



Convergence Program: Pioneering RIA in South-East Europe

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Committee of European Securities Regulators - ECONET
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“Convergence Program”:

Catalyzing Financial Sector Modernization

- A World Bank-Italy SEE initiative to foster:
 - an analytical culture on financial policy matters
 - collaboration between authorities and market participants
- Distinctive features:
 - **practical focus**
 - targeting regulatory changes that make a measurable difference on financial intermediation, via Impact Assessment analyses;
 - **market-friendliness**
 - sourcing micro-regulatory reform issues from both authorities and market participants,
 - **strong implementation orientation**
 - Success measure is regulatory changes enacted - not studies
 - **flexible partnership arrangements** with other institutions.

Convergence's SPI Romania Program

What is SPI Romania?

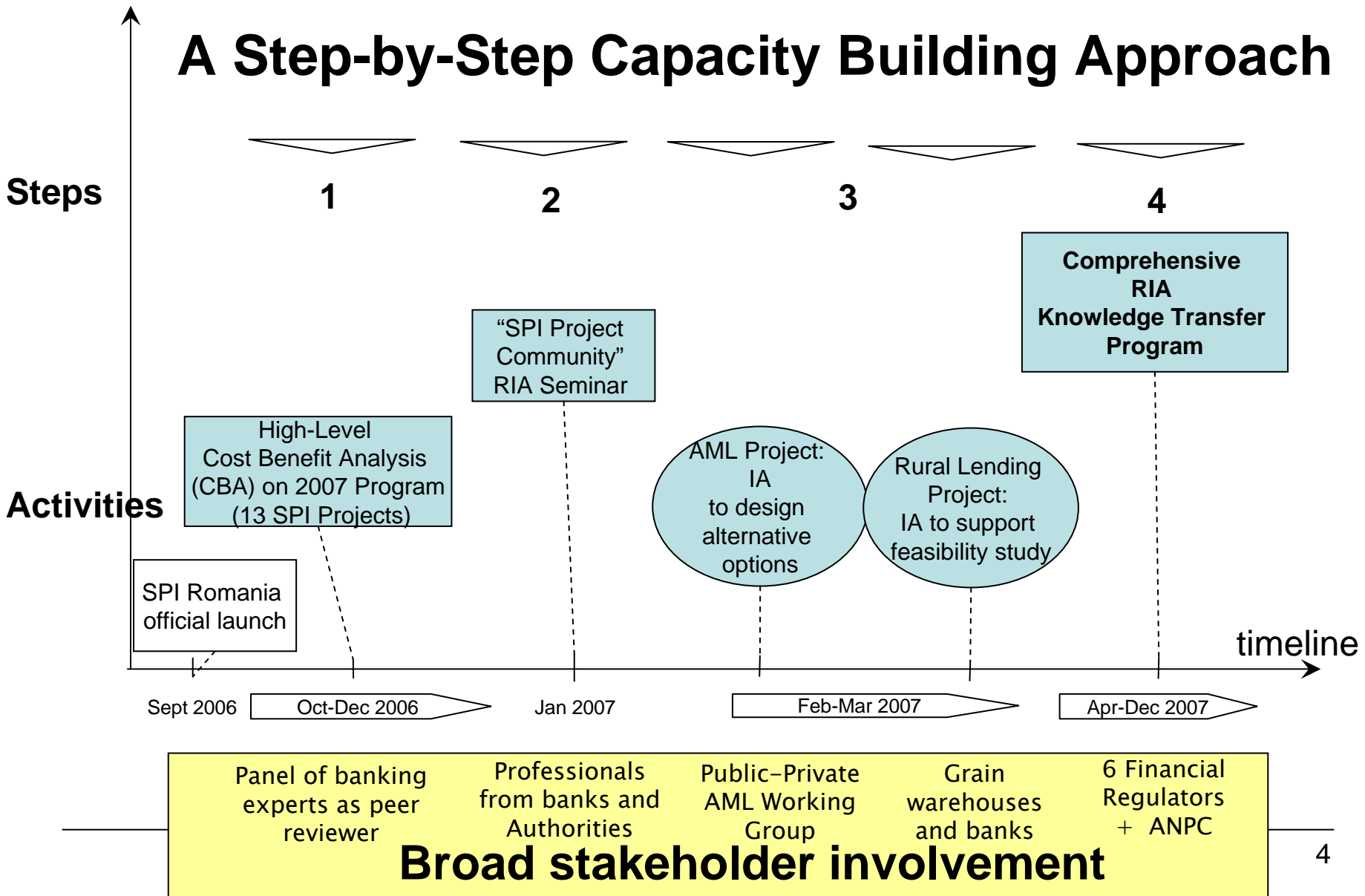
Catalyzed by the Convergence Program, Romanian financial authorities and market participants established a partnership in March 2006 to provide focus and coordination to accelerate modernization of the Romanian financial sector. Website: www.spi-romania.eu.

