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KEY CHARACTERISTICS ELEMENTS OF THE BANKING SUPERVISION SYSTEMS

У статті досліджено основні елементи системи контролю банківської діяльності. Визначено структурні рівні процесу здійснення контролю та відповідний до нього суб'єктний склад. Проаналізовано основні показники діяльності України з позиції банківського нагляду НБУ. Узагальнено результати дослідження стосовно сутнісної відповідності контролю банківської діяльності в Україні до міжнародних стандартів.

This article studies the basic elements of the banking supervision system. The structural levels of the supervision process and an appropriate subject composition have been defined. The basic indicators of Ukraine's performance from the perspective of the NBU banking supervision have been analyzed. The findings from the study of the essential compliance of the banking supervision in Ukraine to international standards have been summarized.

Ключові слова: банківська діяльність, банківський контроль, зовнішній та внутрішній контроль банківської діяльності, Базельські принципи.

Keywords: banking, banking supervision, external and internal banking supervision, Basel principles.

Problem formulation. The stability of the economy of any nation, and Ukraine in particular, largely depends on the efficient operation of its banking sector. This raises the question of banking supervision in terms of the effectiveness and usefulness of the banking sector functioning to ensure sustainable development and performance of the banks in Ukraine and creation of an appropriate competitive environment in the financial market, and as a result to protect the legitimate interests of all banking participants and to create favourable conditions for economic development of Ukraine. The economic effect of effective regulation of banking supervision will reflect in various aspects of the economic environment, both in enhancing the competitiveness of the national banking sector with a stable reputation in the international banking environment and in improving the stability of the national economy in general.

Analysis of recent researches and publications. The issue of banking supervision in the context of various functional appointments in the banking sector was considered by such scholars as G. Bilokin [3], A. Gerasimov [4], L. Dikan [6], N. Deeva [7], A. Kireyev [8], T. Kravtsov [9], V. Savchenko [12], B. Stefanyuk [13] N. Synyuhina [5], N. Shvets [14], and others. But due to essential divergence in determining the supervision essence in the banking sector and the relationship with various types of banking supervision the question of characterising the supervision system remains not enough researched.

Problem definition and goal.

Determination of the fundamental aspects of the need for supervision in the banking sector, for researches of the types of the banking supervision systems and for the proposals aimed at improving the existing supervision system in accordance with the international standards and principles in the banking supervision system.

Statement of the principal research material. Today, against the background of globalization of the processes of economic development the need for supervision becomes important. In a broad sense the essence of the “supervision” definition can be defined as a complex of actions aimed at monitoring the operation of the relative object/subject being under supervision in order to obtain objective and reliable information about its functional features and activity performance. In turn, operation of the banks is subject to supervision of many bodies (the Accounting Chamber, the State Tax Administration, the Main Control and Revision Office, law-enforcement authorities, the NBU, accounting firms, etc.). Each of these bodies and organizations establishes certain goals during the audit, which may vary significantly and even to engage in conflict. Of all of the supervision subjects mentioned above only the National Bank of Ukraine and audit firms are motivated during supervision by the goals of ensuring stability of the banking system, that is contribute to achieving one of the main objectives of banking regulation. This results in the concept of banking supervision as a specific function of managing the second level of the banking system, i.e. commercial banks. The banking supervision is a system of evaluation of the success of the objectives set for the banking system, i.e. comparing actual achievements with the indicators established by regulatory and administrative bodies [6].

Exploring the nature of banking supervision from the perspective of a system approach, it is appropriate to explore its elements, namely goals, objectives, subjects, matters and

object of banking supervision. Thus, the purpose of the banking supervision is objective studying of the actual situation in the sector audited, identifying the factors and conditions that adversely reflected on the execution of the decisions made and achieving the goals set to ensure the reliability and efficiency of the banking system. In turn, the main objective of supervising the commercial banks is to identify matches or deviations (deficiencies) in the regulation of the banking system, to promote the elimination of deviations and to develop effective solutions.

The subject of the banking supervision is the state of economic, organizational, informational, and some other characteristics of the banking system. The objects of supervision in the bank institutions are the banking system as a whole; the bank itself and its branches; transactions carried out by the bank; accounting and reporting; banking.

