and banking group, and adhered to in practice. The supervisor determines that exceptions to established policies, processes and limits receive the prompt attention of and authorization by the appropriate level of management and the Board where necessary.</p>

Description and findings re EC3	<p>NBB regulations require governance arrangements and risk management to be documented, reviewed and updated through the governance memorandum of the bank. However the regulations do not require policies to be submitted to the NBB when reviewed or updated. The Board and senior management must approve the governance memorandum. The memorandum will be adjusted each time a significant change that impact the governance structure occurs. The NBB requires that this process take place at least annually, which is adequate.</p> <p>As discussed in EC1, the Internal Governance Circular articulates certain expectations of the risk management function, however, it does not immediately follow that the supervisor will perform a review of the policies and processes at a minimum frequency for all banks.</p> <p>A critical aspect of EC3 is for supervisors to be satisfied that policies are communicated within the banking group and adhered to in practice. Supervisory activity would need to test or obtain assurances that the policies are adhered to. Exception reporting is an important aspect of EC3. Supervisors endeavor to develop a level of comfort that policies and processes are in place that identify, monitor and report to Board exceptions to policy. One example of a useful of exception reporting for credit risk is loans approved outside of policy or number of overrides (i.e., scorecards). Reporting such as exceptions to policy and overrides helps to ensure Boards are kept aware of the degree to which policy is being adhered to i.e., risk appetite can change through the application of the policy without the policy changing.</p> <p>The self assessment by management will describe and test the control environment and set out remediation activities throughout the next year to address any deficiencies. External audit will then perform a review of the self assessment. The results of the self assessment and the external auditor's report will be submitted to the supervisor annually for all banks. In the absence of any other triggers from the ICAAP, quarterly analysis etc, this report will confirm the integrity of the control environment and risk management.</p>
EC4	<p>The supervisor determines that senior management and the board understand the nature and level of risk being taken by the bank and how this risk relates to adequate capital levels. The supervisor also determines that senior management ensure that the risk management policies and processes are appropriate in the light of the bank's risk profile and business plan and that they are implemented effectively. This includes a requirement that senior management regularly reviews and understand the implications (and limitations) of the risk management information that it receives. The same requirement applies to the board in relation to risk management information presented to it in a format suitable for board oversight.</p>
Description and findings re EC4	<p>One of the expectations of EC4 is that the supervisor arrives at an assessment of the Board's understanding of the nature and level of risk being taken by the bank and how this risk relates to adequate capital levels. Banks are required to prepare an ICAAP annually which the NBB will use in its risk assessment. The ICAAP is a central feature of the risk assessment process performed by the supervisor at least annually as an input into the risk scorecard. However, as part of this process, an assessment of the Board's involvement in the ICAAP is not necessarily performed across all banks. The ICAAP document is reviewed, but the Board is not challenged as to its involvement. Without regular contact with the Board, the assessment as to the Board's understanding of the risk profile and adequacy of capital relies on a review of the ICAAP document rather than the Board's understanding or extent of involvement in this process.</p>

	<p>Article XII.3 of NBB Regulation 15/11/2011 details the requirements associated with the ICAAP. Paragraph 9 specifically states that “The credit institution shall be in a position to provide complete information regarding its ICAAP to the NBB.” While it is clear that the regulations require banks to produce an ICAAP regularly, the regulations do not appear to require the ICAAP to be submitted to the NBB, although this is an expectation of the supervisors.</p> <p>For the larger banks the engagement with senior management will be much more frequent i.e., quarterly than for smaller banks. Engagement with the board however, is less frequent and for independent non-executive directors it was not clear that direct engagement was undertaken.</p>
EC5	The supervisor determines that the banks have an internal process for assessing their overall capital adequacy in relation to their risk profile, and reviews and evaluates bank’s internal capital adequacy assessments and strategies. The nature of the specific methodology used for this assessment will depend on the size, complexity and business strategy of a bank. Non-complex banks may opt for a more qualitative approach to capital planning.
Description and findings re EC5	<p>The basis for this criterion is outlined in the Banking Law Article 43 with a specific requirement for capital risk management are contained in several Circulars, including: NBB Regulation 15/11/2011, article XII.1.; Circular CBFA_2011_03 dated 27 January 2011, comments to Title XII.; and Circular PPB-2007-15-CPB-CPA, 18 December 2007, related to the prudential expectations on ICAAP. Lastly, CEBS guidelines on the Application of the Supervisory Review Process under Pillar 2, January 2006.</p> <p>Banks are required to submit the ICAAP on at least an annual basis. The NBB assesses the ICAAP as part of the SREP process for all banks on an annual basis. The ICAAP considers the risk profile of the bank in relation to the nature of business, size and complexity of its activities and considers whether capital is adequate.</p> <p>The capital setting process takes into account the ICAAP and the risk score which is a comprehensive assessment of the bank across all risk categories. While the ICAAP was demonstrated to be integral to the supervisor’s annual risk assessment of banks, it was not clear how the supervisor became satisfied that the ICAAP was integrated into the risk management and capital settings of the bank. While the ICAAP is required to be signed by senior management and the Board, this does not by itself ensure that the process is integrated into the risk management framework. To determine that the bank has an internal process for assessing overall capital adequacy in relation to the risk profile the supervisor would need to perform a number of activities which tests and evaluates the risk management framework as well as the capital planning and forecasting process.</p>
EC6	Where banks and banking groups use models to measure components of risk, the supervisor determines that banks perform periodic and independent validation and testing of the models and systems.
Description and findings re EC6	There is no minimum cycle for banks that are accredited to use internal models to demonstrate to the NBB a proper and independent validation. When models are approved, typically the NBB will apply conditions of approval. The terms and conditions will typically include the requirement to submit data relating to performance and monitoring over a defined period. The ongoing submission of data, however, is not mandated over the life of the model. Nor will the terms and conditions necessarily require notification if model validation is not completed as per plan or results fail to meet acceptable standards.

	Typically the NBB will perform a comprehensive review of a bank's suite of models via alternative triggers such as a request to introduce a new model. The quantitative models team regularly engages with the industry and will in practice engage with accredited banks regularly. Nonetheless, there is no requirement for an internal model user to advise the NBB if the model's discriminatory ability degrades below a certain level.
EC7	
Description and findings re EC7	<p>Banking Law of 22 March 1993, Article 20 sets out the general requirements related to the safe and sound organization and adequate internal control of credit institutions. NBB Regulation 15/11/2011, article XII.3 related to the ICAAP. Circular PPB-2007-1-CPB, 8 February 2007, updated 27 January 2011, comments to article XII.3. Circular NBB_2011_09 dated 20 December 2011 on the governance of credit institutions.</p> <p>The bank's ICAAP is an important supervisory tool required of all banks to assess the risk profile and capital adequacy on an annual basis. The NBB will perform an assessment on the ICAAP to assess risks.</p>
EC8	The supervisor determines that banks have policies and processes in place to ensure that new products and major risk management initiatives are approved by the board or a specific committee of the board.
Description and findings re EC8	<p>NBB's Circular regarding Internal Governance develops a governance framework for activities which might change the risk profile of the bank such as the introduction of complex structures and/or offshore activities. The Circular states "Launching activities in foreign jurisdictions and/or setting up or selling new complex structures should be subject to a process of internal approval involving the compliance function and/or actuarial function. Internal control on these activities is in proportion with their importance and the associated risks."</p> <p>In these circumstances, the independent control functions of the financial institution and the statutory auditor should have unlimited access to the information and structures, as required by their respective tasks. The auditor should be kept informed of any significant development in the relevant activities.</p>
EC9	The supervisor determines that banks and banking groups have risk evaluation, monitoring and control or mitigation functions with duties clearly segregated from risk-taking functions in the bank, and which report on risk exposures directly to senior management and the board.
Description and findings re EC9	<p>The relevant regulation is the Internal Controls Circular, which sets out certain minimum expectations for the independent risk management function and the way it should be organized. The RCF should be an institution's central organizational feature, structured so it can implement risk policies and control the risk management framework. Large, complex and sophisticated institutions may consider establishing dedicated RCFs for each material business line. However, there should be in the institution a central RCF (including where appropriate a Group RCF in the parent company of a group) to deliver a holistic view on all the risks.</p> <p>The NBB rules require the RCF to be independent of the business and support units whose risks it controls but not be isolated from them. It should possess sufficient knowledge on risk management techniques and procedures and on markets and products. Interaction between the operational functions and the RCF should facilitate the objective that all the institution's staff bears responsibility for managing risk.</p>

	The Internal Governance Circular also contains some general principles regarding the concept of "independent" control function. However, what is not specified in the regulations is for the requirement that risk exposures are reported directly to senior management and to the Board. The most clear example of this relates to the credit risk framework, which does not require exposures over a certain percentage of own funds to be approved by the Board. Equally, the Circular does not require exceptions to policy to be reported to senior management or the Board.
EC10	The supervisor issues standards related to, in particular, credit risk, market risk, liquidity risk, interest rate risk in the banking book and operational risk.
Description and findings re EC10	The supervisor has issued specific guidance in relation to credit, market, liquidity, interest rate risk and operational risk. In these cases the NBB has used explicit reference to the relevant Basel documents to express its minimum expectations.
Additional criteria	
AC1	The supervisor requires larger and more complex banks to have a dedicated unit(s) responsible for risk evaluation, monitoring and control or mitigation for material risk areas. The supervisor confirms that this unit (these units) is (are) subject to periodic review by the internal audit function.
Description and findings re AC1	The expectations of the NBB in respect of systemic and larger banks to have dedicated risk management units are established in the application of the proportionality rules which set that higher standards for complex banks presenting higher risk appetites and risk profiles.
AC2	The supervisor requires banks to conduct rigorous, forward-looking testing that identifies possible events or changes in market conditions that could adversely impact on the bank.
Description and findings re AC2	<p>NBB expects institutions to develop, in the course of their ICAAP, rigorous capital planning and stress testing exercises.</p> <p>NBB expects institutions to develop a sound, comprehensive and rigorous stress testing framework that should encompass all the material risks (both on- and off balance sheet) relevant for the banking group and should be based on a "building block" approach.</p> <p>Such approach will require adequate and sound stress testing governance structures implying actual, reviewed and efficient use of the stress tests programs and results; the use of a range of methodologies undertaking both simple sensitivity analyses and more complex scenario stress testing with a range of severity; a multi-layered approach to stress testing programmes, from simple portfolio-level to comprehensive firm-wide scenario analyses; actual and adequate interactions/implications between the outcomes of stress tests and management intervention/mitigating actions; and finally, the use of rigorous stress tests to assess the viability of the institution's capital plan in adverse circumstances in the context of ICAAP. To develop adequate stress testing framework institutions must follow the 17 principles included in the CEBS's Guidelines on stress testing.</p>
AC3	The supervisor requires banks and banking groups to have in place appropriate policies and processes for assessing other material risks not directly addressed in the subsequent CPs, such as reputational and strategic risks.
Description and findings re AC3	NBB expects institutions to take account of all material risks, including business, strategic and reputation risks, in the course of their ICAAP exercise. If not satisfied with the scope defined by institutions, NBB is empowered to take the necessary remedial actions, including the definition of additional capital requirements.

Assessment of Principle 7	Largely Compliant
Comments	<p>Many of the criteria in CP7 require the supervisor to assess the Board's involvement in the risk management function. Indeed, the Principle focuses on Board oversight of risk management policies and processes. While the regulations require Boards to approve risk management strategies and the ICAAP, the supervisory assessment of the Board's involvement and understanding of risks and risk management will not necessarily involve direct engagement with the Board (independent non-executive directors), even for larger systemic banks on at least an annual frequency. Without direct engagement with the Board to challenge their appreciation of the risks, the implementation of risk management and adequacy of capital, it is difficult to see how the supervisor is able to arrive at an accurate, timely and comprehensive view of the Board's oversight of risk management.</p> <p>Annual meetings with the Board would assist the supervisor to make accurate, timely and comprehensive assessments of the Boards' involvement in the risk management framework as an input in the annual risk assessment process.</p> <p>The documentation requirements for the internal governance memorandum, the ICAAP reporting and the internal control statement could be made more explicit/ better aligned to ensure that all material Board approved policies are submitted to the NBB on at least an annual basis.</p> <p>The Internal Governance Circular should require notification to the NBB if an accredited model fails annual validation with a remediation plan.</p>
Principle 8	Credit risk. Supervisors must be satisfied that banks have a credit risk management process that takes into account the risk profile of the institution, with prudent policies and processes to identify, measure, monitor and control credit risk (including counterparty risk). This would include the granting of loans and making of investments, the evaluation of the quality of such loans and investments, and the ongoing management of the loan and investment portfolios.
Essential criteria	
EC1	The supervisor determines, and periodically confirms, that a bank's Board approves, and periodically reviews, the credit risk management strategy and significant policies and processes for assuming, identifying, measuring, controlling and reporting on credit risk (including counterparty risk). The supervisor also determines, and periodically confirms, that senior management implements the credit risk strategy approved by the Board and develops the aforementioned policies and processes.
Description and findings re EC1	<p>The Banking Law does not make specific reference to credit risk management. The Banking Law does, however, refer more generally to risk management (Art 20). The NBB issued a Circular NBB_2011_09 of 20 December 2011 on internal control which references the Basel Document "Principles of Credit Risk Management" of 2000 as a standard for banks in assessing the adequate organization of their credit risk functions.</p> <p>To satisfy the requirements described in this criterion the NBB relies upon the Basel principles. The NBB will assess compliance with the principles through three main activities:</p> <ol style="list-style-type: none"> 1. On site examinations. Onsite inspections will assess all aspects of the credit risk process, as set out in the inspection manual. Aside from inspections relating to credit risk activities, onsite inspections validate internal model on credit risk focus,

	<p>not only on the statistical methodology, but also on the quality of the credit risk management and organization.</p> <p>2. Report of the management on internal control; The Circular letter NBB_2011_09 of 20 December 2011 on internal control requires the bank management to assess the internal control, including with regard to the credit activities, and report the conclusions to the NBB.</p> <p>3. Reports of accredited auditors: accredited auditors are required, as part of their duties, to maintain a permanent information file with the NBB giving a description and a critical assessment of the organization and internal control of banks with which they have mandate. Credit risk is a key focus of these files. The supervisors regularly assess the quality of these files.</p> <p>The result of the assessment is summarized in the scorecard relating to credit risk. The offsite analysis based on quarterly data submitted by all banks on a solo and consolidated basis forms the foundation for credit risk assessment by the supervisor.</p> <p>There was evidence of detailed horizontal analysis , which had been performed on specific thematic issues such as mortgage portfolios, sovereign credit risk etc. The analysis was of high quality.</p> <p>If an onsite review is warranted, inspections will assess all aspects of the credit risk management process. For banks accredited to use internal models, a separate Circular applies to the bank and a more extensive onsite assessment will be involved.</p> <p>The Circular for credit risk does not require credit risk policies to be submitted to NBB when reviewed and approved by the board or in the event that material changes are made such as in the instance of limits and delegations. Changes in policy often flag a change in underwriting approach and potentially a change in risk appetite. The NBB does, however, have other mechanisms by which it can detect material changes in policies.</p> <p>The assessment of an appropriate credit risk management policy framework for all significant areas will be a component of an onsite credit risk visit and will also test whether the bank effectively implements these policies. Where an onsite review is not performed within an annual period of updating the risk scorecard, the supervisor will rely upon other sources of information such as engagement with internal and external audit, and the internal control report.</p> <p>Since the publication of the Basel document, there have been updates to credit risk management such as in the important area of stress testing, which have not been updated in the NBB's Circular on credit risk. Overall, the regulatory framework appears consistent with this criterion.</p>
EC2	<p>The supervisor requires, and periodically confirms, that such policies and processes establish an appropriate and properly controlled credit risk environment, including:</p> <ul style="list-style-type: none"> • a well documented strategy and sound policies and processes for assuming credit risk; • well defined criteria and policies and processes for approving new exposures as well as renewing and refinancing existing exposures, identifying the appropriate

	<p>approval authority for the size and complexity of the exposures;</p> <ul style="list-style-type: none"> • effective credit administration policies and processes, including continued analysis of a borrower's ability and willingness to repay under the terms of the debt, monitoring of documentation, legal covenants, contractual requirements and collateral, and a classification system that is consistent with the nature, size and complexity of the bank's activities or, at the least, with the asset grading system prescribed by the supervisor; • comprehensive policies and processes for reporting exposures on an ongoing basis; • comprehensive policies and processes for identifying problem assets; and • prudent lending controls and limits, including policies and processes for monitoring exposures in relation to limits, approvals and exceptions to limits.
Description and findings re EC2	<p>This criterion expects the supervisor to perform two types of activities: the first is a regular review of policies. This activity will cover the requirements for banks to have credit risk management strategies, sound policies that cover all aspects of credit risk including problem assets. The regulations, which are based on the Basel principles, do not require banks to submit policies on a minimum cycle i.e., annually. Policies will be reviewed as part of an onsite review or if triggered by an exception. Policies will also be reviewed by Internal Audit.</p> <p>Policies might also be reviewed through other supervisory activities such as horizontal analysis, however it is not mandated that the supervisor would review and assess credit risk policies and strategies prior to updating the scorecard. For the larger systemic banks, the NBB will be in constant contact with many sources of qualitative and quantitative information pertaining to credit risk.</p> <p>The second aspect of this criterion is for the supervisor to confirm that practices align with policy and are prudent. In practice, the minimum supervision cycle for onsite reviews will depend upon the result of the risk scorecard. While the criterion does not prescribe a specific timeframe, scorecards are updated on an annual cycle. For the larger systemic banks it was evidenced that annual reviews are performed that comprehensively cover this criterion. However, for the broader population of banks, the frequency of supervisory activities to assess whether credit practices aligned with policies was not mandated.</p>
EC3	The supervisor requires, and periodically confirms, that banks make credit decisions free of conflicts of interest and on an arm's length basis.
Description and findings re EC3	<p>This criterion requires that credit risk decisions are free of conflicts of interest and credit decisions are made on an arms' length basis. EC3 expects banks to have a policy framework that covers credit decisions across the organization. The supervisor should ensure policies are implemented and controls are in place that confirm policies are designed appropriately, implemented effectively, working as needed and no incidence of conflict. Article 28 of the Banking Law states that credit to a member of the Board or senior management shall be granted at arm's length (under the same considerations as credit to other customers).</p> <p>The NBB will obtain confirmation of compliance with the various regulations from a variety of sources: internal control report, external auditor, internal audit. Article 523 of the Company Law prohibits a member of the Board from participating in a decision when that member has a potential conflict of interest. This applies for credit applications from a shareholder or a Board member.</p> <p>Under the own funds regulation (see title II of own funds regulations), even if the credit is granted on arm's length basis, the credit amount will be deducted from own funds if the</p>

	<p>credit has been used to increase the own funds of the institution or if there's some doubt about the ability of the shareholder to redeem the credit.</p> <p>Pursuant to Article 28 of the Banking Law of 22 March 1993, a credit extended to a member of the board or senior management shall be granted at arm's length condition (same condition as credit granted to the customers).</p> <p>The weakness in the credit risk framework is in relation to the granting of credit to major shareholders to purchase own shares that would increase the own funds of the bank. These decisions are not subject to any particular oversight framework and with only guidance that they should be made under similar conditions to other customers. In practice, it would be difficult for the bank, or an officer of the bank, to refuse credit especially in an instance where the bank needed to raise capital. Furthermore, there is no requirement in the regulations for major credit risk exposures over a certain amount (or percentage of the bank's own funds), to be decided by the bank's senior management or Board. In effect, critical credit decisions could potentially be made by officers of the bank that are under the direction of senior management.</p> <p>This issue has clearly been problematic for the Belgium financial sector in the recent past. We see evidence that the NBB has taken sound measures to account for situations where the bank grants credit to a major shareholder (or to the member of the Board) to increase own funds by deducting the amount from own funds calculation in Pillar 2. Nonetheless, the lack of a clear prohibition in the regulation leaves open the potential for conflicts of interest to occur in the future.</p> <p>It was not evident whether the degree of encumbrance of the share registries across the entire sector had been performed to identify pockets of potential risk.</p>
EC4	The supervisor has full access to information in the credit and investment portfolios and to the bank officers involved in assuming, managing, controlling and reporting on credit risk.
Description and findings re EC4	NBB has full access to all information of a credit nature as per Article 46 of the Banking Law that states "NBB may, for the purpose of the prudential supervision do the following: 1. Require all information relating to the organization, the function, the situation and the operations of a credit institution; 2. Carry out onsite examination; 3. Have access to all documents and information.
Additional criteria	
AC1	The supervisor requires that the credit policy prescribes that major credit risk exposures exceeding a certain amount or percentage of the bank's capital are to be decided by the bank's senior management. The same applies to credit risk exposures that are especially risky or otherwise not in line with the mainstream of the bank's activities.
Description and findings re AC1	There is no specific provision in the law/regulation, which requires a bank to have an approval by the senior management if a credit exposure exceeds a certain amount or risk. Each bank is required to define the credit policy including the delegation of powers with regard to credit granting, which should take into account the size and the risk of credit exposures.

	So while credit institutions are required to define their credit risk policy, there is no mandatory delegation hierarchy where loans over a certain amount or percentage of own funds would only be approved by senior management or the Board.
AC2	The supervisor determines that banks have in place policies and processes to identify, measure, monitor and control counterparty credit risk exposure, including potential future exposure sufficient to capture the material risks inherent in individual products or transactions. These processes should be commensurate with the size or complexity of the individual bank.
Description and findings re AC2	These requirements are part of the Basel principles , which is the standard used by the NBB. Assessments of compliance with these requirements are made through on-site inspections, report of the bank management on internal control and reports of the accredited auditors.
AC3	The supervisor determines that banks have policies and processes to monitor the total indebtedness of entities to which they extend credit.
Description and findings re AC3	<p>This requirement is covered adequately by the NBB's existing regulations , which rely upon the Basel principles. Compliance with these requirements is assessed through on-site inspections, report of the bank management on internal control and reports of the Accredited auditors.</p> <p>The result of the assessment is summarized in the scorecard relating to credit risk. The NBB sets minimum requirements obliging the bank to monitor the credit quality of the entities to which they extend credit and so on, to review the internal rating of the counterparty is a minimum requirements as part of its authorization of a bank to use an internal model for credit risk to calculate the minimum solvency requirements. Compliance with this requirement is assessed also during the validation process of IRB Models.</p>
Assessment of Principle 8	Largely Compliant
Comments	<p>There is no requirement in the regulations for major credit risk exposures over a certain amount or percentage of the bank's own funds, to be decided by the bank's senior management or board.</p> <p>Without this requirement, critical credit decisions can in practical terms be made by officers of the bank who might not be suitably informed of all risks. An effective delegation structure will strengthen the risk management framework to ensure that credit decisions are only taken at an appropriate level. This will also help to avoid unnecessary conflicts of interest, which might arise in relation to the granting of credit. While a conflicts of interest policy is required by the regulations, it might prove inadequate at fully mitigating this risk.</p>
Principle 9	Supervisors must be satisfied that banks establish and adhere to adequate policies and processes for managing problem assets and evaluating the adequacy of provisions and reserves.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to formulate specific policies and processes for identifying and managing problem assets. In addition, laws, regulations or the supervisor require periodic review by banks of their problem assets (at an individual level or at a portfolio level for credits with homogenous characteristics) and asset classification, provisioning and write-offs.

Description and findings re EC1	<p>The regulatory framework governing problem assets, provisions and reserves consists of two layers. First, the accounting framework contains requirements governing the valuation and presentation of assets and liabilities in both general purpose financial statements and in prudential returns. Second, prudential regulation contains additional provisions on the management of credit risk and the solvency treatment of problem assets, provisions and reserves.</p> <p>Accounting standards govern the preparation and presentation of general purpose, publicly disclosed financial statements by banks. The prudential framework refers to the standards in the accounting law and makes them applicable to the preparation and presentation of the prudential information that banks must report on a regular basis to the NBB for solvency purposes. As such, the capital adequacy requirements (in particular for credit risk) are predicated on the values attributed to loans in the accounts of the banks and therefore depends on the accounting classification and provisioning as applied to the loans pursuant to the accounting standards.</p> <p>The accounting framework in Belgium consists of two regimes, BGAAP for banks prepared on a solo basis and IFRS for consolidated accounts.</p> <p>The RD covering BGAAP articulates a general standard and definition for banks to identify impaired loans, distinguishing two degrees of problem assets: “loans with uncertain outcome” and “doubtful loans” (article 35 of the RD). Further distinctions are made depending on the nature of the problems (commercial credit risk and country-related risk). This RD implements the European Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions.</p> <p>A loan classified as doubtful will require an individual (specific) provision in the expectation that full payment of the outstanding principal and interest will not be paid. A loan classified as uncertain will be assigned a general provision for the part that is uncertain. Under the “uncertain outcome” category – as this category is defined in a principle-based way,, there are in practice different subcategories used by banks for internal monitoring and assessment, such as: uncertain still performing; uncertain but 90 days past due; doubtful but recourse guaranteed; or incurred but not reported. It is noted that for prudential purposes (art. VI.87 of the NBB regulation on own fund of 15/11/2011), an exposure is “defaulted” when past-due for more than 90 days and/or it is probable that the debtor will not meet all its commitment (except under special measures such as resorting to guarantees). An exposure that is classified as “uncertain” or “doubtful” in the BGAAP financial statements shall be considered as “defaulted” for prudential purposes (see comments on article VI.87 in the circular letter).</p> <p>Pursuant to Royal Decree of 23 September 1992, the consolidated accounts of credit institution must be prepared in accordance with IFRS. The application of IFRS at consolidated level is, for banks and investment firms, mandatory since 2006. Under IFRS, identification and treatment of problem assets, provision and reserves is governed by IAS39 (Financial Instruments: recognition and measurement) and, for assets other than financial instruments, IAS36 (Impairment of assets).</p> <p>Review of loan classification is one of the central tasks performed by the external auditor, as part of the financial audit which is performed half yearly and annually—the annual audit consisting of a positive assurance.</p>
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	<p>All banks have to report provisioning data as part of the quarterly prudential returns requirements (Schema A, tables 50.10 to 50.15). Detail has to be provided for the gross outstanding amounts, available credit lines and guarantees and collateral.</p> <p>The credit risk management framework requires banks to maintain adequate policies and processes for the oversight and collection of past due or otherwise doubtful loans. In practice banks have to determine policies and procedures regarding provisions and write-offs separately for loans "with uncertain outcome" and for those with "high probability of incomplete recovery." The assessment of the appropriateness of such policies is part of the accredited external auditor.</p> <p>The NBB is empowered to require institutions to:</p> <ul style="list-style-type: none"> - Strengthen their credit policies and procedures; - Provide for additional provisioning if the level thereof is deemed unsatisfactory; if such requirement is not respected, the NBB may impose a capital add on under the Pillar 2 process or a deduction from regulatory own funds for the calculation of the solvency ratio. <p>The accounting provides the basis for banks to formulate policies and processes for problem assets. The governance regulations require policies to be reviewed on an annual basis.</p>
EC2	The supervisor confirms the adequacy of the classification and provisioning policies and processes of a bank and their implementation; the reviews supporting this opinion may be conducted by external experts.
Description and findings re EC2	<p>The external auditor is charged with confirming the adequacy of the classification of provisioning policies and processes, unless an onsite review is performed or other exceptional circumstances.</p> <p>The auditor performs a financial audit and will test whether provisioning aligns with the definitions in the accounting standards. Review of loan classifications is one of the central tasks entrusted to the external auditor of banks, who has to give an opinion on the correctness of loan classification and provisioning in terms of the financial audit on an annual basis. A limited review will be performed semi-annually. The auditor also confirms the reliability of prudential returns. The external auditor is specially accredited by the NBB.</p> <p>Under BGAAP, article 27bis of the RD of 23 November 1992 specifies the methodology to be used for recognizing interest on some specific assets (e.g., zero coupon bonds, perpetual or loans with fixed constant payments). Interest on financial assets that are part of the banking book is recognized on the basis of the effective interest rate methodology (article 35ter, §4 of the RD). Otherwise, accrued but not collected interest can be recognized in P&L and interest is normally not added to principal.</p> <p>As mentioned above, BGAAP distinguishes two degrees of problem assets: "loans with uncertain outcome" and "doubtful loans" (article 35 of the RD). Further distinctions are made depending on the nature of the problems (commercial credit risk and country-related risk).</p> <p>At consolidated level (where IFRS apply), IFRS7 (Financial Instruments: Disclosures) requires entities to disclose additional information on their financial assets that are either past due</p>

	<p>or impaired (IFRS7, paragraph 37). Based on this disclosure requirement, the prudential financial reporting FINREP requires credit institutions to report detailed information on their past due assets (template 10 of FINREP) to the NBB.).</p> <p>Under the prudential framework, defaulted loans receive a specific treatment (notably a higher risk weight in the standardized approach and a probability of default of 100 percent in the IRB model approach). Defaulted loans include "non performing loan (= past due loans from more 90 days), loans that have been restructured with a loss for the bank, and loans that are likely to default in the near future.</p> <p>As both BGAAP and IFRS are principle-based accounting standards, they do not require the recognition of minimum amounts of provisions.</p> <p>The classification of loans and valuation practices and the controls that are around these two practices have a material impact on the level and adequacy of provisioning. Both of these practices are principally confirmed by the external auditor. The extent of analysis by the NBB in these two areas is not established within the supervisory framework on a minimum supervision cycle. Clearly when performing an onsite review the classification of loans will be included in the inspection. However the cycle for an onsite credit review for all banks is not explicitly tied to a risk score or minimum cycle.</p> <p>For the larger systemic banks, more scrutiny is in practice paid to this process, and receives greater attention from onsite credit risks visits, periodic contact with the external auditor, onsite reviews of controls and meetings with senior compliance officers and independent risk management.</p> <p>There were clear examples where banks' provisioning policies and the effective implementation of policies had been assessed as part of horizontal analysis. When the problem became acute in 2011, the Bank reviewed the position of the most exposed banks and issued recommendations on minimum provisioning for those debt instruments.</p>
EC3	The system for classification and provisioning takes into account off-balance sheet exposures.
Description and findings re EC3	<p>At solo level, Article 35, §1 of the RD of 23 September 1992 requires banks to monitor, and when necessary provision off-balance sheet exposures. Pursuant to this provision, account must be taken of the risk that the counterparty does not meet its contractual commitments.</p> <p>Article 35 allows banks to determine the impairment amount item by item or at portfolio level (based on statistical information collected by the bank and taking account of the economic conditions and the bank's policy in respect of such items). Article 35 also specifies the classification applicable to off balance sheet items depending on whether the risk attached thereto is "doubtful" or "with uncertain outcome." Further distinctions are made depending on the nature of the problems (commercial credit risk and country-related risk).</p> <p>At consolidated level, under IFRS most if not all exposures will be reflected on balance sheet. Either as a specific asset (financial instrument, insurance contract, lease contract...) and, in this respect, will be subject to the impairment requirements applicable for that class of asset, or as a provision pursuant to IAS37 (Provisions, Contingent Liabilities and Contingent Assets). IAS37 requires entities to recognize a provision when it has present obligation, which meets the condition of IAS37.14 (past event, probable outflow of resources embodying economic benefits and reliable estimate of the obligation). Pursuant</p>

	to IAS37.27 and seq. only contingent liabilities and contingent assets are not recognized on the balance sheet; these are disclosed in the notes to the accounts.
EC4	The supervisor determines that banks have appropriate policies and processes to ensure that provisions and write-offs reflect realistic repayment and recovery expectations.
Description and findings re EC 4	<p>Compliance with the accounting frameworks (BGAAP or IFRS) requires banks to have appropriate policies and processes to ensure that provisions and write-offs reflect realistic repayment and recovery expectations.</p> <p>In terms of the BGAAP (solo) requirements, valuations, depreciations, write-offs and provisions must meet the criteria of prudence, sincerity and good faith. They must be accounted for systematically on the basis of methodologies adopted by the credit institution. Exposures must account for all foreseeable risk, possible losses and depreciations, which find their origin in past events that occurred before the balance-sheet date (or after).</p> <p>Article 35 of the RD of September 1992 requires credit institutions to apply a forward looking approach in this respect and to reflect realistic repayment and recovery expectations.</p> <p>The impact of collateral is not defined under BGAAP (solo accounts). It generally accepted that collateral is taken into account only when determining the level of provision.</p> <p>For prudential purposes, further quantitative requirements apply on the treatment of collateral pursuant to the chapter V of the NBB Regulation of 15/11/2011 on "own funds." In accordance with article V18, banks can take into the account the value of collaterals when determining the weighted volume of risk to which they are exposed (compensation into the classification is possible in limited cases as set out in article V.21). Section IVIV of Chapter V describes the methodologies to be used for the impact of the risk reducing effect of collaterals. For instance, financial instruments are at fair value, corrected for volatility (V.55 and V.58).</p>
EC5	The supervisor determines that banks have appropriate policies and processes, and organizational resources for the early identification of deteriorating assets, for ongoing oversight of problem assets, and for collecting on past due obligations.
Description and findings re EC5	<p>Compliance with accounting standards requires implicitly that banks have appropriate policies and processes, and organizational resources for the early identification of deteriorating assets, for ongoing oversight of problem assets, and for collecting on past due obligations.</p> <p>The credit portfolio is subject to testing by the external auditor to determine appropriateness of loan classification and adequacy of provisions as well as compliance with valuation policies. For larger loans the oversight is more intense and more frequent. The supervisory process for the larger systemic banks is well defined, however this is not defined for all banks.</p>
EC6	The supervisor is informed on a periodic basis, and in relevant detail, or has access to information concerning the classification of credits and assets and provisioning.

