

Section 1:

Setting the stage:

Background

As the transparency become more challenging and the scope of banks' activities expanded over the years, there is a call for better transparency by regulators and public, investors, market entities as well in Albania.

- The guideline "On the Transparency of the banking operations and services" is effective since 1999 and the banks' activities have become more complex and dynamic.
- There is not a specific regulation on disclosing the information by banks on their activity, financial conditions, progress, risk profile and its management, policies and their processes of administration, as well as accounting policies for the public and the market participants (as imposed by provisions on the new law on banking and international standards). Project regulation "Minimum requirements for disclosure of information by banks and branches of foreign banks".

Section 2:

Scoping the problem

a) What is the problem under consideration?

The level of bank transparency throughout banking operations and services (asymmetric information) to the clients (borrowers/depositors) as well as on the publication of financial position, risk profile and its management, policies and strategies, etc. (public disclosure).

Problem Identification

b) Why is regulatory intervention necessary?

We as regulators (supervisors) believe that we are dealing with regulatory and market failure in case of bank transparency to its customers and market failure with regards to transparency of banking operations and services which cannot be corrected by the market itself.

Definition of Policy objectives

a) General objectives:

- ▶ consumer protection
- ▶ financial stability
- ▶ proper functioning of the financial market.

b) Specific objectives

- ▶ enhancing bank transparency by disclosing the appropriate information for consumers and the market participants

c) Operational objectives

- ▶ ensure the appropriate information to consumers on banking services and products;
- ▶ ensuring compliance with the public disclosure standards on six broad categories of information (financial performance, financial

position including capital, solvency and liquidity, risk management strategies and practices, risk exposures, accounting policies and basic business, management and corporate governance information);

Development of “do nothing” option

The existing regulatory framework on banking operations and services transparency is not going to be updated in accordance with the market developments and the regulation on the minimum requirements for disclosure of information by banks is going to be drafted. This option could not improve the situation evidenced in the market entities during the on-site inspections on banks' transparency issues and in the meantime could not improve the services and products to the clients, the market discipline aiming long-term stability for both individual banks and banking system as well as the interaction between the prudential rules and market players and their incentives.

Alternative Policy options

BoA proposes to update the regulatory requirements and powers improving the existing regulation, also to issue the by-laws related to the new law on banking.

Regulatory design of BoA objectives and principles

The areas to deal with are the following:

- transparency to clients (rights & obligations, terms and conditions of their contractual relationships with the banks clearly defined, informing the clients about changes in

- contractual terms and conditions), and satisfactory proof of customer acknowledgment;
- advertisement practices (truthful ads, no misleading ads);
 - New functions dealing with customer complaints (the customer's book, and setting out the procedure on dealing with customer complaints) [an analysis of customer complaints would allow to update the standards and correspondent communication of public disclosure].

What needs to be done (next steps):

- Legal gap analysis
- Findings of main results from on-site inspections

Project "Minimum requirements for disclosure of information by banks and branches of foreign banks"

- Banks will be obliged to disclose information based on 6 broad categories:
 1. organization structures of the bank and their main activities
 2. Financial performance
 3. financial situation (capital, solvency, liquidity)
 4. strategies and practices of risk administration
 5. risk exposures (credit risk, market risk, liquidity risk, operational and legal risk, etc.)
 6. accounting policies.
- The abovementioned information that need to be disclosed is divided into quantitative and qualitative information on quarterly and annual basis.
- Banks can disclose additional information on voluntary basis.

