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## Appendix B

### G-10 Financial Regulations: Supervisors and Structure

The current trend in G-10 countries is to set up regulatory agencies with responsibility for consolidated oversight of banks and other financial institutions. Although many of these initiatives contemplate some form of “umbrella” supervision of financial conglomerates, there is no international consensus on what governmental authority should exercise this responsibility (Institute of International Bankers 1999). To augment the summary in table 2.9, this appendix provides brief descriptions of the regulatory structures in G-10 countries and Spain, and the existing mechanism for international coordination.<sup>1</sup>

#### Belgium

1. *Dominant authorities:* Banking and Finance Commission (BFC); Securities Regulation Fund (Fund); Office de Controle des Assurances.
2. *Degree of independence:* The Banking and Finance Commission is an autonomous public institution that has its own legal identity. The

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1. The sources for this appendix are as follows. Web sites of Individual Financial Supervisors (see table 2.9 for references). Institute of International Bankers (1999, 2000). European Commission, *Institutional Arrangements for the Regulation and Supervision of the Financial Sector*, January 2000. Economist Intelligence Unit, *Country Finance: Individual Country Reports*: Belgium, February 2000; Canada, June 2000; France, October 2000; Germany, March 2000; Italy, September 2000; Japan, June 2000; the Netherlands, July 2000; Spain, October 2000; Sweden, October 2000; Switzerland, September 2000; the United Kingdom, August 2000; and the United States, March 2000. Bannock, Baxter, and Davis (1998); Barth, Caprio, Jr., and Levine (2001).

Commission is composed of a chairman and six other members appointed by royal decree. The Securities Regulation Fund is an independent public institution. The BFC monitors the way the Fund performs its tasks as market authority, and the National Bank of Belgium carries out the day-to-day management of the Fund.

3. *Definitions of principal financial institutions:* Four types of domestic banks are recognized under Belgian law: commercial banks, savings banks, securities banks (a category that brokers can use to broaden their sphere of activity), and local-authority savings banks. The distinction between commercial banks and savings banks has only historical significance. The major Belgian banks are universal banks, handling commercial and investment banking functions. All the leading banks have ties to the insurance companies, and to leasing and factoring organizations. Most have in-house brokerage divisions and investment arms or stakes in venture capital companies. Three factors have contributed to radical changes in the banking landscape in the past 5 years: the government's withdrawal from bank ownership; mergers, takeovers, and initiatives by domestic banks to extend their service areas; and foreign banks moving into the country.
4. *Supervisory responsibility by type of financial institution:* The Banking and Finance Commission has a central role in local financial affairs. It is responsible for prudential and supervisory control of credit institutions, asset management firms, stockbrokers, securities traders, investment funds, and foreign exchange traders. In addition, it has been endowed with supervisory responsibility for holding companies, the stock market and futures and options market, takeover bids for quoted companies, and detection of insider trading. The Insurance Control Office supervises insurance companies, mortgage lending, and pension funds. The Committee of the Securities Regulation Fund is a supervisory body for the institutions recognized for holding electronic accounts of public debt securities, and for transactions in bonds, strips, and Treasury certificates outside the Brussels Stock Exchange.
5. *Coordination among supervisors:* The Bank of Belgium has a systemic interest in the stability of the financial system as the lender of last resort, but the Banking and Finance Commission and the Securities Regulation Fund supervise institutions on a day-to-day basis. The two institutions exchange data. For example, the "Memorandum between the Banking and Finance Commission and the Securities Regulation Fund on the supervision of the holding of accounts in dematerialized securities of the Belgian public debt" defines ways in which data are shared between the two.
6. *Permissible activities for banking organizations:* See table B.1.

7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator.
8. *Host country supervision of nondomestic banking organizations:* Belgium applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the European Economic Association (EEA) area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to nondomestic banking organizations.
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Law on the Legal Status and Supervision of Investment Firms, on Intermediaries and Investment Advisors, 1995; Royal Decree on the Organization of the Secondary Off-Exchange Market in Linear Bonds, Strips, and Treasury Certificates, 1995; Royal Decree of 14 September 1997.

## Canada

1. *Dominant authorities:* Office of the Superintendent of Financial Institutions (OSFI); Canada Deposit Insurance Corporation (CDIC).
2. *Degree of independence:* OSFI's supervisory mandate makes it independent. OSFI provides prudential review of proposed mergers of financial institutions (along with the competition authority) and makes recommendations to the minister of finance. The minister ultimately has the authority to approve mergers involving institutions under federal jurisdiction. The superintendent is a governor-in-council for seven years and can only be removed for cause. If removed, a report disclosing the reasons must be tabled in Parliament.
3. *Definitions of principal financial institutions:*
  - Commercial banks—banks in Canada are classified into two groups: Schedule I, which are broadly held, and Schedule II, which can have dominant shareholders. Historically, the domestic banks have been Schedule I banks and foreign banks have been Schedule II. A financial-sector policy framework, made public in June 2000, proposes to replace the current two-tier system of bank classification with a three-tier system including large, medium-sized, and small banks, defined by minimum equity limits: over C\$5 billion,