The subject composition of banking supervision can be defined as external (on the part of the government and independent regulatory agencies) and internal. The subjects of the banking supervision on the part of the state are Accounting Chamber of Ukraine, Control Directorate affiliated with the Secretariat of the President of Ukraine, Main Control and Revision Office, Ministry of Economy of Ukraine, the National Bank of Ukraine, State Tax Administration of Ukraine, State Treasury of Ukraine, State Property Fund Ukraine, Antimonopoly Committee of Ukraine, state budget funds (such as Pension Fund), State Commission on Securities and Stock Market, law-enforcement authorities and others in accordance with the acting legislation. The subjects of independent supervision are independent audit firms, and the subject of internal supervision are the supervisory board, audit committee, the Board (Board of Directors), functional units of the bank, its internal audit service (Fig. 1).

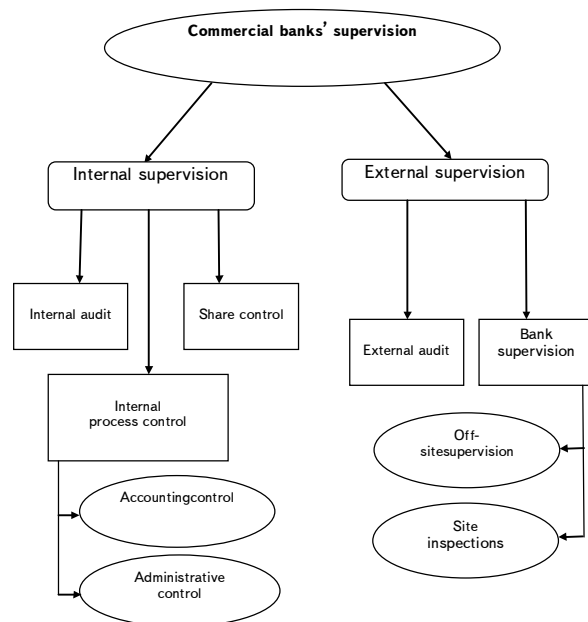


Fig. 1. Banking supervision system of Ukraine [9]

An important part of the banking supervision system is the process of banking supervision of the National Bank of Ukraine. Pursuant to the normative legal acts, the main objective of bank regulation and supervision is safety and financial stability of the banking system, protection of the depositors' and creditors' interests [2].

As of October 1, 2013, 181 Bank of Ukraine (private limited companies) had the banking license of the National Bank of Ukraine to perform banking activities, including one that had the license of the remedial bank.

In the course of the NBU's supervisory policy it was found that the capital of the banks amounted to UAH 181.3 billion or 14.7% of banks' liabilities. In turn, the authorized capital of the banks amounted to UAH 181.0 bln. The banks' liabilities as of October 1, 2013, were UAH 1,052.8 billion. [11].

The main components of liabilities were:

- Funds of individuals — UAH 422.5 bln or 40.1%;
- Funds of economic entities — UAH 220.0 bln or 20.9%;
- Interbank loans and deposits — UAH 105.8 bln or 10.1%.

The structure of the funds of individuals in the banks as of October 1, 2013 was

- Term funds — UAH 335.5 bln or 79.4%;
- Demand deposits — UAH 87.0 bln or 20.6%.

As of October 1, 2013, the assets of the banks of Ukraine amounted to UAH 1,234.1 bln, total assets amounted to UAH 1,367.4 bln.

As of October 1, 2013, the structure of total assets was:

- Cash, precious metals and funds with the NBU — 5.1%;
- Correspondent accounts with other banks — 6.6%;
- Loans granted — 62.9%;
- Investments in securities — 9.3%;
- Receivables — 6.2%;
- Fixed assets and intangible assets — 4.1%;
- Accrued income receivable — 4.0%;
- Other assets — 1.8%.

To ensure more efficient banking supervision, the NBU takes into account information on the main indicators of the Ukrainian banks' operation (see Table 1).

The National Bank of Ukraine carries out banking supervision in the form of inspections and off-site monitoring. In carrying out banking supervision the National Bank of Ukraine has the right to demand from the banks and their executives, bank groups, members of the bank groups to eliminate violations of the banking legislation, to follow regulations of the National Bank of Ukraine to avoid or overcome the adverse consequences that could jeopardize the security of funds trusted to such banks or negatively influence the proper banking activity. If while carrying out banking supervision the National Bank of Ukraine finds that the risk management system is inefficient and/or inadequate, the bank shall, at the request of the National Bank of Ukraine, urgently develop and submit for approval to the National Bank of Ukraine the plan of appropriate measures to eliminate those deficiencies [1].

