# 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

**Guideline "On the transparency of the banking operations and services":**

- **The law on banking has strengthened customer protection, which need to be reflected in the respective by-laws.**
- **Following complaints by clients of the banks on the transparency of the institutions the guidelines expands on the elements that need to be made public to the client. E.g. the loan and deposit contract.**

- The guideline in force is outdated and does not reflect the complexity of the banking products in the market therefore difficult to enforce by both the banks and regulators. A more comprehensive project is needed.
- New structures that will deal with customer complaints: the customer's book, and setting out the procedure on dealing with customer complaints.

**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. | |
| *Sub-optimal choice* | 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). |
| *Reduced choice* | 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. |
| *Higher costs from operational risk* | Looses 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. |
| *Higher costs from financial risks* | Losses that arise to consumers as a result of a default of a firm (e.g., deposited funds cannot be returned). | | Reduction of expected loses and cost associated with financial failure. |
| *Higher costs from systemic risks* | Negative externalities where the default of one entity can trigger further defaults in the system. | | Reduction of expected loses and cost associated with systemic failure. |
| *Higher prices from market power of firms* | Consumers pay excessive prices to an entity exercising its market power. | | Reduction of excessive prices. |
| *Higher costs from transaction* | System inefficiencies in presence of information problems, (e.g. consumers | | Reduction of transaction costs/prices |

| | | |
|---|---|---|
| *system inefficiencies* | need to spent more time to for suitable products or providers). | arising from inefficiencies, including consumer search costs. |
| *Financial exclusion* | 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** | | | | |
| *One-off costs* | 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 time) | Information and training costs arising from knowing and understanding the new regulatory requirement, (including time) | Low |
| *On-going costs* | No costs added | | Publication | Medium |

| | | | | |
|---|---|---|---|---|
| | | | costs | |
| | 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 costs** | | | | |

Tab. 3

| | Regulated firms Benefits | |
|---|---|---|
| On the transparency of the banking operation and services. | Do nothing | Minimum requirements for disclosure of information by banks. |
| 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. | |