**Table B.1 Permissible activities for banking organizations in G-10 countries, 1999**

Country	Securities <sup>a</sup>	Insurance <sup>b</sup>	Real estate <sup>c</sup>	Bank investment in industrial firms <sup>d</sup>	Industrial firm investment in banks
United Kingdom	Permitted; usually conducted through subsidiaries	Permitted through subsidiaries	Permitted	Permitted, subject to supervisory consultation	No statutory prohibition, controlling investment not favored
United States	Permitted	Permitted, but states may impose restrictions	Not permitted	Not permitted, except for grandfathered arrangements	Generally prohibited except for grandfathered arrangements
Japan	Permitted through subsidiaries	Not permitted until 2001	Not permitted	Limited to holding 5 percent interest	Permitted, provided total investment does not exceed investing firm's capital or net assets
Canada	Permitted through subsidiaries	Permitted through subsidiaries	Permitted through subsidiaries	Permitted up to 10 percent interest in industrial firm	Permitted, up to 10 percent interest
Germany	Permitted	Permitted, but only through insurance subsidiaries	Permitted, but subject to limits based on bank's capital	Permitted, but limited to 15 percent of bank's capital in each firm; aggregate limited to 60 percent	Permitted, subject to regulatory consent based on the suitability of the shareholder
Italy	Permitted	Limited to 10 percent of bank's capital in each firm; aggregate limited to 20 percent	Not permitted	Permitted, up to 15 percent of the bank's capital, subject to approval of the Bank of Italy	Permitted, up to 15 percent interest, subject to approval of the Bank of Italy

Netherlands	Permitted	Permitted through subsidiaries	Permitted	Subject to regulatory approval for voting shares in excess of 10 percent	Subject to regulatory approval for voting shares in excess of 5 percent
France	Permitted	Permitted, usually through subsidiaries	Permitted	Permitted, but limited to 15 percent of bank's capital in each firm; aggregate limited to 60 percent	Not prohibited
Switzerland	Permitted through specific license	Permitted through subsidiaries	Permitted	Permitted	Not prohibited, but unusual
Sweden	Permitted	Permitted	Not permitted	Limited	Not prohibited, but unusual
Belgium	Permitted	Permitted through subsidiaries	Not permitted	Permitted, but limited to 15 percent of bank's capital in each firm; aggregate limited to 60 percent	Permitted, but subject to prior approval
Spain	Permitted	Permitted	Permitted	Permitted	More than 5 percent interest requires the approval from the Bank of Spain

G-10 = Group of Ten countries; see note f to table A.1.

a. Securities activities include underwriting, dealing, and brokering all kinds of securities, and all aspects of the mutual fund business.

b. Insurance activities include underwriting and selling insurance as principal or agent.

c. Real estate includes real estate investment, development, and management. Banks are permitted to their own premises, and such ownership is not considered part of "real estate."

d. Including investment in industrial firms through holding company structures.

Note: The table does not summarize the complete range of prudential restrictions that apply to the enumerated activities.

Sources: Institute of International Bankers, *Global Survey 2000: Regulatory and Market Developments*, September 2000; Barth, Brumbaugh, and Wilcox (2000).

C\$1-5 billion, and under C\$1 billion. The five biggest Schedule I banks (Royal Bank of Canada, Canadian Imperial Bank of Commerce, Bank of Montreal, Bank of Nova Scotia, and Toronto Dominion Bank)—created by numerous mergers over the past century among smaller regional institutions—have been the dominant financial institutions in Canada throughout the postwar period. The Schedule I banks have diversified into other services, such as brokerage, fund management, and venture capital. Most of Canada's largest banks created or bought insurance operations after the Bank Act was relaxed in 1992. Regulatory curbs require that insurance subsidiaries be run at arm's length from banking operations and prohibit bank engagement in the auto leasing business.

- Credit unions—owned and controlled by their members, credit unions are cooperative financial institutions and are particularly active in Canada. With about a third of the population belonging to a credit union, the country has the world's highest per capita membership. The credit unions deal mainly with mortgage and consumer finance, and are also a significant financing source for small and medium-sized businesses. Individual credit unions are provincially incorporated and regulated.

4. *Supervisory responsibility by type of financial institution:* OSFI is responsible for supervising the banking system, federally chartered insurance and trust companies, federally registered pension funds, and some credit unions. Deposit-taking institutions are subject to federal audit and regulatory control to the extent that deposits are insured by the CDIC. Securities dealers are regulated at the provincial level, but because banks now own securities dealers, the two levels of government have established an elaborate program of information sharing. Jurisdiction over trust and insurance companies is divided, but generally, the larger institutions come under federal statutes.
5. *Coordination among supervisors:* The minister of finance reports to Parliament on the activities of the Bank of Canada, as well as those of the Office of the Superintendent of Financial Institutions. OSFI is responsible for regulating and supervising "Federally Regulated Financial Institutions." The Bank of Canada is responsible for the oversight of the clearing and settlement systems, with a view to controlling systemic risk. The Bank of Canada, OSFI, and CDIC work closely, and trouble with one usually means trouble with all three. A financial-sector policy framework paper, tabled by the Finance Department in mid-1999, envisages no major change in the regulatory structure.
6. *Permissible activities for banking organizations:* See table B.1.

7. *Supervision over financial conglomerates:* The Office of the Superintendent of Financial Institutions oversees the operations of financial conglomerates at the federal level. Certain companies within a financial conglomerates (e.g., securities firms and insurance companies) may also be subject to supervision by provincial authorities.
8. *Host country supervision of nondomestic banking organizations:* The establishment of nonbank affiliates by nondomestic banks is subject to OSFI approval, but it does not supervise these affiliates on an ongoing basis. In a recent development, Bill C-2 (introduced in Parliament in early 2001) distinguishes between “real” foreign banks and “near” foreign banks. A “real” foreign bank will be permitted to conduct financial services activities with the same treatment as the domestic banks. “Near” foreign banks will be permitted to carry on financial services activities in Canada through unregulated entities unless they decide to carry on an insurance business in Canada or core banking activities (deposit-taking business).
9. *Market risk capital requirements:* Banks are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Bank Act, 1980; Office of the Superintendent of Financial Institutions Act, 1987 (Amendments, 1996); Bill C-2, 2001.