Set-Up

- **5-person SPI Committee**
High-level direction and endorsement
- **13 Public-Private Working Groups**
Recommendations to SPI Committee based on RIA analyses and consultations by about 120 experts
- **SPI Secretariat**
Two persons for overall management and coordination

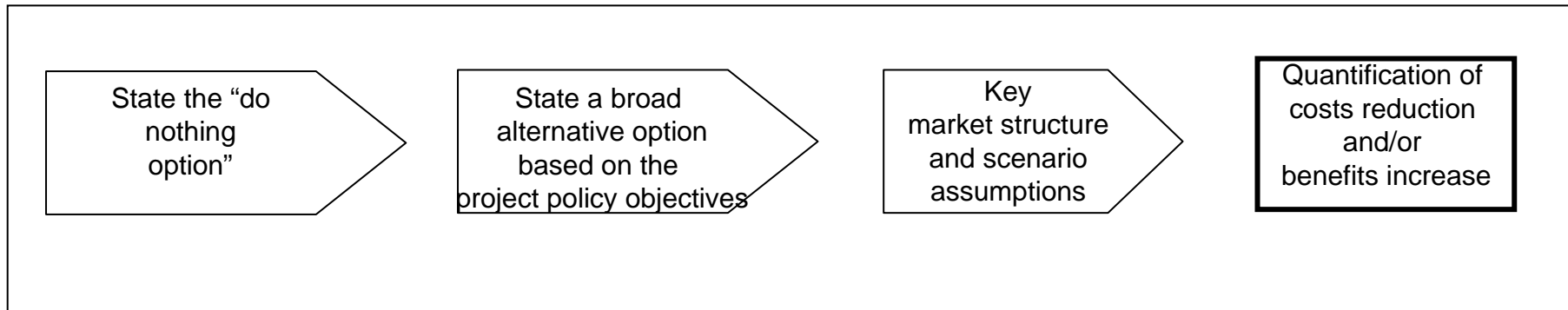
Impact Assessment Skills Are Key To Dialogue

A Step-by-Step Capacity Building Approach



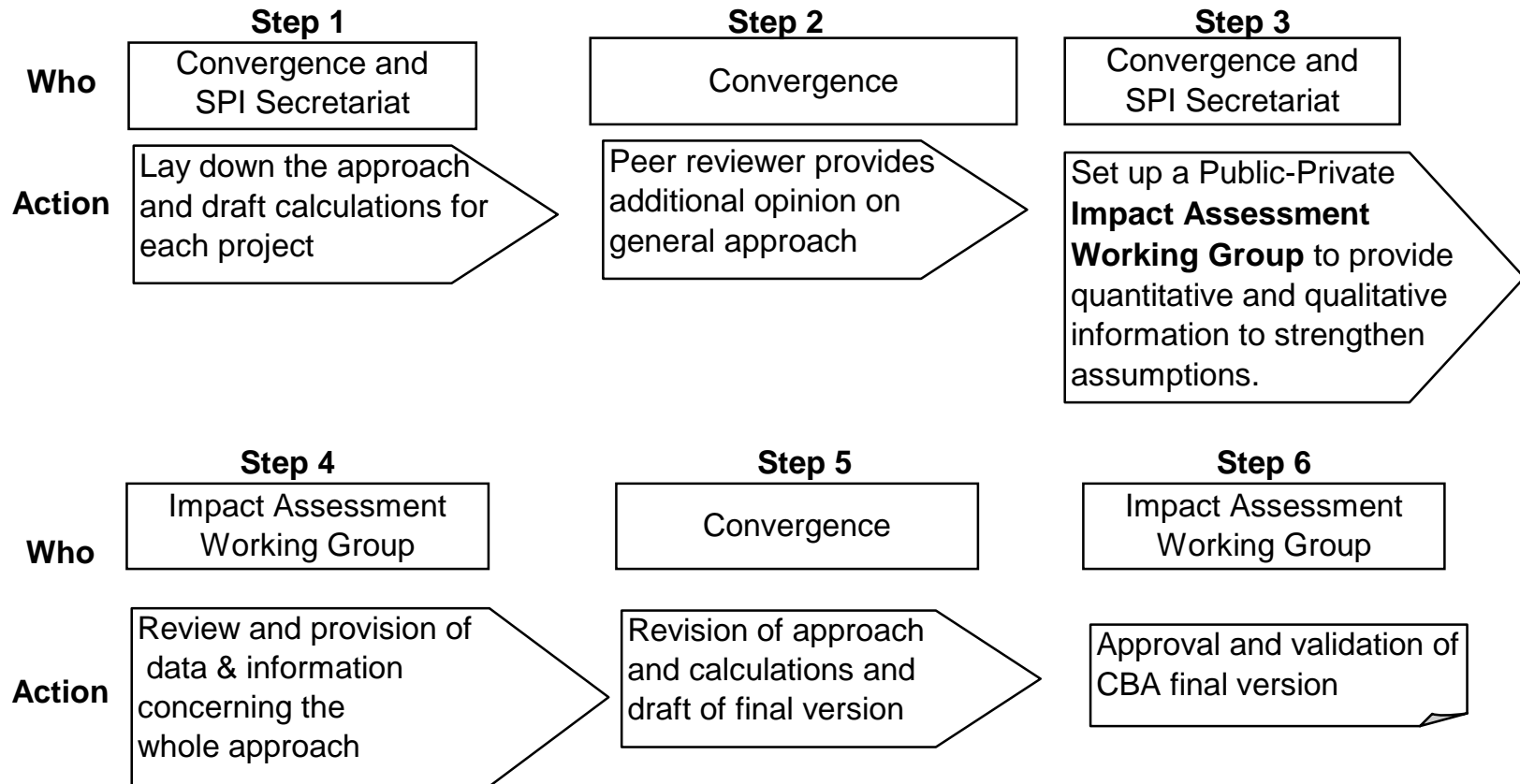
Step 1: High-Level CBA_{1/} on 2007 SPI Program (1)

CBA Assessment Approach



Step 1: High-Level CBA_{1/} on 2007 SPI Program (2)

Validation Process



An Example: Law on Safety

Context

At present, Law no. 333/2003 regulates the goods safeguard, values and persons' protection, whose provisions apply to all commercial companies, including banks.