Description and findings re EC6	<p>As part of the regular prudential reporting, all banks have to file separate, detailed and comprehensive reports with the NBB on doubtful and impaired loans on a quarterly basis. For banks that are approved to use internal models, the NBB will receive information when requested and will provide a detailed analysis of loan classifications and provisioning.</p> <p>For all banks, annual accounts must be submitted to the NBB. Annual accounts provide details consistent with the requirements of this criterion. Where necessary, the Bank can and does request further specific information deemed necessary to for verify and assess the banks' position in relation to problem assets, provisioning and reserving. Clear evidence for larger systemic banks , which had received consistent supervision respond to ad hoc requests.</p> <p>Article 44 and 46 of the Banking Law gives the NBB the power to request from each credit institution all information it deems necessary to fulfill its supervisory duties. The regulations clearly provide for this power and evidence that this was exercised by the NBB.</p>
EC7	<p>The supervisor has the power to require a bank to increase its levels of provisions and reserves and/or overall financial strength if it deems the level of problem assets to be of concern.</p>
Description and findings re EC7	<p>The National Bank of Belgium is not empowered to modify the level of provisions reported by the credit institutions neither in their general purpose financial statements (i.e., in their accounts). However, corrections can be required by the Bank for prudential purposes, pursuant to article II.1, §1.b.v of the NBB Regulation of 15/11/2011 on own funds. This article determines the elements that must be deducted from accounting own funds, in order to determine the regulatory own fund. In this frame, the deduction mentioned in element (v) of this article relates to the possible and predictable losses and costs for which, in the opinion of the NBB, the necessary impairment or provisions have not been accounted for.</p> <p>In practice, if the NBB identifies weaknesses in provisioning, it has a number of tools to remedy, such as to apply an adjustment to regulatory own funds.</p> <p>NBB may also decide, under the Pillar 2 process, to set a capital add on, above the minimum solvency requirements, to take into account the potential risk of under estimation of provision on some exposures (Art 46 & 57).</p>
EC8	<p>The supervisor assesses whether the classification of the credits and assets and the provisioning is adequate for prudential purposes. If provisions are deemed to be inadequate, the supervisor has the power to require additional provisions or to impose other remedial measures.</p>
Description and findings re EC8	<p>The NBB has the capacity and power to review loan classification. In practice, the assessment of the classification of credits and assets will depend upon the risk profile and impact of the bank. At a minimum, the NBB will receive a self assessment from management of the bank including a question as to the frequency of review of loan classifications. There is also a reliance on the external auditor for reviewing policies. Adequacy of loan classification practices is a standard feature of onsite reviews, for those banks that are subject to regular onsite review. As stated above, the NBB has the power to adjust the level of own funds if provisions are assessed as inadequate.</p>

EC9	The supervisor requires banks to have appropriate mechanisms in place for periodically assessing the value of risk mitigants, including guarantees and collateral. The valuation of collateral is required to reflect the net realizable value.
Description and findings re EC9	<p>Chapter V of the NBB Regulation of 15/11/2011 on own funds sets out qualitative (including periodic assessment requirements – article V.28.§1) and quantitative requirements that apply to guarantees and collateral. Specific valuation methods apply depending on the type of collateral (section IV of Chapter V) so as to obtain a reliable net realizable value or market value.</p> <p>The regulations require management to establish a process whereby the risk profile of the bank’s counterparties must be properly determined and continuously monitor in order to determine (a) the potential losses and the impairments or provisions needed to cover these losses and (b) the risk weighted value of the credit for capital adequacy purposes. These process must include sufficient consideration of benchmark or, where available, market information on the client.</p>
EC10	Laws, regulations or the supervisor establish criteria for assets to be identified as impaired, e.g., loans are identified as impaired when there is reason to believe that all amounts due (including principal and interest) will not be collected in accordance with the contractual terms of the loan agreement.
Description and findings re EC10	<p>At a solo level, loans, receivables and debt securities are identified as impaired under different categories of exposures:</p> <ul style="list-style-type: none"> - for debt securities and receivable held as financial fixed assets, when repayment at maturity is partly or fully uncertain or compromised (article 29, §2.2 of the RD); - for all other assets held within the banking book, account must furthermore be taken of the risk that the counterparty does not meet its contractual commitments (see also above for the specific requirements for the impairment of problem assets (article 35 of the RD); - assets held within the trading book are valued at their market price which normally reflects all expectations regarding credit risk. <p>Although these principles are generally high-level, under BGAAP assets are basically identified as impaired when there is a reason to believe that all amounts due will not be collected in accordance with the contractual terms of the loan agreement. Prudential reports require banks to report problem assets by type of assets and by nature of the problem and by valuation approach (portfolio or individual asset approach).</p> <p>For accounts that are prepared on a consolidated basis, a financial asset or a group of financial assets is impaired when there is objective evidence of impairment with a loss event having an impact on the estimated future cash flows. The “incurred loss” model implies that losses expected as result of future events, no matter how likely, are not recognized. Under IFRS, expected losses on loans, receivable and debt securities are not recognized and do not lead to impairment testing.</p>

EC11	The supervisor determines that the Board receives timely and appropriate information on the condition of the bank's asset portfolio, including classification of credits, the level of provisioning and major problem assets.
Description and findings re EC11	<p>The NBB Regulation of 15/11/2011 on own funds contains a number of governance requirements on the monitoring and internal reporting (up to the Board) on the various risks to which the bank is exposed, including asset classification and provisioning.</p> <p>The Board and senior management are responsible for the preparation of BGAAP financial accounts every six months. Senior management is responsible for all other information reported to the NBB and must confirm twice a year that this information is compliant with reporting standards (article 44 of the Law of 22 March 1993). In addition, Pillar III reports are published pursuant to Chapter XIV of the NBB Regulation of 15/11/2011 on the own funds and contain a level of detail regarding credit quality.</p>
EC12	The supervisor requires that valuation, classification and provisioning for large exposures are conducted on an individual item basis.
Description and findings re EC12	The accounting law requires impaired exposures to be treated on an individual basis for valuation and provisions. There was no expressed requirement within the regulations for valuation, classification and provisioning for large exposures to be conducted on an individual item basis.
Additional criteria	
AC1	Loans are required to be classified when payments are contractually a minimum number of days in arrears (e.g., 30, 60, 90 days). Refinancing of loans that would otherwise fall into arrears does not lead to improved classification for such loans.
Description and findings re AC1	<p>No such specific requirements exist in this regard under BGAAP (RD of 23 September 1992) except that, as indicated above, doubtful loans must be treated separately and reported as such to the supervisor (article 35, §2.d of the RD).</p> <p>At consolidated level (where IFRS apply), IFRS7 (Financial Instruments: Disclosures) requires entities to disclose additional information on their financial assets that are either past due or impaired (IFRS7, paragraph 37). Based on this disclosure requirement, the prudential financial reporting FINREP requires credit institutions to report to the National Bank detailed information on their past due assets (template 10 of FINREP).</p> <p>See also assessment of compliance with Principle 8 on credit risk.</p>
Assessment of Principle 9	Compliant
Comments	The NBB should mandate a minimum supervisory cycle with an appropriate mix of offsite and onsite reviews of the adequacy of the classification and provisioning policies and processes of a bank and its implementation. The cycle would ideally be risk-based. .
Principle 10	Large exposure limits. Supervisors must be satisfied that banks have policies and processes that enable management to identify and manage concentrations within the portfolio, and supervisors must set prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties.

Essential criteria	
EC1	Laws or regulations explicitly define, or the supervisor has the power to define, a “group of connected counterparties” to reflect actual risk exposure. The supervisor may exercise discretion in applying this definition on a case by case basis.
Description and findings re EC1	<p>The Belgium regulation on large exposures (LE) is the transposition of the European Capital Requirement Directive (CRD Directive 2006/48/EC). This is incorporated into the regulatory framework through NBB Regulation 15/11/2011, Article X.5.</p> <p>The LE Regime uses the definition of “same counterparty,” which is consistent with the CRD (Article 4), being defined as a natural person or a legal person or a group of (natural or legal) persons who must be regarded as a whole from the point of view of risk. The concept of control is further clarified in a Circular (CBFA_2011_03 dated 27 January 2011) in relation to the own funds regulation for credit institutions and investment firms.</p> <p>The CRD provides for national discretion and the Belgium framework has exercised discretions in relation to the treatment of intra-group transactions.</p>
EC2	Laws, regulations or the supervisor set prudent limits on large exposures to a single counterparty or a group of connected counterparties. “Exposures” include all claims and transactions, on-balance sheet as well as off-balance sheet. The supervisor confirms that senior management monitors these limits and that they are not exceeded on a solo or consolidated basis.
Description and findings re EC2	<p>The LE regime applied in Belgium is largely identical to the Directive 2006/48/EC. The LE Rules apply to all credit institutions and investment firms incorporated in Belgium, on a solo and consolidated level. The regime applies similarly to financial holdings (consolidated basis only).</p> <p>As per Article X.5. of the Royal Decree 15/11/2011, an LE is defined as an institution's exposure to a client or group of connected clients where its value is equal to or exceeds 10 percent of its own funds. In terms of the limit framework, banks are required to adhere to the following definitions:</p> <ul style="list-style-type: none"> • 10 percent or more of a bank's capital is defined as a large exposure; and • 25 percent of a bank's capital is the limit for an individual large exposure to a counterparty or a group of connected counterparties. <p>Consistent with the EU Directive, several types of exposures are not captured in the LE regime, including: in the case of foreign exchange transactions, exposures incurred in the ordinary course of settlement during the two working days following payment; for the purchase or sale of securities, exposures incurred in the ordinary course of settlement during five working days following payments or delivery of the securities whichever the earlier etc.</p> <p>For off-balance sheet the exposure value is calculated as its balance-sheet value (i.e., no risk weight, degree of risk or conversion factor is applicable in this context). The exposure value for derivatives, repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions are determined according to the Credit Counterparty Risk provisions (i.e., MtM Method, Original Exposure Method, Standardized Method, Internal Model Method).</p>

	<p>The LE regime allows for smaller banks to exceed the 25 percent limit. In this instance, where the client is an institution, the value shall not exceed 25 percent of the credit institution's own funds or EUR 150 million, whichever is the higher, provided that the sum of exposure values after taking into account eligible credit risk mitigation techniques to all connected clients that are not institutions does not exceed 25 percent of the credit institution's own funds.</p> <p>Where the amount of EUR 150 million is higher than 25 percent of the own funds of the lending credit institution, the value of the exposure, after credit risk mitigation, shall not exceed "a reasonable limit in terms of the credit institution's own funds." That limit is determined by the credit institution itself, consistent with its policies and procedures to address and control concentration risk and shall not be higher than 100 percent of the credit institution's own funds.</p> <p>Therefore the LE regime permits smaller banks to extend exposures of up to 100 percent of capital after taking credit risk mitigation into account. This concession significantly weakens the regime and exposes smaller banks to considerable risk. In practice, smaller banks do not have access to deep capital markets to quickly raise capital in the event an exposure to an obligor defaults or becomes impaired. Smaller banks typically have less sophisticated risk management systems to monitor and manage exposures with real time data and thus are less able to respond in a timely fashion to changes in risk profile.</p> <p>A small sample of LE data sighted as part of this assessment indicates that the exposures of banks to single counterparties are not insignificant:</p> <ul style="list-style-type: none"> • Bank 1: individual exposure to other credit institution after CRM 71 percent; sovereigns over 10 percent approx 150 percent. • Bank 2: Group 155 percent • Bank 3: 300 percent sovereign. • Bank 4 Unable to report March 2012 • Bank 6: Aggregate LE to 6 corporates above 10 percent in total approx 70 percent Total Capital.
EC3	The supervisor determines that a bank's management information systems identify and aggregate on a timely basis exposure to individual counterparties and groups of connected counterparties.
Description and findings re EC3	Article X13 requires that credit institutions have in place adequate organizational and internal control systems enabling them to identify, record, monitor and manage all large exposures according to their internal policies and procedures.
EC4	The supervisor confirms that a bank's risk management policies and processes establish thresholds for acceptable concentrations of credit and require that all material concentrations be reviewed and reported periodically to the Board.
Description and findings re EC4	The Circular relating to risk management for large exposures was first published in 2006 (Circular PPB-2006-17-CPB of 20 December 2006) and describes best practices and reporting requirements under Pillar 2 for sectoral and geographical concentrations. This Circular was updated more recently by Circular CBFA_2010_27 of 16 December 2010 following the publication of CEBS/EBA guidelines on risk concentrations (GL 31 - 2 September 2010). The Circular requires a bank to have adequate arrangements in place for actively controlling, monitoring and mitigating concentration risk. Banks should also use internal limits, thresholds or similar concepts, as appropriate.

EC5	The supervisor regularly obtains information that enables concentrations within a bank's portfolio, including sectoral, geographical and currency exposures, to be reviewed. The supervisor has the power to require banks to take remedial actions in cases where concentrations appear to present significant risks.
Description and findings re EC5	<p>Reporting requirements of COREP Pillar 1 table 90.18 require, on a quarterly basis, that institutions report all their large exposures (top 20 for IRB banks). The information requested includes: category of exposure, amount of credit risk mitigation, indirect exposures, total exposures before and after weightings, distinction banking and trading book. The example of LE reporting submitted by the NBB does not however, provide sectoral, geographical or currency detail.</p> <p>For financial holding companies reporting of LE data is on a six monthly basis, which accounts for the absence of data reported by Bank 4 in EC2. Quarterly reporting for financial holding companies that are material has been initiated to help comply with EBA reporting requests.</p> <p>The NBB only receives geographical concentration data from regulated banks on an annual basis, as opposed to more frequently such as the quarterly frequency of other prudential returns. The EC requires "regular" information of a geographical and sectoral nature be provided to the supervisor. The majority of prudential reporting is quarterly, which allows the supervisor to perform an integrated and comprehensive risk assessment. The reporting could be increased to allow supervisors to respond to risk signals in a timely fashion especially where exposures within the same asset class demonstrate divergent risks depending upon geographical characteristics.</p>
Additional criteria	
AC1	<p>Banks are required to adhere to the following definitions:</p> <ul style="list-style-type: none"> • 10 percent or more of a bank's capital is defined as a large exposure; and • 25 percent of a bank's capital is the limit for an individual large exposure to a counterparty or a group of connected counterparties.
Description and findings re AC1	<p>As foreseen by EU Directive, some temporary deviations are authorized ex ante under conditions for large concentrations resulting from trading book positions.</p> <p>The NBB has indicated that minor deviations from the above limits may be acceptable, especially if explicitly temporary or related to very small or specialized banks.</p>
Assessment of Principle 10	Largely compliant
Comments	The LE regime permits small banks to extend exposures of up to 100 percent of capital after taking account of credit risk mitigation. This significantly weakens the regime for this group of banks, allowing those banks the ability to build-up excessive risk concentrations. In practice, smaller banks do not have access to deep capital markets to quickly raise capital in the event an exposure to an obligor defaults or becomes impaired. Smaller banks typically have less sophisticated risk management systems to monitor and manage exposures with real time data and thus are less able to respond to changes in risk in a

	<p>timely fashion.</p> <p>The credit risk management framework does not require large exposures to be approved/reviewed by senior management or the Board. Without this requirement, excessively large exposures could be made by less experienced staff of the bank that are not in the position to monitor risk concentrations (the credit risk framework is discussed in CP8).</p> <p>The substance of this Principle requires supervisors to establish prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties. Furthermore, without the requirement for large exposures to be approved/reviewed by the Board could result in smaller banks approving large exposures, which results in a build-up of excessive risk.</p>
Principle 11	Exposures to related parties. In order to prevent abuses arising from exposures (both on balance sheet and off balance sheet) to related parties and to address conflict of interest, supervisors must have in place requirements that banks extend exposures to related companies and individuals on an arm's length basis; these exposures are effectively monitored; appropriate steps are taken to control or mitigate the risks; and write-offs of such exposures are made according to standard policies and processes.
Essential criteria	
EC 1	Laws or regulations explicitly provide, or the supervisor has the power to provide, a comprehensive definition of "related parties." This should consider the parties identified in the footnote to the Principle. The supervisor may exercise discretion in applying this definition on a case by case basis.
Description and findings re EC1	<p>The Belgium regulatory framework for related party exposures is comprised of a number of separate documents.</p> <p>There is no specific Circular explicitly defining related party exposure. However, Article 28 of the BL, requires "each credit institution to grant loans, credit facilities or guarantees to its officers or managers under the same conditions, up to the same amounts and against the same securities as those applicable to their clients." Article 28 also requires reporting to the NBB of related party transactions to companies or institutions in which their officers or managers or spouses personally own a direct or indirect qualifying holding. What is missing from the definition in Article 28 is a reference to transactions with material shareholders of the credit institution. Without a reference to material or significant shareholders, it is questionable whether the definitions contained within the Banking Law could be considered comprehensive. Further, loans to shareholders could potentially be a feature across the banking sector and not an insignificant practice in Belgium banking.</p> <p>To some extent, the LE regime is applicable as it provides limits on exposures to counterparties, though the LE regime does not define a related party nor does it explicitly reference related parties.</p> <p>The Belgium accounting law as well as regulation over supplementary supervision (transposing the EU Directive on conglomerates) define groups and related companies. Identification of group relationships, both up- and downstream, is required. In this case, the accounting law provides a more comprehensive set of definitions and importantly includes shareholders.</p>

	<p>In the reporting requirements, the NBB, defines “connected or related parties,” with regard to:</p> <ul style="list-style-type: none"> • all corporates upstream and downstream within the group as well as companies in which such corporates have a significant influence; • individual shareholders and their direct kin; • directors and managers and their close relatives as well as corporates in which these hold a significant stake or a board or management responsibility. <p>Where Art 28 provides for a much fuller definition of exposures, Article 20 only refers to investment services. In the absence of an explicit reference to conflicts of interest policies that deal with loans it is ambiguous at least that this part of the law can be relied upon to manage and mitigate risk from related party transactions. Article 20 also does not refer to shareholders.</p> <p>Pursuant the own funds regulations, credits to shareholders may be deducted from own funds under certain conditions , which is a mitigant through the Pillar 2 approach.</p> <p>The Banking Law clearly applies to all credit institutions, however, for a consolidated group the Banking Law is not relevant for non-credit institutions such as stock broking firms related by the NBB, insurance and reinsurance, and investment management firms.</p> <p>The NBB consider the conflict of interest policy the most effective part of the framework to control risk of related party transactions with respect to director transactions.</p> <p>Internal governance Circular refers to EBA guidelines and includes a wide range of coverage. This translates into an internal governance memorandum. This area is one area that would be considered in terms of related party transactions and is assessed by the NBB for compliance (reference is Number 62 of the Circular).</p> <p>The Governance Circular explicitly states that the Conflicts of interest policy apply at both a solo and consolidated level.</p> <p>The regulations mentioned above do not mention specifically the requirement for a board approved policy on related party exposures. The Banking Law and the Circular on Internal Governance does require risk management policies.</p> <p>It is questionable whether the current regulatory regime for exposures to related parties can be considered comprehensive as required by this EC. It is likely that the regulatory regime does not assist supervisors to take prompt corrective actions.</p>
EC2	Laws, regulations or the supervisor require that exposures to related parties may not be granted on more favorable terms (ie for credit assessment, tenor, interest rates, amortization schedules, requirement for collateral) than corresponding exposures to non-related counterparties.
Description and findings re EC2	The Banking Law requires integrity policy (article 20, §3). The Banking Law does not however require the policy to include specific measures to manage and mitigate the risks associated with exposures to related parties or provide definitions of related parties. Article 20bis §2 does explicitly make reference to measures to prevent conflicts of interests between banks and directors and employees for what concerns investment services. Article 28 explicitly states that credit institutions are by law requested to grant credits, directly or indirectly, and issue guarantees to their directors and managers at the same conditions

	than those prevailing for their customer and breaches are criminally prosecutable.
EC3	The supervisor requires that transactions with related parties and the write-off of related-party exposures exceeding specified amounts or otherwise posing special risks are subject to prior approval by the bank's Board. The supervisor requires that Board members with conflicts of interest are excluded from the approval process.
Description and findings re EC3	<p>The regulations relevant to exposures to related parties as described in EC1 do not refer to requirements for write-off or limits that would need to be approved by the board. It is questionable whether the regulatory framework works together in practice to allow supervisors the ability to appropriately mitigate and monitor this risk or provide at least guidance about write offs.</p> <p>Strategic decision requirement in the Banking Law (include reference) could be considered as a possible way to capture the risk of transactions with a related party of a certain importance. As far as they are considered a strategic decision, they require decision by the bank's Board and prior approval by the NBB. It is very unclear, however, how banks would interpret the application of the strategic decisions requirements to related parties and as such difficult to consider this a reliable mechanism for board approval.</p> <p>The provisions in the Sound Governance Circular (PPB-2007-6-CPA) relating to a conflicts of interest policy do not give guidance about how exposures to related parties should be treated to account for their specific prudential risk. The Circular describes a number of appropriate ways to manage conflicts of interest, however there is not a level of detail that aligns with the requirements in this criterion. The result being that a bank could have in place a conflicts of interest policy , which takes account of the Circular but does not adequately mitigate the special risks associated with exposures to related parties. For example, there is no reference to the need for exposures to related parties to be approved by board.</p>
EC4	The supervisor requires that banks have policies and processes in place to prevent persons benefiting from the exposure and/or persons related to such a person from being part of the process of granting and managing the exposure.
Description and findings re EC4	The Internal Governance Circular (principle VIII) requires that internal conduct rules are enacted and that appropriate measures are taken by the bank regarding, amongst other things, conflicts of interests.
EC5	Laws or regulations set, or the supervisor has the power to set on a general or case by case basis, limits for exposures to related parties, to deduct such exposures from capital when assessing capital adequacy, or to require collateralisation of such exposures. When limits are set on aggregate exposures to related parties those are at least as strict as those for single counterparties, or groups of connected counterparties.
Description and findings re EC5	In its regulation on capital adequacy, the supervisor has reserved itself the right, for all exposures granted under more favorable terms than "at arm's length" ⁵ , to deduct such exposures from the own funds, thus requiring full coverage of these exposures by own funds. Credit granted to shareholders in order to subscribe capital instruments, or when there's no evidence that the shareholders may redeem the credit on basis of other financial resources than its investments in the related bank, shall also be deducted from own funds.

⁵ Regardless of the counterpart or its relationship to the bank or its leaders.

	<p>This requirement was recently introduced.</p> <p>The relevant regulations and rules text include: NBB Regulation 15/11/2011, article II.1; Circular PPB-2007-1-CPB, comments to article II.1 §§ 1 and 5; and Large exposure regime (see CP 10).</p> <p>The LE regime provides for exemptions for intra-group transactions, which would negate the limit framework.</p> <p>In practice, the NBB also deals with this risk via its Pillar 2 assessment and deducts from capital accordingly.</p> <p>In terms of intra-group exposures, the Belgian rules were modified during the transposition of Directive 2009/111/EC (CRD II) , which does not impose limits on intra-group transactions. . The NBB has commenced a transition to a tougher requirement , which will impose a limit of 100 percent of own funds for intra-group transactions, mainly where the group counterparty is domiciled outside of Belgium. In practice, the treatment of intra-group exposures under the Large Exposure Regime will apply to Belgian institutions within a cross-border group. A transitional period until 31 December 2012 has been permitted until the new treatment comes into force. Existing LE rules currently in place include:</p> <ol style="list-style-type: none"> 1. For those exposures to group entities, which receive a 0 percent risk weight under the Standardised Approach, no limit is applicable. 2. Subject to NBB's prior approval, exposures to a domestically regulated subsidiary, the parent company or a subsidiary of that parent company, are exempted from the LE Regime provided that the following conditions are met: (a) funding is mainly provided by professional counterparts and (b) non-professional deposits are limited in volume relative to the Belgian banking sector. 3. Exposures to subsidiaries subject to a control on a consolidated basis are exempted from the LE Regime. 4. Exposures to the parent company or other subsidiaries of that parent company, that are subject to a control on a consolidated basis or equivalent, are subject to the Large Exposure Regime up to 25 percent of own funds. In practice, the limit is thus set at 100 percent of the own funds.
EC6	<p>The supervisor requires banks to have policies and processes to identify individual exposures to related parties as well as the total amount of such exposures, and to monitor and report on them through an independent credit review process. The supervisor confirms that exceptions to policies, processes and limits are reported to the appropriate level of senior management and, if necessary, to the Board, for timely action. The supervisor also confirms that senior management monitors related party transactions on an ongoing basis, and that the Board also provides oversight of these transactions.</p>
Description and findings re EC6	<p>The Belgium rules text for exposures to related parties does not specifically address the requirements in this criterion.</p> <p>The criterion refers to the supervisor requiring banks to identify total amount of exposures to related parties. The relevant text of the Banking Law (regulations do not include a limit framework that would apply. The other aspect of this criterion relates to the need for an independent credit review process for related party exposures. In the case of exposures to material shareholders, the Circular for Internal Governance is not referred to in the Banking Law it is not apparent how a bank would design its policy framework to account for this risk and ensure an independent credit approval process would be established.</p>

	<p>Board approval and oversight is not explicit within the regulations to exercise governance (principle VIII) do not align with the with the requirements of this EC.</p> <p>An integrated process for the identification, monitoring and reporting are approval by the board but is not explicitly provided for in the regulations.. If each of the regulations are applied specifically to related party exposures, the special risks of exposures to related parties might be addressed. There is however, an inherent weakness in the regulatory framework where there is reliance on various regulations to mitigate a specific risk, where the regulations are not designed with the intent of mitigating that risk.</p>
EC7	The supervisor obtains and reviews information on aggregate exposures to related parties.
Description and findings re EC7	In the reporting provided to the NBB by credit institutions on a solo basis, information on related companies, their balance sheet, their profit and loss account and the off-balance sheet commitments is submitted. In the public annual accounts on a solo basis, banks have to disclose any transactions with a related companies or individuals. On a consolidated basis, this information is based on the international accounting standard IAS 24 "Related party disclosures" and these disclosures are made public. In the reporting transmitted to the NBB on consolidated basis, information on balance sheet, profit and loss account and off-balance sheet items is included.
Assessment of Principle 11	Compliant
Comments	An integrated process for the identification, monitoring and reporting of exposures to related parties approved by the board is not explicitly provided for in the regulations.
Principle 12	Country and transfer risks. Supervisors must be satisfied that banks have adequate policies and processes for identifying, measuring, monitoring and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining adequate provisions and reserves against such risks.
Essential criteria	
EC1	The supervisor determines that a bank's policies and processes give due regard to the identification, measurement, monitoring and control of country risk and transfer risk. Exposures are identified and monitored on an individual country basis (in addition to the end-borrower/end-counterparty basis). Banks are required to monitor and evaluate developments in country risk and in transfer risk and apply appropriate countermeasures.
Description and findings re EC1	<p>The NBB has not issued specific guidance on country and transfer risk (other than guidance relating to credit risk and concentration risk in general). As a result, country and transfer risk is a subset of credit risk and the regulatory framework for country and transfer risk consists of the credit risk Circular (Circular letter NBB_2011_09 of 20 December 2011) on internal control, which uses as its base the Basel Document "Principles of Credit Risk Management" of 2000.</p> <p>When banks extend credit internationally, an assessment of the credit risk is made against the principles of credit risk generally rather than with an explicit consideration of country and transfer risk. The result of the assessment is summarized in the credit risk scorecard which is updated at least annually. The assessment criteria are those described in the Basel</p>

	<p>Document “Principles of Credit Risk Management” of 2000, although this document does not refer to country and transfer risk. It could be argued that Principle 3: of the BCBS document informs this requirement , which states “Banks should identify and manage credit risk inherent in all products and activities. Banks should ensure that the risks of products and activities new to them are subject to adequate risk management procedures and controls before being introduced or undertaken.” However, without there is no minimum expectations of risk management.</p> <p>The NBB assesses compliance with credit risk of which country and transfer risk is a subset through its main supervisory activities i.e., onsite examinations; report to management on credit risks; and reports of an accredited auditor.</p> <p>Without specific requirements for country and transfer risk, it is not certain how the NBB would ensure that banks are applying a consistent risk management approach or whether indeed there is a minimum standard that would be expected. No specific guidance has been produced for banks outside of the general BCBS credit risk framework.</p> <p>The lack of explicit guidance also impacts the work of the external auditors. It weakens the quality of the control reports that the NBB utilizes: self assessment of internal controls and the external auditors report.</p> <p>In the assessment of estimates of PD and LGD for internal model users, there is consideration of country risks. Indeed, the NBB recently assessed more specifically the exposures to sovereign assets within the eurozone and the PD/LGD assigned to these exposure in order to assess the appropriateness of these estimates. But internal model accreditation is a small percentage of the regulated population (in terms of number of accredited banks for internal models) and the assessment by the NBB was initiated after considerable issues with this portfolio where transfer risk had crystallized.</p> <p>The NBB has issued a Circular letter (Circular letter CBFA_2010-27 of 13 December 2010) relating more specifically to the management and monitoring of risk concentration. The Circular does include reference to sectoral and geographical concentrations. This addition enhances the regulatory framework somewhat.</p>
EC2	The supervisor confirms that banks have information systems, risk management systems and internal control systems that accurately monitor and report country exposures and ensure adherence to established country exposure limits.
Description and findings re EC2	<p>Pursuant the different rules mentioned in EC1, (Basel Document “Principles of Credit Risk Management” of 2000 and Circular letter CBFA_2010-27 of 13 December 2010 – banks are required to identify, control and report country risk exposures. This is a general requirement rather than specifically relating to this criterion.</p> <p>The assessment of compliance with country and transfer risks is the same as described in EC1.</p> <p>Exposure to country risk is mainly assessed through prudential reporting. Quarterly reports to the NBB (table 40.80) indicate the amount of assets and debts according to the localization of the counterparties. On an annual basis, each institutions report also (table 90.34 of prudential reporting), on consolidated basis, their risk exposures (as defined by the solvency regulation) per country when these exposures exceed 3 pc of their own funds. These reports enable the NBB to monitor the evolution of country risk. The NBB receive</p>