## France

1. *Dominant authorities:* Banking Commission; Banking and Financial Regulatory Committee; Credit Institutions and Investment Committee; National Credit and Securities Council; Commission des Opérations des Bourses; and Commission de Contrôle des Assurances.
2. *Degree of independence:* Three major supervisors of credit institutions, the Banking Commission, the Banking and Financial Regulatory Committee, and the Credit Institutions and Investment Committee, are cross-managed by the Banque de France and the Ministry of Economic Affairs and Finance. The structure reflects the balance between the two. Supervisors are accountable to the Parliament.
3. *Definitions of principal financial institutions:* The largest French banks are the three main commercial banks, BNP Paribas, Société Générale, and Credit Lyonnais. The French financial system has been transformed in the past several years by mergers, privatization, and integration among banking, insurance, brokerage, and other suppliers of

services. Domestic consolidation, epitomized by the merger between the Banque Nationale Paris and investment bank Paribas in August 1999, has created a small number of large universal banks. The banking and insurance industries have absorbed the stock brokerage business since reforms in 1987 authorized them to acquire stockbrokerage companies. Banks or insurance companies now either partially or wholly own all of the 40 or so brokerage houses in Paris.

4. *Supervisory responsibility by type of financial institution:* The Banque de France, chairing the Banking Commission, is in charge of banking supervision. The National Credit and Securities Council advises the government on credit policies. The Council is composed of representatives from various banks, organized labor, industry and commerce, regional bodies, and so on. Council members serve on two important committees. The Credit Institutions and Investment Committee (chaired by the governor of the Banque de France) has the power to permit or refuse any type of credit, and it verifies compliance with legal and regulatory supervisions. The Banking and Financial Regulatory Committee (chaired by the minister for economic affairs and finance) authorizes the establishment of banking networks, enforces credit norms and accounting regulations, and monitors relations between credit establishments and clients (see also table 2.9). The committees' decisions are conveyed to banks and clients through the French Credit Establishments Association, to which all banks belong. The French stock market is regulated by the Commission des Operations des Bourse.
5. *Coordination among supervisors:* The National Credit and Securities Council, chaired by the minister of the economy and finance, and deputy-chaired by the governor of the Banque de France, studies and issues opinion on subjects such as customer relations and the means of payment. Members of supervisory institutions, other than the Banking Commission, are appointed from among the members of this council. The Monetary and Financial Authorities Liaison Committee, set up in 1988, provides an additional link among regulators.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator.
8. *Host country supervision of nondomestic banking organizations:* France applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to domestic or nondomestic banking organizations.

9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Banking Act, 1984; Financial Activity Modernization Act, 1996.

## Germany

1. *Dominant authorities:* Federal Banking Supervisory Office (FBSO); Federal Securities Supervisory Office (FSSO); Federal Insurance Supervisory Office (FISO); Bundesbank.
2. *Degree of independence:* The FBSO, FSSO, and FISO are independent, superior federal authorities within the ambit of the Federal Ministry of Finance. For example, the FBSO reports directly to the Federal Ministry of Finance. The president of the FBSO is nominated by the Ministry and appointed by the president of the Federal Republic.
3. *Definitions of principal financial institutions:*
  - Universal banks—Germany is known for its universal banks. These banks provide a wide range of financial services within a single corporate structure. In some continental European countries, like Germany and the Netherlands, universal banks have combined the roles of commercial banks, investment banks, insurance, and brokerage.
  - Savings banks—public-sector savings banks are mostly small and lend predominately to private individuals, but most have commercial-banking functions as well. Most of these savings banks are owned by regional or municipal government authorities.
  - Landesbanken—the public-sector Landesbanken are important commercial and investment banks. The Landesbanken are a primary source of long-term credit for international firms, they play a major role in the mortgage business and provide the public sector with long-term financing.
4. *Supervisory responsibility by type of financial institution:* Although monetary policy for Germany and the other 11 euro zone countries is run by the European Central Bank, financial institutions in Germany continue to report to the Bundesbank's supervisory authorities and the Federal Banking Supervisory Office (FBSC). The FBSC must approve the opening of any new bank, including foreign bank branches, and it is responsible for enforcing regulations that govern the banking

sector. Asset managers and financial brokers are subject to supervision by the Federal Securities Supervisory Office. Insurance companies, meanwhile, are regulated by the FISO. The Third Financial Markets Promotion Law, effective April 1998, allows financial services firms to offer a wider range of services without having to be registered as banks. They may, for example, combine brokerage operations, discretionary portfolio management, own-account trading in financial instruments, and financial transfer operations. Since April 1998, these firms require a license from and are regulated by the Federal Banking Supervisory Office.

5. *Coordination among supervisors:* When issuing guidelines concerning capital and liquidity ratios, the Federal Banking Supervisory Office is required to reach agreement with the Bundesbank. In other areas, the Bundesbank merely has to be consulted. The Bundesbank is fully involved in the day-to-day surveillance of credit and financial services institutions.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator. However, because most financial conglomerates are universal banks, the de facto umbrella regulator is the Federal Banking Supervisory Office.
8. *Host country supervision of nondomestic banking organizations:* Germany applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the European Economic Association (EEA) area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to domestic or nondomestic banking organizations.
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Banking Act, 1961; Sixth Act Amending Banking Act, 1998; Securities Trading Act, 1998.