Banks are confronted with some practical difficulties in applying the provisions of the law (e.g. complicated and lengthy approval procedures, transportation plans for valuables subject to police approval).

In this context, the SPI Committee wants to propose amendments to the current law to reduce the cost of compliance to the banking system.

Market Participant Impact Taxonomy (1)

Industry competitiveness	Banking and financial regulation	Prudential Supervision Banking compliance with National Central Bank (included transparency, accounting & reporting) Regulation-related risk management activities and databases Balance sheet, accounting principles and international accounting standard - IAS Safety net
	Rule of law and contract enforcement	Civil, penal and administrative regulation affecting banking activity Corporate law Insolvency law and foreclosures
	Taxation	Banks and financial intermediaries Financial activities/banking products and services Labor/borrowed money/equity Source/harmonization Auditing and tax collection
	Labor Market	Unemployment Fund and other social contributions Collective labor contract Any other further integrating labor arrangement Regulation on labor

Type of Regulatory Optimization

Business development	Financial market infrastructure	Payment systems Public/private credit registries Primary/Secondary Markets Trading and post-trading services Investment banking Stock Exchange
	Financial products/services	Corporate lending Retail lending Other lending Payment products/services Asset management Investment banking

Industry reputation	Market confidence (negative externality, market power) Consumer protection (information asymmetry, market power) Public awareness (positive externality)
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Market Participant Impact Taxonomy (2)

Balance Sheet and Income Statement items affected

BALANCE SHEET

Assets

Customer Loans
 Other Loans
Total Customer Loans

Problem Loans - memo
 Other non-performing Loans
Total Problem Loans
Total Loans - Net

Other Earning Assets
 Due from Other Banks
 Other Securities
 Investment Securities
 Trading Securities
Total Securities

Equity Investments
 Other Investments
Total Other Earning Assets

Non-Earning Assets
 Cash and Due from Banks
 Intangible Assets
 Other Non Earning Assets
Total Non Earning Assets

Fixed Assets
 Total Fixed Assets

Liabilities

Deposits
 Customer Deposits
 Banks Deposits
Total Deposits

Money Market Funding
 Other Negotiable Instruments
Total Money Market Funding

Other Funding
 Other Bonds
 Subordinated Debt
 Other Funding
Total Other Funding

Loan Loss and Other Reserves
 Other Non Equity Reserves
Total Loan Loss & Other Reserves

Other Liabilities
 Other Liabilities

Total Liabilities

Equity Reserves
 Retained Earnings
 Other Equity Reserves
 Minority Interests
 Total Equity Reserves

INCOME STATEMENT

Interest Income
 Interest Expense
Net Interest Revenue

Commision Income
 Commision Expense
Net Commision Revenue

Net Trading Income
 Other Operating Income
Total Operating Income

Personnel Expenses
 Other Admin Expenses
 Other Operating Expenses
 Loan Loss Provisions
 Other Provisions
Total Operating Expense

Non-Operating Income
Pre-Tax Profit

Taxes
Post Tax Profit

Focus:

Capital
 Tier 1 Capital Ratio
 Total Capital Ratio

Measuring Impact of Regulatory Options

Main policy choices

- “Allow banks to use risk based analysis in order to determine the requirements, the measures, the means, and the forms of ensuring the safeguard of values and the protection of persons”;
 - “Allow for the use of standard projects for the electronic security systems tailored by categories of units of an entity”;
 - “The safeguard plans get approved only if the risk based analysis indicates that the safeguard is ensured with dedicated personnel”;
-

**Each item
impacting
on...**

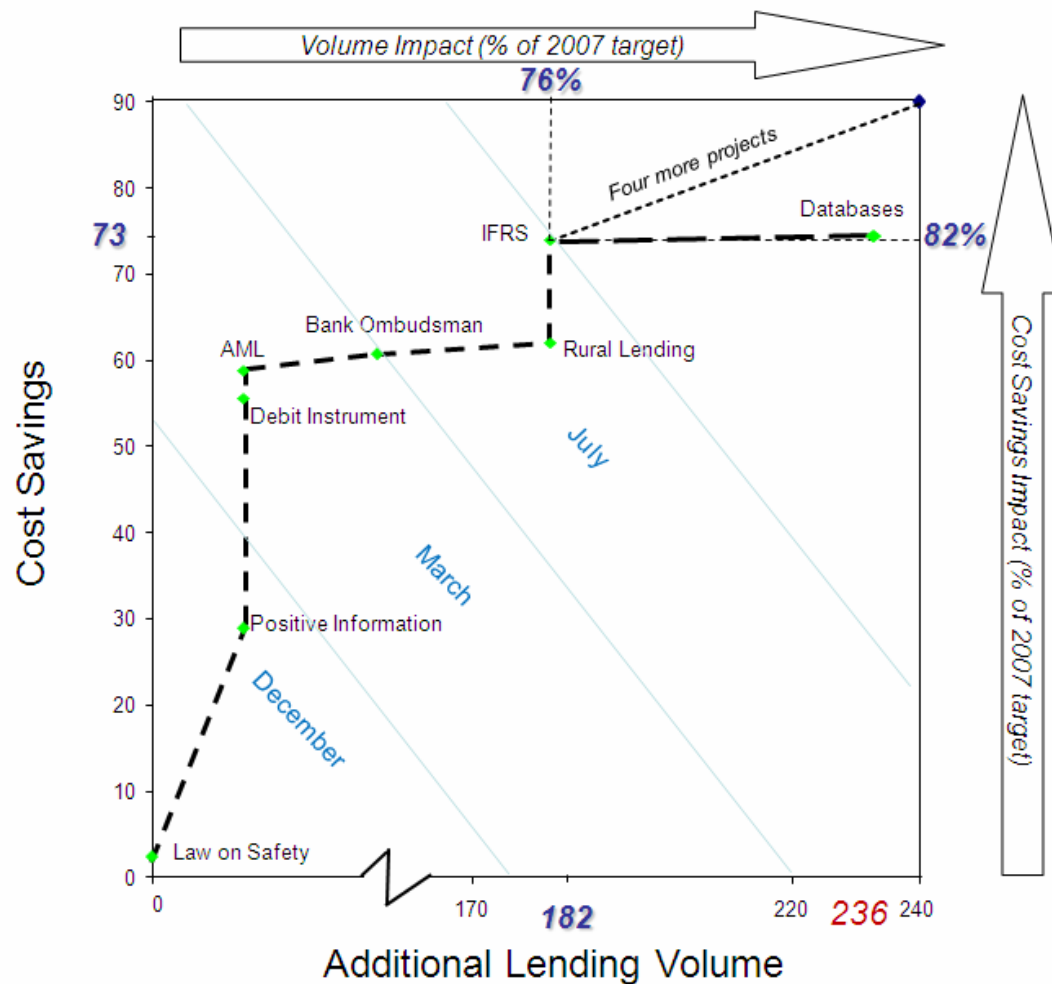
Main Balance Sheet and Income Statement items affected

