

Basel II

Central Bank Of Kenya

Key Implementation Challenges
14 December 2009

Key implementation challenges

- Extent of work, commitment and dedication to implementing Basel II should not be under-estimated.
- For its successful implementation, Basel II has to be driven from the top.
- The first challenge is to strengthen the infrastructure.
- Without the proper foundations in place, this could pose impediments to the implementation of Basel II.

Key implementation challenges

- Regulators want protection against surprises.
- Confidence that their ability to react as regulators, is up to the task.
- Necessary to work closely with the banks through a structured process.

What are some of the challenges that Supervisors are likely to face?

Key implementation challenges

- **Importance of planning**
 - A detailed roadmap and implementation schedule is very necessary.
 - Timelines need to be managed vigorously.
 - On-going feedback to top management is very necessary.
- **Dealing with cultural changes**
 - Cultural changes are the difficult to deal with.
 - Introduce and create a BII awareness program throughout the department
 - Basel II training should be mandatory
 - Training should be on-going and targeted across various different levels.

Key implementation challenges

- **Basel II Education**
- Top management education is of utmost importance.
 - a “general understanding” of Basel II.
 - provide an “effective challenge”.
 - aware of the obligations and responsibilities under Basel II.
 - training should be on agenda of every meeting.
 - Focused on specific risks and all 3 Pillars.
- **Identifying gaps early in the process**
 - Gaps identified need to be prioritised and managed.
 - Projects should be sliced and diced.
 - Specific deadlines should be set
 - Champions should ideally spearhead projects.
 - Train the trainer concept should be introduced.

Key implementation challenges

- **Undertaking self-assessments**
 - Self assessments should be based on the revised regulations and Accord requirements.
 - Devise template to measure compliance
 - Regularly monitor extent of compliance.
 - Focus on and prioritise key issues.
- **Dealing with cross border issues**
 - For branches of foreign banks, this area is difficult.
 - Comply with host country and home country requirements.
 - Also need to comply with regulations and laws within jurisdiction of operation.
 - Engaging with home supervisors is necessary
 - Attending supervisory colleges held by home supervisors assists the supervision process.
 - Where domestic banking institutions have presence outside their borders the same applies.

Key implementation challenges

- Addressing national discretions items timeously
- Recognising ECAs – lengthy process
- State-of-readiness assessments – dynamic process
- Self –assessments – Banks and Supervisor

Key implementation challenges

- **Dealing with cross border issues**
 - Foreign banks complying with capital requirements.
 - Regulatory capital of foreign banks based on home country requirements.
 - Home/host reliance to reduce the burden of dual reporting.
- **Undertaking parallel runs**
 - Do not under-estimate the importance parallel runs.

Key implementation challenges

Reporting of capital

- Biggest issue of all is the reporting of capital;
 - understanding of the Regulations & Banks Act
 - providing technical guidance can cause problems
 - Robust reporting infrastructure
 - Governance measures to be put into place
- Banks ability to calculate and report its numbers correctly have been challenged.
- Supervisors ability to challenge the reporting will be tested.

Key implementation challenges

Reporting of capital

- Certification of the financial returns by the bank's external auditors is another area of contention.
- Banks did not undertake parallel runs early enough.
- Lots of resistance despite considerable debate.
- Detail guidance and principles were put out.
- Costs and time were the two main issues.

Key implementation challenges

Quality of submissions of the financial returns

- Some banks did not give adequate attention to the accurate submissions of the financial returns.
- Considerable pressure was made to bear on senior management.
- Data submitted was often incomplete.
- No sanity checks were undertaken in some cases.
- Little emphasis was given to implement a proper regulatory framework for reporting.

Key implementation challenges

Preparedness for verification work

- Regulators randomly carry out on-site verification work in some key areas for example;
 - to assess the banks ability to accurately report regulatory capital.
 - to verify the numbers being reported its integrity, accuracy and completeness of the capital calculator.
 - reliability of the source of the information.
 - integrity of the databases.
 - Skills and resources to perform a reporting function.
 - Governance structure for reporting.
 - Internal audit's report on the above.

Key implementation challenges

- **Preparedness for verification work**
- Several problems were experienced in this area.
- Inability to clearly explain issues and have a constructive discussion.
- Lack of involvement from senior management to drive the process.
- Lack of training programs implemented.
- Excessive reliance on external auditors to sort out problems.
- Over-reliance on parent or head office to charge in the case of foreign banks.

Recommendations

Regulatory reporting framework

- Such a framework is highly recommended.
- Ensure that sanity checks are undertaken by senior management.
- Appropriate validation rules are in place and work.
- Easy to identify gaps – understanding and interpretations.
- Ensure submissions are in compliance with the regulatory framework.
- Comfort that the returns have gone through the proper sign-off process.

Thank You