## Italy

1. *Dominant authorities:* Bank of Italy; Ministry of Finance; Commissione Nazionale per le Società e la Borsa (Consob); Istituto per la Vigilanza Sulle Assicurazioni Private e di Interesse Collettivo (ISVAP).

2. *Degree of independence:* Different supervisors stand independent from each other. New rules were announced in September 1999 on central bank approval for mergers and takeovers involving listed banks. When the rules take effect (they are not yet finalized), approval will have to be sought before a merger or takeover bid is made public. The governor of the central bank is appointed by the Bank of Italy's Executive Board, with the concurrence of the president of the Republic and the prime minister.
3. *Definitions of principal financial institutions:*
  - Commercial banks—universal banks are emerging in Italy. As a result of mergers and acquisitions since the mid-1990s, all the leading banks combine retail and wholesale banking; short-, medium-, and long-term credit; funds management; investment banking; leasing; and insurance. Banks have been allowed since January 1999 to sell banking products through insurance companies. Banks have been moving into insurance much more than insurance companies into banking. Although they are permitted to do so, Italian banks have not taken equity stakes in industrial firms. Many banks have major industrial groups among their own shareholders.
  - Savings, popular, and cooperative banks—savings banks are indistinguishable from other commercial banks, although most have kept their original names. Many are being subsumed into partnership with commercial banks. “Popular” banks are still covered by separate legislation and are a major force. The key difference between popular banks and other institutions is that popular banks must have at least 200 shareholders, and no single shareholder may hold more than 0.5 percent of the shares. Institutions formerly in the rural and artisans' bank category have been reclassified as cooperative banks, similar to popular banks.
4. *Supervisory responsibility by type of financial institution:* The Bank of Italy is responsible for supervising the banking and asset-management system; wholesale markets in government securities; interbank funds; and clearing, settlement, and guarantee systems for transactions involving securities and derivatives. Approval from the Bank of Italy is needed to establish or acquire a bank or securities trading company. For listed financial institutions, the lead supervisor is the stock market regulator, the National Financial Markets Commission (Consob). The Institute for Supervision of Private and Collective Interest Insurance (ISVAP) has a regulatory role in the insurance markets similar to that of the central bank in its sector. ISVAP's activity is financed by a levy on insurers that amounts to 2 percent of premiums.

5. *Coordination among supervisors:* The Bank of Italy is charged with safeguarding stability, whereas Consob is responsible for transparent and proper conduct of individual institutions. The Bank is charged with defining the prudential rules for limiting risk. The supervision of bank holding companies temporarily lies in the Treasury.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator.
8. *Host country supervision of nondomestic banking organizations:* Italy applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland).
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Amato-Carli, 1990; Consolidated Law on Financial Intermediation, 1998.

## Japan

1. *Dominant authorities:* Financial Services Agency (FSA) (the Financial Supervisory Authority was renamed in January 2001); Financial Reconstruction Commission (FRC); Securities and Exchange Surveillance Commission (all under the Prime Minister's Office).
2. *Degree of independence:* The FSA reports directly to the Prime Minister's Office and is independent of the Ministry of Finance (MoF), although consultations occur if its action is deemed to have a "grave impact" on the financial system. The Bank of Japan is not part of the government but remains a semigovernment corporation, 55 percent of which is owned by the MoF. The Bank has no statutory role in the supervision of financial institutions, other than as a lender of last resort. The autonomy of the central bank from the government, especially the MoF, has been a contentious matter in recent years. The passage of a revised Bank of Japan Law in April 1998 laid a path toward a more independent central bank.
3. *Definitions of principal financial institutions:*
  - Commercial banks—Japan's commercial banking industry is made up of city banks, regional banks, trust banks, and long-term-credit

banks. City banks, with assets accounting for about half the combined assets of all the commercial banks, are the most powerful private financial institutions in the country. They provide a wide range of services, including consumer credit, cash management, foreign exchange facilities, securities sales, and leasing services. In the past, city banks primarily served major corporations. Five of the larger city banks (Sakura, Bank of Tokyo-Mitsubishi, Sumitomo, Fuji, and Dai-Ichi Kangyo) are directly affiliated with corporate groups (keiretsu). However, the development of capital markets has decreased the loan demand from large corporations, and the city banks have shifted more of their attention to small companies and to other types of financing. The process of phasing in mutual entry of firms between banking, securities, and trust businesses was initiated in 1993. Through subsidiaries, the lines between city banks, long-term credit banks, trust banks, and securities companies are increasingly blurred.

- Financial holding companies—as a precursor to a universal banking system, banks, securities companies, and insurers can organize financial holding companies under the Financial Holding Companies Law of March 1998. A bank holding company is permitted to hold more than 50 percent of the shares in each subsidiary in the areas of banking, securities, trust banking, insurance, and investment advisory services. Securities and insurance holding companies are permitted to have securities and insurance subsidiaries, respectively. However, a bank holding company must not have nonfinancial companies under its control.
  - Postal savings system—the Japanese postal savings system is the largest depository institution in the world, holding ¥260 trillion in personal deposits and savings (a size comparable to the nation's entire commercial banking sector, which had ¥288 trillion in personal deposits and savings). Postal accounts include savings, annuities, and insurance policies. The primary reason that the Japanese government, via the postal savings system, is in the banking business is to provide an inexpensive source of financing for its own projects. In fact, most of the funds are routed to the Trust Fund of the Bureau of the Ministry of Finance. Proposals for dismantling the system have been debated recently but only modest reforms are planned to scale back the size of the postal savings system.
4. *Supervisory responsibility by type of financial institution:* The creation of the FSA in June 1998 replaced traditional MoF guidance to financial institutions. The MoF now plays a policy role with respect to planning the overall working of the financial system. The FSA is responsible for the supervision of all possible financial activities and institutions, from retail banking to insurance.