- Personnel costs;
- Other administrative costs;

**DETAILED ANALYSIS SHOWN
IN ANNEX**

2007 SPI Program High-Level CBA

Financial Impact of Finalized SPI Projects (Mln, EUR) – First Full Year



Step 2: “SPI Project Community” RIA Seminar (1)

Setting a common language

Aims of the Seminar

The seminar objectives were:

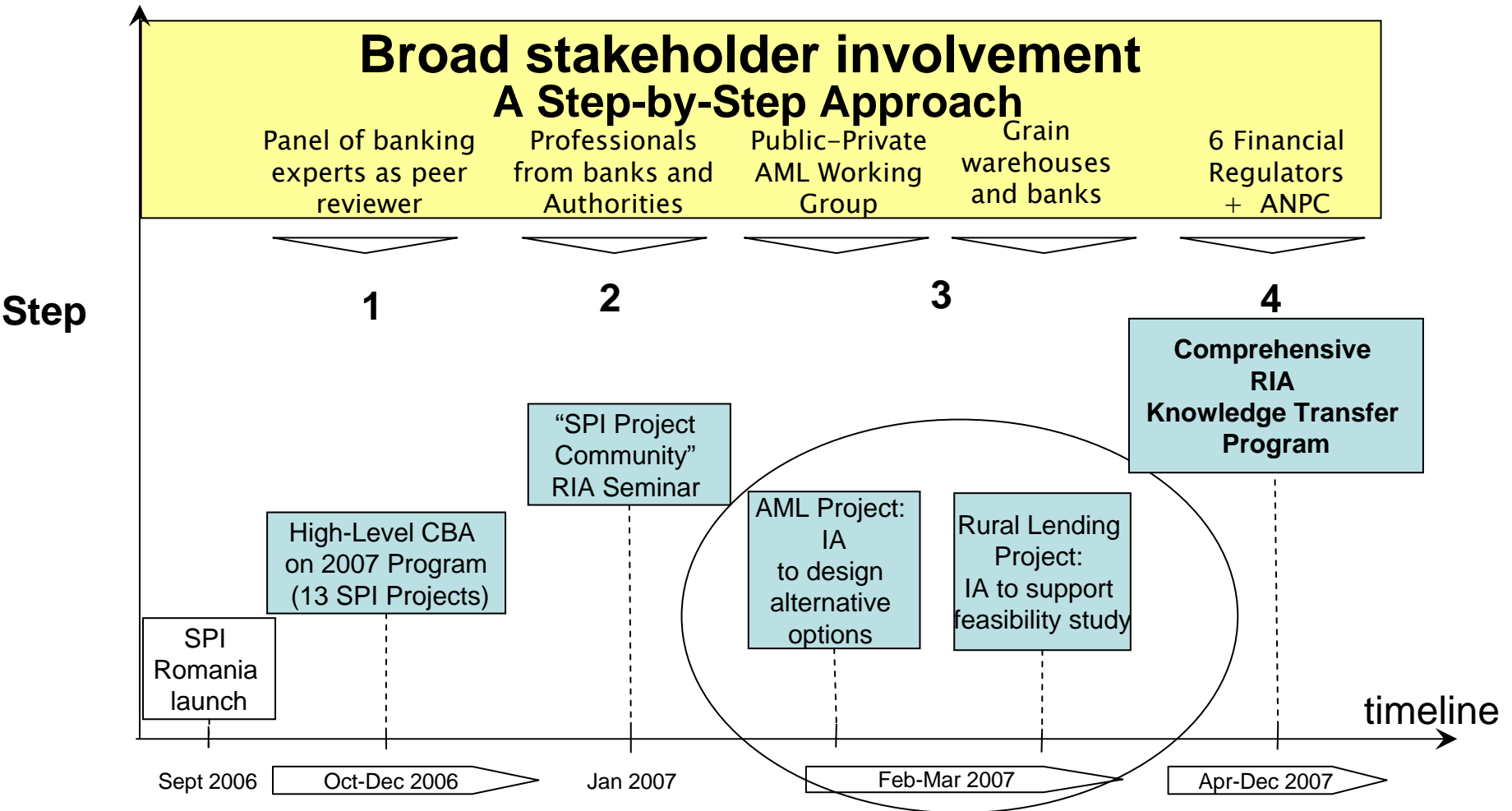
- To illustrate the methodology and findings of high level CBA on 2007 SPI Program to a broader community;
- To help PWG members use RIA tool to assess regulatory options discussed within Working Groups.
- To develop awareness among “SPI Project Community” about the economic relevance of each project;
- To improve understanding of preliminary RIA estimates and rationale;
Targeted attendants are Project Managers, Deputy Project Managers and Working Group members of all SPI Projects.