	<p>quarterly and annual information, which allows them to assess a bank's exposure to countries.</p> <p>The NBB also carries out periodic assessments of risk of some countries where Belgian banks have material exposures to better assess the risks taken by these banks and challenge them. These macro-financial analyses incorporate developments in the real and the financial sector include as well an assessment of the main risks. These analyses are presented in the Macro Financial Committee and the NBB Board of Directors. The main countries that have been considered are: Greece, Spain, Italy, Hungary, Ireland, The Netherlands, France and Germany (which a specific attention on the real estate market for these three last countries). This is exceptional analysis rather than part of the quarterly monitoring that would be performed by supervisory teams.</p>
EC3	<p>There is supervisory oversight of the setting of appropriate provisions against country risk and transfer risk. There are different international practices , which are all acceptable as long as they lead to risk-based results. These include:</p> <ul style="list-style-type: none"> • The supervisor (or some other official authority) decides on appropriate minimum provisioning by setting fixed percentages for exposures to each country. • The supervisor (or some other official authority) sets percentage ranges for each country, and the banks may decide, within these ranges, which provisioning to apply for the individual exposures. • The bank itself (or some other body such as the national bankers' association) sets percentages or guidelines or even decides for each individual loan on the appropriate provisioning. The provisioning will then be judged by the external auditor and/or by the supervisor.
Description and findings re EC3	<p>The NBB has not issued specific guidance of appropriate provisions against country and transfer risk. There are specific examples where the NBB has required value adjustments on exposures such as in the case of Greek sovereign bonds to haircut the value in trading books.</p> <p>Nonetheless, there was no evidence of supervisors assessing country and transfer risk with a consistent framework using minimum provisions or fixed percentages to exposures on a country by country basis.</p> <p>Since the introduction of IFRS accounting rules on consolidated basis, NBB has no power to impose additional value adjustments covering specifically country and transfer risk at an early stage. NBB may nevertheless require additional value adjustments for own funds purposes when it assesses, on case by case basis, that the institution has not made a sufficiently prudent adjustments. On the basis of an assessment of value adjustments made by insurance and banks, NBB has issued some recommendations (additional value adjustment) to some institutions.</p> <p>For banks using IRB Models, the NBB will assess whether models take into account the country risks for the calibration of PD and LGD. However, data suggests a significant divergence in estimates exist for LGD estimates as an example: we saw reports, which showed that estimates of LGD for Greek Sovereign bonds ranged from 20 percent to 70 percent; Portugal from 10 percent to 40 percent; Ireland 10 percent to 40percent. While it is not expected that internal models will produce precisely the same estimates, the divergence and impact on RWA's for quite significant portfolios could be considered</p>

	<p>material.</p> <p>At a minimum, the annual assessment of the ICAAP (including stress testing process) provides the NBB with an opportunity to assess the level of these risks and the adequacy of the policies and procedures for identifying and monitoring the country and transfer risk. While the NBB is able to point to some oversight and supervisory actions, monitoring is not yet systematic and ongoing.</p>
EC4	The supervisor obtains and reviews sufficient information on a timely basis on the country risk and transfer risk of individual banks.
Description and findings re EC4	<p>Credit institution report to the NBB on a quarterly basis (table 41.80), the amount of assets and debts according to the localization of the counterparties. On an annual basis, each institutions report also (table 90.34 of prudential reporting), on consolidated basis, their risk exposures (as defined by the solvency regulation) per country when these exposures exceed 3 pc of their own funds. These reports enable the NBB to monitor the evolution of country risk.</p> <p>While the consolidated requirements of the reporting structure are clear, the solo requirements are not. Annual reporting is not sufficiently timely. The reporting requirements in Belgium require annual returns to be lodged by no later than six months after the end of financial year, which in practice together with the lag in supervisors reviewing the data, would not be sufficiently timely for the supervisors to react timely to a build-up in risks.</p>
Assessment of Principle 12	Largely compliant
Comment	The NBB has not issued specific guidance on country and transfer risk (other than guidance relating to credit risk and concentration risk in general), and may not impose any more specific reserves against such risks.
Principle 13	Market risk. Supervisors must be satisfied that banks have in place policies and processes that accurately identify, measure, monitor and control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposures, if warranted.
Essential criteria	
EC1	The supervisor determines that a bank has suitable policies and processes that clearly articulate roles and responsibilities related to the identification, measuring, monitoring and control of market risk. The supervisor is satisfied that policies and processes are adhered to in practice and are subject to appropriate Board and senior management oversight.
Description and findings re EC1	<p>The core of the market risk regulatory framework is a general reference in Article 20 of the Banking Law regarding a sound and safe banking organization. The more specific market risk requirements contained in the Circulars listed below align with the European Directive (revised most recently 2010/76/EU of 24 November 2010):</p> <ul style="list-style-type: none"> • NBB Regulation 15/11/2011, articles I.6 and IX.84. • Circular NBB_2012_03, 10 May 2012, transposing the CEBS/EBA guidelines related to the management of operational risks in market-related activities.

	<ul style="list-style-type: none"> • Circular D1/2002/4, 2 August 2002 related to market risk models. • Circular D1/2001/10, 7 December 2001 related to the organization of market activities. • Circular B 90/1, 17 April 1990 related to the organization of market activities. <p>The Directives follow the Basel rules text and revisions to the Basel II market risk framework updated as of 31 December 2010. The regulations require banks to have policies and processes that adequately identify, measure, monitor and control market risk. The regulations also require the policies to be regularly (at least annually approved by the Board.</p> <p>The supervision plan outlining the supervisory activities for each bank is determined by the risk assessment (scorecard). The activities available to supervisors are generally divided into off-site and on-site to determine whether these policies are appropriate.</p> <p>In terms of the offsite analysis, the control report by the external auditor will form the basis for the supervisor confirming that market risk policies are being complied with. An onsite inspection will not typically take place for all banks on an annual basis unless they are higher risk (determined by the scorecard) or one of the larger systemic banks.</p> <p>Credit institutions are subject to quarterly reporting on market risk. Quarterly reports are analyzed by the financial analysts within the banking supervision teams. On at least an annual basis, the supervisor will also perform a SREP analysis, which involves a meeting with senior management of the bank i.e., CEO, CRO and CFO and the external auditor at a separate meeting.</p> <p>The regulatory regime for market risk does not require policies to be submitted to the NBB. Policies must be updated but updates are not communicated to the NBB. As a result, supervisors may be unaware of changes in risk appetite, expanded trading activities, introduction of new products based on reporting requirements.</p> <p>For banks accredited to use internal models, the results of model validation are not required to be submitted to the NBB unless as an exception. There is no positive assurance framework for confirmation that validation has been performed in a timely fashion with positive results.</p>
EC2	<p>The supervisor determines that the bank has set market risk limits that are commensurate with the institution’s size and complexity and that reflect all material market risks. Limits should be approved by the Board or senior management. The supervisor confirms that any limits (either internal or imposed by the supervisor) are adhered to.</p>
Description and findings re EC2	<p>The suite of market risk Circulars described in EC1 entail a number of requirements to impose market risk limits on trading book activity. The most common market risk measurement tool is Value-at-Risk (VaR) to limit positions. A weakness in the regulatory framework is that there is no specified minimum for the period to calculate VaR. It appears banks are using a range of minimum periods. The lack of consistent rule weakens the ability of offsite analysis to compare and contrast peers and to identify outliers.</p> <p>Typically Belgium credit institutions will develop limits based on sensitivities such as basis point values (BPV) - global and per time bucket - or delta/vega’s, liquidity limits, limits per counterparty, stop loss limits, stress tests. While supervisors will perform periodic financial</p>

	<p>analysis (based on quarterly and annual submission), the main method employed by the NBB to assess compliance with market risk limits is via onsite examinations.</p> <p>The frequency of an onsite review is based on the output from the scorecard process, but will be considered at least annually for banks with large or more complex portfolios and trading strategies. The frequency of onsite reviews is considerably less than on an annual basis for the majority of banks where the supervisory cycle would exceed one year.</p> <p>The BCBS texts require Boards and senior management to approve market risk limits. The current approach is to assess limit breaches as part of the annual SREP program. The regulatory regime is not precise about the requirement for limit breaches to be reported immediately to the NBB. The absence of this requirement combined with the potential for fast pace of market volatility is a weakness and could inhibit the ability of the supervisor to take prompt corrective action if required. It is recognized however, that traded markets activity in the sector is not extensive and in run off for many banks. Nonetheless, at a time when risk aversion abates, enhanced reporting of limit compliance, possibly quarterly, could strengthen the early warning indicators supervisors receive.</p>
EC3	<p>The supervisor is satisfied that there are systems and controls in place to ensure that all transactions are captured on a timely basis, and that the banks' marked to market positions are revalued frequently, using reliable and prudent market data (or, in the absence of market prices, internal or industry-accepted models). The supervisor requires banks to establish and maintain policies and processes for considering valuation adjustments/reserves for positions that otherwise cannot be prudently valued, including concentrated, less liquid, and stale positions.</p>
Description and findings re EC3	<p>NBB Regulation 15/11/2011, Articles I.6 & I.7 relates to ensuring rigorous and prudent valuation practices by institutions. NBB's supervisory and audit teams are in charge of verifying the compliance of institutions with these principles and the frequency of their work will depend upon the output from the scorecard.</p> <p>Off-site controls are mainly based on the analysis of the quarterly prudential reports (COREP tables) as well as on institutions' internal risk reports, submitted annually. The quarterly reporting forms the basis for interviews with institutions' market risk management (frequency quarterly for larger banks and annually for all others). All credit institutions are required to measure and report their trading book positions per instrument categories in the prudential reporting on capital adequacy (COREP tables 90.10 to 90.15).</p> <p>Onsite examinations are the main tool to assess the adequacy of bank policies and processes for valuation adjustments on less liquid positions. The NBB will perform interviews with banks to make the assessment. It is not clear on what information the NBB will form a view about the appropriateness of valuations unless they receive a very detailed report, which goes beyond the existing reporting requirements. There is evidence to suggest that the NBB has acted to address valuations for Greek sovereign bonds in trading portfolios, however, indicating that it is able and willing to examine emerging risks as they are identified.</p> <p>On-site assignments are performed in order to verify ongoing compliance with the regulations and Circulars mentioned above. The scorecarding system is using an indicator of materiality based on the ratio "notional amount of trading derivatives / balance sheet total" and an indicator of riskiness based on the capital requirements for market risk. The</p>

	<p>quantitative indicators will not give any information about quality of risk management or risk appetite.</p> <p>Horizontal analysis is also performed by the specific market risk teams in order to identify possible areas of concern. Liaison with the external auditor is a key component of reviewing the valuation of mark to market positions and the accuracy of valuations. Like many banks globally, the liquidity of market risk portfolios and therefore the valuation has been an issue for Belgium banks.</p>
EC4	The supervisor determines that banks perform scenario analysis, stress testing and contingency planning, as appropriate, and periodic validation or testing of the systems used to measure market risk. The supervisor confirms that the approaches are integrated into risk management policies and processes, and results are taken into account in the bank's risk-taking strategy.
Description and findings re EC4	<p>Two Circulars set the requirements for periodic scenario analysis: NBB Regulation 15/11/2011, articles IX.84 and IX.85; and Circular D1/2002/4, 2 August 2002 specifically related to market risk models. The Circulars align with the EU Directive and the BCBS recommendations, elements such as back testing, validation and stress testing in the context of market risk internal models. The use test is also one criterion that is considered when validating internal models.</p> <p>The supervisory activity is less well defined and developed. In practice, a credit institution with a moderate risk score will not require supervisory attention such as an onsite examination to actively test effectiveness of the control environment by the supervisor. Furthermore, it is not clear in the requirements that the results of stress testing and scenario analysis needs to be submitted to the supervisor, or indeed if stress tests or scenarios breach limits need to be reported to the supervisor.</p>
Additional criteria	
AC1	The supervisor requires that market data used to value trading book positions are verified by a function independent of the lines of business. To the extent that the bank relies on modeling for the purposes of valuation, the bank is required to ensure that the model is independently tested.
Description and findings re AC1	NBB Regulation 15/11/2011, articles I.6 and I.7. In particular, article I.6 (b) determines that internal control systems should ensure that information used to value trading book positions is made independent from (and verified independently of) the dealing room. Article I.7 § 4 specifies that the valuation model should be developed or approved by an independent unit (i.e., independent from the dealing room).
Assessment of Principle 13	Compliant
Comments	Consider implementing a number of additional early warning indicators for market risk to complement existing market risk measurement tools, mainly VaR. Measures might include risk tolerances across a number of market risk metrics and clearly linked to a risk appetite statement. Other tools to identify changes in risk might include notification of new product approvals.

Principle 14	Liquidity risk. Supervisors must be satisfied that banks have a liquidity management strategy that takes into account the risk profile of the institution, with prudent policies and processes to identify, measure, monitor and control liquidity risk, and to manage liquidity on a day-to-day basis. Supervisors require banks to have contingency plans for handling liquidity problems.
Essential criteria	
EC1	The supervisor sets liquidity guidelines for banks. These guidelines take into consideration undrawn commitments and other off-balance sheet liabilities, as well as existing on-balance sheet liabilities.
Description and findings re EC1	<p>The NBB's liquidity regime is based on three key requirements.</p> <ol style="list-style-type: none"> 1. A regulatory stress test. The objective of this test is for the bank to survive a short-dated stress using NBB assumptions for the run off of liabilities and a standard definition of liquid assets that fall into four categories. The stress period is over one week and one month and is applicable to all credit institutions at a solo and consolidated basis and financial holding companies. The stress test was implemented over a two year period from 2009 to 2011. Committed lines and contingent facilities are included in the calculations. 2. A mandatory liquidity reporting scheme that allows for the calculation of the regulatory stress test ratios as well as a set of additional liquidity metrics such as level of liquid assets, maturity mismatches, support from related parties, contingent liquidity risks, funding concentration, level of wholesale funding etc. 3. Qualitative requirements for banks' liquidity management implementing the internationally agreed Basel Committee 2008 principles for the sound management of liquidity (these requirements were introduced in 2009, compliance checked on the basis of a self assessment and further on-site inspections). <p>The Belgium Liquidity regime draws from the Basel Committee's Sound Principles paper on liquidity risk management published in 2008 and was implemented in 2009 as an observation ratio through Circular letter CBFA 2010-21. Both the qualitative guidelines and the quantitative ratios cover contingent liquidity risks related to off-balance sheet items as well as on-balance sheet risks.</p> <p>The NBB scorecarding system incorporates a mix of quantitative (scores on prudential liquidity ratios) and qualitative (compliance with Basel core principles) elements to determine the level of risk embedded in the bank's liquidity position and its management.</p> <p>The NBB has established a "liquidity risk" team that is tasked with regularly informing and sharing information among NBB staff about the state of play of banks' liquidity risk positions, management and regulation as well as to detect risks and outliers and to oversee the consistent application of the NBB's liquidity policy.</p> <p>The Belgian liquidity policy will in the future be increasingly governed by international standards. The Basel III liquidity standards and monitoring tools will be introduced also for Belgian banks.</p>

	<p>The NBB monitors the liquidity position of major banks on a daily basis through management information and calls with banks' treasurers. The NBB has in place daily liquidity reporting for the larger systemically important credit institutions. This is a mix of top down qualitative information from those in the markets area of the NBB and bottom up bank specific information.</p> <p>Since 2006, the NBB has organized and conducted annual liquidity stress test exercises and high level meetings on liquidity risk with the major banks. The 2011 liquidity (stress-test) exercise focused on three main areas: 1) developments in the Belgian regulatory stress test ratio for liquidity risk and other indicators of liquidity risk calculated by the NBB based on prudential reporting; and 2) the results of the QIS on Basel III liquidity standards and 3) the internal liquidity stress tests of banks. At the end of the exercise, the NBB produces a feedback note analyzing each bank's results and comparing them with their peers.</p> <p>The regulatory stress test allows intra-group support to meet the test and there is no limit as to the extent of intra-group support. The implication being that in extremis, credit institutions within a group would not have to hold a minimum level of own-liquidity (on its own balance sheet) to meet the test. Furthermore, the group providing the liquidity is not assumed to be under stress, which assumes no contagion and fungible excess liquidity at the parent. The assumption of unlimited intra-group support means the stress is not a stand-alone test of a credit institution.</p> <p>The other observation regarding the stress test is that credit institutions only need to meet the test on an aggregate basis and not across individual currencies in the liabilities schedule.</p>
EC2	<p>The supervisor confirms that banks have a liquidity management strategy, as well as policies and processes for managing liquidity risk, which have been approved by the Board. The supervisor also confirms that the Board has an oversight role in ensuring that policies and processes for risk-taking are developed to monitor, control and limit liquidity risk, and that management effectively implements such policies and processes.</p>
Description and findings re EC2	<p>The minimum expectations of the NBB in regards to a liquidity policy framework are described in the BCBS Sound Principles - specifically Principle 3. The liquidity regime requires banks to develop a strategy, policies and practices to manage liquidity risk and to ensure that the bank maintains sufficient liquidity and for the board of directors to review and approve these at least annually.</p> <p>The supervisory activity to confirm that banks have effectively implemented such policies and processes will be the qualitative requirement. The qualitative requirements apply to all credit institutions. When the BCBS document was introduced all institutions performed a self assessment against the principles in the document. The outcome of the assessment was entered into the scorecard creating a risk-based assessment of liquidity risk management. The ongoing evaluation of the effectiveness of risk management for liquidity is focusing on specific requirements such as stress tests, governance, monitoring systems, reporting, intra-group relations etc. rather than a fully-fledged assessment of the full spectrum of BCBS requirements for all banks. More attention is paid to the liquidity management in banks that exhibit less robust liquidity positions.</p>

EC3	The supervisor determines that a bank's senior management has defined (or established) appropriate policies and processes to monitor, control and limit liquidity risk; implements effectively such policies and processes; and understands the nature and level of liquidity risk being taken by the bank.
Description and findings re EC3	The regulatory regime requires a bank's senior management to develop policies and practices to manage liquidity risk articulated in principle 5 of the BCBS document adopted by the NBB. The main means of confirming that the policies and practices are implemented effectively is the annual internal control report, the external audit reports, and the annual meeting with credit institutions. Onsite examinations will be performed where required.
EC4	The supervisor requires banks to establish policies and processes for the ongoing measurement and monitoring of net funding requirements. The policies and processes include considering how other risks (e.g., credit, market and operational risk) may impact the bank's overall liquidity strategy, and require an analysis of funding requirements under alternative scenarios, diversification of funding sources, a review of concentration limits, stress testing, and a frequent review of underlying assumptions to determine that they continue to be valid.
Description and findings re EC4	<p>The BCBS Principles for Sound Liquidity Risk Management sets out the requirements to satisfy this criterion. Principle 5 of this document requires banks to have a sound process for identifying, measuring, monitoring and controlling liquidity risk. Principle 6 requires credit institutions to monitor and control liquidity across legal entities, business lines and currencies taking into account limitations to the transferability of liquidity. The regulatory framework is clear regarding policies and processes.</p> <p>While Principle 6 requires the establishment of a funding strategy that provides for effective diversification the fact that the regulatory stress test does not limit the extent of intra-group support to meet the outflow of funds is contrary to the diversification principle.</p> <p>The NBB regulatory stress test ratios for liquidity risk compare the potentially required liquidity (net stressed outflows calculated as the sum of the stressed mismatch and a percentage of the bank's contingent claims) with the liquidity available to the bank (calculated as the liquidity buffer composed of unencumbered liquid assets and the potential support from related parties) for a one week and one month horizon, both on a consolidated and a legal entity basis. The ratio actually uses the same methodology as the forthcoming Basel III Liquidity Coverage Ratio but includes different parameters and definitions.</p> <p>These ratios were used as internal measures until the financial crisis, introduced as non-binding observation ratios in 2009 and as binding regulatory standards since the beginning of 2011. A ratio higher than 100 percent implies a liquidity shortage if the stress scenario would materialize at the reporting date (potentially required liquidity > potentially available liquidity). The assumptions do allow some less stringent ideas: full convertibility between currencies (within a time frame of one week).</p> <p>The Belgian liquidity standard, compared to the LCR, is generally less severe with regard to the definition of the liquidity buffer, but this is compensated by stricter assumptions on the stress scenario and liquidity outflows.</p>

EC5	The supervisor obtains sufficient information to identify those institutions carrying out significant foreign currency liquidity transformation. Where a bank or banking group's foreign currency business, either directly, or indirectly through lending in foreign exchange to domestic borrowers, is significant, or where a particular currency in which the bank has material exposure is experiencing problems, the supervisor requires the bank to undertake separate analysis of its strategy for each currency individually and, where appropriate, set and regularly review limits on the size of its cash flow mismatches for foreign currencies in aggregate and for each significant individual currency.
Description and findings re EC5	<p>The liquidity reporting scheme is reported separately for the position in EUR, the aggregate position in convertible currencies (G-10 + EU countries' official currencies) and individual positions in non-convertible currencies. Separate reporting of the position in convertible currencies (mainly USD positions) is only delivered by the major banks.</p> <p>In the context of the monitoring of the Basel III Liquidity Coverage Ratio the NBB require banks to fill in LCR templates in USD if their positions are significant. For banks that maintain significant positions Principle 5 of the qualitative requirements (Basel principles) determines that a bank should assess its foreign currency needs, determine acceptable mismatches, be capable to manage risk arising from foreign currency deposits and foreign currency assets funded in domestic currency and develop contingency strategies.</p> <p>Belgian banks submit a standardized liquidity reporting scheme (tables 90.31-33) to the NBB on a monthly basis. The reporting tables incorporate information on the unencumbered liquid assets, projected in- and outflows, contingent liquidity risks etc. of the firm. Reporting is submitted both on a entity level as well as the consolidated level.</p> <p>The Bank Performance Report (BPR) calculates a number of prudential liquidity metrics on the basis of this input. These ratios are complemented with data on funding concentration and the standing in debt markets (short term credit ratings) of firms to determine the quantitative elements of the institution's score for liquidity risk.</p> <p>Horizontal analysis will assess potential outliers for these ratios in order to signal potential outliers to the operational supervisors and the NBB's hierarchy. This analysis is incorporated in a quarterly liquidity and funding review that is presented to the NBB Board.</p> <p>The NBB also receives the major banks' liquidity management info daily on the basis of which the following standard liquidity dashboard is edited and distributed within the NBB:</p> <p>Not all banks are required to test their liquidity by currency and to ensure sufficient diversification of their funding sources by currency.</p>
EC6	The supervisor determines that banks have contingency plans in place for handling liquidity problems, including informing the supervisor.
Description and findings re EC6	Principle 11 of the Sound Principles requires banks to have a formal contingency funding plan that clearly sets out the strategies for addressing liquidity shortfalls in emergency situations. These plans have been effectively activated by a number of institutions during the last few years. At the introduction of the revised qualitative requirements in 2009, compliance was checked on the basis of a self assessment and an implementation plan generated by the banks. On-site inspections were conducted at a selected number of individual institutions, including all large banks, to check compliance, though not across all

	<p>credit institutions and investment firms were not included. Contingency funding plans are not required to be submitted or vetted by the NBB on an ongoing basis.</p> <p>While all credit institutions were required to complete a self assessment against the sound principles upon introduction, fully-fledged inspections were not carried out across the broader population of banks. Dedicated deep dive inspections into banks identified as outliers are however conducted. Nevertheless, since the self assessment exercise, no indication that the NBB intends to carry out of a systematic follow up to monitor how banks are progressing, especially if significant remedial action required.</p> <p>The NBB's liquidity reporting scheme and ratios cover position in euro, the aggregate of convertible currencies and important positions in individual non-convertible currencies (virtually non-existing). If foreign currency funding risks are relevant to the bank's business the NBB's qualitative guidelines require banks to assess currency mismatches (see standards' assessment), foresee contingency measures and analyze the issue non-convertibility of currencies in their stress testing.</p> <p>The issue of foreign currency risk is included the annual stress testing exercise but the NBB does not require banks to perform individual stress tests for specific currencies. The new European Basel III LCR stress test reporting that will be introduced from next year onwards will complement the NBB reporting scheme and will require each bank to report in each currency in which the bank has a significant position.</p>
Additional criteria	
AC1	The supervisor determines that, where a bank conducts its business in multiple currencies, foreign currency liquidity strategy is separately stress-tested, and the results of such tests are a factor in determining the appropriateness of mismatches.
Description and findings re AC1	Principle 5 of the Sound Principles sets out the requirements for a bank to assess its foreign currency needs and determine acceptable mismatches. Principle 9 on stress testing requires banks to include the issue of FX convertibility and access to foreign exchange markets in its tests if relevant to its business.
AC2	The supervisor confirms that banks periodically review their efforts to establish and maintain relationships with liability holders, maintain the diversification of liabilities, and aim to ensure their capacity to sell assets.
Description and findings re AC2	The NBB adopted the Basel Committee's September 2008 Principles for Sound Liquidity Risk Management as its set of qualitative guidelines according to which it expects banks to govern their liquidity risk management. Principle 7 of these requirements refers to funding diversification and to the maintenance of market access as an essential component of ensuring funding diversity. A bank is requested to build strong relationships with current and potential investors, develop markets for assets sales and strengthen arrangements under which it can borrow secured or unsecured.

Assessment of Principle 14	Compliant
Comments	<p>The regulatory requirements for liquidity risk are well advanced with a quantitative test similar to the Basel LCR in place since 2011. Daily reporting for larger systemic banks robust.</p> <p>Consider applying certain limitations to either the timing or the extent to which intra-group support can meet the regulatory stress test. This will strengthen the individual liquidity position of a bank.</p>
Principle 15	Operational risk. Supervisors must be satisfied that banks have in place risk management policies and processes to identify, assess, monitor and control/mitigate operational risk. These policies and processes should be commensurate with the size and complexity of the bank.
Essential criteria	
EC1	The supervisor requires individual banks to have in place risk management policies and processes to identify, assess, monitor and mitigate operational risk. These policies and processes are adequate for the size and complexity of the bank's operations, and the supervisor confirms that they are periodically adjusted in the light of the bank's changing risk profile and external market developments.
Description and findings re EC1	<p>Articles 20, 46 and 43 of the Banking Law set the regulatory framework for operational risk. Article 43 forms the basis for the NBB Regulation of 15 November 2011 on the capital of credit institutions and investment firms, which includes Pillar 1 and Pillar 2 requirements for operational risk and other risk categories. Title VIII of the NBB Capital regulation lays down the Pillar 1 capital requirements for operational risk. Title XII holds the Pillar 2 ICAAP and SREP regulation (including for operational risk). The NBB Capital regulation mirrors the European CRD/CAD Directives, which are largely consistent with the Basel Capital Accord.</p> <p>NBB's Communication NBB_2011_05 of 27 October 2011 formally advised banks that the BCBS Principles for the Sound Management of Operational Risk of June 2011 set new prudential expectations and that these principles will be used when assessing a bank's operational risk management.</p> <p>Qualitative criteria prescribed by the NBB Regulation of 15 November 2011 on the capital of credit institutions and investment firms (and by the guidelines to that Regulation) for banks using the Standardized Approach or the Advanced Measurement Approach, imposes additional and specific requirements regarding these elements, mainly based on EBA/CEBS guideline.</p> <p>The NBB has issued a number of specific Circulars regarding components of operational risk such as sound management of outsourcing, of business continuity planning and of financial services providing via the internet. Additional recommendations regarding business continuity management for systematically important institutions were issued by the Committee for Financial Stability on October 20th, 2004.</p> <p>On and off-site supervision of operational risk at individual banks is performed by the supervisor and, specifically for information technology aspects and for mathematical model validations, by the risk specialist teams. Under the umbrella of the Risk Committee, a</p>

	<p>dedicated "Operational Risk Team" has been established providing a structured forum for regular information sharing between those different departments, for dealing with possible level playing field considerations, etc.</p> <p>A separate committee (OCCO) monitors the implementation of the additional recommendations issued on October 20th, 2004 regarding business continuity management by the systematically important institutions. Operational risk is a dedicated risk category in the overall periodic scorecard.</p> <p>The NBB requires banks to put in place a comprehensive operational risk management framework through the application of the BCBS Sound Principles. The provisions of the Circular are applied on a proportional basis by the NBB depending upon the risk profile through the scorecard. Relevant changes in risk profile have to be reported to the NBB in effective management reports on internal controls as prescribed by Circular letter 2011_09 of 20 December 2009.</p> <p>The quarterly reporting for operational risk for those credit institutions using the basic indicator and Standardized approach does not have a level of granularity that would identify changes in risk profile.</p> <p>A new supervisory process has been added for the larger credit institutions to submit to the NBB a new product approval document, which appears to be a good tool in periodically assessing the risk management framework as it applies to new lines of business. While the new product approval document is available to the NBB, there is no requirement to be submitted to the NBB.</p>
EC2	<p>The supervisor requires that banks' strategies, policies and processes for the management of operational risk have been approved and are periodically reviewed by the Board. The supervisor also requires that the Board oversees management in ensuring that these policies and processes are implemented effectively.</p>
Description and findings re EC2	<p>The BCBS document explicitly refers to the role of the Board of directors in approving policies for operational risk (Principles 1, 3 & 4). As a Pillar 1 risk and part of the risk scorecard, operational risk will be assessed at least annually by the supervisor as part of the SREP. For higher risk banks, operational risk might be assessed on a more regular basis on a case by case basis. The principle tools used by banks for identifying and assessing operational risks are:</p> <ul style="list-style-type: none"> i) descriptions of business processes with their key risks and key controls ii) periodic self assessments (e.g., scenarios) iii) loss data registration (including performing a "lessons learned" analysis) iv) testing/monitoring the operational effectiveness of the key controls v) internal risk reporting. <p>These tools serve as an input for the effective management's reports on internal controls.</p>

	<p>EC2 requires Board oversight of operational risk and that the policies and processes have been approved by the Board and vetted by senior management. It is expected that there would be a review and approval of operational risk management policies by Board at least annually (and more frequently if the environment or business is changing).</p> <p>While the regulatory framework requires Board oversight, it is not a requirement that policies are submitted to the NBB on an annual basis.</p>
EC3	The supervisor is satisfied that the approved strategy and significant policies and processes for operational risk are implemented effectively by management.
Description and findings re EC3	<p>The NBB evaluates the operational risk framework through offsite and onsite reviews. A particularly valuable input into the supervisory framework for operational risk is the annual internal controls report submitted by credit institutions to the NBB as a self assessment of the control environment and forms the basis for much of the offsite analysis.</p> <p>As a general rule, the frequency for an onsite review of the larger systemically important credit institutions will be on an annual cycle, though not mandated by the supervisory framework. For the rest of the regulated population of credit institutions, the frequency of onsite inspections will vary between one and five years for IT and will depend upon the risk of the institution.</p> <p>Onsite inspections relating to operational risk can roughly be classified into three categories:</p> <p>a) inspections of a more general nature that—amongst other risk categories--also include operational risk (for instance: the so-called "gang van zaken"-inspections, inspections relating to risk management; ICAAP-inspections; etc.)</p> <p>b) inspections targeting operational risk management</p> <p>c) inspections targeting specific elements of operational risk (for instance inspections re the AMA-approach under the Basel Capital Accord; IT-inspections; Business Continuity-inspections; inspections re outsourcing; etc.).</p> <p>In order to properly identify and assess the operational risks within banks, the NBB has at its disposal different information sources and tools. Important information sources are the regulatory (financial) reports on operational risks, loss data bases, spontaneous event driven reports and the annual effective management's reports on internal controls.</p> <p>The results of NBB's monitoring and evaluation activities are included in the scorecards, which also serve as a benchmarking between peer banks.</p> <p>It is only through independent testing of control effectiveness that the supervisor could obtain a sufficient level of comfort that the policies are implemented effectively. Outside of an onsite review performed by the NBB, reporting from the external auditor is the main supervisory tool to obtain comfort about the control environment from an independent source. However, the testing of risk management and control design to form a positive assurance is not performed by the external auditor as part of the annual Internal Control Report.</p>