5. *Coordination among supervisors:* With the prolonged banking crises of the 1990s, the resolution of failed banks became a headache issue. The FRC, established in October 1998, was given authority both for reorganizing and recapitalizing failed banks. With the exception of rights to issue and eliminate existing licenses, general supervision of financial institutions is delegated to the FSA. Financial crisis management required cooperation between the new FRC and the MoF. The FSA also cooperates with the MoF. The FRC was unsuccessful in this effort and was absorbed by the FSA in 2001.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* A single regulator (FSA) oversees the activities of all financial conglomerates.
8. *Host country supervision of nondomestic banking organizations:* Supervision of the capital adequacy of nondomestic banks relies on consolidated supervision by the home country, but Japanese standards are applied to the other financial activities of the branches or nondomestic banks. Japanese authorities do not apply their umbrella supervision to nondomestic banking organizations.
9. *Market risk capital requirements:* Banks are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Financial Reconstruction Law, 1998; Financial Functions Early Strengthening Law, 1998; Law on the Establishment of the Financial Reconstruction Commission, 1998; Financial Holding Company Law, 1998.

## The Netherlands

1. *Dominant authorities:* Nederlandsche Bank; Securities Board; Insurance Board.
2. *Degree of independence:* The Nederlandsche Bank is independent of the Ministry of Finance and other ministers. The governor of the bank is appointed by the royal decree and is not accountable to the ministry. The Bank Council is the decision-making body of the bank. The Securities and Insurance Boards are also independent agencies.
3. *Definitions of principal financial institutions:* Through their affiliates and their close ties with large institutional investors, domestic universal banks can provide financing of every type. The distinctions between different kinds of banks, especially between universal banks and savings

banks, have effectively disappeared. All the major bank groups operate as universal banks, offering a wide range of retail and wholesale banking services and financial products. There are also no restrictions on the lending practices of financial institutions.

4. *Supervisory responsibility by type of financial institution:* The Netherlands Bank supervises both retail and wholesale banks. Retail banking is classified under “credit institutions,” which include universal banks, savings banks, cooperative banks, security credit institutions, and mortgage banks. Wholesale banking is classified under “investment institutions,” which include securities-issuing institutions that deal in the primary market, and securities institutions that trade in the secondary market. The Securities Board of the Netherlands supervises securities trading in the country. Insurance companies and pension funds are supervised by the Insurance Board.
5. *Coordination among supervisors:* The Council of Financial Supervisors brings together the Netherlands Bank, the Securities Board, and the Insurance Board. The council has a coordinating function with respect to the supervision of conglomerates, the integrity of the financial sector, and providing of information to consumers.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator. The Council of Financial Supervisors has a coordinating function.
8. *Host country supervision of nondomestic banking organizations:* The Netherlands applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to domestic or nondomestic banking organizations.
9. *Market risk capital requirements:* Banks are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Act on the Supervision of the Credit System, 1992; Exchange Offices Act, 1995; Banking Act, 1998.

## Spain

1. *Dominant authorities:* Banco de España; Comision Nacional del Mercado de Valores (CNMV); and Directorate General Insurance of the Ministry of Economy and Finance.

2. *Degree of independence:* Supervision is ultimately the responsibility of the government and the Ministry of Finance (Ministerio de Hacienda). A direct supervisory role is assigned to the Banco de España and the other financial regulators. All supervisors are fully independent, but are obliged to cooperate with each other when necessary (see below).
3. *Definitions of principal financial institutions:*
  - Commercial banks—Spain’s financial markets have long been dominated by a number of large private commercial banks, which engage in a variety of financial operations, ranging from extending short-term credit to investing in manufacturing companies. Spanish commercial banks are primarily active in short-term credits and discounting of commercial bills. They supply about 40 percent of the total credit volume in Spain. Commercial banks offer a full range of banking services, including the financing and management of syndicated loans in foreign currencies, and investment banking operations. Although smaller in size than their European counterparts, Spanish commercial banks are now among the most profitable in Europe. The two Spanish banking giants—Grupo Banco Santander Central Hispano (BSCH) and Grupo Banco Bilbao Vizcaya Argentaria (BBVA)—control almost one-third of the lending and deposit markets.
  - Savings banks—*cajas de ahorro*—are an important source of medium- and long-term loans, though they tend to concentrate on specific sectors, such as agriculture, small business, and construction. They play an important role in retail banking and in the mortgage-lending market. Spanish savings banks, led by La Caixa, accounted for 40 percent of total lending, 52 percent of deposits and 52 percent of all mortgage lending in 1999. Although traditionally concentrated on long-term housing and agriculture projects, savings banks now compete with commercial banks in most business segments.
4. *Supervisory responsibility by type of financial institution:* The Banco de España supervises all credit institutions (commercial banks, saving banks, credit cooperatives, and finance companies) and monitors the interbank, foreign exchange, and book-entry public debt markets. Securities firms and collective investment undertakings are supervised by the Comisión Nacional del Mercado de Valores. The CNMV is exclusively responsible for overseeing financial markets (stock, private bond, and derivative markets) and entities operating in those markets. Insurance companies and pension funds are supervised by the Directorate General Insurance of the Ministry of Economy and Finance.