Building an IA local community

PUBLIC STAKEHOLDER	# PWG Members
AML Office	1
Credit Bureau	2
FGCR	1
Ministry of Agriculture	1
MPF	7
NBR	12
NACP	1
Transfond	1
Total	26

PRIVATE STAKEHOLDER	# PWG Members
Alphabank	5
Banca Anglo Romana	1
Bancpost	7
BCR	11
BRD-GSG	4
CEC	2
Finansbank	1
HVB Tiriac Bank	1
Mindbank	1
OTP Bank	2
Raiffeisen	3
RIB	1
RZB Romania	5
Unicredit Romania	4
Total	48

Step 3: Detailed RIA To Support Decisions



Step 4: RIA Knowledge Transfer Program

Aim of the Program:

To transfer Regulatory Impact Assessment (RIA) reference knowledge and build practical RIA experience for financial regulator staff. (Similar to CESR-ECONET Initiative)

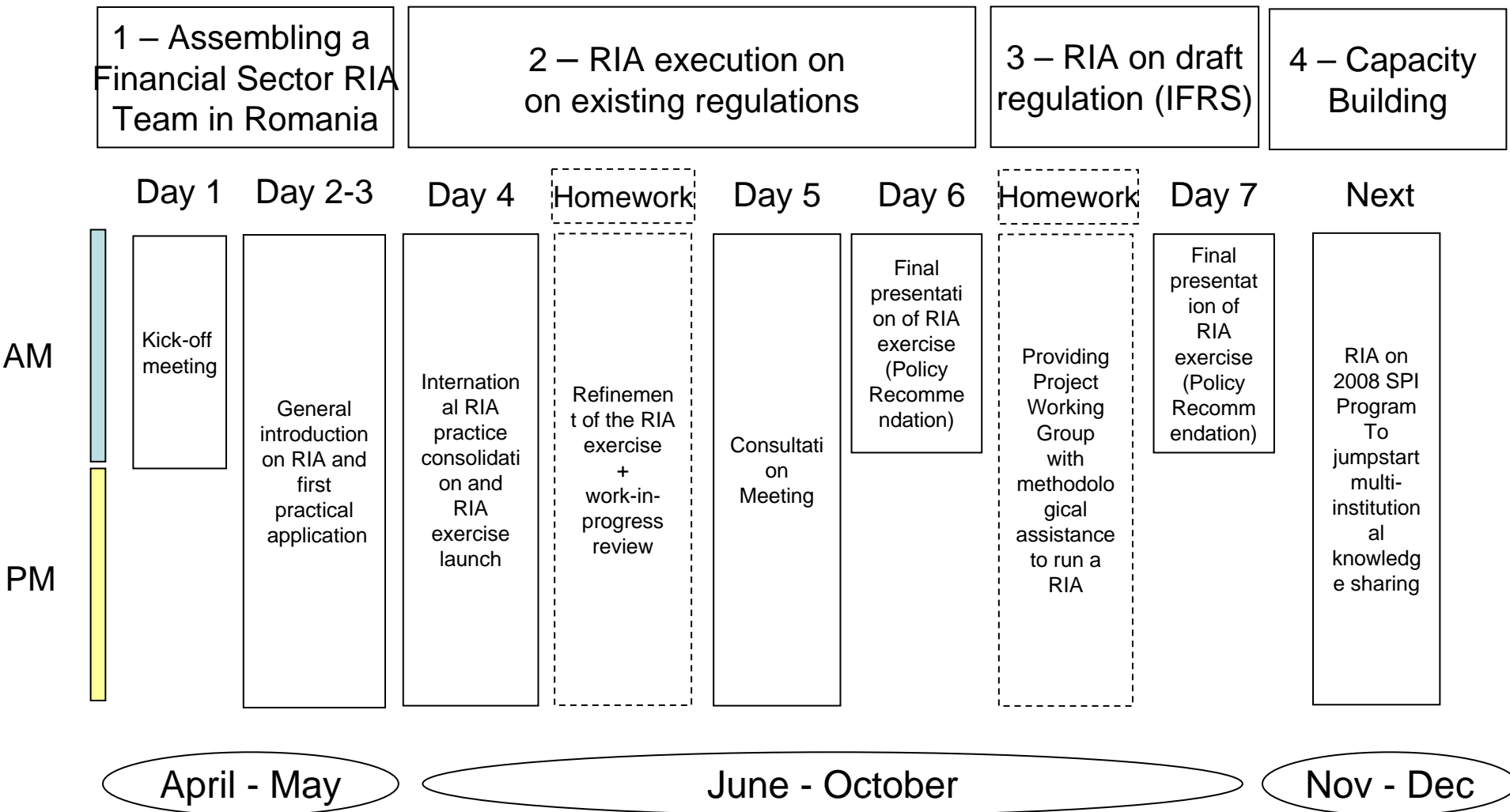
Participating authorities:

- General Secretariat of the Government;
- National Bank of Romania;
- Ministry of Economy and Finance;
- National Securities Commission;
- Insurance Supervision Commission;
- Commission for Supervision of Private Pensions System;
- National Authority for Consumer Protection.