	<p>An onsite review must be performed periodically to derive comfort that implementation is effective. The frequency would be determined by the risk profile using other evidence such as discussions with senior management, BPR etc.</p>
EC4	<p>The supervisor reviews the quality and comprehensiveness of the bank's business resumption and contingency plans to satisfy itself that the bank is able to operate as a going concern and minimise losses, including those that may arise from disturbances to payment and settlement systems, in the event of severe business disruption.</p>
Description and findings re EC4	<p>The NBB requirements for business continuity are captured in the BCBS principles (in particular Principle 10 regarding business resilience and continuity). In addition, a dedicated Circular letter PPB 2005/2 of 10 March 2005, provides guidance on sound business continuity management practices.</p> <p>An assessment of the adequacy of the business resumption and contingency plans is included in the standard onsite examination.</p> <p>The supervisory process for the larger systemic credit institutions appears to be relatively well established, however, the processes for the wider population of banks is less established. While all credit institutions are required to perform regular BCP and DR testing, the NBB will not necessarily receive the results of that testing. Should a credit institution fail its own test or the test identifies certain weaknesses, there is no requirement that the NBB be notified.</p>
EC5	<p>The supervisor determines that banks have established appropriate information technology policies and processes that address areas such as information security and system development, and have made investments in information technology commensurate with the size and complexity of operations.</p>
Description and findings re EC5	<p>EC5 is seeking to determine the extent of specific IT requirements in the operational risk regulations. IT is critical to banking operations and as such reliable and stable IT is an important contributor to financial stability. Given its importance specific requirements by the NBB have been put in place in addition to the more general operational risk requirements.</p> <p>The BCBS principles (in particular principle 9, §§ 47 to 53) cover elements of IT. In addition, the dedicated Circular letter PPB 2005/2 of 10 March 2005 of the CBFA providing guidance on sound business continuity management practices includes specific ICT-related guidance. A dedicated Circular letter CBFA_2009_17 of 9 April 2009 contains the NBB's prudential expectations relating to the provision of financial services via the Internet. These expectations refer to legal risks, operational risks and reputational risks, and include aspects such as management responsibility, contractual relationships, security, availability, continuity, outsourcing, client identification, an attachment to that Circular letter provides specific sound practices relating to the management of Internet security risks and are presented to banks according to the "comply or explain" principle.</p> <p>Onsite examinations are critical for EC5. The NBB has a team of eight IT risk specialists , which cover approximately 170 firms regulated by the NBB. It is challenging for this small team to cover the regulated population. The NBB uses the risk scorecard to help identify higher risk banks, critical to directing scarce resources to the highest risk banks. This places</p>

	a high reliance on the effectiveness of the risk scorecard to identify at risk banks.
EC6	The supervisor requires that appropriate reporting mechanisms are in place to keep the supervisor apprised of developments affecting operational risk at banks in their jurisdictions.
Description and findings re EC6	<p>EC6 requires appropriate reporting to the authorities of operational risk metrics. The BCBS Principles (in particular principle 8) covers some elements of this criterion. Important sources of information for the NBB are the effective management reports on internal controls (Circular letter NBB_2011_09 of 20 December 2011) that have to be transmitted to the NBB annually by all credit institutions.</p> <p>The legal framework requiring strategic decisions (including those regarding operational risk) to be submitted to the NBB, is also a useful tool. In addition, the NBB receives the following reporting:</p> <ul style="list-style-type: none"> • in a quarterly table (90.16) all banks report their operational risk capital requirement calculations • in a yearly table (90.17) all AMA banks report their past year's operational risk losses • banks have to report spontaneously events such as major frauds or suspect operations regarding market-risk related activities (Circular letter NBB_2012_03 of 10 May 2012), any security incidents Internet services or IT infrastructure security incidents (Circular letter CBFA_2009_17 of 9 April 2009) and material outsourcing arrangements (Circular letter PPB 2004/5 of 22 June 2004).. <p>Furthermore, Circular letter CBFA_2009_19 of 8 May 2009 (relating to the mission of a bank's external auditor as co-operator to prudential supervision) holds specific reporting tasks (see Section F re information exchange) requesting the external auditor to communicate certain events spontaneously (some of which may be operational risk related) to the NBB.</p>
EC7	The supervisor confirms that legal risk is incorporated into the operational risk management processes of the bank.
Description and findings re EC7	EC7 requires explicit consideration of legal risk as part of the operational risk management process. There is no explicit reference to legal risk in the BCBS document. This is a deficiency in the operational risk framework.
EC8	<p>The supervisor determines that banks have established appropriate policies and processes to assess, manage and monitor outsourced activities. The outsourcing risk management programme should cover:</p> <ul style="list-style-type: none"> • conducting appropriate due diligence for selecting potential service providers; • structuring the outsourcing arrangement; • managing and monitoring the risks associated with the outsourcing arrangement; • ensuring an effective control environment; and • establishing viable contingency planning. <p>Outsourcing policies and processes should require the institution to have comprehensive contracts and/or service level agreements with a clear allocation of responsibilities between the outsourcing provider and the bank.</p>

Description and findings re EC8	<p>EC8 requires explicit consideration of outsourcing risk in the regulatory framework. The BCBS principles (in particular principle 9, § 54) cover most elements of EC8. In addition, a dedicated Circular letter PPB 2004/5 of 22 June 2004 of the CBFA provides guidance on sound outsourcing management practices. The Circular letter includes all the necessary references.</p> <p>The NBB uses the principles of Circular letter PPB 2004/5 of 22 June 2004 as the framework to assess outsourcing arrangements using a risk based approach, through off site analyses of service letter agreements and monitoring reports and through on site inspections.</p>
Additional criteria	
AC1	The supervisor determines that the risk management policies and processes address the major aspects of operational risk, including an appropriate operational risk framework that is applied on a group-wide basis. The policies and processes should include additional risks prevalent in certain operationally intensive businesses, such as custody and correspondent banking, and should cover periods when operational risk could increase.
Description and findings re AC1	The supervisor has a number of inputs into the assessment of external factors such as loss data collected from industry, major loss information reported and ad hoc information requests.
Assessment of Principle 15	Compliant.
Comments	<p>As a general rule, for the large banking groups, an onsite assessment is performed annually in includes a review of outsourcing arrangements. For medium sized and small banks, the frequency of onsite inspections varies between one and five years for IT, following a risk based approach.</p> <p>While all credit institutions are required to perform regular BCP and DR testing, the regulations do not require banks to submit results of testing should a bank fail its own test.</p>
Principle 16	Interest rate risk in the banking book. Supervisors must be satisfied that banks have effective systems in place to identify, measure, monitor and control interest rate risk in the banking book, including a well defined strategy that has been approved by the Board and implemented by senior management; these should be appropriate to the size and complexity of such risk.
Essential criteria	
EC1	The supervisor determines that a bank's Board approves, and periodically reviews, the interest rate risk strategy and policies and processes for the identification, measuring, monitoring and control of interest rate risk. The supervisor also determines that management ensures that the interest rate risk strategy, policies and processes are developed and implemented.
Description and findings re EC1	Chapter 1 of the annex to the NBB Circular PPB-2006-17-CPB lays out minimum requirements for the internal management of interest rate risk. Section §2.2 includes an explicit requirement for the installment of control and procedures approved by the Board for the identification, measurement, monitoring and control of interest rate risks.

	<p>The Circular also requires internal risk limits and an internal control system to be developed in accordance with the strength of the institution and that there should be sufficient flows of information with the supervisor. The Circular requires the Board to be involved in determining strategies and approving all important policies, as well as the effective supervision of the implementation.</p> <p>The regulatory framework requires involvement of the Board in setting policies and processes. The NBB guidelines are strongly aligned with the relevant international texts of BCBS and CEBS/EBA.</p> <p>The Circular treats both qualitative aspects (adequacy of internal risk management and risk measurement systems) and quantitative aspects, in line with the international rules and guidance (BCBS & CEBS). The Circular explicitly references the two documents as the basis of the NBB's expectations. These texts are quasi completely aligned with each other and at its turn. The circular incorporates them into the Belgian, which provides for a flexible way to pick up progress made at the EBA and the likely developments in the banking union. The NBB's IRRBB regime has two main features:</p> <ol style="list-style-type: none"> 1. Regulatory IRRBB stress test ratios requiring banks to hold sufficient capital to cover economic value losses related to adverse structural interest rate changes in order not to be identified as an outlier bank.. 2. Qualitative requirements for banks' IRRBB management implementing the internationally agreed Basel Committee 2004 principles for the management and supervision of interest rate risk, and implementing the CEBS 2006 "Technical aspects of the management of interest rate risk arising from non-trading activities under the supervisory review process." <p>The NBB organizes annual IRRBB stress test exercises as part of the European solvency stress tests, which integrate both interest rate risk and spread scenarios.</p> <p>The NBB scorecarding system incorporates a mix of the quantitative (scores on IRRBB ratios) and qualitative (compliance with Basel core principles) criteria. To further strengthen the supervisory toolkit for IRRBB, the NBB is developing a tool to monitor the IRRBB position of major banks on a quarterly basis.</p> <p>The NBB has observed divergences in approaches used by banks to measure and calculate IRRBB, and take this into account in its supervisory appraisal of reported IRRBB indicators. Going forward, the NBB will further analyze both the qualitative and quantitative aspects of these divergences to ensure a full comprehension of interest rate risks. Concerning qualitative aspects, attention will be paid to factors such as i.e., combining views of ALM and treasury departments on IRRBB and ensuring the functional separation between Head of Treasury and Head of Markets at banks.</p> <p>While the regulatory framework is clear and comprehensive regarding the Board's involvement, the supervisory framework is less clear to determine how well the Board is meeting its obligations set out in this criterion. The frequency of engagement with the board by the supervisor is not mandated by the supervisory framework. In practice, the supervisor will meet frequently with the larger systemic banks, which would typically include the CFO, CEO and CRO. The engagement does not, however, extend systematically</p>
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	<p>to the board of directors of all banks.</p> <p>The supervisor does perform assessments of board reports carried out at least annually when the scorecard is updated as part of the SREP. The board reporting and minutes cover a number of risk areas.</p>
EC2	<p>The supervisor determines that banks have in place comprehensive and appropriate interest rate risk measurement systems and that any models and assumptions are validated on a regular basis. It confirms that banks' limits reflect the risk strategy of the institution and are understood by and regularly communicated to relevant staff. The supervisor also confirms that exceptions to established policies, processes and limits should receive the prompt attention of senior management, and the Board where necessary.</p>
Description and findings re EC2	<p>Chapter 1 of the annex to the NBB Circular PPB-2006-17-CPB requires institutions to be able to calculate both the earnings and value sensitivity to interest rate risk in the banking book, using internal measurement techniques adapted to the size and complexity of a bank's activities and related risks. The engagement of the Board is required when setting strategies and approving all important policy decisions, including the effective supervision of the implementation of risk management.</p> <p>The NBB receives quarterly reporting based on common assumptions and common scenarios. The scenarios are limited to the impact of upward and downward parallel shifts in the yield curve shocks of 1percent, 2 percent and 3 percent on both the economic value of the banking book and on the net interest income for the coming three years (COREP table 90.30 in figure 1). Banks are allowed to use internal measurement systems to calculate the impact under a set of common assumptions such as the treatment of equity, the duration of deposits and the time dynamics of interest rate shocks.</p> <p>The ratios that are required by the NBB to be reported include:</p> <ul style="list-style-type: none"> • the impact of interest rate shocks on the economic value of the banking book • impact of interest rate shocks on expected net interest income <p>The prudential approach does not capture all types of (firm-specific) interest rate risks. As a result, supervisors are required to follow-up with firms to assess bespoke information requests. As IRRBB is a Pillar 2 risk, and peer data is an important component of the analysis.</p> <p>These focus both on economic value (VaR, BPV) and on interest income perspectives (e.g., Earnings at Risk). IRRBB is a pillar 2 risk and is monitored both through internal and prudential reporting.</p> <p>To calculate the tier 1 capital requirement, the impact of a 200bps parallel shift in the yield curve measured against the capital base with the data taken from the quarterly prudential returns. This amount is then adjusted according to the supervisor's assessment of the bank's interest rate risk management. The result is entered into the scorecard. The supervisor of the particular bank has the discretion to influence this amount based on their judgment of the interest rate risk profile of the bank (within limits).</p>

	<p>As IRRBB is a Pillar 2 risk, the internal models used to calculate this risk are not required to be approved by the NBB. In this context, there might be a divergence in quality of modeling, quality of data inputs into the models, differences in assumptions and modeling approaches all leading to different model outputs. Without a detailed analysis of the various factors, an appreciation of the inherent risk profile might be difficult to identify let alone compare against a peer group.</p> <p>The NBB recognizes that more attention should go to the follow-up of risk positions by supervisors (i.e., inputs to the calculations), and to the profitability component in measuring the risk. Enhancements of reporting does not always include all material exposures and risks.</p>
EC3	The supervisor requires that banks periodically perform appropriate stress tests to measure their vulnerability to loss under adverse interest rate movements.
Description and findings re EC3	<p>The requirement for banks to perform period stress tests is clearly set out in the regulations. §2.2 of chapter 1 of the annex to the NBB Circular PPB-2006-17-CPB states that in accordance with international guidelines on IRRBB, the interest rate risk management function of banks should include the incorporation of possible stress scenarios such as considerable shocks, changes in correlations and changes in behavioral assumptions.</p> <p>In practice, the NBB has observed through inspections that many banks do perform interest rate risk stress tests, largely focused on the impact of a set of different interest rate scenarios, both general and specific to the institutions (e.g., basis risk). More attention seems needed in stress testing changes in behavioral assumption (e.g., duration of deposits, convexity in prepayments). It is also unclear to what extent top management is exposed to the results. The sophistication of stress testing practices at the non-systemic banks is an area for improvement.</p>
Additional criteria	
AC1	The supervisor has the power to obtain from banks the results of their internal interest rate risk measurement systems, expressed in terms of the threat to economic value, including using a standardized interest rate shock on the banking book.
Description and findings re AC1	Banks report the results of their internal interest rate risk measurement systems quarterly, expressed in terms of the threat to economic value and net interest income. For the larger systemic banks, the analysis of this data is relatively well developed and comprehensive. Requirements under chapter 1 of the annex to the NBB Circular PPB-2006-17-CPB require banks report quarterly the outcome of a standardized interest rate shock on the banking book (COREP table 90.30). The Banking Law sets out powers for the NBB to obtain any reporting it considers relevant to the supervision of a credit institution.
AC2	The supervisor assesses whether the internal capital measurement systems of banks adequately capture the interest rate risk in the banking book.
Description and findings re AC2	The annual analysis of the ICAAP is the main exercise that considers the internal capital measurement system. The ICAAP review includes IRRBB as a Pillar 2 risk. For certain large complex banks, the NBB base prudential capital requirements on the internal analysis, for

	other banks the NBB has opted to use the SREP analysis as these better capture the interest rate risk in the banking book.
AC3	The supervisor requires stress tests to be based on reasonable worst case scenarios and to capture all material sources of risk, including a breakdown of critical assumptions. Senior management is required to consider these results when establishing and reviewing a bank's policies, processes and limits for interest rate risk.
Description and findings re AC3	The requirement for the stress tests to consider a worst case scenario is not explicitly mentioned.
AC4	<p>Interest rate risk management at large institutions is assigned to ALM departments, which report separately from risk-taking departments. From a functional perspective, the NBB regulations and guidance do not formally require a separation of staff responsible for Treasury and markets activity and this has been a prudential issue for the NBB. However, recent on-site examinations of liquidity risk management and of dealing room activities of large banks have resulted in specific NBB recommendations to separate the treasury function and such risk-taking activities.</p> <p>Even though such supervisory actions and the growing awareness of the large banks result in increasing adherence to this best practices, this matter remains a specific area for attention by the NBB.</p>
Description and findings re AC4	<p>Interest rate risk management at large institutions is assigned to ALM departments, which report separately from risk-taking departments. From a functional perspective, the NBB does not require separation of staff responsible for Treasury and markets activity and this has been a prudential issue for the NBB.</p> <p>This is a specific area for attention by the NBB to require function separation of treasury staff and markets staff.</p>
Assessment of Principle 16	Compliant
Comments	<p>The regulatory and supervisory framework for managing interest rate risk is well established and executed. The NBB has made strong efforts to implement new standards and has embedded interest rate risk in its core work. The program could be further enhanced as follows:</p> <ul style="list-style-type: none"> • Write a single regulation to replace multiple rules texts. Include requirements for stress testing, limit that NBB reflects their risk appetite. • Strengthen the regulatory framework with a requirement for a functional and operational separation of markets and treasury function. • Requirement of an ALCO for all credit institutions, which will enhance the quality, timeliness and management of this risk. • Extend cross-sectoral analysis to a greater number of banks. Improve the identification of outliers and strengthen the transfer of skills to supervisor.

Principle 17	Internal control and audit. Supervisors must be satisfied that banks have in place internal controls that are adequate for the size and complexity of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations.
Essential criteria	
EC1	Laws, regulations or the supervisor establish the responsibilities of the Board and senior management with respect to corporate governance to ensure that there is effective control over a bank's entire business.
Description and findings re EC1	<p>The responsibilities of the Board and senior management with respect to corporate governance and effective control is established in the Banking Law Article 20 and further articulated in the Circular PPB-2007-6CPB-CPA (CBFA's prudential expectations on financial institutions' sound governance, Principle II, paragraph 22).</p> <p>Article 20 states that "the persons entrusted with the effective management of the credit institution, which may be the management committee, must take any necessary steps to ensure adherence to the provisions under the supervision of the statutory body [the Board]." The Article goes further to articulate the role of the Audit Committee.</p> <p>Senior management of the bank has, according to Article 20, § 5, sixth part, the duty to report, at least once a year, to the Board and the external auditor about the internal control, the internal audit function, the compliance function, the risk management function, the financial reporting and the role of the external auditor, including the follow-up of the recommendations made by the external auditor. The Banking Act requires senior management to send a copy of the report to the NBB.</p> <p>Circular letter NBB_2011_09, dated 20.12.11 details what is to be included in the self assessment by management regarding the control framework. The report has to include a descriptive part, an evaluation and a list of actions taken. A separate part of the report should cover internal controls and their evaluation of investments services and activities.</p> <p>In drafting the report, senior management must use a generally accepted methodology (NBB suggested COSO was preferred but there is no mandated approach). The Circular letter contains illustrative lay-outs of this report, detailing the areas to be discussed and when completed the report has to be sent to the NBB and the external auditor within a month after year-end.</p> <p>Once management's own assessment of the control environment is completed, the auditor will verify whether management's report is supported by sufficient documentation. The external auditor carries out a series of procedures including: obtaining a sufficient understanding of the bank and its environment and a sufficient understanding of the internal control system of the bank, a review of the minutes of the executive committee, the audit committee and the Board as well as of all documents used by senior management to draft the report, to proceed to inquiries of knowledgeable persons and to attend meetings of the Board and its audit committee. The activities of the external auditor in this</p>

	regard are set out in Circular letter CBFA_2009_19 dated 20.12.2011.
EC2	<p>The supervisor determines that banks have in place internal controls that are adequate for the nature and scale of their business. These controls are the responsibility of the Board and/or senior management and deal with organizational structure, accounting policies and processes, checks and balances, and the safeguarding of assets and investments. More specifically, these controls address:</p> <ul style="list-style-type: none"> • Organizational structure: definitions of duties and responsibilities, including clear delegation of authority (for example, clear loan approval limits), decision-making policies and processes, separation of critical functions (for example, business origination, payments, reconciliation, risk management, accounting, audit and compliance). • Accounting policies and processes: reconciliation of accounts, control lists, information for management. • Checks and balances (or “four eyes principle”): segregation of duties, cross-checking, dual control of assets, double signatures. • Safeguarding assets and investments: including physical control.
Description and findings re EC2	<p>Article 20, §1 of the Banking Law sets out the requirements for internal controls such as: organizational structure; administrative and accounting organization; control and security measures relating to electronic data processing; and an appropriate internal control. The requirements are further set out in the Circular letter D1 97/4 dated 30.06.97 about internal controls and internal audit (currently under revision to be updated) in line with the BCBS document about The internal audit function in banks)...</p> <p>The auditor’s report is received and reviewed by the NBB. It is used in the overall scorecarding approach to help make an assessment of risk management and audit functions. Supervisors will also take account of the remedial actions undertaken by management. If there is no adverse information, the external audit report will not trigger any action by the NBB. Importantly, there is no systematic verification by the NBB of the completeness or comprehensiveness of management’s self assessment or the work of the external auditor. Verification is done in the context of the off-site examinations, the on-site inspections or when periodically meeting with the external auditor and the head of the internal audit function (according to Circular letter D1 97/4 dated 30.06.97).</p> <p>While the regulations appear to be satisfactory, the process entails a self assessment process by management and certification by the auditor regarding the process. There is no positive assurance as to the design of controls or to the effectiveness of controls. It would also appear that the NBB does not conduct its own testing of the control environment.</p> <p>The external auditor, based on the report of senior management, examines the internal control measures taken by the bank and sends his/her observations to the NBB with a copy to the bank. These legal obligations are complemented by two Circular letters. In providing the report, the auditor is not required to give a positive assurance of the control environment. The Circular does not provide guidance regarding the extent of testing required to arrive at the audit opinion. Moreover, there was no automatic supervisory activity for the NBB to examine the control testing of the auditor.</p>

EC3	Laws, regulations or the supervisor place the responsibility for the control environment on the Board and senior management of the bank. The supervisor requires that the Board and senior management understand the underlying risks in their business and are committed to a strong control environment.
Description and findings re EC3	<p>When certain quantitative thresholds have been passed (balance sheet total, turn-over, number of employees), a credit institution is indeed required to set up an Audit Committee (see art. 20 §2bis, third paragraph of the Banking Law). At subsidiary level, it may be possible, under certain conditions, to obtain a waiver of this requirement in case there is an Audit committee at group level (art. 20 §2bis, fourth paragraph).</p> <p>The minimum tasks of the Audit Committee are described in art. 20 §5, second paragraph. The audit committee does not itself make decisions and must report to the Board, which then makes necessary decisions upon the recommendations of the committee.</p> <p>In the case where the credit institution must set up a Board Audit Committee or a Remuneration Committee, at least one member of these committees must be a non-executive director that meets the independence criteria as set out in art. 526ter of the Company Law Code (art. 20 § 2bis, first paragraph and §2ter, first paragraph Banking Law).</p> <p>While the NBB requires at least one independent director at the subsidiary level, as a counterweight for the group influence, it is questionable whether a single independent director is satisfactory. The requirement is in accordance with article 41 of the European Directive 2006/43/EC of 17.05.2006.</p> <p>According to the law and the related Circular letter, senior management should set up an adequate internal control system and ensure that it is assessed at least once a year. At least once a year, the senior management reports to the Board on the state of the internal control system, through the audit committee if one exists. The NBB supervises the correct implementation of these requirements via its on-site and off-site examinations.</p>
EC4	The supervisor has the power to require changes in the composition of the Board and senior management to address any prudential concerns related to the satisfaction of these criteria.
Description and findings re EC4	<p>Fit and proper powers allow for the NBB to change the composition of the Board as it has a collective element and has been expanded to extend to executive and non-executive directors. The Communication includes the Fit & Proper forms as per the CBFA 2009 20 of 8 May 2009 permits the NBB to issue an opinion regarding the reappointment of a non executive director. However, the Circular does not extend to persons who perform control functions at the highest level (compliance officer, auditor general, risk manager, appointed actuary) or senior managers and are these are therefore beyond the scope of the NBB's powers.</p> <p>Even though (see EC 8 of Principle 3), it is part of a credit institution's overall governance obligations that persons appointed to prudentially significant executive services or key functions (internal audit officer, compliance officer, risk management officer, appointed actuary, etc.) are fit and proper and have the necessary knowledge and experience. The NBB can evaluate this as well as part of overall governance supervision. The fit and proper requirements are not explicitly extended to persons outside of the directors of board, but this will be covered in the upcoming new fit and proper regulation.</p>

EC5	The supervisor determines that there is an appropriate balance in the skills and resources of the back office and control functions relative to the front office/business origination.
Description and findings re EC5	<p>Circular letter B90/1 dated 17.04.90 specifically describes how market activities should be organized, managed and followed-up. It describes the various risks including exchange risks, interest rate risk, liquidity risk, counterparty risk and country risk. The Circular emphasizes the importance of an appropriate organizational structure. Supervisory testing of implementation would come from a number of inputs: annual internal controls, external auditor report confirming management's self assessment, contact with the credit institution and onsite inspections.</p> <p>Onsite inspection would be the most effective supervisory activity in arriving at this determination but would not necessarily be performed annually for all credit institutions. Risk scorecarding will determine the onsite review cycle.</p>
EC6	The supervisor determines that banks have a permanent compliance function that assists senior management in managing effectively the compliance risks faced by the bank. The compliance function must be independent of the business activities of the bank. The supervisor determines that the Board exercises oversight of the management of the compliance function.
Description and findings re EC6	<p>Article 20, § 3, third part of the Banking Act complemented by Circular letter D1 2001/13 dated 18.12.01 on the compliance function (under revision) require all banks to have an independent and effective compliance function. The same article requires banks to elaborate an integrity policy, which is regularly updated based on a risk assessment.</p> <p>The integrity policy covers at least all relevant laws, including money laundering, financing of terrorism, fraud, discrimination, and internal codes. The compliance function ensures the effective implementation of the integrity policy of the bank.</p> <p>Banks have one compliance function under the responsibility of a member of senior management. The compliance function is responsible for compliance with all laws and regulations. The new draft Circular letter is a joint document of the NBB and the FSMA and lists the various legislation, each regulator is responsible for (e.g., money laundering is a responsibility of the NBB and rules of conduct a responsibility of the FSMA). Nevertheless, article 20, § 4 of the banking act states that there is one compliance function under the responsibility of the NBB.</p> <p>The new draft Circular letter has been published for consultation.</p>
EC7	The supervisor determines that banks have an independent, permanent and effective internal audit function charged with (i) ensuring that policies and processes are complied with and (ii) reviewing whether the existing policies, processes and controls remain sufficient and appropriate for the bank's business.
Description and findings re EC7	<p>Article 20, § 3n second part of the banking act complemented by circular letter D1 97/4 dated 30.06.97 on internal control system and internal audit function require banks to have an independent and effective internal audit function.</p> <p>The internal audit function</p> <ul style="list-style-type: none"> - provides the bank's senior management with an independent assurance about the adequacy and effectiveness of the internal control system;

	<ul style="list-style-type: none"> - has to be independent of the auditees; - covers all the activities of the bank or the banking group, including the outsourced activities; - has an unrestricted access to all staff, data and records necessary for its work; - should have sufficient qualified resources (human and others) to accomplish its missions; - should pay proper attention to training of its member ; - the head of the internal audit function has the right to contact on its own initiative the chair of the Board or of the audit committee or the external auditor when he/she believes this is in the interest of the bank. <p>The responsibilities, position, missions, authority, communication and reporting of the internal audit function are described in an internal audit charter, approved by senior management and confirmed by the Board.</p> <p>The internal audit function's methodology should include a risk based approach, work programs, working papers and written reports (including findings and recommendations) and follow up of previous recommendations.</p> <p>The supervisory practice is aligned with the legal provisions. NBB controls the correct implementation of requirements via on-site and off-site examinations.</p> <p>The circular letter will be revised to take into account the recently published BCBS document about <i>The internal audit function in banks</i>.</p> <p>At least annually, the supervisor will need to update the risk scorecard , which includes an assessment of risk management i.e., the audit function, governance and internal controls. The inputs for this assessment include: information received from the credit institution; the risk scorecard results from offsite and onsite work. However, it is not mandatory for the supervisor to perform an onsite review of a credit institution to arrive at the assessment.</p> <p>The supervisory program for credit institutions will involve a meeting with the external auditor at least annually. This meeting will provide the NBB an opportunity to gain the external auditor's insight and assessment of the internal audit function and is one way of satisfying the criterion. In the absence of the NBB meeting with the Internal audit function or thorough review of associated material, the NBB will be relying to some extent, on the views of the external auditor to satisfy this criterion.</p> <p>The onsite review that tests the control environment and performed by the NBB is arguably the most informative tool to make this assessment.</p>
EC8	<p>The supervisor determines that the internal audit function:</p> <ul style="list-style-type: none"> • has sufficient resources, and staff that are suitably trained and have relevant experience to understand and evaluate the business they are auditing; • has appropriate independence, including reporting lines to the Board and status within the bank to ensure that senior management reacts to and acts upon its recommendations; • has full access to and communication with any member of staff as well as full access to records, files or data of the bank and its affiliates, whenever relevant to the performance of its duties; • employs a methodology that identifies the material risks run by the bank; • prepares an audit plan based on its own risk assessment and allocates its

	<p>resources accordingly; and</p> <ul style="list-style-type: none"> • has the authority to assess any outsourced functions.
Description and findings re EC8	<p>There is no systematic process for the supervisor to make an assessment of the internal audit function across all banks on at least an annual cycle. The NBB may obtain the internal audit plan and will be informed of major adverse audit findings. Whilst these inputs might come to the attention of the NBB, there was no systematic supervisory process to ensure this is so for smaller banks. For the larger systemic banks, the frequency of engagement with the internal audit function was clearly apparent.</p>
Additional criteria	
AC1	<p>In those countries with a unicameral Board structure (as opposed to a bicameral structure with a Supervisory Board and a Management Board), the supervisor requires the Board to include a number of experienced non-executive directors.</p>
Description and findings re AC1	<p>The NBB strongly recommends that the Board is made of a majority of non-executive directors but this is not mandated.</p> <p>Where the financial institution has instituted a management committee, it should allocate the functions of e.g., chairman of the board of directors and chairman of the management committee to different persons, namely a non-executive and an executive director respectively.</p>
AC2	<p>The supervisor requires the internal audit function to report to an audit committee, or an equivalent structure.</p>
Description and findings re AC2	<p>The primary reporting line of the internal audit function is to senior management. Senior management has to inform the Board at least once a year about the state of the internal control system through the audit committee. This existing practice will be revised to take into account the recently published BCBS document about <i>The internal audit function in banks</i>: awaiting the formal transposition of this BCBS document, the NBB has taken a proactive approach towards principle 12 of this document.</p>
AC3	<p>In those countries with a unicameral Board structure, the supervisor requires the audit committee to include experienced non-executive directors.</p>
Description and findings re AC3	<p>Article 20, §2bis of the banking act requires states that only non-executive directors may be member of the audit committee.</p>
AC4	<p>Laws or regulations provide, or the supervisor ensures, that banks must notify the supervisor as soon as they become aware of any material information , which may negatively affect the fitness and propriety of a Board member or a member of the senior management.</p>
Description and findings re AC4	<p>This is not explicitly provided for in laws or regulations, but as part of a general transparency obligation towards the supervisor, there is an expectation that banks would do so.</p> <p>Also, the current NBB's fit and proper test is repeated every time a director must be re-appointed (which is in Belgian corporate practice usually every three to six years), so</p>

	<p>regular re-assessment is done in practice.</p> <p>As mentioned under EC 8 of principle 3, the NBB's fit & proper policy is under review and an ongoing reporting obligation around the fit & proper character is envisaged.</p>
Assessment of Principle 17	Largely Compliant
Comments	<p>The NBB will perform a variety of supervisory activities on a risk-based protocol (e.g., off-site examinations, the on-site inspections or meeting with the external auditor and the head of the internal audit function). However, there is no fixed or mandated frequency of onsite examinations by the NBB to test the effectiveness of the control environment for all banks. These issues are however recurring themes of the NBB's supervision. Indeed, it is apparent that for the larger systemic banks assessment of controls and internal audit is performed regularly. For the smaller banks, the frequency is not mandated at a minimum.</p> <p>In the absence of an onsite review performed by the NBB, considerable reliance is placed on the external auditor to verify the effectiveness of the control environment. The frequency, depth and comprehensiveness of the testing of the control environment by the NBB should be mandated at a minimum frequency of annually.</p>
Principle 18	Abuse of financial services. Supervisors must be satisfied that banks have adequate policies and processes in place, including strict "know-your-customer" rules, that promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, for criminal activities.
Essential criteria	
EC1	Laws or regulations clarify the duties, responsibilities and powers of the banking supervisor and other competent authorities, if any, related to the supervision of banks' internal controls and enforcement of the relevant laws and regulations regarding criminal activities.
Description and findings re EC1	<p>AML/CFT obligations of financial institutions are defined by the Law of 11 January 1993 on the prevention of the use of the financial system for money laundering and terrorism financing and modified by the Laws of 18 January 2010 and 26 November 2011, the Programme Law (I) of 29 March 2012 and the Royal Decrees of 6 May 2010, 3 March 2011 and 2 June 2012.</p> <p>The rules on practical enforcement of that Law were defined, for the financial sector, by the Regulation of 23 February 2010 of the Banking, Finance and Insurance Commission on the prevention of money laundering and terrorism financing approved by the Royal Decree of 16 March 2010.</p> <p>As regards coercive measures and sanctions in the field of AML/CFT, the provisions were described in § 512 of Belgium's REM of June 2005.</p>
EC2	The supervisor must be satisfied that banks have in place adequate policies and processes that promote high ethical and professional standards and prevent the bank from being used, intentionally or unintentionally, for criminal activities. This includes the prevention and detection of criminal activity, and reporting of such suspected activities to the appropriate authorities.