Summary Problem Scoping (client transparency)				
Market failure				
Asymmetric information	Market power	Positive externalities	Negative externalities	
X	X		X	
(Existing) Regulatory failure				
Regulation wrongly prescribed for the market	Regulation succeeded in addressing the failure; a different market failure (e.g. side effect)	Regulation made it worse	Regulation so far has failed to work; maybe in due course	Existing regulation needs to be revised
				X

Summary Problem Scoping (publication transparency)				
Market failure				
Asymmetric information	Market power	Positive externalities	Negative externalities	
X	X		X	
(Existing) Regulatory failure				
Regulation has not existed	Regulation wrongly prescribed for the market	Regulation succeeded in addressing the failure; a different market failure (e.g. side effect)	Regulation made it worse	Regulation so far has failed to work; maybe in due course
X				

Section 3:

Summary: impact analysis evidence

Tab.1

Explanation of detriment			Potential benefits of regulations
Types of consumers detriment in the absence of regulation	The transparency of the banking operation and services.	Minimum requirements for disclosure of information by banks.	
<i>Sub-optimal choice</i>	Mis-choice of financial products. Consumers can not evaluate the characteristics of a product.	Mis-oriented in decision making regarding investment in banking system.	Consumers can take better decisions (they can evaluate the characteristics of a product).
<i>Reduced choice</i>	In case of imperfect information consumers can not evaluate the characteristics of the products and the quality of the producer (bank). The lack of consumer confidence may make it not worthwhile for firms to offer certain types of product, reducing the choices available to the customers.		Consumers benefit from the increased choices.
<i>Higher costs from operational risk</i>	Losses faced by customers because of operational failure (mis-selling, negligent advice, fraud, system breakdown). Higher prices if costs are passed to consumers.		Reduction of expected losses and other costs associated with operational failure.
<i>Higher costs from financial risks</i>	Losses that arise to consumers as a result of a default of a firm (e.g., deposited funds cannot be returned).		Reduction of expected losses and cost associated with financial failure.
<i>Higher costs from systemic risks</i>	Negative externalities where the default of one entity can trigger further defaults in the system.		Reduction of expected losses and cost associated with systemic failure.
<i>Higher prices from market</i>	Consumers pay excessive prices to an entity exercising its market power.		Reduction of excessive prices.

<i>power of firms</i>		
<i>Higher costs from transaction system inefficiencies</i>	System inefficiencies in presence of information problems, (e.g. consumers need to spent more time to for suitable products or providers).	Reduction of transaction costs/prices arising from inefficiencies, including consumer search costs.
<i>Financial exclusion</i>	Even in the case of market efficiency, some consumers may not be able to gain adequate or affordable access to financial services.	Value consumers derive from improved access to financial services.

Tab.2

Regulated institutions costs	“Do nothing”	On the transparency of the banking operation and services.	Minimum requirements for disclosure of information by banks.	Qualitative summary results (High, medium, Low)
Compliance costs				
<i>One-off costs</i>	No costs added	Setting up a policy to deal with the negotiations with dissatisfied consumers.		Low
	No costs added	Setting up a new unit to treat consumers complains (recruiting staff, salaries, IT costs).		Medium
	No costs added	Information and training costs arising from knowing and understanding the new regulatory requirement (including	Information and training costs arising from knowing and understanding the new regulatory requirement, (including	Low

		time)	time)	
<i>On-going costs</i>	No costs added		Publication costs	Medium
	No costs added	Maintenance of equipment of the new unit and revise the policy decided.		Low
	No costs added	Staff costs: salaries	Staff costs: salaries	Low
Indirect				
Regulated firms Benefits				

Tab. 3

<i>On the transparency of the banking operation and services.</i>	<i>Do nothing</i>	<i>Minimum requirements for disclosure of information by banks.</i>
Decreased information asymmetry (between the bank and the consumer).	Unchanged information asymmetry.	Decreased information asymmetry (more information available in the financial market).
Increased product quality; (Better understanding of the consumers' needs. Better management for products offered to clients).	Unchanged conditions regarding understanding of the products by the clients and the overall market confidence.	Increased market confidence.
Increased consumer confidence.	Unchanged consumer confidence and financial stability.	Enhanced financial stability.
Reduction of nonperforming loans.	Unchanged efficiency.	Reduced cost of capital (if listed in a stock exchange).
Better risk management.	Unchanged risk management.	
Increase the soundness of the financial system.	Unchanged efficiency.	Increased efficiency in competition.
Increased efficiency in competition.	Unchanged efficiency in competition.	