International partners:

Institution	Expert
Uk Financial Services Authority	Mr. Stephen Dickinson
Irish Financial Regulator	Mr. John Pyne
German Ministry of Finance	Mr. Claus-Michael Happe
Oxera	Mr. Paul Gower

Step 4: RIA Program At-A-Glance



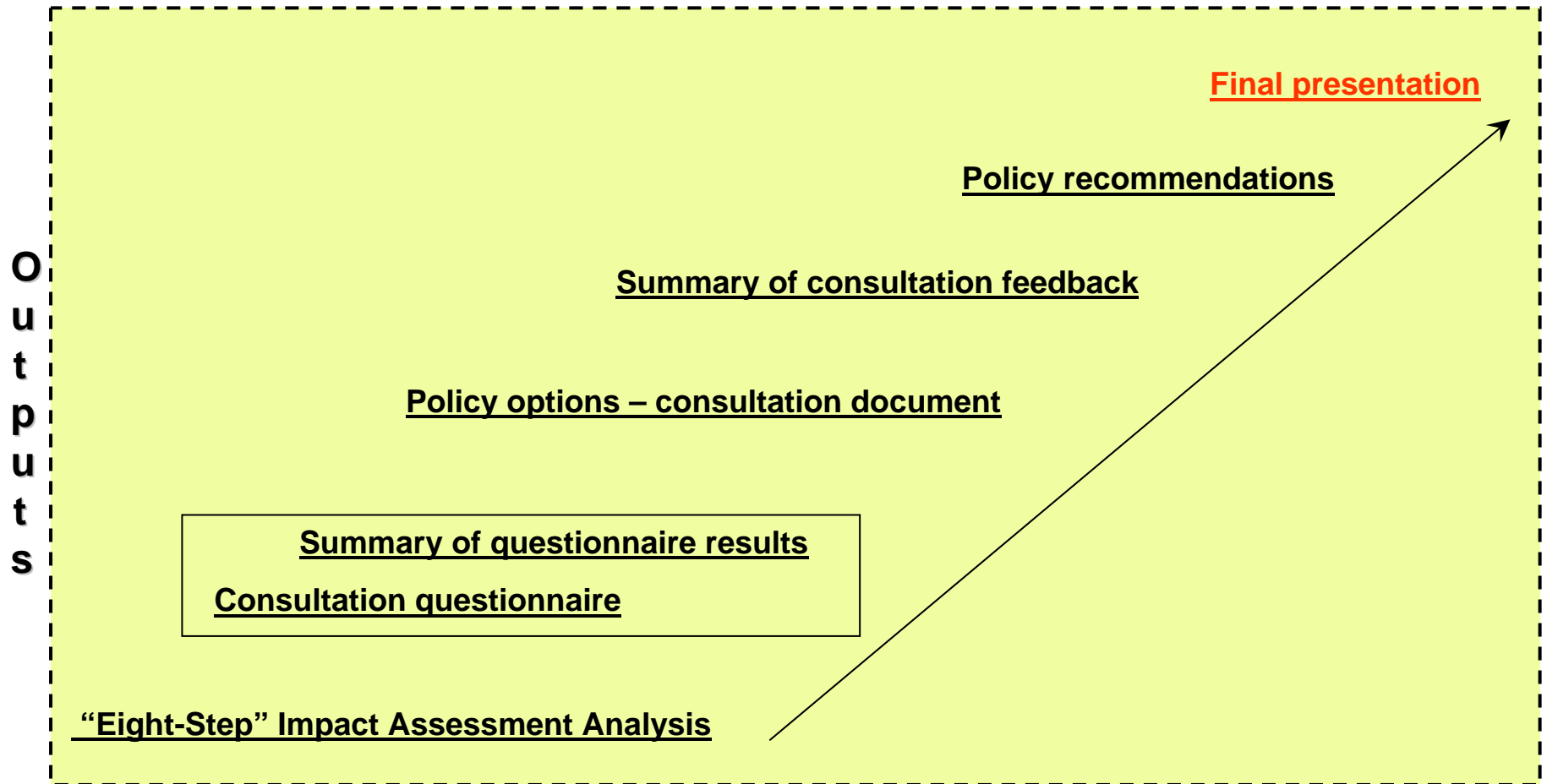
Our Core IA Template

Steps of the RIA Process	Purpose of each RIA Step
Scoping of problem	
1. Problem identification	To understand a market/regulatory failure analysis in order to establish whether or not there is an economic case for regulatory intervention
2. Definition of policy objectives	To identify the effects of policies. This is useful to check whether the regulatory action brings the market closer in line with organizational regulatory objectives.
3. Development of “do nothing option”	To identify and state the status quo
4. Development of alternative policy options	To identify and state alternative policies (among them the “market solution” which consists of relying on market forces alone to solve the problem).
Analysis of impact	
5. Costs to users	To identify and state the costs borne by consumers under all options considered
6. Benefits to users	To identify and state the benefits yielded by consumers under all options considered
7. Costs to regulated firms and regulator	To identify and state the costs borne by regulator and regulated firms under all options considered
8. Benefits to regulated firms and regulator	To identify and state the benefits yielded by regulator and regulated firms under all options considered
Consultations	
9. Data Questionnaire	To collect market structure data to feed into cost and benefit analysis
10. Policy Document	To learn market participant opinions on various policy options (backed by CBA)
Conclusion	
11. Final Recommendations	Final report to decision-makers, based on CBA and market feedback