5. *Coordination among supervisors:* The Banco de España cooperates with the Comision Nacional del Mercado de Valores, and the Directorate General Insurance of the Ministry of Economy and Finance, whenever undertakings included in a banking group are subject to supervision by these authorities on an individual basis. Specifically, when book-entry trading in public debt, which in principle falls under the supervision of the Banco de España, is considered an official market, there is supervisory coordination between the Banco and the CNMV.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* The lead regulator for a financial conglomerate is determined on the basis of the financial conglomerate's principal activity.
8. *Host country supervision of nondomestic banking organizations:* Spain applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to nondomestic banking organizations.
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Law on Discipline and Intervention of Credit Institutions, 1998; Law of Autonomy of the Banco de España, 1994 (First Amendments, 1997; Second Amendments, 1998); Securities Market Law, 1988 (Amendments, 1999).

## Sweden

1. *Dominant authorities:* Financial Supervisory Authority (FSA); Riksbank; Ministry of Finance.
2. *Degree of independence:* The Riksbank is directly responsible to the Riksdag (parliament), not to the government. The FSA is funded by levies on the regulated industries rather than by general government revenues. Such funding secures the agency's independence from the Ministry of Finance, to which the FSA ultimately reports.
3. *Definitions of principal financial institutions:* In Sweden, the lines of demarcation between commercial banks and savings banks have

largely faded away. The four most important banks in Sweden are Svenska Handelsbanken, Skandinaviska Enskilda Banken (SEB), ForeningsSparbanken, and MeritaNordbanken. Consolidation in the banking-financial-insurance sector continues as well. Insurance companies are taking an increasingly aggressive role and have become integrated with banks, both through direct mergers and by starting their own banks.

4. *Supervisory responsibility by type of financial institution:* The Riksbank has the general responsibility of steering credit policies. The dominant supervisory authority is the Financial Supervisory Authority. Through its Banking, Securities, and Insurance departments, the FSA supervises banks and other credit institutions, securities companies and fund management companies, stock exchanges and clearinghouses, insurance companies, brokers, and friendly societies.
5. *Coordination among supervisors:* The Riksbank is responsible for oversight, and the Financial Supervisory Authority is responsible for direct supervision. The Riksbank influences the supervisory system either by contacting bank executives and simultaneously informing the FSA, or by providing general analysis of the financial system through its annual publication, *Financial Market Report*.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* A single regulator, the Financial Supervisory Authority, oversees the activities of all financial conglomerates.
8. *Host country supervision of nondomestic banking organizations:* Sweden applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to nondomestic banking organizations.
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Banking Act, 1987; Swedish Insider Legislation, 2001.

## Switzerland

1. *Dominant authorities:* Swiss National Bank; Swiss Federal Banking Commission (SFBC); Federal Office of Private Insurance.

2. *Degree of independence:* The Swiss Federal Banking Commission is an administrative authority of Switzerland, which is independent of the individual directives of the Federal Council and is not a part of the central government administration. Administratively, however, it is integrated within the Federal Department of Finance.
3. *Definitions of principal financial institutions:* The two biggest universal banks are UBS and Credit Suisse, which rank among the world's largest 10 banks. Within Switzerland, UBS and Credit Suisse compete with cantonal banks, regional and savings banks, and cooperatives. In recent years, the number of big banks has continued to decline through mergers, while boundaries have faded between national, cantonal, and private banks, as well as between insurers and capital-market participants.
4. *Supervisory responsibility by type of financial institutions:* The Swiss National Bank's regulatory authority is limited to the imposition of minimum-reserve requirements on banks and the supervision of domestic bond issues. The dominant authority is the Swiss Federal Banking Commission. It is elected by the Federal Council and oversees the banks, investment trusts, and the SWX Swiss Exchange. No bank may operate without the SFBC's authorization, which may be withdrawn if a bank ceases to fulfill required conditions. The blurring of lines between traditional banking and insurance resulted in close cooperation between the SFBC and the Federal Office of Private Insurance—the federal insurance supervisor.
5. *Coordination among supervisors:* The Swiss Federal Banking Commission is in permanent contact with the Federal Department of Finance and other federal departments, as well as the Swiss National Bank. In addition, the SFBC maintains regular contacts with various associations, foremost the Swiss Bankers' Association, the Association of Investment Funds, and the Swiss Institute of Certified Accountants and Tax Consultants.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* Financial conglomerates operate without an umbrella regulator.
8. *Host country supervision of nondomestic banking organizations:* Switzerland applies its own regulatory standards, in addition to any non-EU home-country regulations. The EU Second Banking Directive, extended to the EEA area, grants primary responsibility to home countries in the EU and EEA (including Iceland, Liechtenstein, Norway, and Switzerland). Financial authorities do not apply umbrella supervision to domestic or nondomestic banking organizations.

9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* Stock Exchange Act, 1997; Last Amendments to the Banking Law (1934), 1999.