Description and findings re EC2	<p>Since 1 April 2011 the NBB is charged with the regulation, monitoring and sanctioning as regards AML/CFT for credit institutions as well as stockbroking firms, insurance undertakings, settlement institutions and institutions equivalent to settlement institutions, payment institutions and electronic money institutions.</p> <p>The NBB has a range of processes at its disposal to become satisfied with banks risk management for this Principle: offsite analysis; onsite reviews; meetings with internal and external auditors; meetings with compliance officers/MROs etc. A systematic supervision plan for all credit institutions was not evidenced, which would help determine how the supervisory tools are deployed in a risk-based approach. In a situation where an onsite review or meeting with auditors is not performed, the NBB will rely on information such the annual activity reports submitted by the senior management of the financial institution (per Article 35 § 4, of the CBFA regulation of 23 February 2010).</p> <p>Where the NBB deems necessary, credit institutions are required to submit off-site reporting on particular occasions. When the 2010 rules were put in place all banks were required to report on the transition to new rules with escalation of process where answers were unsatisfactory. A further review of compliance is planned for December 2012. The NBB has also undertaken special reviews acting on information received from the financial intelligence unit.</p> <p>It was not evidenced from the review that the NBB had performed an assessment of transition plans for compliance with the new rules systematically across the population of banks to become satisfied with the adequacy of policies and processes to satisfy Principle 18.</p>
EC3	<p>In addition to reporting to the financial intelligence unit or other designated authorities, banks report to the banking supervisor suspicious activities and incidents of fraud when they are material to the safety, soundness or reputation of the bank.</p>
Description and findings re EC3	<p>Financial institutions are not required to transmit a copy of all suspicious transactions that are sent to the CTIF/CFI in accordance with the Law of 11 January 1993 on AML/CFT to the NBB. The minimum reporting requirements for reporting is the annual activity report of the AML officer.</p> <p>However, under Article 39, § 2, of that Law, the competent supervisory authorities "<i>may require from the organizations and individuals subject to their supervision (...) all the information they deem appropriate as regards the manner in which these organizations and individuals implement Articles 7 to 20, 23 to 30 and 33.</i>" Similarly, Article 46, paragraph 4, of the Banking Law of 22 March 1993 states that "<i>the Bank may ask for information about the financial positions and transactions of credit institutions, and also about the way in which they are organized and operate.</i>" These provisions also apply to suspicious transaction reports submitted to the CTIF/CFI.</p> <p>In the absence of immediate reporting requirements to the NBB of suspicious transactions, the NBB must rely on other sources of information to become aware of situations where a particular financial institution fails to correctly comply with its reporting obligations, which may inhibit the NBB's ability to react quickly and enforce prompt corrective action.</p> <p>The CTIF is obliged to inform the NBB in all cases where a bank has failed to comply with reporting obligations. The NBB is obliged to inform the CTIF when it imposes a sanction related to a failure to report.</p>

EC4	<p>The supervisor is satisfied that banks establish “know-your-customer” (KYC) policies and processes, which are well documented and communicated to all relevant staff. Such policies and processes must also be integrated into the bank’s overall risk management. The KYC management program, on a group-wide basis, has as its essential elements:</p> <ul style="list-style-type: none"> • a customer acceptance policy that identifies business relationships that the bank will not accept; • a customer identification, verification and due diligence program; this encompasses verification of beneficial ownership and includes risk-based reviews to ensure that records are updated and relevant; • policies and processes to monitor and recognize unusual or potentially suspicious transactions, particularly of high-risk accounts; • escalation to the senior management level of decisions on entering into business relationships with high-risk accounts, such as those for politically exposed persons, or maintaining such relationships when an existing relationship becomes high-risk; and <p>clear rules on what records must be kept on consumer identification and individual transactions and their retention period. Such records should have at least a five year retention period.</p>
Description and findings re EC4	<p>In the 2005 mutual assessment of Belgium, the FATF deemed the procedures in place in the Belgian financial sector to be largely compliant with Recommendation 5 (know-your-customer), including measures for identification and verification of identity of customers and beneficial owners and the exercise of due diligence in respect of business relationships and occasional transactions. The existing provisions were also deemed to be largely compliant with Recommendation 6 (PEPs).</p> <p>The requirement of written reports relating to unusual transactions and the obligation to submit these reports to the AML/CFT officer in the financial institution were described in Belgium’s 2005 REM (see in particular §§ 335, 338, 341 and section 3.6.1). The FATF deemed the mechanisms for monitoring the operations and business relationships to be fully compliant with Recommendation 11 (unusual transactions).</p> <p>As regards the group approach, the FATF deemed the system in place in the financial sector to be largely compliant with Recommendation 22.</p> <p>Article 16, § 2, of the Law of 11 January 1993 on preventing use of the financial system for purposes of money laundering and terrorist financing requires that; "... credit institutions ... set up a coordinated program and introduce a coordinated structure and coordinated procedures for the entity they form with their subsidiaries and branches regarding their obligations with respect to the prevention of money laundering and terrorist financing."</p> <p>The 2010 regulation, incorporates by reference the BCBS "Consolidated Know Your Customer Risk Management" paper dated of October 2004 (introduction to section 10.3.2).</p> <p>The Circular requires each financial group with a Belgian parent to develop a global AML/CFT risk management program that must be effectively implemented by each entity of the group; to include, <i>inter alia</i> the client identification process and the customers acceptance policy;</p>

	<p>The Circular requires the CDD and customers acceptance standards defined at the group level must provide for a coherent assessment of the risks associated to the customer regardless the entity of the group , which enters into business relationship with that customer. This includes a coherent risk classification allowing the identification of higher risks [nb. i.e., higher risks customers (i.a., but not exclusively, PEPs) and of higher risk business relationships (i.a., but not exclusively, correspondent banking relationships)], as well as a coherent implementation through all the group of specific rules regarding the review of customers applications and the decision to enter into a relationship. (Section 10.3.2.2.1)</p> <p>The Circular requires the AML/CFT program at group level must allow a coherent on-going monitoring of transactions and business relationships through the entire group, based on a coherent definition of major risk criteria, as well as coherent processes and procedures regarding the analysis of unusual transactions and the decision to be taken in respect of such transactions. (Section 10.3.2.2.2). The Circular states that it is also the responsibility of the Belgian parent company to verify, including through on-site visits by the group internal audit department, that these measures are effectively implemented by each branch and subsidiary abroad (Section 10.3.2.2.3).</p> <p>The Circular also requires that groups develop an adequate framework to allow the exchange within the group of all information that is relevant for an effective implementation of the group's AML/CFT program. (Section 10.3.2.2.4)</p> <p>While Belgian AML/CFT Law does not apply directly to foreign branches and subsidiaries, (these branches and subsidiaries being submitted in first instance to their local Law and Regulation in this matter), it is expected that the Belgian mother companies ensure that their branches and subsidiaries abroad effectively implement preventive measures that are at least equivalent with those that are required by the Belgian Law and Regulation (section 10.3.2.1).</p>
EC5	<p>The supervisor is satisfied that banks have enhanced due diligence policies and processes regarding correspondent banking. Such policies and processes encompass:</p> <ul style="list-style-type: none"> • gathering sufficient information about their respondent banks to understand fully the nature of their business and customer base, and how they are supervised; and • not establishing or continuing correspondent relationships with foreign banks that do not have adequate controls against criminal activities or that are not effectively supervised by the relevant authorities, or with those banks that are considered to be shell banks.
Description and findings re EC5	<p>According to article 12, § 4, of the Belgian AML/CFT law, credit institutions that engage in cross-border correspondent banking relationships with respondent institutions from third countries shall:</p> <ul style="list-style-type: none"> • gather sufficient information about the respondent institution in question to understand fully the nature of its business and to determine from publicly available information its reputation and the quality of the supervision to which it is subject;

	<ul style="list-style-type: none"> • assess the respondent institution's anti-money laundering and anti-terrorist financing controls; • obtain approval from a sufficiently senior management level before establishing new relationships; • document in writing the respective responsibilities of each institution; • with respect to payable-through accounts, be satisfied that the respondent institution has verified the identity of and performed ongoing due diligence on the customers having direct access to accounts of the correspondent and that it is able to provide relevant customer due diligence data to the correspondent institution, upon request. • They shall not enter into or continue a correspondent banking relationship with a shell bank and shall take appropriate measures to ensure that they do not engage in or continue correspondent banking relationships with a bank that is known to permit its accounts to be used by a shell bank. <p>The regulations satisfy the criterion for enhanced due diligence policies and processes regarding correspondent banking. The supervisory activities perform a comprehensive assessment of the due diligence policies and processes was not evidenced during the review.</p>
EC6	The supervisor periodically confirms that banks have sufficient controls and systems in place for preventing, identifying and reporting potential abuses of financial services, including money laundering.
Description and findings re EC6	<p>Compliance with requirements to have such controls in place forms part of the off-site monitoring and of the on-site inspection program. The NBB has demonstrated that it undertakes detailed examinations of this are of concern while on-site. As described above, periodic off-site reporting has also been undertaken.</p> <p>It is unclear how monitoring of compliance is done for those small banks that are subject only infrequently to on-site inspections.</p>
EC7	The supervisor has adequate enforcement powers (regulatory and/or criminal prosecution) to take action against a bank that does not comply with its obligations related to criminal activities.
Description and findings re EC7	<p>According to Article 40 of the Belgian AML/CFT Law, the NBB may, in case of non-compliance by financial institutions with Articles 7 to 20, 23 to 30 and 33 of this Law, with Regulation (EC) No 1781/2006 of the European Parliament and of the Council of 15 November 2006 on information on the payer accompanying transfers of funds or with their implementing decrees:</p> <ul style="list-style-type: none"> • publish, in accordance with terms it determines, the decisions and measures it shall adopt; and • impose an administrative fine of not less than EUR 250 and not more than EUR 1 250 000. <p>The AML/CFT Law explicitly states that this specific sanction power is additional to the measures laid down by other laws or regulations. The NBB can thus use all its enforcement powers as laid down by the Law of 22 March 1993 in case a credit institution fails to comply with the AML/CFT legal or regulatory requirements.</p>

EC8	<p>The supervisor must be satisfied that banks have:</p> <ul style="list-style-type: none"> • requirements for internal audit and/or external experts to independently evaluate the relevant risk management policies, processes and controls. The supervisor must have access to their reports; • established policies and processes to designate compliance officers at the management level, and appointed a relevant dedicated officer to whom potential abuses of the bank's financial services (including suspicious transactions) shall be reported; • adequate screening policies and processes to ensure high ethical and professional standards when hiring staff; and <p>ongoing training programmes for their staff on KYC and methods to detect criminal and suspicious activities.</p>
Description and findings re EC8	<ul style="list-style-type: none"> • The internal controls and internal audit function as contemplated under CP 17 also cover the AML/CFT measures in place. • By virtue of Article 18 of the Law of 11 January 1993, "the organizations and individuals subject to supervision (...) shall appoint one or more persons in charge of implementation of this Law within their organization or profession. These persons shall be responsible primarily with the implementation of the measures and procedures referred to in Articles 16 and 17 as well as the examination of written reports prepared in accordance with Article 14, § 2, so as to adopt, if necessary, measures as required under Articles 23 to 28." • According to Article 17, second indent, of the AML/CFT Law, the institutions and persons subject to that law shall introduce appropriate procedures upon recruitment or appointment of their employees, or upon appointment of their representatives, to verify whether they show appropriate reliability depending on the risks associated with the tasks and duties to be carried out. • According to Article 17, first indent, of the AML/CFT Law, the institutions and persons subject to that law shall take appropriate measures to make their employees and representatives aware of the provisions of this Law. These measures include the participation of their employees and representatives in special training programmes to help them recognize transactions and facts that may be related to money laundering or terrorist financing and to instruct them on how to proceed in such cases.
EC9	<p>The supervisor determines that banks have clear policies and processes for staff to report any problems related to the abuse of the banks' financial services to either local management or the relevant dedicated officer or to both. The supervisor also confirms that banks have adequate management information systems to provide managers and the dedicated officers with timely information on such activities.</p>
Description and findings re EC9	<p>In addition to the text in EC8, banks are required to develop and implement adequate first line (i.e., ex ante and human) monitoring and second line (i.e., ex post and automated) monitoring of all transactions and business relationships allowing the detection of "atypical" transactions and the filling of internal written reports to the AML/CFT officer who his responsible for the analysis of these reports and the determination if transactions concerned are suspicious in the sense of the law and need to be reported to the FIU.</p> <p>In the framework of the "first line monitoring" system that banks are required to implement, staff members who become aware that a transaction is atypical are required to fill an internal written report to the AML/CFT officer. The latter must have access to all needed information allowing him to conduct his analysis of these transactions and to determine if the transaction is suspicious and if a suspicious transaction report must be</p>

	<p>filled with the FIU.</p> <p>It was not evidenced that the supervisor had a process in place to systematically review banks' policies and processes to satisfy this criterion across the banking population.</p>
EC10	Laws and regulations ensure that a member of a bank's staff who reports suspicious activity in good faith either internally or directly to the relevant authority cannot be held liable.
Description and findings re EC10	Article 32 of the Law of 11 January 1993 on AML/CFT explicitly provides that no civil, criminal or disciplinary proceedings may be instituted nor any professional sanctions imposed against persons or organizations referred to in the Law, or against their managers, employees or representatives, on the basis of a suspicious transaction report to the CTIF/CFI made in good faith.
EC11	The supervisor is able to inform the financial intelligence unit and, if applicable, other designated authority of any suspicious transactions. In addition, it is able, directly or indirectly, to share with relevant judicial authorities information related to suspected or actual criminal activities.
Description and findings re EC11	<p>Article 31 of the Law of 11 January 1993 on AML/CFT states that <i>"the supervisory authorities referred to in Article 39 who find in the course of inspections they perform with organizations and individuals within their jurisdiction, or in any other manner, facts that could be related to money laundering or terrorism financing, are required to immediately notify in writing or by electronic means the Belgian Financial Intelligence Processing Unit."</i></p> <p>Professional secrecy provisions imposed on the bank, its managers and its employees (see the answer provided as regards principle 1.6) do not apply where they are called upon to testify in court.</p>
EC12	The supervisor is able, directly or indirectly, to cooperate with the relevant domestic and foreign financial sector supervisory authorities or share with them information related to suspected or actual criminal activities where this information is for supervisory purposes.
Description and findings re EC12	The mechanisms as regards cooperation with foreign counterparts are described in paragraphs 829-836 of REM 2005.
Additional criteria	
AC1	If not done by another authority, the supervisor has in-house resources with specialist expertise for addressing criminal activities.
Description and findings re AC1	[This was not able to be fully assessed during the time of the assessment.]
Assessment of Principle 18	Largely Compliant
Comments	The IMF (Mr. Richard Lalonde, Legal Department), the FATF and the Belgian delegation agreed previous to the on-site visit of the assessment team that this FSAP examination would not include a comprehensive assessment of the AML/CFT measures in place. These measures will be assessed by the FATF against its new 40 Recommendation in the fall of 2014. As agreed, the assessment of CP18 is thus based on succinct information.

	Several criteria in Principle 18 require the supervisor to confirm that banks have sufficient controls and systems in place for preventing, identifying and reporting potential abuses of financial services, including money laundering etc. It was not sufficiently evidenced that the supervisor had a systematic process to verify adequacy of risk management across the population of banks.
Principle 19	Supervisory approach. An effective banking supervisory system requires that supervisors develop and maintain a thorough understanding of the operations of individual banks and banking groups, and also of the banking system as a whole, focusing on safety and soundness, and the stability of the banking system.
Essential criteria	
EC1	The supervisor has policies and processes in place to develop and maintain a thorough understanding of the risk profile of individual banks and banking groups.
Description and findings re EC1	<p>The NBB employs a Supervisory Review and Evaluation Process (SREP) which is a comprehensive system building on multiple inputs to assess the risk profile of an institution and to determine the appropriate supervisory actions that should flow from that analysis.</p> <p>The SREP builds on a range of information inputs which include:</p> <ul style="list-style-type: none"> • direct supervisory reporting from the firm; • reports from the external auditors (see also CP17); • the credit institution's Internal Capital Adequacy Assessment Process (ICAAP); • direct supervisory contact between the firm and the NBB. <p>The SREP focuses on the institution's exposure to risks, the adequacy of an institution's risks identification, measure and monitoring processes, the adequacy of an institution's own funds and capital resources, and compliance with prudential regulations and requirements. Quantitative and qualitative assessment of risks as well as their management by institutions are an essential component of the SREP. Analysis of all risk components is supported by a structured "scorecarding" approach (see EC3).</p> <p>On the basis of the analysis of the scorecard, the ICAAP and stress tests the NBB concludes on a final assessment of the firm's risk profile and devises the supervisory actions that are needed including the capital decision for the entity or group. In the case of groups that are active within the EU there will be joint decisions made on the capital adequacy of the group and its component entities as required by the CRD (2006/48/EC as revised). Of the four systemic firms in Belgium, the NBB is the host supervisor of two and the home supervisor for two.</p> <p>The assessors discussed the process, reviewed documents, which illustrated the process and discussed the supervisory process with individual banks.</p>
EC2	The supervisor monitors and assesses trends, developments and risks for the banking system as a whole. The supervisor also takes into account developments in non-bank financial institutions through frequent contact with their regulators.
Description and findings re EC2	A global assessment of risks and trends for the banking sector is carried out and is mainly performed by the Prudential Policy and Financial Stability department. Regular horizontal analysis is performed on various risks and issues (such as liquidity risks, capital, market risks

	<p>or business models). These analyses are also supported by peer reviews when data are available. Example of recent studies are: sovereign risks (global risk, solvency by comparing PDs and LGD of banks for these exposures, accounting methods), credit risks and in particular corporate risks and interest rate risks. These analyses are regularly presented to the NBB Board, which decides upon policy actions if risks are considered to be significant. These horizontal analyses complement the vertical analysis performed by the operational department, which aims at assessing the risk of individual institution.</p> <p>Furthermore, the internal NBB architecture has developed a broader framework for risk assessment through the introduction (July 2011) of two new committees - the Risk Committee and Macro-Financial Committee. The objective of the new committees is to enhance the quality of the risk based dimension of supervision by taking into account the macro and micro dimension and their interaction.</p> <p>The main objectives of the Risk Committee are to: (i) provide the Board with advice on relevant regulatory and supervisory issues; (ii) foster cooperation and create synergies among the prudential departments, by directing or steering the analysis of horizontal teams and (iii) provide horizontal analysis on different risks such as liquidity, accounting or solvency (based on input from the risk teams). The RC also acts as a key point between the Board and the risk teams of experts, which have been created within the prudential departments, and the RC can act as a "project manager" for longer term projects (additional monitoring tools are being developed).</p> <p>The Macro-Financial Committee (MFC) seeks to foster the interaction and the synergies between the core central bank activities of the NBB and supervision. In particular, the objectives of the Macro-financial Committee are (i) to enhance the cooperation and create synergies in the field of macro-prudential surveillance among different NBB departments, in particular, Research, Statistics, Financial Markets and prudential policy department, the department of microeconomic information and International and Eurosystem Coordination; (ii) to enhance the exchange of information in particular on macro-financial development on a cross border basis with jurisdictions , which are of particular relevance to Belgian financial institutions and on issues , which may affect financial stability; and (iii) to provide the Risk Committee and the Board of Directors with information on new macro-financial risks and suggest areas of future analysis.</p> <p>Analysis and risks identified in the MFC are communicated to the prudential departments, for example regular country analyses. While it is recognized that it can be very challenging to translate analysis of the macro-environment into concrete policy actions, this is the objective of the MFC. To date there have been tangible outputs from the MFC in a number of areas, such as stress testing of specific risks, country exposures and business models.</p> <p>Working together, the common objectives of the RC and MFC are to determine, each year, the main risks to financial stability, which need to be analyzed by the prudential departments (in essence a "top-down" prioritization). This objective is the newly introduced annual "Risk Review." Issues, which have been identified for the coming year include: real estate, liquidity, interest rates, slow growth. Secondly the committees are to develop macro-prudential policies.</p> <p>The main trends, developments and risks of the Belgian financial system are summarized in the NBB's annual Financial Stability Review.</p>
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	Discussion with NBB staff indicated that the introduction of the RC and MFC had been valuable in identifying issues that previously would not have surfaced in a timely manner.
EC3	The supervisor uses a methodology for determining and assessing on an ongoing basis the nature, importance and scope of the risks to which individual banks or banking groups are exposed. The methodology should cover, inter alia, the business focus, the risk profile and the internal control environment, and should permit relevant comparisons between banks. Supervisory work is prioritized based on the results of these assessments.
Description and findings re EC3	<p>The structured analysis of risks under the SREP is provided by the <i>scorecarding</i> system. This system creates the underpinning framework that supports the documentation of assessments and structured dialogue with institutions, their accredited external auditors and other relevant prudential authorities. The overall risk assessment, to which the scorecarding contributes, forms the foundation of prioritizing prudential activity and allocation of resource.</p> <p>Three scores are applied to each institution: (1) an impact score representing the importance of an institution and its activities to the Belgian financial system, (2) a risk score representing the risk profile of an institution and (3) a score representing the quality of an institution's shareholder including their capacity (or will) to support the institution. Supervisory planning takes all three of these scores into account. The scorecarding approach itself provides the detailed structured analytics to develop the specific global risk score for each institution and group.</p> <p>An institution's risk score draws together an analysis of four main elements:</p> <ul style="list-style-type: none"> • the overall environment of the institution, (ie governance and financial position); • the horizontal control and support functions, such as the internal audit, compliance and risk management functions; • the risks inherent in the institution's activities; and • the institution's internal process of assessing its capital needs (ICAAP). <p>The <i>scorecarding</i> process has the following objectives:</p> <ol style="list-style-type: none"> 1. To summarize prudential analyses and risk assessments; 2. To define the risk profile of institutions; and 3. To help prioritize prudential actions and resource allocation. <p>A set of instructions and guidance (methodology and guidance on individual risks and control aspects of the firm) supports the consistency of application of the scorecarding process within the supervision teams.</p> <p>Inputs into the scorecarding approach are: individual risks (weighted according to materiality for the firm); the environment (e.g., governance, financial ratios, economic context); firm-wide factors (e.g., audit, compliance, risk management); and the ICAAP itself. All individual scores are weighted and aggregated, feeding into a global score.</p> <p>The scorecard system was designed so that it also complies with the stipulations of the European Banking Authority (EBA) on joint analysis of the risks of cross-border institutions, as laid down by Article 129(3) of European Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions.</p>

	<p>A scoring scale covering both quantitative assessment of the level of risks and qualitative aspects of the quality of management control is applied. If the level of risk or quality of control is, for some reason, unknown, it is assigned a level “3” score, which could trigger prudential actions to remedy the lack of information.</p> <p>There is an annual validation process before the information contained in the scorecarding system is archived (at this point it is a historical, point in time, reference for the risk profile of the institution) and the next scorecard is opened. Indeed the next scorecard cannot be opened until the previous one has been validated and archived. The validation process takes place at the end of the calendar year and involves peer group checking at peer group and divisional level (ie more than one layer of hierarchy) to obtain a clear view on consistency of approach.</p> <p>Together with the review of the ICAAP and stress tests, the output of the scorecarding process feeds into the overall risk assessment of the institution and is the basis on which supervisory actions will be determined and planned. Within the EU joint decisions are now made for the capital adequacy of groups and the individual solo entities within the group. The final capital decision must be approved by the NBB board. In the context of the joint EU decision making process, the various competent authorities are encouraged to reach a joint decision. This means that the overall group decision is made by the NBB for consolidated groups. In these scenarios, a member state with an incorporated entity always has the right to make the final decision, even if not agreed by the college. However, the EU directives have created mediation mechanisms and also introduced a requirement to have regard to the impact of an individual capital decision on the stability of other group entities and neighboring jurisdictions.</p>
EC4	The supervisor confirms banks’ and banking groups’ compliance with prudential regulations and other legal requirements.
Description and findings re EC4	This confirmation is performed in the context of the SREP, which as noted in EC1 has a range of inputs, including both off-site assessment and focused on-site activity with the supervised institutions. A major component of supervisory assessment of prudential and legal compliance is the annual submission of the institution’s self assessment of the quality of its internal controls. (Note that the external auditors must give an opinion on the completeness and accuracy of this report – please see CP17 and EC1 of CP20).
EC5	The supervisor requires banks to notify it of any substantive changes in their activities, structure and overall condition, or as soon as they become aware of any material adverse developments, including breach of legal or prudential requirements.
Description and findings re EC5	The NBB expects all institutions to promptly notify its supervisory contacts should major developments emerge or be contemplated. Indeed a substantive change in activities (for a systemic firm) would require approval as a strategic decision and the NBB would expect to be made aware of such changes to ensure the firm remained in compliance with Article 20 of the Banking Law. In addition, the external auditors are expected to alert the NBB should they become aware of any material breach of regulation or adverse change (please see also EC1 of CP20).
EC6	The supervisor has an adequate information system, which facilitates the processing, monitoring and analysis of prudential information. The system aids the identification of areas requiring follow-up action.