Source: Convergence Program elaboration based on CESR 3L3 Draft IA Guidelines

RIA Knowledge Transfer – Key Steps

Structured Regulatory Development Process



IA Capacity Building Lessons

- “Law and Economics” approach was new to the local financial community
 - Cost Benefit Analysis is a good start to practice it
- Practicing real RIA cases helps the learning process a lot;
 - IA on local regulations makes knowledge transfer process much more effective;
- Regulators appreciate usefulness of market feedback before policy decisions;
- Feedback to CESR: Please refer to modified IA sequence and structured IA work process (#16-17)

Pioneering RIA: Overall Lessons

- CCSR Impact Assessment Template very useful to guide market-friendly policy formulation
 - Small adjustments based on experience (slides #16-17)
- A simple Cost Benefit Analysis helps explore interface between Law and Economics
 - Once “lack-of-data” panic is overcome
 - Good thinking discipline
- Greatest challenges:
 - Market Failure definition
 - Acknowledgement of past Regulatory Failures
- Greatest opportunities:
 - IA: language and grammar for “better regulation”
 - Dialogue between authorities and market participants.

Other Convergence SEE

RIA Capacity Building Activities

Center of Excellence of Finance (Ljubljana)

- 3-day seminar:
 - I – Introduction to Financial RIA;
 - II - International case studies;
 - III –RIA exercise by participants.
- 23 participants from Albania, Bulgaria, Croatia, Kosovo, Macedonia, Montenegro, Romania and Slovenia;
- 92.5% participants' approval rate;
- Follow-up: Bulgaria.

Bulgarian Financial Supervision Commission

- Two-Phase two-month seminar:
 - I – Introduction to Financial RIA
 - II - International case studies
 - III – Practice on local regulations
- Broad local attendance:
 - Authorities:
 - Financial Supervision Commission; Bulgarian National Bank; Ministry of Finance; Bulgarian Stock Exchange; Central Depository AD.
 - Market participants:
 - Associations of Banks in Bulgaria; Bulgarian Association of Asset Management Companies.
- 92.5% participants' approval rate.

Other Convergence RIA Work

Albania

- Financial intermediation impact from higher banking share of remittances
- Lending volume and bank margin impact from proposed collateral law reform

Croatia

- Foreign debt and bank profitability impact from proposed securitization law

Romania: An Expanded IA Platform

2008 Financial Sector Modernization Program

European Central Bank CRITERIA					
Italian Banking Association CRITERIA	Asymmetric information	Completeness of the market	Increased opportunities to engage in financial transactions	Reduced transaction costs	Increased competition
Business development		1. Increasing bank lending under PPPs 2. Promoting refinancing through securitization 3. Green Banking 4. Organizing T-bill OTC market 5. Modernizing T-bill regulatory framework 6. BSE Listing T-bills	1. Development of Interbank Direct Debit 2. Standardization of the contractual framework for repo and derivative transactions 3. Securing down payments made by individuals for real estate projects 4. Facilitating structural lending 5. Supporting thermal rehabilitation of houses 6. Developing lending to municipalities		
Industry competitiveness	1. Database for risk rating the corporate clients 2. Centralized database for AML purposes		1. Improving access to and availability of the basic banking products 2. Electronic employment register and services	1. The banks' future contributions to RDGF 2. Improving account stopping regulation 3. Reducing the paper-based documents 4. Centralized tax roll 5. Facilitating bad debts recovery	1. Improving the payments framework
Industry reputation	Better information on saving products	1. Expanding Banking Mediator 2. Bank Code of Conduct 3. Ombudsman knowledge transfer	1. Standardizing the minimal information for basic bank products and services 2. Standardizing the advice on selected bank products and services 3. Enhancing Corporate Social Responsibility in the Banking Industry	1. Improving the quality of the education and professional training in the banking field 2. Improving consumer protection framework	1. Enhancing financial consumer's protection 2. Responsible borrowing
	3	9	11	7	3

Thank You!

- More information on SPI Romania RIA work:

<http://www.spi-romania.eu/ria-capacity-building/>

- Convergence Program contact:

convergence@worldbank.org

A CBA Example

Law on Safety

Gathering The Numbers...

Analytics - 1

Total territorial units of banks	a)	3,845
Average number of transportation plans over a year drawn by each unit for police approval (#)	b)	24
% total territorial units that externalize the transport of valuables	c)	40%
Time needed by each unit to take care of the approval procedure (FTE)	d)	
Average unit that rely on internal services	d1)	0.25
Average unit that externalize	d2)	0.50
Gross daily cost of a bank staff (RON)	e)	222
Costs of complying with police approval for transportation plans (Mln, RON)	f)=a*b*d*e	7.2
Average number of records for 1 working day of non-stop	g)	1
Rate of positive records over a month (%)	h)	2%
Unitary cost of each negative record (opportunity cost + storing cost) (RON)	i)	1.5
Number of records needed every year [#]	i)	264
Costs of complying with storing "blank" records in each of the territorial unit (Mln, RON)	j)	1.5

		2007	2008	2009	2010	2011	5-year NPV
PV - Costs of complying with police approval for transportation plans (Mln, RON)	i)	6.7	6.3	5.8	5.4	5.1	29.3
PV - Costs of complying with storing "blank" records in each of the territorial unit (Mln, RON)	ii)	1.4	1.3	1.2	1.1	1.1	6.1