## United Kingdom

1. *Dominant authority:* Financial Services Authority (FSA).
2. *Degree of independence:* The Head of the FSA is appointed and removed by Her Majesty's Treasury. The FSA is accountable to the Ministry of Finance, and independent from the Bank of England.
3. *Definitions of principal financial institutions:*
  - Commercial banks—privately owned banks that operate checking accounts, receive deposits, take in and pay out notes and coin, and make loans domestically through their branches.
  - Building societies—institutions that accept deposit, upon which they pay interest, and make loans for house purchases secured by mortgages. They are owned by its members, who also represent their customers. Elsewhere, similar functions are performed by savings banks, and savings and loan associations (in the United States).
  - Clearinghouse—an institution that settles mutual indebtedness between a number of organizations. In England and Wales, the Cheque and Credit Clearing Company Ltd operates a bulk clearing system for cheques and other paper credit items paid into banks other than those upon which they were drawn.
  - Unit trust—an organization that invests funds subscribed by the public in securities, and in return issues units that it will repurchase at any time (similar to a mutual fund in the United States). The units, which represent equal shares in the trust's investment portfolio, produce income and fluctuate in value according to the interest and dividends paid and the stock exchange prices of the underlying investments. The trustees that actually hold the securities are usually banks or insurance companies, and are distinct from the management company.
4. *Supervisory responsibility by type of financial institution:* The FSA has been assigned supervisory responsibility over all possible financial activities and institutions, from retail banking to insurance. Various

commissions and boards that regulate different financial sectors are now in the process of merging into the FSA.

5. *Coordination among supervisors:* Since 1997, the Bank of England no longer has supervisory powers over individual financial institutions. It remains responsible for the overall stability of the financial system. The FSA is the primary supervisor for all financial institutions. The joint Committee of Treasury/Bank/FSA has been the coordinating body since March 1998.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* A single regulator, FSA, oversees the activities of all financial conglomerates as a whole.
8. *Host country supervision of nondomestic banking organizations:* The United Kingdom applies its own supervisory standards apart from the home country. However, within the European Union, relationships among bank supervisors are governed by the Second Banking Directive, which establishes a “home-country” supervisory system for banks incorporated in a member state. Under these arrangements, a member (home) state permits a bank to branch throughout the European Union, and the home-country supervisor has the primary responsibility for the operation of the bank throughout the European Union. The UK financial authorities apply their umbrella supervision to nondomestic banking organizations.
9. *Market risk capital requirements:* Banks and securities firms are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for risk-based capital-adequacy requirements.
10. *Domestic legal framework:* First Banking Act, 1979; Financial Services Act 1986; Bank of England Act 1998; Financial Services and Market Bills 1999.

## United States

1. *Dominant authorities:* The Federal Reserve, Office of the Comptroller of the Currency (OCC—Treasury Department); Office of Thrift Supervision (OTS—Treasury Department); Federal Deposit Insurance Corporation (FDIC); Securities and Exchange Commission (SEC).
2. *Degree of independence:* The Federal Reserve, FDIC, and SEC are independent from the Treasury Department. However, supervision of important financial institutions is the responsibility either of the central bank (Fed) or Treasury.

3. *Definitions of principal financial institutions:* The US banking system was historically a diverse collection of institutions with limited geographical service areas, generally confined to a single state. US banks were prohibited from several important financial activities that were permitted for banks in other major countries. As a consequence of ingenious legal strategies and regulatory tolerance, the geographical and activity boundaries became increasingly blurred in the 1980s and 1990s. The Financial Services Modernization Act, also known as the Gramm-Leach-Bliley Act (GLBA) of October 1999 made it easier for banks, insurers, and securities firms to enter each other's businesses. GLBA permits the creation of a "financial holding company" (FHC), which can have subsidiary corporations that engage in any activity considered "financial in nature," "incidental" to finance, or "complementary" to it. The new law does away with the 25 percent revenue ceiling for nonbanking financial activities that was a core feature of the former bank holding company statute. Proponents of the bill (almost the entire financial industry) see this as a breakthrough that enables them to compete with the universal banks of Europe and the post-1998 "Big Bang" banks of Japan.
4. *Supervisory responsibility by type of financial institution:* The Federal Reserve has primary responsibility for supervising and regulating all bank holding companies, their nonbank subsidiaries, and their foreign subsidiaries together with state-chartered banks that are members of the Federal Reserve System (state member banks) and their foreign branches and subsidiaries. Depending on whether the bank is part of a holding company or conducts securities or insurance activities in an operating subsidiary, other supervisors, such as the FDIC or the SEC, may have some supervisory authority. The Federal Reserve shares supervisory and regulatory responsibilities with the OCC (national banks), the FDIC (state nonmember banks), and the OTS (thrift holding companies, savings and loan associations).
5. *Coordination among supervisors:* The Federal Financial Institutions Examination Council (FFIEC), established by statute in 1978, consists of the chairpersons of the FDIC and the National Credit Union Administration, the comptroller of the currency, the director of the OTS, and a governor of the Federal Reserve Board appointed by the board chairman. Its goal is to harmonize federal principles and standards, and to promote coordination both among federal agencies and between federal and state agencies. GLBA conferred the lead supervisory role on the Federal Reserve.
6. *Permissible activities for banking organizations:* See table B.1.
7. *Supervision over financial conglomerates:* The Federal Reserve oversees the activities of all financial conglomerates as the "umbrella" supervisor. Before passage of GLBA, nonbank financial conglomerates were not

regulated at the group level. Since the new law, banks have been able to affiliate through holding companies with all types of financial institutions, and the Federal Reserve is the “umbrella” supervisor for the group.