Description and findings re EC6	<p>Data that is reported to the NBB by firms is collected, sorted and subjected to validation tests before it is fed into the “Bank Performance Report (BPR).” The BPR is an in-house IT tool, processing all standardized, quantitative information collected from firms. It allows off-site monitoring of firms’ financial position, performance and risk s (including liquidity) and is thus the interface NBB staff use to access, analyze and manipulate prudential data.</p> <p>The BPR comprises:</p> <ul style="list-style-type: none"> • A series of basic indicators, such as ROE, ROA, Cost/Income ratio, interest margin • A series of pre-defined tables (calculated automatically from reported information) , which examine a range of supervisory elements, including under Solvency: Basel Pillar 1 and 2 risks - e.g., credit, market, concentration liquidity and interest rate risk; and under Financial: Global activity, securities portfolio, loans and advances, funding, derivatives, profitability, financial assets impairments, financial instruments. These tables automatically highlight breaches of regulatory thresholds. • Pre-defined dashboard, providing an overall picture of the firm with key figures on performance, financial and solvency <p>The BPR system permits analysis by entity, by risk, by peer group, over time (identifying trends or new developments) and a considerable degree of flexible manipulation of data is possible. Be-spoke templates can be created by staff using Excel to create ad hoc analysis or reports and such templates can be saved.</p> <p>There is a shared (“ecorporate”) database for banks, their external auditors and the NBB, which houses a number of qualitative reports such as the external auditor reports, the internal control reports and information on the quality of shareholders. This shared database provides an easy monitoring tool to ensure that the reports held are updated in a timely manner.</p> <p>The Scorecarding database contains all the files (solo and consolidated basis) of firms’ individual scorecards. The database receives an automatic feed of prudential data that updates the quantitative components of the relevant risk cards and which proposes a risk score. The analyst can over-ride this score but should provide justifications for doing so (such information is input and held within the data base).</p> <p>The database is flexible and can be interrogated for peer analysis or for the update and analysis of an individual entity. In other words, the scorecarding application can produce bespoke reporting documents to provide feedback on the risk profile of a given institution for a peer group or industry sectoral group. Equally, the database can deliver “global” assessment card or individual assessment cards (by risk element/theme). Finally, the scorecarding application produces a benchmark table.</p> <p>The scorecarding application does not provide an automatic prompt for regular updating, although the date at which a scorecard was last refreshed is held on the system. It is intended that scorecards should be updated regularly and at the very least in preparation for a major supervisory activity such as college of supervisor work on a joint capital assessment, or following an on-site inspection by NBB staff.</p>
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	<p>A dashboard has recently been designed in order to provide an overview of an institution's risk profile, its position amongst its peers and the wider industry.</p> <p>The existing supervisory tools provide considerable scope for a wide range of information to be interrogated both on a horizontal view across the system at a point in time or for a more "through time" historical analysis for trend analysis. However, the NBB has identified a number of enhancements to its supervisory tools, which it wishes to put in place. To this end it has embarked on a program ("PRIME") with a range of key projects including in particular, "Risk profiles" the next generation scorecarding (new IT environment but also more advanced analytical underpinning) and the development of a "Macrodashboard" which will better integrate micro and macro prudential data. Additionally the project will make the NBB ready for and support the integration of new reporting required by the incoming changes to regulation of CRD4 and Solvency 2.</p>
Additional criteria	
AC1	The supervisor employs a well defined methodology designed to establish a forward-looking view on the risk profile of banks, positioning the supervisor better to address proactively any serious threat to the stability of the banking system from any current or emerging risks.
Description and findings re AC1	Although there are no specific "forward looking" or "early warning" indicators, the methodologies and processes mentioned above under EC1 to EC3 are intended to provide a forward-looking perspective upon which pro-active supervision can be built, for example by seeking to pay attention to the development of trends (in risk exposure and management control).
Assessment of Principle 19	Compliant
Comments	<p>The supervisory staff of the NBB are conducting an excellent quality of supervision. Staff demonstrated a strong command of their portfolios, a view which was reinforced by the banks the Assessors met with. A sample review of analyses and reports by the NBB supervisors indicated that thorough and professional work is being undertaken.</p> <p>Supervisory resource is allocated on a risk based principle taking into account three key factors: the impact of failure of a firm, the risk of failure of a firm and the strength of potential shareholder support. A sound analytical framework to understand the risks of the institutions, ie the risk of failure, is in place (the scorecarding methodology). This methodology distinguishes between an assessment of the inherent risk and the quality of the management or control of that risk. This approach represents best practice.</p> <p>Nevertheless, in order to better differentiate the degree of risk in the institutions, the NBB is looking to develop its risk analytics more deeply in two particular dimensions. First, to improve the quality of risk analysis itself topic by topic (whether, for example, interest rate risk in the banking book or strategic risk) and upgrade the guidance available to the supervisors to assist their risk assessment. Secondly, upgrading of the IT system as part of the "PRIME" project will permit an even more flexible interrogation of the data held in the system and may promote a more systematic approach to updating the scorecard assessments following any supervisory action or interaction with the institution. Both of these developments have the scope to assist in making the NBB risk approach more forward looking and its supervisory planning more effective.</p>

	<p>It was noted that the global risk assessments for group included insurance risk (for groups where this was relevant). This finding was encouraging as this approach is not yet standard in all supervisory authorities. As yet there is no systematic scorecarding underpinning this analysis, but this is planned. Enhancements in the integration of the insurance dimension in the group assessment will be important and the NBB is urged to make progress.</p>
Principle 20	Supervisory techniques. An effective banking supervisory system should consist of on-site and off-site supervision and regular contacts with bank management.
Essential criteria	
EC1	<p>The supervisor employs an appropriate mix of on-site and off-site supervision to evaluate the condition of banks, their inherent risks, and the corrective measures necessary to address supervisory concerns. The specific mix may be determined by the particular conditions and circumstances of the country. The supervisor has policies and processes in place to assess the quality, effectiveness and integration of on-site and off-site functions, and to address any weaknesses that are identified.</p>
Description and findings re EC1	<p>NBB carries out both on and off-site activities and also makes use of examinations conducted by the external auditors of the credit institutions. It sometimes describes this approach as the “three layers.”</p> <p>On and off-site supervision falls under the banking supervision department. The off-site function is divided between the complex banking groups on the one hand and the international and domestic banks on the other hand. At the time of the mission the assessors were informed that the supervisory department had approximately 86 staff of which 35 were allocated to non-systemic firms. This includes a separate inspection team, headed by a coordinator, for work in all credit institutions. At the time of the mission, only approximately 10 staff were available in this team, due to 3 vacancies and the past transfer of several staff members in order to strengthen the supervisory teams of complex banking groups. Additional contribution comes from two complementary inspection teams, operating from a different, horizontally based, prudential department (“specific operational functions for prudential supervision”), and specializing in IT audits and risk models.</p> <p><u>Off-site</u></p> <p>There is an annual supervisory plan for each institution, based on the risk assessments and which is updated to reflect any significant development in the risk profile of the institution. The supervisory planning process starts at the beginning of the year with the “opening” of the new scorecard (the previous scorecard having been validated and archived – see EC3 of CP19).</p> <p>Off-site supervision is organized through multidisciplinary teams composed of a coordinator, a financial risk analyst (with one or more deputies), and an institutional specialist (with one or more deputies). The coordinator is responsible for the coherent planning and timely execution of supervisory activities, coordinating not only within the NBB and other relevant supervisory authorities but with the credit institution’s internal and external auditor. The financial analyst(s) conducts the financial risk assessments and institutional specialist(s) is responsible for the institutional/legal aspects and non-financial risks of the institution. A supervisory team for a systemically important group would typically have a dedicated team of 5-6 individuals. There is a single team and single</p>

	<p>coordinator for the systemically important institutions, but the mid-size and smaller institutions will not have dedicated teams. In this case each supervised institution will have a designated point of contact within the supervisory team.</p> <p>The off-site team is responsible for the financial analysis of the institution. A “quick look” financial analysis is required quarterly for all firms and a full (ie extensive) analysis is required at least 6 monthly for systemic firms and at least annually for non-systemic firms.</p> <p>While the multidisciplinary teams mainly work off-site they also have regular discussions mainly on-site with bank management, reflecting the nature, importance and sensitivity of the issue. Periodic contact are maintained with the chief financial and risk officers of the banks, as well as with the compliance function. The frequency of the contacts depends on the size and systemic importance of the financial institution. For the systemically significant firms, the NBB will hold quarterly meetings with main risk functions in the group management and at least annual contact with the board of the institution and with the internal audit function. In addition, the supervisory team for all firms will regularly meet with the accredited external auditor and the internal auditor of each bank.</p> <p><u>On-site</u></p> <p>The on-site function is separate from the off-site function and has dedicated full-time examiners, headed by a coordinator, who rotate between institutions in order to promote consistency of approach across the system and to promote independence of approach. The on-site team was separated out from the supervisory teams following a management decision of the NBB in July 2011.</p> <p>An annual inspection plan is drawn up – at the start of the year - on the basis of the needs of the specific supervisory teams and as demand exceeds supply, the allocation of resource has to balance the needs of firm specific risk based priorities with the need to ensure a regular periodic on-site inspection for all firms. The topics of the missions are identified by the off-site teams as a result of their supervisory analysis but the detailed design of the mission is determined by the inspectors.</p> <p><u>Auditors</u></p> <p>The Banking Law (Article 55) places an obligation on banks’ external auditors to cooperate with the supervision carried out by the NBB and as such the external auditor plays an key role in the overall supervisory approach. The law further provides (Articles 51-54) that the auditor is subject to prior accreditation by the NBB, is obliged to co-operate with the NBB and must act also as the statutory auditor.</p> <p>In practice (and as set out in a regulatory Circular), the external auditors’ role is to:</p> <ul style="list-style-type: none"> - Periodically confirm the accuracy and completeness of prudential reporting; - Give an opinion on the quality of the bank’s organization and internal control; - Check compliance with applicable laws and regulations; - Submit, when required, special reports on specific issues and situations; - Provide a timely report of any material breach of regulation or adverse change of which they become aware. <p>The assessors reviewed several examples of on-site and off-site action plans, alerts, analysis and risk assessments. They also discussed with NBB staff how the off-site and on-site programs operate together, in particular the coordination through the supervisory team meetings that review progress on supervisory actions for an institution. When an onsite</p>
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	inspection has taken place the inspector will continue to participate in the team meeting until all recommendations arising from the on-site visit have been satisfactorily concluded. It is the on-site inspector who decides on when the outstanding issues can be signed off.
EC2	The supervisor has in place a coherent process for planning and executing on-site and off-site activities. There are policies and processes in place to ensure that such activities are conducted on a thorough and consistent basis with clear responsibilities, objectives and outputs, and that there is effective coordination and information sharing between the on-site and off-site functions.
Description and findings re EC2	<p>In terms of the planning and delivery of a coherent on and off-site program of supervisory activity, coordination is expected between the inspection teams and the off-site teams. The head of the inspection team is responsible for planning and delivery (e.g., planning, reporting, coaching, and debriefing with the supervisory teams periodically on the roll out of missions).</p> <p>Planning takes place at the beginning of each year to determine how the on-site resources will be allocated. Interim reviews of mission planning are also undertaken during the year (as in 2012) to assess progress and, as necessary, take into account the constraints on the level of resources.</p> <p>The supervisory teams determine the focus of the missions, but the on-site teams design the specificities of the mission (including budget). For the systemically important institutions in particular, the identification of needs will also draw on the supervisory college discussions and joint risk assessments. Furthermore, the recently instituted annual "risk review" which identifies key risks for the financial system will also be taken into account at the planning stage. It may be noted that there are different forms of on-site missions and activity and this is discussed in more detail in EC3 below, and the processes discussed in this EC relate primarily to the first and third type of on-site visit.</p> <p>In order to promote a unified and consistent supervisory approach across different institutions and sectors and although not formally approved by the management of the NBB, internal guidance providing standards for the supervisory work of the risk teams and inspection team, documented in the handbook "ProControl," are currently under review (in the NOVA project). There is no formal model for determining the baseline frequency of on-site activity for institutions.</p> <p>In terms of practical coordination between the on and off-site functions, NBB processes support continued contact between the two teams from the preparation of the mission to the formal closing of the report (only the inspection team can sign off that recommendations flowing from their report have been satisfactorily met by the firm). Before the start of the mission, the supervisory team briefs the inspection team in order to communicate an understanding of the organization and risks of as well as any concerns regarding the bank to be examined. During the process of the inspection close contact is maintained between the inspection team and the supervisory teams, including alerts of any early findings of key importance or urgency. If wished the supervisory team can participate in the on-site work with the inspection team. The supervisory team also has the opportunity to comment on and challenge the draft report prepared by the inspection team before the report, which includes recommendations, is submitted to the bank.</p>

	<p>The follow up process after the inspection report is jointly managed between the inspection team and the supervisory team: the inspection team takes the lead in assessing the action plan submitted by the bank in response to the examination report while the supervisory team is responsible for following up the effective implementation of any corrective measures. As noted above, the report is not considered to be closed and completed until the recommendations arising from the report have been acted upon by the institution to the satisfaction of the inspection team and the inspection team will continue to participate in the formal supervisory team meetings until the inspection report is closed.</p>
EC3	<p>On-site work, conducted either by the supervisor's own staff or through the work of external experts, is used as a tool to:</p> <ul style="list-style-type: none"> • provide independent verification that adequate corporate governance (including risk management and internal control systems) exists at individual banks; • determine that information provided by banks is reliable; • obtain additional information on the bank and its related companies needed for the assessment of the condition of the bank, the evaluation of material risks, and the identification of necessary remedial actions and supervisory actions, including enhanced off-site monitoring; and • monitor the bank's follow-up on supervisory concerns.
Description and findings re EC3	<p>The NBB distinguishes between four main kinds of on-site examinations:</p> <ol style="list-style-type: none"> 1. Deep dive inspections: based on risk assessment of the bank and planned in an annual action plan (revised quarterly). 2. Thematic inspections: based on macroprudential and sectoral analyses, essentially aimed at peergroup benchmarking, explaining outliers, exploring evolutions in new risk types, or focusing on specific areas such as AML. 3. Inspections targeting specific issues or in reaction to specific information (crisis management, fraud). 4. On-site information gathering: on-site visits aiming at updating the supervisory information and assessment of the bank, its activities and risk management. <p>In other words, on-site missions can be very comprehensive in scope or highly targeted. Missions might be conducted due to a need to conduct a thematic horizontal investigation in the sector or alternatively in response to the risk assessment of the individual institution. For complex groups there are likely to be targeted missions to examine specific issues (e.g., risk management, valuation models); thematic missions (e.g., liquidity, e.g., quality of reporting or dealing rooms) and missions driven by the risk assessment of the individual institution. For other groups (domestic and international banks) prioritization is carried out on the basis of clustering analysis, on a multi-year planning cycle, thematic missions (e.g., interest rate risk, liquidity risk) or missions driven by issues identified during the risk analysis/scorecarding process.</p> <p>The most recurrent topics examined during an on-site examination are: internal governance, control functions (internal audit, compliance, risk management), qualitative and quantitative assessment of interest rate risk, credit risk, market risk, liquidity risk, operational risk, derivatives, ICAAP, supervision of commercial networks. On-site missions can be used to verify the reliability of prudential and other data that is submitted but the NBB more typically looks to the verification of financial data (including prudential data) performed by the external auditors as formally, twice a year, the accuracy and completeness of the data is confirmed by the external auditors.</p>

	<p>Broadly speaking, missions which were finalized in 2012 (a number of which began in 2011) were divided evenly between those focuses on the systemic firms and those focused on the international and domestic banks. Topics under consideration included control environment (internal controls, risk management, compliance), specific risk focused inspections (e.g., market risk, ALM).</p> <p>The NBB has also concluded, as an output of internal management review mid 2012, that moving forward it was important for inspections to be more risk focused, to put greater emphasis on testing, to be more focused in the specification of the mission and for reports to provide a greater indication of work carried out on site. These new management expectations and guidelines have already been put into place.</p> <p>The assessors reviewed samples of on-site reports.</p>
EC4	<p>Off-site work is used as a tool to:</p> <ul style="list-style-type: none"> • regularly review and analyse the financial condition of individual banks using prudential reports, statistical returns and other appropriate information, including publicly available information; • follow up on matters requiring further attention, evaluate developing risks and help identify the priorities and scope of further work; and • help determine the priorities and scope of on-site work.
Description and findings re EC4	<p>Off-site work is used to assess financial and institutional risk for each credit institution.</p> <p>The off-site teams conduct a regular risk assessment and report the analysis and findings to the supervisory team and management of the NBB, for discussion. Each institution will be assessed on an annual basis at a minimum (as required by EU law) but this can be more frequent. Typically for institutions assessed in colleges there will be at least 6 monthly updates.</p> <p>Off-site work is based on:</p> <ul style="list-style-type: none"> • Analysis of a range of data notably including (but not limited to) prudential returns (many of which are subject to OLAP ("on line analytical processing") which provides standard analysis, trends and peer group comparisons), ICAAP submission, published financial reports, reports from external auditors, annual management reports on internal controls, compliance • On-site inspection reports • Horizontal and thematic inputs and reviews conducted by the NBB • Meetings with the institutions, which in addition to regular contact with management will include contact with finance, risk management (frequency proportionate to size and systemic nature of institution); annual meetings with the internal and external auditor <p>When the analysis is performed, reports are made to the supervisory team and the management of the NBB, for discussion, to feed into the scorecarding approach (see CP19), the identification of the risk profile, and the determination of the priorities for the annual supervisory including remedial measures if necessary.</p> <p>The assessors reviewed samples of on-site reports and assessments.</p>

EC5	Based on the risk profile of individual banks, the supervisor maintains sufficiently frequent contacts as appropriate with the bank's Board, non-executive directors, Audit Committee and senior and middle management (including heads of individual business units and control functions) to develop an understanding of and assess such matters as strategy, group structure, corporate governance, performance, capital adequacy, liquidity, asset quality and risk management systems.
Description and findings re EC5	<p>Contacts with bank management, at all relevant levels, are scheduled as part of the annual supervisory plan for the individual institution. The objective is to have at least one comprehensive discussion at the highest management level a year with all banks.</p> <p>As a general principle the level at which contacts with banks take place depends largely on the nature, importance and sensitivity of the issue. For the systemically important banks, more regular contacts with the bank management are planned: there are quarterly discussions with the chief financial officers and the chief risk officers of the banks as well as bi-annual meetings with the compliance officer. In addition, regular meetings with the management or staff of the bank are organized in light of the follow-up of on-site inspections or other supervisory actions.</p> <p>For the most significant, ie systemic, firms, the NBB management will have direct contact with Board members, including non executive directors, on a formal and informal basis. In principle the head of supervision of the prudential department for banking supervision will meet the executive management of the systemic and mid-size banks at least annually. It is standard practice for the NBB to meet the chair of the audit committee. The systemic firms with whom the assessors had meetings confirmed that the NBB maintained a regular contact with them, both through on-site presence and meetings at management level. The records of supervisory activity for large and mid size firms confirm that there is a consistent pattern of meeting between the NBB and these categories of firms.</p>
EC6	On an ongoing basis during on-site and off-site supervisory activities, the supervisor considers the quality of the Board and management.
Description and findings re EC6	<p>The assessment of the quality of governance and management is one of the basic components of the annual assessment exercise made by the team: the quality of the Board and management is assessed in the yearly scorecarding approach (the quality of governance and of management control is subject to separate analysis).</p> <p>The on and off-site functions will have periodic meetings and discussions with the Board and management through the year. Irrespective of the focus of an on-site mission, the inspectors will open and close the examination with meetings with the executive management. Supporting information is gathered including the allocation of tasks between the different members of the management committee of the bank, and the minutes of the meetings of the supervisory and management bodies (Board of Directors, Audit Committee, Executive Board) and the establishment of the committees of the Board (e.g., audit, remuneration, risk management).</p>
EC7	The supervisor evaluates the work of the bank's internal audit function, and determines whether, and to what extent, it may rely on the internal auditors' work to identify areas of potential risk.

Description and findings re EC7	<p>The NBB deploys on and off-site processes to assess the work of the internal audit function of the supervised institutions. The prudential expectations regarding internal audit are based on Article 20 of the Banking Law and expanded upon in Circular D1 97/4 of 30 June 1997.</p> <p>Ultimately the assessment of the internal audit function is drawn together during the annual scorecarding analysis but this will draw on the work of the on and off-site teams. The off-site function analyzes a number of inputs including:</p> <ul style="list-style-type: none"> - The governance memorandum, which is expected to contain the audit charter and specify the location and reporting lines of internal audit within the organization of the bank. - The management report on internal controls. - The audit plan. - The AML/CFT and compliance reports. <p>Assessment of the internal audit function is a recurrent item for on-site examination, which will pay attention, among other aspects, to whether the internal audit has sufficient standing and authority within the bank. For the systemic firms, contact with the audit committee is an important and regular component of supervisory contact.</p>
EC8	<p>The supervisor communicates to the bank the findings of its on- and off-site supervisory analyses by means of written reports or through discussions or meetings with management.</p>
Description and findings re EC8	<p>The findings of the off-site supervisory process is communicated to the management of the bank through correspondence or meetings with the relevant level of management. For the systemic firms there is a regular program of contact that includes, inter alia, quarterly meetings with the chief risk officer. The NBB does not make a practice of sending an annual letter setting out the planned supervisory program for the year, but will share the output of the joint risk assessment of a firm/group with the entity in question (following the EU system of joint assessment and capital decisions). This is not an automatic process under the EU requirements but the NBB places value on transparency with the institution.</p> <p>An on-site examination is followed by a report, which will include recommendations but an information visit is followed by a letter in which recommendations for action may not be necessary. The assessors reviewed samples of letters and reports (with recommendations) sent to firms following on-site examinations.</p> <p>At the end of a non-site examination, as noted above, an informal debriefing of the findings takes place with the management, followed by a draft written report to the management. The management can comment on the report, recommendations and conclusions. The inspection team will incorporate the management's reactions in finalizing its report.</p> <p>The inspection team will also evaluate the management's proposed action plan which must be submitted to the NBB within one month of having received the final report of the NBB. A formal response to the action plan is then sent to the management and there is continuous monitoring of progress of corrective actions against the plan by the NBB until the recommendations have been concluded to the satisfaction of the supervisory team in consultation with the inspection team.</p>

Additional criteria	
AC1	The supervisor meets periodically with senior management and the Board to discuss the results of supervisory examinations and the external audit. The supervisor should also meet separately with the independent Board members, as necessary.
Description and findings re AC1	The NBB indicated that it will meet separately with independent Board members, in some institutions, depending on the level and nature of the risks concerned, in particular when issues have already emerged or where high risks have been identified. This is an important power for the NBB to have but it falls short of being a systematic practice at this time.
Assessment of Principle 20	Largely Compliant
Comments	<p>The supervision performed by the NBB comprises good quality on and off-site supervisory practices. The Assessors saw evidence, in particular, of a comprehensive supervisory approach taken toward the systemic firms. The challenge for the NBB, as it recognizes itself, however is to achieve effective “globally balanced supervisory planning” and to ensure that this extends to all institutions within its scope of supervision.</p> <p>The perception of the Assessors, confirmed in dialogue with senior NBB staff, was an absence of a systematic approach to the supervisory program that covers the entire population of credit institutions, specifically meaning the non-systemic firms. The Assessors recognize that the NBB management can and does monitor the supervisory activities within all firms at a global level and also that there is a clearly documented supervisory action plan for each individual institution and group.</p> <p>What is missing is a risk based approach to ensure that each institution systematically receives the appropriate intensity of supervisory attention proportionate to its profile. Some supervisory authorities adopt the term “baseline” supervision by which they seek to ensure that for a given overall level of risk an institution will be subject to specific, consistent supervisory practices according to a specific frequency. For example, a low risk institution might receive a comprehensive on-site inspection every 5 years while a medium risk institution might expect on-site activity to be 3 every three times. Frequency of in depth comprehensive off-site analysis (as opposed to quick checks), frequency of contact with executive management, Board, chief risk management, audit and control functions, and risk areas, frequency of comprehensive or more tailored risk visits are other examples of elements that can be built into a baseline approach. The structured plan ought also to indicate the required level of internal management reporting, so that there is a clear and shared understanding of the frequency of reporting by the prudential department to the NBB’s Board in respect of individual institutions and for relevant peer groups. Should more urgent priorities emerge for the supervisory authority, the baseline structure ought to assist in ensuring a sound risk-based approach to any necessary decisions on what activities need to be postponed and for which institutions, as well as ensuring that the Board is kept informed of the need for such actions. In other words a baseline approach can provide insights into appropriate, desired, or minimum levels of resourcing.</p> <p>The assessors consider that much of the risk-based approach inherent in a “baseline” approach is taking place de facto based on the skilled and informed senior management decisions. It is clear, for example, that there are multi-year inspection programs that have been put in place for individual institutions. It is less clear that such programs are applied</p>

	<p>consistently to all similar institutions. There is a lack of documentation and full overview to monitor and ensure that two similar institutions are indeed receiving appropriately similar supervisory attention.</p> <p>Importantly, the NBB is in the course of developing new tools that will be critical to achieving this greater structural consistency in supervisory processes, namely its work on “clustering” and on “proportionality.” The first project is designed to improve the peer group clustering on a more refined and risk-focused basis. The “proportionality” project is intended to permit adjustments to the profile of institutions in the scorecarding application on the basis of their impact/risk classification and is thus linked with the clustering project. The successful outcome of these projects, coupled with a “baseline” analysis of supervisory needs should position the NBB strongly to deliver a stable, systematic and risk-sophisticated approach to supervision.</p> <p>It is also noted that the supervisory tools supporting data and analysis of the insurance companies are also being upgraded as a separate part of the overall PRIME program. Opportunity should be taken, as is intended, to enhance the depth and integration of risk assessment of the insurance interests within banking and conglomerate groups.</p>
Principle 21	Supervisory reporting. Supervisors must have a means of collecting, reviewing and analyzing prudential reports and statistical returns from banks on both a solo and a consolidated basis, and a means of independent verification of these reports, through either on-site examinations or use of external experts.
Essential criteria	
EC1	The supervisor has the power to require banks to submit information, on both a solo and a consolidated basis, on their financial condition, performance, and risks, at regular intervals. These reports provide information on such matters as on- and off-balance sheet assets and liabilities, profit and loss, capital adequacy, liquidity, large exposures, asset concentrations (including by economic sector, geography and currency), asset quality, loan loss provisioning, related party transactions, interest rate risk and market risk.
Description and findings re EC1	<p>On the basis of the Article 44 of the Belgian Law on the supervision of credit institutions (22 March of 1993), the NBB has power to request information on a regular basis from banks.</p> <p>Banks are required to report both prudential returns , which are submitted on a quarterly basis and financial accounts , which are submitted quarterly at consolidated level, and monthly at solo level.</p> <p>The consolidated prudential reporting framework is aligned with the reporting regime referred to as Finrep (Financial reporting). This framework is based on the guideline published by the Committee of European Banking Supervisors in 2005. To assess capital adequacy both on a solo and a consolidated basis, the NBB has imposed COREP (Common reporting). This framework is based on the guidelines published by the Committee of European Banking Supervisors in 2006.</p> <p>The Corep and Finrep framework is in line with Basel II and Basel 2.5. It includes information on the composition of own funds, the capital requirements, the credit risk under SA approach or IRB approach, market risk, currency risk, settlement risk, operational risk and on large exposures. For Pillar 2 requirements, NBB has also imposed a liquidity reporting (liquidity of assets, cash in and cash out) and a concentration report covering</p>

	<p>data by economic sector and by geography. An interest rate risk report, based on different assumptions on changes of the yield curve, is also required.</p> <p>To assess the financial position of institutions on a solo basis, the NBB has imposed since 1994 its own reporting (Schema A). This reporting includes information regarding on and off balance sheets assets and liabilities, profit and loss, asset quality, loan loss provisioning, related party transactions. This framework is based on Belgian GAAP. On a solo basis, banks have to report their annual accounts using a mandatory chart , which is completed with additional information when reported to the supervisor.</p> <p>At a consolidated level, banks have to prepare their annual accounts on the basis of IFRS and there is no mandatory chart of accounts. However, for prudential purposes, the NBB requires reporting of the consolidated entity using the European FINREP standardized format.</p>
EC2	The supervisor provides report instructions that clearly describe the accounting standards to be used in preparing supervisory reports. Such standards are based on accounting principles and rules that are widely accepted internationally.
Description and findings re EC2	<p>The NBB has developed detailed instructions for each of these reporting requirements and the instructions are publically available on the website of the NBB. For Finrep (consolidated reporting), banks use IFRS. Belgian GAAP is applied for solo reporting. For Corep, either IFRS or BEGAAP is used as starting point for calculations. Instructions are also based on Basel regulation.</p> <p>The availability of different accounting methodologies does add a dimension of complexity to performing offsite analysis to understand different accounting treatments, specifically in the area of valuations.</p>
EC3	The supervisor requires banks to utilize valuation rules that are consistent, realistic and prudent, taking account of current values where relevant.
Description and findings re EC3	<p>Consolidated reporting in Finrep uses IFRS for valuation of assets. For reporting on a solo basis in Schema A, BGAAP is used and a rule of prudence is included.</p> <p>Under BGAAP, the use of market value is more limited. Derivatives other than those qualifying as hedging are measured at market value and differences between capital gains and losses are accounted for in profit and loss when there is an active market. If there is no active market only capital losses are recorded in profit and loss. For derivatives qualifying as hedge accounting, gains and loss are recorded in profit and loss on a pro rata temporis. Investment portfolios are at LOCOM (Lower of cost or market) instead of at fair value through equity as in IFRSs.</p> <p>BGAAP entails some degree of questioning whether the valuation rules are consistent, realistic and prudent and takes into account current values. Specifically, investment portfolios are valued on the basis of the LOCOM methodology , which is the lower of cost or market value. The impact of different accounting treatments between banks within the same group could potentially result in different capital and performance outcomes. The availability of different accounting methodologies for valuations does not meet this criterion.</p>

EC4	The supervisor collects and analyses information from banks at a frequency (e.g., monthly, quarterly and annually) commensurate with the nature of the information requested, and the size, activities and risk profile of the individual bank.
Description and findings re EC4	<p>The frequency for all credit institutions to submit data is consistent across the sector regardless of size, activities and risk profile. For financial information, capital adequacy and interest rate risk, the frequency is quarterly for the large majority of items. For liquidity, the frequency is monthly and for concentration it is annually. For public, information it is only mandatory on an annual basis for solo accounts based on a mandatory chart of accounts.</p> <p>The frequency for data associated with concentration risk is annual. This is one area of the data collection , which does not align with the same quarterly frequency of other material prudential data.</p>
EC5	In order to make meaningful comparisons between banks and banking groups, the supervisor collects data from all banks and all relevant entities covered by consolidated supervision on a comparable basis and related to the same dates (stock data) and periods (flow data).
Description and findings re EC5	<p>Regarding supervisory reporting, the scope and the periodicity are the same for all banks. For public information, the publication of general purpose financial statement is mandatory on an annual basis. The reporting requirements of the NBB enable a satisfactory degree of transparency across banks.</p> <p>The Corep, the Finrep and the liquidity reporting are collected for holding companies.</p>
EC6	The supervisor has the power to request and receive any relevant information from banks, as well as any of their related companies, irrespective of their activities, where the supervisor believes that it is material to the financial situation of the bank or banking group, or to the assessment of the risks of the bank or banking group. This includes internal management information.
Description and findings re EC6	Article 44 of the Belgian Law gives the NBB the power to request and receive any relevant information, including internal management information. Examples were provided to evidence that the NBB use this power to receive reporting on a higher frequency in exceptional cases. For example, the NBB has mandated daily liquidity reporting for larger systemic banks since the crisis.
EC7	The supervisor has the power of full access to all bank records for the furtherance of supervisory work. The supervisor also has similar access to the bank's Board, management and staff, when required.
Description and findings re EC7	On the basis of article 46 of the Belgian law on the supervision of credit institutions, the NBB has access to all bank records to fulfill its tasks by way of on-site inspection or off-site inspection.
EC8	The supervisor has a means of enforcing compliance with the requirement that the information be submitted on a timely and accurate basis. The supervisor determines that the appropriate level of senior management is responsible for the accuracy of supervisory returns, can impose penalties for misreporting and persistent errors, and can require that inaccurate information be amended.