Discount rate (%)	7.10%
Discount factor	0.933707 0.871808 0.814013 0.76005 0.709664

Gathering The Numbers...(2)

Analytics - 2

Data and assumptions:

a) % total territorial units that externalize the transport of valuables		40%
b) Time needed by each unit to take care of the approval procedure (FTE)		
i) Average units that rely on internal services	0.25	
ii) Average units that externalize	0.50	
c) Gross daily cost of a bank staff (RON)		222
d) Average number of records for 1 day of non-stop video (#)		
e) Rate of positive records over a month (%)		2%
f) Unitary cost of each negative record (opportunity cost + storing cost) (RON)		2
g) Number of records needed every year [#] (<i>1 record per working day</i>)		264

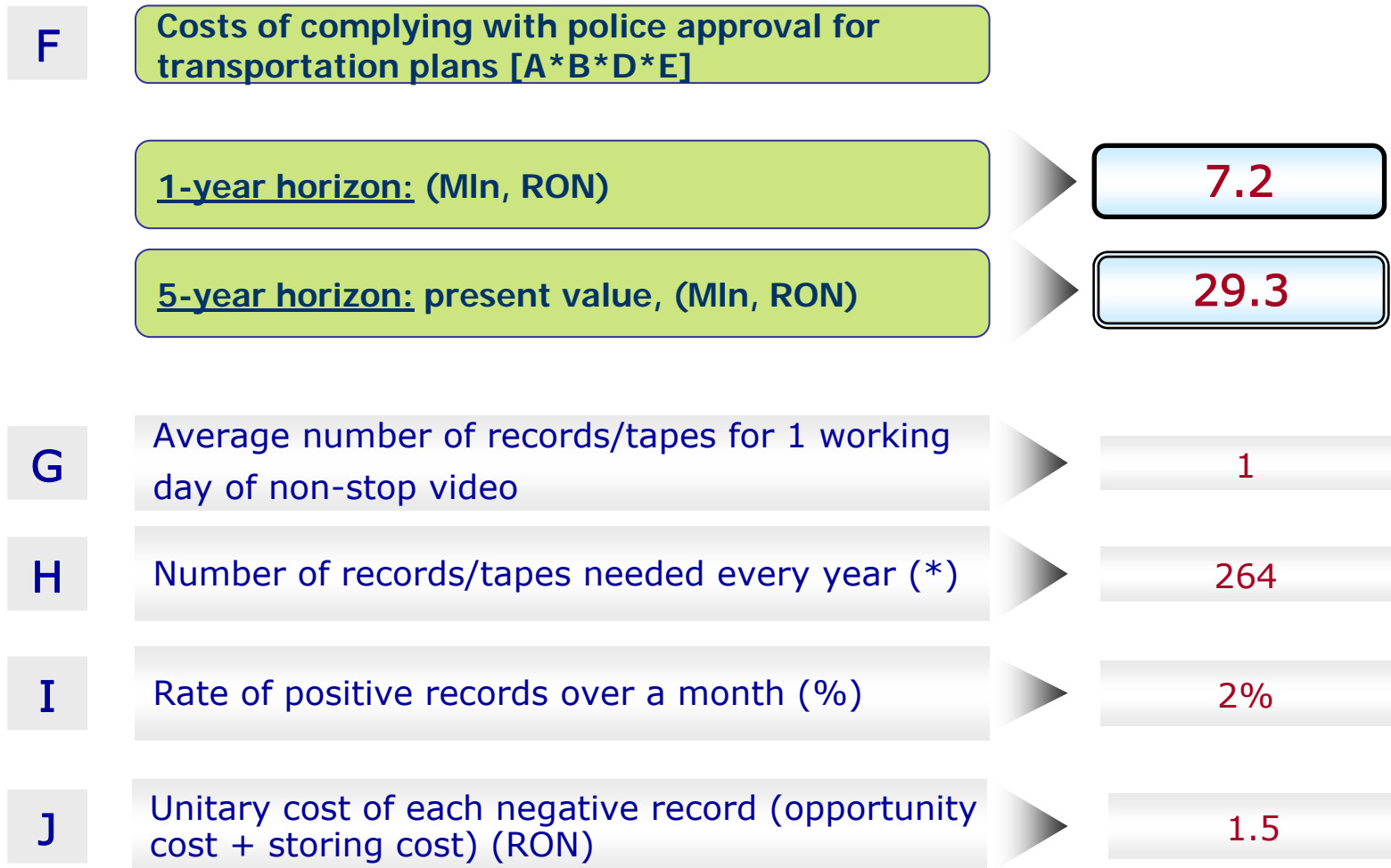
...Running the Analysis...

Economic impact assessment - 1

A	Total territorial units of banks (#)	3,845
B	Average number of transportation plans over a year drawn by each unit for police approval	24
C	% total territorial units that externalize the transport of valuables	40%
D	Time needed by each unit to take care of the approval procedure (FTE)	
D-1	Average unit that rely on internal services	0.25
D-2	Average unit that externalizes	0.50
E	Gross daily cost of a bank staff (RON)	222

...Running the Analysis... (2)

Economic impact assessment - 2



... Reaching an Overall Estimate

Economic impact assessment - 3

K

Costs of complying with storing "blank" records in each of the territorial unit

1-year horizon: (Mln, RON)

1.5

5-year horizon: present value, (Mln, RON)

6.1

L

Overall impact [F+K]

1-year horizon: (Mln, RON)

8.7

5-year horizon: present value, (Mln, RON)

35.4