8. *Host country supervision of nondomestic banking organizations:* The United States applies its own supervisory standards in addition to whatever standards may be applied by the home country. As with domestic banks, the OCC is the primary regulator for federal branches and agencies, and the states are the primary regulator for branches and agencies licensed under their laws. The Federal Reserve has examination authority over the combined US operations of international banks, including their branches and agencies. The Federal Reserve is also the umbrella supervisor of non-domestic banking organizations. In determining whether to permit an international bank to conduct activities in the United States, the Federal Reserve makes its own assessment of the adequacy of an international bank’s global capital.
9. *Market risk capital requirements:* Banks are subject to risk-based capital requirements for market risk. Banks are permitted to use internal models to measure market risk for the purpose of capital-adequacy requirements.
10. *Domestic legal framework:* International Banking Act, 1978; Financial Services Modernization Act, 1999.

## **The European Union and International Coordination**

As shown in table 2.9, the mechanism for regulatory coordination over the financial sector exists at the European and international levels. In contrast to the provisions of the Banking Directive of the European Common Market, financial-market liberalization under NAFTA was not directed toward regulatory harmonization (Haar and Dandapani 1999). Through provisions such as de jure national treatment and MFN, however, there was increased pressure for more deregulation in the US market, culminating in the passage of the Financial Services Modernization Act of 1999.

### **Banking**

#### European Union

- European Commission Banking Advisory Committee (BAC): The BAC was established in 1978 under the First Banking Coordination

Directive. The BAC assists the Commission in the proper implementation of the European Banking Directives. Its tasks range from authorization requirements for banks to establishing ratios for the solvency, liquidity, and profitability of credit institutions. However, the BAC does not discuss specific problems relating to individual credit institutions. This remains the exclusive competence of the national banking supervisory authorities. Its members include 15 EU countries as well as the European Commission. The European Central Bank, Norway, Iceland, and Liechtenstein participate as observers.

#### International

- **Basel Committee on Banking Supervision (BCBS):** The Basel Committee was established in 1974 after serious disruptions in international banking and currency market (notably the failure of Bankhaus Herstatt in Germany). The committee does not—and never was intended to—have legal force. It formulates and recommends best practices; national authorities are then left to implement what is best suited to their national systems. The BCBS is one of three committees of the Bank for International Settlements; the other two are the Committee on Payment and Settlement System, and the Committee on Global Financial System. The BCBS is best known for its recommendations on bank capital ratios and its development of the 1997 *Core Principles for Effective Banking Supervision*.

#### Securities

##### European Union

- **The High Level Securities Supervisors Committee (HLSSC):** At the EU level, four groups exist for coordination over securities and derivatives market regulations (table 2.9). The HLSSC is one of the four and assists the European Commission in the preparation of new proposals of securities legislation, which cover listing conditions, access to markets, investor compensation schemes, and so on. The HLSSC is an informal working group with no legal basis. Its membership includes national securities supervisor of the EU countries and officials of finance ministries.

##### International

- **International Organization of Securities Commissions (IOSCO):** IOSCO was created in the early 1980s as a forum for securities regulators around the world. Its main tasks are to establish standards, exchange information, and provide mutual assistance to promote the integrity

of the markets. Through its permanent committee structure and joint activities with other institutions, it aims to promote high standards and implement them. The need for monitoring the adoption of best practices led to the addition of an Implementation Committee in 1998. In 1999, the Technical Committee set up a special task force on Hedge Funds and Other Highly Leveraged Institutions.

## Insurance

### European Union

- Insurance Committee (IC): The IC was set up by an EU Directive in 1992. It is attached to the European Commission and assists the Commission in preparing legislation for the supervision of the EU insurance sector. Prudential issues related to the supervision of financial conglomerates provided strong motivation for creating the IC, as an analogue to the existing system of coordination between banking and securities regulators.

### International

- International Association of Insurance Supervisors (IAIS): The IAIS was established in 1994 to provide insurance regulators around the world with an official forum to discuss regulatory issues. Before its inception, an informal forum existed under the National Association of Insurance Commissioners (NAIC), the umbrella organization of US state insurance regulators. Its main functions are standard setting and information gathering, like its counterparts in banking and securities sectors. In 1997, the IAIS issued its first four reports: *Insurance Supervisory Principles*; *Guidance on Insurance Regulation and Supervision for Emerging Market Economies*; *Insurance Concordat*; and *Model Memorandum of Understanding*. Additional standards on licensing, on-site inspection, and derivatives were issued in 1998.

## Cross-Sector

### European Union

- Banking Advisory Committee/Insurance Committee/High Level Securities Supervisors Committee (BAC/IC/HLSSC): No single cross-sector forum exists in the European Union to discuss specific supervisory issues arising from cross-border financial conglomerates. On a pragmatic basis, however, three sectoral regulatory bodies under the

European Commission have been coordinating supervision on financial conglomerates since 1991. A first meeting of the three bodies took place in 1994. After consulting the BAC, IC, and HLSSC, the Commission set up and mandated under these three parental bodies a new technical group on possible EU legislative response to financial conglomerates.

#### International

- **The Joint Forum on Financial Conglomerates:** The Forum was constituted in 1996 to advance the work of the Tripartite Group of banking, securities, and insurance supervisors that was established in 1994. It operates under the aegis of the BCBS, IOSCO, and IAIS. It was mandated to facilitate the exchange of information between supervisors and to enhance supervisory coordination, and to develop principles toward the more effective supervision of financial conglomerates.
- **Financial Stability Forum:** See box 3.2.
- **Committee on Global Financial System (CGFS):** It has been a forum since 1960s—formerly called the Euro-Currency Standing Committee—for the regular exchange of views among senior central bank officials. It has been responsible for developing and overseeing the implementation of BIS statistics on banking, derivatives, and foreign exchange market activities. Its work focuses on financial stability, especially the potential impact of financial innovations on systemic risk.