Description and findings re EC8	<p>On the basis of the article 103 of the Belgian law on the supervision of credit institutions (22 March of 1993), the supervisor has the power to enforce compliance with the requirement that information be submitted on a timely and accurate basis. On basis of this article, the supervisor can impose penalties with a maximum of 2.500.000 millions of Euros or 50.000 Euros by day of delay if the information is not corrected.</p> <p>Article 44 states that the "effective management of the credit institution must declare to the Bank (NBB) that the periodic reports sent to it by the institution at the end of the first six months and at the end of its financial year, accurately reflect the accounts and inventories." In this statement, the Board is held responsible for the accuracy of the financial accounts.</p>
EC9	The supervisor utilizes policies and processes to confirm the validity and integrity of supervisory information. This includes a programme for the periodic verification of supervisory returns by means either of the supervisor's own staff or of external experts.
Description and findings re EC9	<p>For all templates included in the reporting, the NBB has defined a set of validation rules. If these validation rules are not respected, an automatic message of error is sent to the banks. NBB financial analysts regularly review the quality of the data submitted to the NBB. Examples of team meetings where the outcome from offsite analysis is discussed and outcomes agreed. The analysis looked to be of high quality.</p> <p>For the reporting transmitted at year-end and half year-end, the bank's external auditor has to inform the NBB on the results on his/her audit of the reporting (full for the annuals and limited review for half yearly).. In addition, he/she has to confirm that the reporting contains all data from the accounting records and other inventories and that the same measurement criteria as used for the annual accounts have been applied.</p>
EC10	The supervisor clearly defines and documents the roles and responsibilities of external experts, including the scope of the work, when they are appointed to conduct supervisory tasks and monitors the quality of the work. External experts may be utilized for routine validation or to examine specific aspects of banks' operations.
Description and findings re EC10	<p>Article 55, section 1, paragraph 2 of the Belgian law on the supervision of credit institutions (22 March of 1993) defines the role of the banks' external auditors.</p> <p>For the reporting transmitted at year-end and half year-end the bank's external auditor has to inform the NBB on the results on his/her audit of the reporting. In addition, he/she has to confirm that the reporting contains all data from the accounting records and other inventories and that the same measurement criteria as used for the annual accounts have been applied. A principle of materiality applies.</p>
EC11	The supervisor requires that external experts bring to its attention promptly any material shortcomings identified during the course of any work undertaken by them for supervisory purposes.
Description and findings re EC11	<p>The Banking Law states that the bank's external auditor should inform the NBB as soon as he/she becomes aware of</p> <ul style="list-style-type: none"> • decisions, facts or developments that may influence significantly the bank's financial position or its administrative/accounting system or its internal control;

	<ul style="list-style-type: none"> • decisions or facts that may indicate that the bank has infringed company law, the bank's bylaws, the banking act and its related decisions and regulations; • other decisions of facts that could lead to a refusal to certify the annual accounts. <p>A Circular letter of the NBB explaining these legal obligations has been published (it contains a list of examples of decisions/facts/developments that may be of interest to the NBB).</p>
Assessment of Principle 21	Compliant
Comments	<ul style="list-style-type: none"> • The availability of different approaches to accounting methodologies does raise the question of consistency. Largely regards a solo vs consolidated requirements and whether the NBB has regulatory requirements that are consistent. • Reporting dates for major balance sheet and risk items not aligned. For instance, there is monthly solo financial and prudential returns submitted 11 (to 25) days after end of period, however for the reporting lag for IRRBB and FINREP, COREP consolidated, concentration risk is 2.5 months. Lack of consistency in reports of data doesn't support comprehensive and timely analysis of prudential data where supervisors often become more attuned to management information. This should be addressed in the PRIME project.
Principle 22	Accounting and disclosure. Supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with accounting policies and practices that are widely accepted internationally, and publishes, on a regular basis, information that fairly reflects its financial condition and profitability.
Essential criteria	
EC1	The supervisor has the power to hold bank management and the bank's Board responsible for ensuring that financial record-keeping systems and the data they produce are reliable.
Description and findings re EC1	<p>Banking Law explicitly gives this power derived from three separate Articles of the Banking Law 1993. Firstly, Article 20, §1 of the Banking Law states that a bank should notably have: (i) an appropriate administrative and accounting system; and, (ii) an appropriate internal control system. Secondly, pursuant to the §32 of the same article, banks must have in place an appropriate internal control system that provides reasonable assurance that the process for financial reporting is reliable and that the accounts are drawn up in accordance with the applicable regulation.</p> <p>In accordance with article 44, paragraph 2, senior management must explicitly confirm that the returns reported to the NBB conform with the accounts and the inventories. Additionally, management must explicitly confirm that the information reported to the NBB conforms with the instructions given by the NBB. The references however do not mention specifically the responsibility of the board.</p>
EC2	The supervisor has the power to hold bank management and the bank's Board responsible for ensuring that the financial statements issued annually to the public receive proper external verification and bear an external auditor's opinion.
Description and findings re EC2	Article 55 of the Banking Law requires that annual and semi-annual prudential returns are verified by the external auditors. The verification consists in a full audit of the annual

	<p>reporting and in a limited review of semi-annual reporting.</p> <p>The verification is provided by the external auditor required by the Banking Law and the external auditor is licensed as a professional auditor and must also obtain a preliminary authorisation from the NBB - only auditors having this authorization may audit the financial statements of a bank (article 50 of the banking act).</p> <p>All credit institutions incorporated under Belgian Law must make available a yearly Pillar 3 report in accordance with the Title XIV of the regulation of the NBB dated 06.12.2011 implementing the CRD.</p> <p>Explicit reference in the Banking Law for the responsibility of the Board is less clear.</p>
EC3	The supervisor requires banks to utilize valuation rules that are consistent, realistic and prudent, taking account of current values where relevant, and to show profits net of appropriate provisions.
Description and findings re EC3	<p>The Royal Decree of 23.09.1992 on annual accounts of banks sets out the Belgian accounting rules (BGAAP), including measurement rules, for banks. The governance of accounting rules is articulated in Article 44 of the Banking Act). The principle of consistency, realism and prudence are covered by this Royal Decree in Articles 15 to 19.</p> <p>The accounting rules for solo are based upon BGAAP and for consolidated IFRS. The valuation principles applicable at the consolidated level are those set out in IFRS. Given that two accounting approaches are applicable it is hard to see how the goal of consistency is achieved. For example, on a consolidated basis, securities are allocated to the following portfolios: trading, loans and receivables, available for sale and held to maturity. On a solo basis, a trading portfolio at market value through profit and loss and an investment portfolio at LOCOM. Securities are classified in the investment portfolio if they are held to obtain a return in long term.</p> <p>The NBB has performed work to determine the main differences between IFRS and BGAAP. The latest review of differences between IFRS and Belgian GAAP has been made in connection with the work done within EBA on the definition of implementing measure for leverage ratios. Earlier, in March 2008, the CBFA contributed to a workshop organized with external experts on the feasibility of the application of IFRS to solo accounts. A number of differences between IFRS and BGAAP were analyzed at that occasion.</p> <p>In practice, the NBB has observed a divergence between banks in valuation of traded products, some using a mark-to-market approach and others using a mark-to-model. The example of one bank was given, which says less about the differences between IFRS and BGAAP and more about the need for clear regulatory guidance regarding appropriate valuation methodologies. This principle could be extended to the banking book also.</p> <p>The assessors would question whether it is easy to continuously understand the differences between the accounting methodologies of IFRS and BGAAP to make sense of the differences in quarterly reporting within a consolidated group.</p>
EC4	Laws or regulations set, or the supervisor has the power, in appropriate circumstances, to establish, the scope of external audits of individual banks and the standards to be followed in performing such audits.
Description and findings re EC4	Pursuant to article 55, the NBB can define further the scope of external audits of individual banks in specific circumstances, for supervisory purposes. The NBB has the powers to require a special purpose audit - see article 55, section 1, 3°. Costs have to be borne by the

	bank. The NBB has the powers to require a special purpose audit - see article 55, section 1, 3°. Costs have to be borne by the bank. The NBB was able to point to recent examples where they have exercised this power.
EC5	Supervisory guidelines or local auditing standards determine that audits cover such areas as the loan portfolio, loan loss reserves, non-performing assets, asset valuations, trading and other securities activities, derivatives, asset securitisations, and the adequacy of internal controls over financial reporting.
Description and findings re EC5	All credit institutions incorporated under Belgian Law must make available a yearly Pillar 3 report in accordance with the Title XIV of the regulation of the NBB dated 06.12.2011 implementing the CRD. In this context (accounting rules and implemented CRD), quantitative and qualitative information related to related party transactions, risk exposures, restructured loans, provisioning, and risk management practices must be disclosed.
EC6	The supervisor has the power to reject and rescind the appointment of an external auditor that is deemed to have inadequate expertise or independence, or not to be subject to or not to follow established professional standards.
Description and findings re EC6	NBB approves the external auditor and in the future after a fixed term expires the external auditor will need to be rotated. According to article 53 of the banking act, the appointment of a bank's external auditor has to be approved by the NBB. The NBB can review letters of engagements and audit contracts.
EC7	The supervisor requires banks to produce annual audited financial statements based on accounting principles and rules that are widely accepted internationally and have been audited in accordance with internationally accepted auditing practices and standards.
Description and findings re EC7	<p>Article 44 of the Banking Law, BGAAP accounting rules applicable to banks at solo level must be defined by Royal Decree that can be adopted after consultation of the NBB. On the basis of article 38 of the 1992 Royal Decree, the NBB has the power to give waivers to the application of these accounting rules. In addition, the NBB can provide guidelines on the accounting principles to be followed for the preparation and presentation of the solo prudential reporting (Schema A).</p> <p>Financial statement prepared on a consolidated basis are based on IFRS as issued by the IASB and endorsed for application in the EU pursuant to the Regulation EC 1606/2002 on the application of international accounting standards.</p> <p>There is no plan to apply IFRS on a solo basis and there is no quantitative evaluation of differences between Belgian GAAP and IFRS.</p>
EC8	Laws, regulations or the supervisor require periodic public disclosures of information by banks that adequately reflect the bank's true financial condition. The requirements imposed should promote the comparability, relevance, reliability and timeliness of the information disclosed.
Description and findings re EC8	<p>Banks are required to publish complete information in a timely and regular basis regarding their activities, financial position and performance. These disclosure requirements were adopted pursuant to EU Directives on company law and annual accounts. The requirements are basically set out in the Company Law Code (article 92 to 129) and in two specific accounting regulations applicable to bank.</p> <p>All credit institutions incorporated under Belgian Law must make available a yearly Pillar 3</p>

	<p>report in accordance with the Title XIV of the regulation of the NBB dated 06.12.2011 implementing the CRD. In this context (accounting rules and implemented CRD), quantitative and qualitative information related to related party transactions, risk exposures, restructured loans, provisioning, and risk management practices must be disclosed.</p> <p>The NBB is currently preparing a horizontal assessment of the Pillar 3 reports of some major Belgian credit institutions.</p>
EC9	The required disclosures include both qualitative and quantitative information on a bank's financial performance, financial position, risk management strategies and practices, risk exposures, transactions with related parties, accounting policies, and basic business, management and governance.
Description and findings re EC9	The requirements on general purpose financial statements and on (Pillar 3) risk report include both qualitative and quantitative information on a bank's financial performance, financial position, risk management strategies and practices, risk exposures, transactions with related parties, accounting policies, and basic business, management and governance. Banks are required to report quarterly prudential returns and half yearly accounts and a full set of annual accounts. The Internal Controls Report by management and accompanied with a report from the external auditor will comment on governance.
EC10	Laws, regulations or the supervisor provide effective review and enforcement mechanisms designed to confirm compliance with disclosure standards.
Description and findings re EC10	Banks are required to publish Pillar 3 reports annually available to the public to enhance market discipline. The reports are included in the supervisory process. Management reports and published accounts are used by the supervisor as an input into the risk scorecarding process.
EC11	The supervisor or other relevant bodies publish aggregate information on the banking system to facilitate public understanding of the banking system and the exercise of market discipline. Such information includes aggregate data on balance sheet indicators and statistical parameters that reflect the principal aspects of banks' operations (balance sheet structure, capital ratios, income earning capacity, and risk profiles).
Description and findings re EC11	The NBB publishes an annual financial stability report that can be located on the website.
Additional criteria	
AC1	The supervisor meets periodically with external audit firms to discuss issues of common interest relating to bank operations.
Description and findings re AC1	<p>It was evident that the NBB's supervision plan included frequent meetings with the external auditor given the auditors role as collaborator in the supervision framework.</p> <p>The NBB has the right to meet the external auditors without the approval of the bank. According to the banking act, the external auditor is seen as a collaborator of the NBB (see article 55, section 1 of the banking act).</p>
AC2	External auditors, whether or not utilised by the supervisor for supervisory purposes, have the duty to report to the supervisor matters of material significance, for example failure to comply with the licensing criteria or breaches of banking or other laws, or other matters ,

	which they believe are likely to be of material significance to the functions of the supervisor. Laws or regulations ensure that auditors who make any such reports in good faith cannot be held liable for breach of a duty of confidentiality.
Description and findings re AC2	A safe harbour provision exists (which is compliant with the EC safe harbour provision). See article 55, section 2 of the banking act.
AC3	Laws, regulations or the supervisor require banks to rotate their external auditors (either the firm or individuals within the firm) from time to time.
Description and findings re AC3	The standards of the audit profession requires a rotation of the engagement partner after six years or in the case of a sole practitioner, to transfer the audit to another external auditor after six years (standard relating to the independence of external auditors dated 29.06.2008 - paragraph 6.2).
AC4	The supervisor requires banks to have a formal disclosure policy.
Description and findings re AC4	According to Article 20ter of the banking act the NBB determines the minimum information that credit institutions must disclose. However, there is no specific requirement for a bank to have a formal disclosure policy.
AC5	The supervisor has the power to access external auditors' working papers, where necessary.
Description and findings re AC5	The NBB has no such power. The working papers of an external auditor are confidential and only the quality control inspectors or an examining magistrate have to power to access the working papers of the external auditors.
Assessment of Principle 22	Compliant.
Comments	<ul style="list-style-type: none"> IFRS is applied only at consolidated level and BGAAP at the solo level. Currently there is no plan to migrate accounting requirements for all banks to IFRS. A comprehensive review of the differences between BGAAP and IFRS has not been performed, although some ad hoc work has been completed i.e., most recently in regards to the differences in the application of the leverage ratio.
Principle 23	Corrective and remedial powers of supervisors. Supervisors must have at their disposal an adequate range of supervisory tools to bring about timely corrective actions. This includes the ability, where appropriate, to revoke the banking license or to recommend its revocation.
Essential criteria	
EC1	The supervisor raises supervisory concerns with management or, where appropriate, the Board, at an early stage, and requires that these concerns are addressed in a timely manner. Where the supervisor requires the bank to take significant remedial actions, these are addressed in a written document to the Board. The supervisor requires the bank to submit regular written progress reports and checks that remedial actions are completed satisfactorily.
Description and findings re EC1	When applying remedial measures (under Article 57 of the Banking Law - see EC6) the NBB may either apply a timetable by which the credit institution must comply or, in cases of extreme urgency may proceed without determining a timescale. Remedial actions under Article 57 are communicated formally to the board of directors of

	the credit institution in a written document and requires that progress reports are submitted to the NBB in writing. The assessors were able to review examples of interactions between the NBB and credit institutions and follow the file of a recent case that required the use of Article 57 powers by the NBB.
EC2	The supervisor participates in deciding when and how to effect the orderly resolution of a problem bank situation (which could include closure, or assisting in restructuring, or merger with a stronger institution).
Description and findings re EC2	<p>Under Article 57<i>bis</i> of the Banking Law and when acting in the interests of the stability of the state or of the international financial system, the King (i.e., the Federal Government) either on his own initiative or at the recommendation of the NBB can issue a Royal Decree for the resolution of a credit institution. The Royal Decree is agreed following consultation with the Council of Ministers. If the initiative for resolution does not come from the NBB, its opinion must be sought although it is not binding.</p> <p>The Royal Decree may require the transfer or sale of:</p> <ul style="list-style-type: none"> • assets and liabilities, one or more branches of activity, or all or a part of the rights and obligations of the credit institution in question; • any securities or shares whether or not they represent capital, whether or not they grant voting rights by the credit institution. <p>The NBB has powers (Article 57) to impose certain reorganization/ recovery measures such as the designation of a special commissioner and the total or partial suspension or prohibition of activities if it judges such measures adequate to preserve or re-establish the financial position of a credit institution. To the extent it affects the rights of third parties in other Member States the measures taken need to be publicly disclosed (Article 109/1 et seq.).</p>
EC3	The supervisor has available an appropriate range of supervisory tools for use when, in the supervisor's judgment, a bank is not complying with laws, regulations or supervisory decisions, or is engaged in unsafe or unsound practices, or when the interests of depositors are otherwise threatened. These tools include the ability to require a bank to take prompt remedial action and to impose penalties. In practice, the range of tools is applied in accordance with the gravity of a situation.
EC4	The supervisor has available a broad range of possible measures to address such scenarios as described in EC 3 above and provides clear prudential objectives or sets out the actions to be taken, which may include restricting the current activities of the bank, withholding approval of new activities or acquisitions, restricting or suspending payments to shareholders or share repurchases, restricting asset transfers, barring individuals from banking, replacing or restricting the powers of managers, Board directors or controlling owners, facilitating a takeover by or merger with a healthier institution, providing for the interim management of the bank, and revoking or recommending the revocation of the banking license.
Description and findings re EC3 and EC4	<p>Remedial and restructuring measures available to the NBB are set out in the Banking Law (Articles 57 and 57<i>bis</i>).</p> <p>Under Article 57 and in response to a situation where the NBB finds that a credit institution is not operating in accordance with the provisions of this Law and its implementing decrees</p>

	<p>and regulations, that its management policy or its financial position is likely to prevent it from honouring its commitments, that it does not offer sufficient guarantees of its solvency, liquidity or profitability, or that its management structure, administrative and accounting procedures or internal control systems present serious deficiencies, it shall determine the deadline within which the situation must be rectified and the NBB may therefore:</p> <ul style="list-style-type: none"> - appoint a special commissioner, whose approval is required for all or part of the acts and decisions of the credit institution; - enforce additional requirements with regard to solvency, liquidity, risk concentration; - require the concerned credit institution to limit the amounts of variable remuneration; - suspend for a certain period all or part of the credit institution's activities and can require an institution to transfer the shares it holds in accordance with Articles 32, sections 4 and 5 Banking Law; - order the institution's directors to be replaced or, failing compliance with the order, appoint one or more temporary directors; and finally, - revoke the credit institution's authorization. <p>Under Article 57<i>bis</i>, via Royal Decree (see EC2), and when financial stability is threatened, the NBB may order the disposal of:</p> <ul style="list-style-type: none"> - assets and liabilities, one or more branches of activity, or all or a part of the rights and obligations of the credit institution in question; - any securities or shares whether or not they represent capital, whether or not they grant voting rights by the credit institution. <p>The NBB also possesses of a range of administrative orders and sanctions as described in Articles 102 and 103 Banking Law</p> <p>If an institution were to fail to comply with the order within the set timescale, the NBB may impose a fine up to a maximum of 2.5million Euros or 50,000 Euros for each day of delay, (Article 103). The NBB may also impose an administrative fine of between 2,500 and 2.5 million Euros (Article 103). The NBB may publicly disclose the failure of a credit institution to comply with orders to adhere to the Banking Law or its implementing decrees (Article 102). It may be noted that such penalties and fines would have to be imposed by the Sanctions Committee but at present no Sanctions Committee is constituted at the NBB.</p> <p>Criminal sanctions can be also imposed upon individual management and board members (Article 104 of the Banking Law) but the NBB is not the competent authority for such proceedings.</p> <p>The NBB must apply the principle of proportionality in exercising its powers.</p>
EC5	<p>The supervisor has the power to take measures should a bank fall below the minimum capital ratio, and seeks to intervene at an early stage to prevent capital from falling below the minimum. The supervisor has a range of options to address such scenarios.</p>

Description and findings re EC5	<p>The NBB can impose specific solvency requirements upon a credit institution (Article 43, section 3 of the Banking Law).</p> <p>If the NBB judges the capital requirements policy of a credit institution inappropriate for its risk profile, the NBB can - besides the exceptional measures as described in Article 57 (see EC6 below) - impose requirements on solvency, liquidity, risk concentration en risk positions in addition to the criteria and procedures that apply to all credit institutions.</p>
EC6	The supervisor applies penalties and sanctions not only to the bank but, when and if necessary, also to management and/or the Board, or individuals therein.
Description and findings re EC6	<p>Should the NBB find serious deficiencies in an institution (Article 57) it will determine the timeframe within which the credit institution must rectify the situation (though may act faster in an emergency). If the situation has not been rectified by the imposed deadline, the NBB's powers include the ability to:</p> <ul style="list-style-type: none"> - appoint a special commissioner, whose approval is required for all or part of the acts and decisions of the credit institution (in practice this means that for all acts and decisions of all organs of the credit institution the written, general or specific authorization of such commissioner is obligatory. The NBB can limit the kind of operations for which such a written authorization is required); - order the institution's directors to be replaced or, failing compliance with the order, appoint one or more temporary directors; and finally, <p>The NBB must apply principle of proportionality in exercising its powers.</p> <p>Criminal sanctions can be also imposed upon individual management and board members (Article 104 of the Banking Law) but the NBB is not the competent authority for such proceedings.</p>
Additional criteria	
AC1	Laws or regulations guard against the supervisor unduly delaying appropriate corrective actions.
Description and findings re AC1	<p>There are no laws or regulations in place that guard against the supervisor unduly delaying appropriate corrective actions. In practice the NBB will contact the concerned credit institution as soon as it is aware of non-compliance with laws and regulations or if there are concerns with respect to the safety and soundness of the institution.</p> <p>The basic principle is that a credit institution in breach of the Banking Law and related regulations has to be given a period of time to take corrective action. However, the law also determines that recovery measures can be taken immediately in case of urgency.</p>
AC2	The supervisor has the power to take remedial actions, including ring-fencing of the bank from the actions of parent companies, subsidiaries, parallel-owned banking structures and other related companies in matters that could impair the safety and soundness of the bank.
Description and findings re AC2	<p>In accordance with Article 57bis the NBB can formally initiate such actions, although its recommendations need to be ratified through Royal Decree.</p> <p>The NBB noted that given its strong powers under Article 57 and 57bis, it has frequently and recently been possible to use powers of suasion with an institution without resorting to</p>

	full legal remedy. The assessors discussed instances and reviewed documentation illustrating cases where the NBB had found such powers of suasion to be practical and effective and the institution had complied with NBB recommendations on a "voluntary" basis.
AC3	When taking formal remedial action in relation to a bank, the supervisor ensures that the regulators of non-bank related financial entities are aware of its actions and, where appropriate, coordinates its actions with them.
Description and findings re AC3	Article 59 imposes an obligation on the NBB to inform the FSMA or other relevant supervisory authorities within the EEA of its actions under Articles 56 and 57 (i.e., withdrawal of authorization and exceptional measures). The notification obligation set out in Article 59 is ex post and not ex ante. The law does not impose an obligation to cooperate and exchange information with supervisory authorities outside the EEA as professional secrecy cannot be assumed but the NBB does seek to ensure that cooperation arrangements are put in place.
Assessment of Principle 23	Compliant
Comments	<p>The NBB enjoys a broad range of powers and there is evidence that it is able and ready to use such remedies. Moreover, the strong powers open to the NBB have clearly meant that there are occasions where the supervisory authority has been able to use suasion rather than needing to resort to legal remedies in the first instance.</p> <p>The NBB has indicated it is at present examining the possibility of making its disciplinary powers more graduated and proportionate to the severity of the offence committed by the supervised institution.</p> <p>Specifically, the NBB would like the Board to be able to impose periodic penalty payments upon firms. At present, the NBB Organic Law (as amended by the Twin Peaks Royal Decree) provides for the NBB Sanctions Committee to impose fines ("geldboete"/"amende") and periodic penalty payments ("dwangsom"/"astreinte") upon the supervised institutions. These two measures are seen as fundamentally different. Periodic penalty payments ("dwangsom"/"astreinte") are intended to create an incentive to respect a requirement, while the purpose of fines is to punish an illicit behavior on ex post basis⁶. The procedures and processes for submitting a case to the Sanctions Committee are much more elaborate, as is fitting for the consideration of a "sanction" for a firm and various principles of due process, such as separation of the prosecution process from the assessment process must be observed (Articles 36/9 and seq. of the Organic Law of the NBB). However, in the law governing the FSMA, (Law of August 2nd 2002 as modified by the Twin Peaks Law of 2 July 2010), the imposition of periodic penalties is not classified as a formal sanction and therefore such penalties can be imposed by the FSMA Board. Therefore it is now intended to adopt a new law removing the qualification of "administrative sanction" from the periodic penalty payments ("dwangsom"/"astreinte") in respect of the NBB, thus permitting the NBB model to mirror that of the FSMA.</p>

⁶ Preparatory Documents, Parliament (Chambre des Représentants), 2001-2002, n°50-1842/1, p. 288.

	Also, it should be noted, there is draft EU legislation (the Capital Requirements Directive “CRD IV”) that is intended to introduce greater consistency between EU jurisdictions with respect to sanctioning powers.
Principle 24	Consolidated supervision. An essential element of banking supervision is that supervisors supervise the banking group on a consolidated basis, adequately monitoring and, as appropriate, applying prudential norms to all aspects of the business conducted by the group worldwide.
Essential criteria	
EC1	The supervisor is familiar with the overall structure of banking groups and has an understanding of the activities of all material parts of these groups, domestic and cross-border.
Description and findings re EC1	<p>The NBB applies supervision on a consolidated basis (Article 49, sections 2 and 4 of the Banking Law), both where the parent entity of the group is a credit institution and where the parent is a financial holding company. To support this supervision and its risk assessment processes (see CP19) the NBB obtains and assesses comprehensive information from the group such as periodic reports such as consolidated financial statements, the ICAAP at group level, intra-group transactions, fit and proper assessments of group management and ad hoc requirements. In particular the NBB requires a “group memorandum” to be submitted (the Circular on internal governance). While this is a more descriptive/qualitative document it serves as a clear basis to analyze groups under the supervision of the NBB. The elements the memorandum should cover include:</p> <ul style="list-style-type: none"> • description of the objectives and interests of the group, its fields of activity and the interests of the subsidiaries; • organization of the supervision of the subsidiaries by the group; • allocation of responsibilities between the parent company and the subsidiaries, inter alia as regards the subsidiaries’ own responsibilities; • the organization chart, including all corporate bodies and/or persons with a responsibility for policy and strategy, the operational management of the group and its entities, including business lines and centralized services and all control functions within the parent company and the subsidiaries (e.g., internal audit, compliance, risk management, appointed actuary, accounting, etc.); • the policy and rules applied by the group for intragroup outsourcing, management of conflicting interests, etc., as described above. <p>Furthermore, the NBB enhances its understanding of the group through on-site inspection in group context (legal basis for on-site inspection is stated in Article 49, section 2 of the Banking Law). The NBB staff discussed the importance of understanding group structure and where the power lay within a group. Particularly when the NBB was not the ultimate home state supervisor, it was important to understand who within the Belgian subsidiary could and would act in the interests of the entity rather than the group more widely. These were topics on which the NBB liked to see direct evidence from on-site visits. Such topics were brought into focus by the fact that at the time of the mission there were surplus deposits held within Belgian entities and incentives exist for the parent (or other group entity) to seek to transfer assets into Belgium to access this funding. It was important to understand whether the quality of these assets was acceptable and whether the local management had full decision making powers in respect of such portfolios.</p> <p>The NBB takes account the specific features of the group and the institutions that are part of it, such as the nature, size, complexity and risk profile of each of the enterprises concerned, the nature of their stakeholders, and the scope as well as binding character -</p>

	<p>both from a legal and practical point of view - of the financial solidarity between the entities of the group.</p> <p>There are comprehensive legal and regulatory requirements placed on credit institutions (such as Article 20 of the Banking Law and the Internal Governance Circular) to ensure that their internal governance, controls and knowledge of their own group activities are appropriate and that the group is able to provide all relevant information concerning the group to the supervisory authority.</p>
EC2	The supervisor has the power to review the overall activities of a banking group, both domestic and cross-border. The supervisor has the power to supervise the foreign activities of banks incorporated within its jurisdiction.
Description and findings re EC2	<p>The scope of the NBB's powers of consolidated supervision are clearly set out in the Banking Law. Banking groups where the parent entity is a credit institution or a Belgian or foreign holding company are subject to consolidated supervision (Article 49 sections 2 and 4). The NBB can also include entities that are not full subsidiaries (i.e., participations and affiliates) in the scope of consolidation.</p> <p>The NBB also applies consolidated supervision to non-typical group structures such as when the bank is part of a consortium or where an undertaking is in control, alone or together with other undertakings, over a bank.</p> <p>In addition, the NBB has the power to approve significant changes in the group structure such as a new shareholder at the level of the bank (Article 24 of the Banking Law) or at the level of the financial holding company (Article 4, section 3 of the Royal Decree of 12 August 1994). Following this approval, the scope of the group for the purpose of group-wide supervision is modified if deemed necessary.</p> <p>The NBB has extensive information and supervision powers under Article 49 sections 2 ("the NBB may prescribe or require that the credit institutions concerned, their subsidiaries and any other consolidated companies, supply all information relevant for the exercise of supervision on a consolidated basis."). Hence the information powers extend to non-regulated undertakings of the group. If the banks do not comply, the NBB is empowered to request the information directly from the non-regulated undertakings. (See also AC1)</p> <p>Powers for on-site verification of information received are granted to the NBB under Article 13 of the Royal Decree of 12 August 1994. In the context of consolidated supervision, the NBB can perform on-site inspections in the banks or other any undertakings of the group included in the scope of consolidated supervision and located in Belgium or, under certain conditions (essentially coordination and communication with the host authorities), also abroad.</p> <p>Furthermore, to an extent, the NBB's powers of consolidation have a forward looking dimension in the sense that if there is an evolution at EU level regarding the scope of group supervision, the NBB will be able to implement the necessary changes through Royal Decree. Banking Law Art 49 Section 2.</p>
EC3	The supervisor has a supervisory framework that evaluates the risks that non-banking activities conducted by a bank or banking group may pose to the bank or banking group.
Description and findings re EC3	The Royal decree of 12 August 1994 (Article 1) gives a very broad basis to extend group supervision to both regulated and unregulated entities. The scope of consolidation includes banking sector entities (meaning "credit institutions," "investment firms" and "financial institutions" as defined in Article 1 of the Royal Decree of 12 August 1994) but also

	<p>undertakings from other financial sectors (insurance companies, asset managers) and undertakings outside the financial sector.</p> <p>The Royal Decree of 12 August 1994 also pays special attention to the relationship with insurance undertakings when part of the banking group, e.g., at the moment of licensing (Article 9, paragraph 2), for shareholder control purposes (Article 24 section 4), for solvency purposes (Article 2 section 3).</p> <p>In instances where non-financial activities are part of a group, the Royal Decree of 12 August 1994 gives the NBB powers of group supervision over banks that are held by so called "mixed holdings" (Article 8, 8bis and 9). A mixed holding company and all its subsidiaries must be able to give all the information needed to assess the influence on the bank(s). In particular there is scrutiny with respect to transactions between the bank and the mixed holding company or its subsidiaries. Should such transactions threaten the soundness of the bank, the NBB can put restrictions on them. Examples of such restrictions were discussed with the assessors. The assessors were also able to review group risk assessments incorporating analysis of non-banking risks within groups. The supervisors demonstrated a thorough understanding of the complex group structures in place and a familiarity with the non-banking entities within the group.</p> <p>The Royal Decree of 21 November 2005 (based on Article 49bis of the Banking Law) considers the relationship between banks and insurance undertakings when part of the same group, as in this case the provisions of the EU Financial Groups Directive (re conglomerates) are likely to apply. Financial conglomerates are identified based on the definition of "financial conglomerate" in the Royal Decree of 21 November 2005 (see in particular Articles 1 and 2).</p> <p>The Royal Decree of 12 August 1994 (Article 2, section 3) also considers the relationship with insurance undertakings when part of a banking group. If banks and insurance companies are part of the same group, the provisions of the EU Financial Groups Directive (re conglomerates) will apply. Financial conglomerates are identified based on the definition of "financial conglomerate" in the Royal Decree of 12 August 1994 (see in particular Articles 1 and 2).</p> <p>With respect to conglomerate supervision, the NBB has a range of powers:</p> <ul style="list-style-type: none"> • Ownership of a financial conglomerate is subject to supervision in a similar manner to that applied in the sectoral regimes (Article 14 of the Royal Decree see also CP4) • Directors and, where applicable, other senior management, of a mixed financial holding company must be fit and proper, (with reference to the sectoral fit and proper regulations). • Access to and information from all regulated and unregulated entities that belong to the financial conglomerate "group," even if they are excluded from the scope of the supplementary supervision (Article 21 of the Royal Decree). • The requirement of have sufficient transparency in the conglomerate cannot be explicitly derived from the Royal Decree, but is treated indirectly. • Conglomerate supervision includes capital adequacy, risk concentration and intra-group transactions, and the internal control and risk management needed to support this (Article 13 of the Royal Decree). • Administrative sanctions towards regulated institutions that belong to a financial conglomerate (Article 27 of the Royal Decree), but also towards the mixed financial holding company, or towards a financial holding company or an insurance holding
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	<p>company that are part of a financial conglomerate. The sanctioning power is set in the context of "avoiding or trying to avoid sectoral regulation" and is thus supplementary to sectoral sanctioning powers.</p> <p>The Royal Decree also contains requirements for non-typical financial conglomerates, ("other financial groups" as defined by Article 18 of the Royal Decree). Ultimately the NBB has a legal basis for applying supplementary group supervision to any group structure which contains at least one regulated entity.</p> <p>When recent amendments in the European Financial Conglomerates Directive come into force, it will be possible to apply the consolidated banking supervision and the supplementary conglomerate group supervision together and at the same (highest) level in a group that qualifies as a financial conglomerate.</p>
EC4	The supervisor has the power to impose prudential standards on a consolidated basis for the banking group. The supervisor uses its power to establish prudential standards on a consolidated basis to cover such areas as capital adequacy, large exposures, exposures to related parties and lending limits. The supervisor collects consolidated financial information for each banking group.
Description and findings re EC4	<p>The NBB has the power to impose prudential standards on a consolidated basis through the Banking Law (Article 49). Consolidated supervision covers the following areas:</p> <ul style="list-style-type: none"> • the soundness of the financial position of the consolidated group as a whole, based on the consolidated periodic reports; • the governance of the group (such as (i) intragroup transactions, (ii) appropriate risk management and internal control procedures, (iii) the qualities required of the shareholders, (iv) the "four eyes" principle for management, including fitness and probity and the qualities required of the senior management, and (v) the statutory auditor's tasks. • assessment of the influence on each other exercised by the companies included in the consolidation scope, primarily of course the influence on the banks; • limitations on holdings and participations by banks • solvency and risk concentration, as well as the requirement to have an appropriate internal capital adequacy assessment policy • certain publication requirements (see Article 20ter of the Banking Law) <p>The NBB participates in colleges with other supervisors, reaching joint decisions on (e.g.,) the capital adequacy of cross boarder groups on consolidated and solo basis.</p>
EC5	The supervisor has arrangements with other relevant supervisors, domestic and cross-border, to receive information on the financial condition and adequacy of risk management and controls of the different entities of the banking group.
Description and findings re EC5	<p>There is supporting legal framework for the cooperation, coordination and joint work of the relevant supervisory authorities in relation to consolidated supervision.</p> <p>Royal Decree of 12 August 1994 (Articles 9bis to 13) sets out the cooperation arrangements that the NBB can and must establish with other supervisory authorities, both within the EU and outside the EU, in order to exercise consolidated banking supervision.</p>

	<p>When colleges of supervisors have been established, within the EU (non-EU supervisors may be invited to participate), the Royal Decree (Article 9bis, section 5) sets out the expectations imposed on the participating authorities, namely to exchange information, assign tasks and delegate powers (on a voluntary basis, if appropriate), develop prudential supervision programs, avoid unnecessary duplication of requirements and apply the prudential requirements set out in the EU directive 2006/48/EC (the "capital requirements directive"). EU colleges of supervisors seek to reach joint decisions in a range of areas – for example on capital adequacy for the group, and the consolidating supervisor (the supervisor of the parent entity) will make the final decision in the case of disagreements.</p> <p>The Royal Decree establishes legal obligations for the NBB to work closely together with other supervisory authorities of undertakings within the banking group. The NBB has gateways to share all confidential information with these authorities that is needed to exercise the consolidated supervision. In fact, the NBB must on its own initiative share all information deemed "essential" (Article 9bis, section 1 of the Royal Decree of 12 August 1994), including information on the structure of the group, procedures to collect information from undertakings in the consolidation scope, adverse developments, major sanctions and exceptional measures that are imposed including additional capital charges.</p> <p>Furthermore, (Article 9bis, section 1 of the Royal Decree of 12 August 1994), the NBB must consult with other competent authorities responsible for the supervision of entities that are part of a group over which there is consolidated supervision in matters relating to changes to the shareholder, organization or management structure, approvals or of internal methodologies for the calculation of solvency requirements and measures and sanctions.</p> <p>The NBB participates in 12 supervisory colleges of which 5 as home authority and 7 as host authority.</p> <p>Bilateral arrangements with non EU supervisory authorities are also possible and the NBB has agreed bilateral MoUs (subject to confidentiality provisions at least equivalent to those required by Belgian and EU law) which are published on the NBB website.</p> <p>At a domestic level, and as noted in CP1(6) EC1, there are currently outstanding legal amendments required to the Twin Peaks law to provide the full legal basis for exchange of information between the NBB and the FSMA. While in practical terms information exchange is taking place there are continuing discussions on an MoU to formalize modalities of cooperation to ensure each authority has full information necessary for the discharge of its own supervisory functions and in order to take necessary supervisory decisions.</p>
EC6	<p>The supervisor has the power to limit the range of activities the consolidated group may conduct and the locations in which activities can be conducted; the supervisor uses this power to determine that the activities are properly supervised and that the safety and soundness of the bank are not compromised.</p>
Description and findings re EC6	<p>The NBB has powers under the Banking Law (Article 57 and 57bis, see also CP23) to impose measures, including prohibition of the exercise of certain activities of the bank. This power can be applied in the context of groupwide activities.</p> <p>The NBB has the power to block banking groups' projects to acquire or to establish subsidiaries or branches (notably through Articles 30 and 34), if such projects threaten the safe and sound conduct of the group or increases the risk profile of that group beyond its risk bearing capacity.</p>

	<p>For banks or financial holding companies that are recognized as domestic systemically important firms, there are specific provisions on the approval that the NBB needs to give at the occasion of strategic decisions, such as the range of activities of the group (Article 36/3 of the Organic Law NBB).</p> <p>The NBB also analyses all material disposals in order to assess the impact on the risk profile of the group, as well as on the sustainability of the overall business model of the group and its future profitability.</p> <p>Importantly, the setting up of an subsidiary abroad requires notification to the NBB (Article 33 bis of the Banking Law). While there are no explicit powers of approval or refusal, the NBB must be mindful of the fact that a group structure may never hinder the prudential supervision over the bank(s) (Article 20, section 7 of the Banking Law) and may thus oppose the establishment of a subsidiary.</p> <p>Additionally it may be noted that Article 32 of the Banking Law , which applies on a consolidated level, sets limits on the nature of the shareholdings a bank can hold, thus imposing a structural limitation on the range of activities the bank can participate in through its group.</p> <p>For limitations on intragroup exposures, see EC 2 of Principle 10.</p>
EC7	<p>The supervisor determines that management is maintaining proper oversight of the bank's foreign operations, including branches, joint ventures and subsidiaries. The supervisor also determines that banks' policies and processes ensure that the local management of any cross-border operations has the necessary expertise to manage those operations in a safe and sound manner and in compliance with supervisory and regulatory requirements.</p>
Description and findings re EC7	<p>Banks are required to have in place appropriate governance mechanisms at group level (Article 20 of the Banking Law). These must ensure that information within the group is share both bottom up and top down. Branches and subsidiaries should be included in group-wide internal control and risk management procedures. Also fit and proper policies must be in place at group-wide level.</p> <p>The principles laid down in the Internal Governance Circular (PPB-2007-6) are applied to parent companies subject to NBB supervision and to their Belgian regulated subsidiaries. The Internal Governance Circular states: "Although group supervision as applied to groups whose activity presents an international dimension and whose structure includes entities governed by various jurisdictions is by nature more complex than that of purely national groups, the fundamental principles remain. However, such group supervision requires international consultation and must, in accordance with the provisions of the supervisory laws and/or bilateral or multilateral agreements, duly take into account the different rules and supervisory schemes to which certain entities are subject."</p> <p>The NBB expects that the mechanisms applied to address group wide risks are also applied to foreign subsidiaries whether or not they are regulated entities. Also, group governance and control are without prejudice to the application of any local supervisory rules to which these foreign subsidiaries may be subject.</p>

	In practice the supervisory colleges provide a structured framework to discuss group wide risks including internal controls and risk management.
EC8	<p>The supervisor determines that oversight of a bank's foreign operations by management (of the parent bank or head office and, where relevant, the holding company) includes: (i) information reporting on its foreign operations that is adequate in scope and frequency to manage their overall risk profile and is periodically verified; (ii) assessing in an appropriate manner compliance with internal controls; and (iii) ensuring effective local oversight of foreign operations.</p> <p>For the purposes of consolidated risk management and supervision, there should be no hindrance in host countries for the parent bank to have access to all the material information from their foreign branches and subsidiaries. Transmission of such information is on the understanding that the parent bank itself undertakes to maintain the confidentiality of the data submitted and to make them available only to the parent supervisory authority.</p>
Description and findings re EC8	<p>There are obligations placed on the senior management of both a parent bank or a financial holding company in respect of the group's internal controls and risk management (see also CP17) and for the verification of the completeness and accuracy of group reporting (Article 6 section 3 of the Royal Decree of 12 August 1994). Furthermore the Royal Decree of 12 August 1994 (Article 12) requires free information flow between all the entities in the consolidation scope, including the financial holding company and any subsidiaries, even those that may have been excluded from the scope of consolidation, or which represent a minority interest within the consolidated group. In respect of information sharing within the group, the NBB adopt the Basel Committee paper on "Know your customer" risk management (2004) as a main reference.</p> <p>Assessing and evaluating the internal controls and management of a group comes within the overall risk assessment carried out by the NBB. This includes the scope of the internal controls throughout the group, the groupwide organization and conduct of risk management, the quality of management information and the review carried out by management. In particular the NBB checks the group internal governance memorandum to assess whether the group has the necessary internal arrangements for an optimal intra-group flow of information, that may, if necessary, overcome any such restrictions e.g., through contractual agreements between the bank / financial holding and an entity in which it has just a participation. Specifically, paragraph 99, point ii of the Internal governance Circular requires that the group internal governance memorandum must explain how the steering of the group shall be performed and how the bank / financial holding company will supervise its subsidiaries (where "subsidiaries" can be understood in a broad sense, as including all the entities in the prudential consolidation scope).</p> <p>In the event of restriction on the flow of information within the group, the NBB has remedial measures (notably under Articles 57 and 57bis) which would permit it to restrict activities or, under certain circumstances (jeopardizing financial stability) require the disposal of the subsidiary or business lines in question.</p>
EC9	<p>The home supervisor has the power to require the closing of foreign offices, or to impose limitations on their activities, if:</p> <ul style="list-style-type: none"> • it determines that oversight by the bank and/or supervision by the host supervisor is not adequate relative to the risks the office presents; and/or • it cannot gain access to the information required for the exercise of supervision on a consolidated basis.
Description and	The NBB has powers to restrict activities, or even when financial stability issues are a

findings re EC9	<p>concern, to require disposals (Articles 57 and 57bis of the Banking Law). In a cross-border context there would be coordination with the host and within the EU the directives provide a structure for such coordination, including a binding mediation mechanism in case of disputes.</p> <p>The NBB's experience of colleges is that host supervisors generally cooperate with the home supervisor. In its capacity of home supervisor the NBB aims to make at least an annual visit to the host supervisor and the local entity when the risks of that local entity are material from the group perspective. Such bilateral visits have been felt to enhance the mutual trust and understanding amongst supervisors and the on-site meetings at the premises of the local entity have provided good insights into the quality of the local management and its organization. (See also AC3).</p> <p>In instances where the subsidiary is not regulated, if the group does not cooperate in providing the information on that subsidiary, the NBB would contemplate closing the entity, on top of a prudential enforcement action against the group for its lack of cooperation and/or supervision of its local non-regulated entity.</p>
EC10	<p>The supervisor confirms that oversight of a bank's foreign operations by management (of the parent bank or head office and, where relevant, the holding company) is particularly close when the foreign activities have a higher risk profile or when the operations are conducted in jurisdictions or under supervisory regimes differing fundamentally from those of the bank's home country.</p>
Description and findings re EC10	<p>The legal framework, (Article 9bis, section 5 of the Royal Decree of 12 August 1994) imposes an explicit task upon the NBB, when it is consolidating supervisor, to plan the supervisory activities for the group based on the group's risk profile, involving other relevant authorities as appropriate.</p> <p>The Banking Law and secondary regulation also provides a clear framework of expectation on the bank's management that it must have in place a consolidated oversight of the group structure, activities and the risks of its subsidiaries and branches. The management must ensure on a group wide basis, for example, appropriate organization, governance, risk management, compliance, and internal audit. (Article 20 sections 1-2 of the Banking Law and the Internal Governance Circular).</p> <p>While there is no single technique the NBB employs to determine the appropriate scope and intensity of the firm's own risk-based management, the supervisor reaches its assessment through the operation of the overall supervisory program (see also CP19 and 20). The starting point is that input from the bank's management should be risk-based. ICAAP reporting, as required by NBB Circulars, must be performed on solo and group-wide basis (see also CP7), and internal control statements must be drawn up on solo and group-wide basis (see also CP17). The NBB Circulars clarify that the bank's / group's management must not only identify risks, but also assess them and take into account their relative importance for the overall risk profile of the group.</p> <p>As discussed in CP17 the NBB's supervisory program pays specific attention to the group's organization of its internal control functions. This will be reflected in the scorecarding approach. The NBB requests that all material group entities have independent audit, risk management and compliance functions that report to the group wide functions in addition to the senior management and board at the subsidiary level. The audit committee, risk committee or other specialized committees of the Board should have a groupwide scope and appropriate arrangements for the flow and exchange of information. Importantly the</p>

	<p>group must have procedures to escalate material governance, risk, audit or compliance issues as necessary.</p> <p>The NBB applies the principle of proportionality in its supervisory evaluation approach and this approach informs the consideration of the cross-border activities of consolidated groups. The NBB discussed a range of examples where specific risks and issues had been of concern and had resulted in follow up action including on-site visits by the NBB to non-domestic entities.</p> <p>See also above for the principle on offshore activities / know your structure principle (EC 1).</p>
Additional criteria	
AC1	<p>For those countries that allow corporate ownership of banking companies:</p> <ul style="list-style-type: none"> - the supervisor has the power to review the activities of parent companies and of companies affiliated with the parent companies, and uses the power in practice to determine the safety and soundness of the bank; and - the supervisor has the power to establish and enforce fit and proper standards for owners and senior management of parent companies.
Description and findings re AC1	<p>Although the financial holding companies and non-regulated subsidiaries are included in the scope of consolidated banking supervision, this does not mean they can be supervised on a solo stand-alone basis. However, as noted in EC2, the NBB has extensive information and review powers in the context of its consolidated banking supervision.</p> <p>If the non-regulated entities are non-domestic the NBB can demand the information through the Belgian regulated entities. Where the information is already available with another authority, however, the NBB would seek to request the information through that channel to the extent possible.</p> <p>Importantly, even subsidiaries that are not included in the scope of consolidation must be able to provide information to the supervisor when needed (Article 10 of the Royal Decree of 12 August 1994).</p> <p>The NBB can make on-site inspections in all entities mentioned in the paragraph above. Where the entity is non-domestic, the NBB will of course coordinate with the foreign authorities as appropriate (see Article 13 the Royal Decree of 12 August 1994)</p> <p>As discussed under CP4 the NBB has powers to consider change in the ownership of an institution, including ultimate beneficial owner (Article 24 of the Banking Law; Article 4, section 3 of the Royal Decree of 12 August 1994).</p> <p>Executive (or where applicable other senior management) and non-executive directors of financial holding companies must be fit and proper (Article 4 section 4 of the Royal Decree of 12 August 1994; see also principle EC 8 of BCP 3).</p>
AC2	<p>The home supervisor assesses the quality of supervision conducted in the countries in which its banks have material operations.</p>
Description and findings re AC2	<p>The harmonized legal framework for consolidated supervision set out in EU legislation contains the concept of "mutual recognition" and therefore the NBB does not formally assess the quality of supervision conducted in EU/EEA Member States.</p>

	<p>With respect to non-EU/EEA jurisdictions, there is legal provision (Article 7bis section 2 of the Royal Decree of 12 August 1994) that requires the NBB to assess whether the parent of the regulated Belgian institution is subject to consolidated supervision that is equivalent to supervision standards set out in the Decree. The NBB shall consult with the other EU/EEA competent authorities on the equivalence that consolidated supervision also taking into account any guideline issued by the European Banking Committee.</p>
AC3	<p>The supervisor arranges to visit the foreign locations periodically, the frequency being determined by the size and risk profile of the foreign operation. The supervisor meets the host supervisors during these visits. The supervisor has a policy for assessing whether it needs to conduct on-site examinations of a bank's foreign operations, or require additional reporting, and has the power and resources to take those steps as and when appropriate.</p>
Description and findings re AC3	<p>In its capacity of home supervisor the NBB aims, in principle, to visit the non-domestic jurisdictions, which are material for the Belgian banking group. A typical visit comprises a meeting with the local supervisors in order to discuss in detail the risk profile and assessment of the subsidiary, as well as a joint visit at the premises of the subsidiary for in-depth discussions with the local management of the bank. Such visits are in addition to periodic college meetings.</p> <p>Furthermore, whether as the home or host supervisor for groups with EU/EEA parent entities, the NBB participates in the annual global risk assessment of the consolidated group that is coordinated by the consolidating supervisor.</p> <p>The NBB regularly conducts joint on-site examinations at parent and local level and employs a proportionate risk based approach. This is common practice in the field of ICAAP assessments and IRB model validation. Themes of joint inspections have included governance and internal control functions. The assessors were able to review documentation covering regular visits by the NBB team for a systemic bank to the most material foreign subsidiaries.</p>
Assessment of Principle 24	Compliant
Comments	<p>The NBB has the necessary legal powers and has implemented the necessary regulatory structure to facilitate the practice of consolidated supervision. An effective practice of consolidated supervision depends not only on legal framework and access to data but also on the relationships with other relevant supervisory authorities for the consolidated group and this dimension is highly relevant to the Belgian authorities given the cross border nature of the systemically relevant groups.</p> <p>The evolution of the international regulatory framework, particularly at the EU level with the introduction of more structured colleges of supervisors (see also CP25) has provided a vehicle for an enhanced oversight of consolidated groups that operate on a cross border basis. The NBB is actively using the college environment to create opportunities to test out the quality of risk focused management within groups by their own management as well as to ensure an adequate distribution of capital within the group. The NBB noted that governance requirements for groups could be enhanced by stating more explicitly what is expected of the parent company in respect of coordinating and controlling the group in a holistic way. The assessors agree and would encourage the NBB to act on this.</p>

	<p>International regulatory reform is increasingly turning the spotlight on the regulatory perimeter , which may affect the future scope of consolidation. The regulatory agenda also encourages the greater understanding of the interaction of risks within larger and more diverse groups. In the context of consolidated supervision the challenge is to ensure that non-banking and, as necessary, non-financial risks within the group are fully understood, even though these risks may appear present within only a small part of the group. The ability to communicate and cooperate effectively with all domestic regulators as well as international authorities is critical to this task. It is therefore recommended (as also noted in CP 1(6)) that the NBB and the FSMA quickly finalise the MoU setting out the modalities of cooperation.</p> <p>Consolidated supervision comes under stress at time of crisis and during a crisis period not all significant decisions will necessarily be made within the purely supervisory community. Indeed there are separate arrangements for crisis management even if the supervisory authorities prepare the groundwork for other national authorities (notably ministries) to make key decisions. The methodology does not require comment on the extent or effectiveness of supervisory cooperation in crisis conditions but it is noted that the financial crisis wrought significant change on the structure of the Belgian financial system leading to the NBB becoming not only the home but also the host supervisory authority for systemic groups active in Belgium. In respect of consolidated supervisory practices, it is to the considerable credit of the NBB that it has managed this transition well so far.</p>
Principle 25	Home-host relationships. Cross-border consolidated supervision requires cooperation and information exchange between home supervisors and the various other supervisors involved, primarily host banking supervisors. Banking supervisors must require the local operations of foreign banks to be conducted to the same standards as those required of domestic institutions.
Essential criteria	
EC1	Information to be exchanged by home and host supervisors should be adequate for their respective roles and responsibilities.
Description and findings re EC1	<p>The supervision of cross-border banking groups and the home-host relationship are governed by the relevant European directives on prudential supervision of banks (notably directive 2006/48/EC and its subsequent amendments) , which have been transposed into Belgian legislation. In fact the EBA has drafted a template for multilateral cooperation and coordination agreements for EU/EEA groups, although supervisors from non EU/EEA jurisdictions are not excluded.</p> <p>As governed by the directives, there is a structured framework for exchange of information to support the work of colleges of supervisors (e.g., preparation of joint risk assessment and joint capital decision; follow-up of college meetings) and legal gateways to facilitate the exchange of prudential information on the supervisor's own initiative.</p> <p>This information sharing is mostly, but not exclusively, related to the following topics: strategy and activities of the group, changes in the group structure or the business model, EC restructuring plan, financial situation, prudential ratios and risk profile, model validation, ICAAP, EBA stress tests, findings of on-site inspections. In crisis situations, such sharing of information will have a higher frequency and will be more comprehensive, intensive and focused.</p>

	<p>In accordance with European law (see the amendments to Directive 2006/48/EC) EU colleges have, since 2011, been required to make a joint risk assessment, and a joint ICAAP assessment for each cross-border group. This assessment process (SREP) must lead to a joint decision regarding the capital adequacy of the group and the minimum capital requirements that each entity within the group must hold. This risk assessment constitutes the basis of the joint home/host supervisory plan.</p> <p>The practice of information sharing is well established. A regular information exchange during and in between meetings contributes to the spirit of cooperation amongst college members. Mutual trust and building supervisory relationships are seen as key for effective information sharing.</p> <p>The assessors discussed exchanges of information and college practices with the NBB and were able to review extensive documentation illustrating the range and depth of information exchange.</p>
EC2	<p>For material cross-border operations of its banks, the supervisor identifies all other relevant supervisors and establishes informal or formal arrangements (such as memoranda of understanding) for appropriate information sharing, on a confidential basis, on the financial condition and performance of such operations in the home or host country. Where formal cooperation arrangements are agreed, their existence should be communicated to the banks and banking groups affected.</p>
Description and findings re EC2	<p>In its capacity as home supervisor, the NBB has carried out a mapping exercise identifying all EEA and non-EEA subsidiaries and branches within a group in order to set up and organise the relevant supervisory colleges in accordance with the organization, scale and complexity of the group. This exercise is intended to determine which supervisors should become member of the college and be invited to sign the college MoU laying out the basis for the functioning of the college (including regarding the exchange of confidential information). Whereas the EEA members are required to sign a formal MoU for the supervision of a EEA-bank of banking group, non-EEA members participate in the colleges on the basis of either formal bilateral MoU's with the home supervisor (and other hosts), an exchange of letters or informal arrangements for the day-to-day conduct of the college work. As noted above the NBB participates in 12 supervisory colleges of which 5 as home authority and 7 as host authority. The NBB has signed 26 MoUs altogether, of which 18 are intra-EU (this excludes insurance MoUs).</p> <p>The NBB informs the (banking) group of the setting of the college and the agenda of the meetings and debriefs the group on the main conclusions. Senior management of the group is regularly invited to attend part of the college meetings in order to provide information on the group (e.g., status of restructuring plan and strategy, main risks of the group, the impact of Basel III) to all participating host supervisors. The banks with whom the assessors met commented positively on their experience of being involved in and informed of college processes by the NBB.</p>

EC3	<p>The home supervisor provides information to host supervisors, on a timely basis, concerning:</p> <ul style="list-style-type: none"> • the overall framework of supervision in which the banking group operates; • the bank or banking group, to allow a proper perspective of the activities conducted within the host country's borders; • the specific operations in the host country; and • where possible and appropriate, significant problems arising in the head office or other parts of the banking group if these are likely to have a material effect on the safety and soundness of subsidiaries or branches in host countries. <p>A minimum level of information on the bank or banking group will be needed in most circumstances, but the overall frequency and scope of this information will vary depending on the materiality of a bank's or banking group's activities to the financial sector of the host country. In this context, the host supervisor will inform the home supervisor when a local operation is material to the financial sector of the host country.</p>
Description and findings re EC3	<p>The exchange of information is one of the main tasks of the college and the NBB (as home supervisor) puts effort into optimizing the information exchange of key information to the college members. The NBB's experience is that current practices of exchange of information at college meetings relate to standard topics and are generally deemed adequate. Typically, at college meetings, each college member will give a presentation of the risk assessment of the entity, which falls under its supervision. This assessment will include an estimate of the materiality of those risks for the group. College meetings also typically collect and share information on the planned supervisory actions of each supervisor.</p> <p>As a home supervisor, the NBB's main focus is upon the following:</p> <ul style="list-style-type: none"> • functioning of the college in conformity with the European or international regulation, and according to observed good practices; • finalisation of a joint risk assessment, joint ICAAP assessment and of a joint capital decision; • joint home/host supervisory plan; and the execution of joint on and off site investigations; • set up of infrastructure to deal with important crises; • extension of the role and competence of the college to new topics, including macro-prudential control, IT risks and non-financial risks; and • EBA stress-tests. <p>Once a year, each college summarises in a formal joint risk assessment report all the material risks to which the group and its entities are exposed. This report is extensively discussed and endorsed by the participating supervisors. (See also EC1 above)</p> <p>The NBB uses the full range of communication channels to enable a continuous and timely exchange of information on the group structure and activities, the main risks and financial position (liquidity, profitability, solvency ratios) as well as on the supervisory actions (e.g., model validation, ICAAP, EBA stress tests, findings of on-site inspections): college meetings, bilateral meetings, secured college webtool, official letters, mail, conference calls and bilateral phone calls.</p>

	<p>The secured college webtool is used to structure and standardize the information exchange within the college. This tool enables a straight through process of information and communication flows between college members, instant planning and organization of supervisory activities and serves as a central hub for the gathering and disseminating of prudential knowledge and expertise. The tool contains an updated contact list of college members.</p> <p>The NBB noted that as college practices were maturing (and partly as a result of the greater requirements imposed by the directives and the guidelines developed by CEBS and the EBA) host authorities were gaining more confidence within colleges. It was becoming more common for host members to organize events to focus on particular supervisory issues and invite the wider college. In the view of the NBB this development is not only welcome but a testament to the growing trust and effectiveness of communication within the colleges. Although supervisory authorities from outside the EU are invited to EU based colleges, they are obviously not bound by EU directive requirements relating to exchange of information, cooperation and joint risk and capital assessments. Here too, though, the NBB had observed strongly increasing contributions from non EU members.</p> <p>Bilateral contacts also continue to be an important component of supervisory relationships and frequently serve to exchange information on specific issues.</p>
EC4	<p>The host supervisor provides information to home supervisors, on a timely basis, concerning:</p> <ul style="list-style-type: none"> • material or persistent non-compliance with relevant supervisory requirements, such as capital ratios or operational limits, specifically applied to a bank's operations in the host country; • adverse or potentially adverse developments in the local operations of a bank or banking group regulated by the home supervisor; • adverse assessments of such qualitative aspects of a bank's operations as risk management and controls at the offices in the host country; and • any material remedial action it takes regarding the operations of a bank regulated by the home supervisor. <p>A minimum level of information on the bank or banking group, including the overall supervisory framework in which they operate, will be needed in most circumstances, but the overall frequency and scope of this information will vary depending on the materiality of the cross-border operations to the bank or banking group and financial sector of the home country. In this context, the home supervisor will inform the host supervisor when the cross-border operation is material to the bank or banking group and financial sector of the home country.</p>
Description and findings re EC4	<p>The NBB (as host supervisor) informs the home supervisor and the college of the activities, the developments, the main risks and the financial position of the local group entity under its supervision as well as on the supervisory activities and measures. Any adverse development, or material concern or non-compliance by the entity would be reported to the home supervisor on a timely or urgent basis as appropriate.</p> <p>The frequency of information exchange can be periodically (at college meetings) or ad hoc (adverse developments with potentially significant spill-over effects for the group). The bilateral and, for EU colleges, multilateral MoUs aim to ensure that there is a full and effective flow of information between the home and host with the home authority acting as the "hub," which will also ensure dissemination of information effectively through the supervisory authorities and the assessors saw documentation confirming that the NBB is as</p>

	<p>active a host member of a college as it is when it is the home authority. As noted above, there are joint risk assessments for banking groups within the EU framework and the NBB participates as a host supervisor as well as home supervisor.</p> <p>In practicing risk based supervision, the NBB allocates supervisory resource proportionately, but in any case, the NBB is the host authority for two institutions , which are of domestic systemic relevance, so participation in college practices is a priority as is the maintenance of bilateral dialogue with the relevant home country authorities to ensure the effective consolidated supervision of the entire group. As a host authority, the NBB mainly focuses on the following topics:</p> <ul style="list-style-type: none"> • active contribution to the work of the (core) college; and • specific interest in the risks taken by the entity in the home country (including intragroup exposures and asset and liabilities transfers).
EC5	A host supervisor's national laws or regulations require that the cross-border operations of foreign banks are subject to prudential, inspection and regulatory reporting requirements similar to those for domestic banks.
Description and findings re EC5	<p>Belgian laws or regulations make no distinction in terms of prudential, inspection and regulatory reporting requirements between domestic banks and banks with foreign ownership. Moreover, Belgium is subject to EU law , which stipulates that non-EU entities may not be treated more leniently in regulatory standards than domestic entities.</p> <p>With respect to branches specifically, EU law determines that the responsibility for the operation of cross border branches (within the EU/EEA) rests with the home authority except in relation to the treatment of AML/CTF and liquidity supervision (the latter not yet being subject to harmonized regulatory treatment in the EU).</p>
EC6	Before issuing a license, the host supervisor establishes that no objection (or a statement of no objection) from the home supervisor has been received. For purposes of the licensing process, as well as ongoing supervision of cross-border banking operations in its country, the host supervisor assesses whether the home supervisor practices global consolidated supervision.
Description and findings re EC6	<p>For subsidiaries and non-EEA branches, the NBB has to consult the home supervisor before issuing a licence (Articles 9 and 79 of the Banking Law and in conformity with Article 15 of Directive 2006/48/EC). For EEA-branches, the licence is based on the prior notification of the establishment of a branch , which the home supervisor must send to the host supervisor (Article 65 of the Banking Law).</p> <p>For the supervision of "regulated enterprises" (including credit institutions) the Royal Decree of 12 August 1994 on consolidated supervision states , which regulator is responsible for consolidated supervision. For non-EEA banking groups in Belgium, the Belgian regulation requires the NBB to ascertain that there is consolidated supervision exercised by the home supervisor that is equivalent to that exercised by supervisors in EEA.</p>
EC7	Home country supervisors are given on-site access to local offices and subsidiaries of a banking group in order to facilitate their assessment of the group's safety and soundness and compliance with KYC requirements. Home supervisors should inform host supervisors of intended visits to local offices and subsidiaries of banking groups.
Description and findings re EC7	The NBB (in its capacity of home supervisor), has never experienced an instance of refusal of on-site access to local offices and subsidiaries.

	<p>The NBB frequently arranges on-site visits to material subsidiaries and branches in order to deepen its understanding of their activities and to discuss with the local supervisor the main risks to which it is exposed, including compliance risks. An on-site visit typically includes a meeting at the premises of the host supervisor and a joint visit to the premises of the local entity with “deep dive” working sessions with local management and staff. Where the NBB is the home country supervisor it seeks to ensure at least annual visits to material subsidiaries and branches, including joint-on-site examinations both inside and outside the EU.</p> <p>It is standard procedure for the NBB to notify its intention to conduct an on-site visit at a host entity and to forward the agenda prior to the visit to the host supervisor. Most of the time, the host supervisor accompanies the NBB in the on-site visit, but this is not mandatory nor always the case.</p>
EC8	The host supervisor supervises shell banks, where they still exist, and booking offices in a manner consistent with internationally agreed standards.
Description and findings re EC8	Not applicable.
EC9	A supervisor that takes consequential action on the basis of information received from another supervisor consults with that supervisor, to the extent possible, before taking such action.
Description and findings re EC9	<p>The supervisory practices in respect of exchange of information are such that as a general rule, and as codified in MoUs, the exchange specifies the use that can or is expected to be made of the information and a prior consultation takes place on the intentions of the receiving supervisor to take consequential action on the basis of this information.</p> <p>Within the EU/EEA it is mandatory for the NBB to consult with its peer college authorities before making a final determination on a number of issues (such as capital or models approval).</p> <p>There have been a number of documented instances of the NBB having taken consequential action arising from information received from another supervisory authority.</p>
Additional criteria	
AC1	Where necessary, the home supervisor develops an agreed communication strategy with the relevant host supervisors. The scope and nature of the strategy should reflect the size and complexity of the cross-border operations of the bank or banking group.
Description and findings re AC1	<p>A communication strategy is agreed upon in the college on beforehand or, where necessary, on an ad hoc basis.</p> <p>As a general rule, the home supervisor communicates the college's decisions and requests on consolidated basis to the parent bank. Such is the case for the notification of the joint risk assessment, joint capital decision and the validation of IRB-models. The communication by the home supervisor to the group does not prevent the host supervisors from discussing the local implications of college decisions with the local entity under their supervision.</p>

Assessment of Principle 25	Compliant
Comments	<p>Home and host relationships are critical to the successful supervisory oversight of the financial system in Belgium. Of the systemic institutions, all except one is significantly active on a cross border basis, and the NBB is the home authority for only two of these systemic institutions. While EU legislation provides an articulated framework for the operation of colleges of supervisors in the EU, including requiring joint assessment and decision making processes (with arbitration options if necessary), it is clear that the NBB places great value on this process and is strongly motivated to contribute to and participate in the home-host relationships as fully and as effectively as possible. The depth and quality of information sharing, the joint projects undertaken, the documentation of exchanges of views between authorities and actions arising from such debates attest to a maturing dialogue between supervisors, which should serve the NBB well and for which the NBB's own attitude should be given significant credit.</p>