The efficiency of the banking supervision carried out by the National Bank of Ukraine is based on its adequate legal infrastructure that covers three levels: 1) the current law — the Law of Ukraine On Banks and Banking allows the National Bank of Ukraine broad

formal rights to supervise the commercial banks. These rights were improved and are set out in a new version of the Law of Ukraine On the National Bank of Ukraine, which allows drawing a conclusion that there is a full-scale legislative process in this sphere; 2) regulatory rules – determining by the banking supervision service of interpreting requirements or restrictions for banks in line with their authority, approved by the National Bank of Ukraine; 3) temporary clarifications that are used by the banking supervision service to work out in detail their actions in accordance with applicable laws or regulatory rules and have the form of letters, telegrams, etc.

The National Bank of Ukraine has the right to introduce a special regime for supervising bank operation and appoint a curator of the bank.

The special supervision regime is an additional tool for banking supervision that is usually used in conjunction with measures of influence, namely:

- Written warning;
- Convening of a General Meeting of the members of the Supervisory Board, the Board (Board of Directors) of the bank;
- Signing a written agreement with the bank pursuant to which the bank or the person specified in this agreement undertakes to take corrective actions to eliminate deficiencies, improve bank's financial condition, increase efficiency of the risk management system functioning and/or adequacy, etc;
- Suspending of dividend payments or capital allocation in any other form;
- Establishing increased economic standards of the bank;
- Increasing of the reserves to cover possible loan related losses and other assets;
- Restriction, suspension or termination of certain types of transactions carried out by the bank;
- Prohibition of providing unsecured loans;
- Imposition of fines.

When applying this special regime of the bank supervising the National Bank of Ukraine has the right to prohibit the bank from using direct correspondent accounts for payments and/or demand from the bank to make payments only using consolidated correspondent account.

It should be noted that an important element of the banking supervision carried out by the National Bank of Ukraine is compliance with international standards and principles. In 1997, the Basel Committee on Banking Supervision developed the Core Principles for Effective Banking Supervision, which have been approved by the international financial community at the annual meeting of the International Monetary Fund and the World Bank. [14] The Core Principles for Effective Banking Supervision are used by the states as the standards to assess the quality of supervision systems and prudential regulation, as well as planning activities in this area to achieve the basic level of effective and sound supervisory practices and regulatory policy. The Core Principles for Effective Banking Supervision are also used by the International Monetary Fund and the World Bank in the context of the Financial Sector Assessment Program, namely to assess the current situation of how a country fulfils these principles.

Table 1.

Main indicators of performance of the banks in Ukraine [10]

S. No	Indicator	01.01.2008	01.01.2009	01.01.2010	01.01.2011	01.01.2012	01.01.2013	01.09.2013
1	2	3	4	5	6	7	8	9
1.	Number of the banks according to the Register	198	198	197	194	198	176	180
2.	Excluded from the State Register during the year	1	7	6	6	0	26	0
3.	Number of the banks being liquidated	19	13	14	18	21	22	19
4.	Number of the banks with banking licenses	175	184	182	176	176	176*	178*
4.1	Of them: with foreign capital	47	53	51	55	53	53	51
4.1.1	Including with 100% foreign capital	17	17	18	20	22	22	21
5.	Share of foreign capital in the banks' statutory capital, %	35.0	36.7	35.8	40.6	41.9	39.5	33.8
	ASSETS							
I.	Banks' assets	599,396	926,086	880,302	942,088	1,054,280	1,127,192	1,212,228
	Total assets (not adjusted for the reserves for active operations)	619,004	973,332	1,001,626	1,090,248	1,211,540	1,267,892	1,350,621
1.	Cash and precious metals	18,313	20,668	21,725	26,749	27,008	30,346	32,075
2.	Funds in the National Bank of Ukraine	19,120	18,768	23,337	26,190	31,310	33,740	36,196
3.	Correspondent accounts with other banks	26,293	40,406	51,323	67,596	78,395	99,472	93,634
4.	Loans granted	485,368	792,244	747,348	755,030	825,320	815,327	844,552
	Of them:							
4.1	Loans granted to economic entities	276,184	472,584	474,991	508,288	580,907	609,202	638,490
4.2	Loans granted to individuals	153,633	268,857	222,538	186,540	174,650	161,775	165,992
5.	Long-term loans	291,963	507,715	441,778	420,061	426,430	394,246	399,174
5.1	Of them : long-term loans granted to economic entities	156,355	266,204	244,412	262,199	290,348	276,683	288,474
6.	Overdue loans	6,357	18,015	69,935	84,851	79,292	72,520	75,282

Table 1.

7.	Investments in securities	28,693	40,610	39,335	83,559	87,719	96,340	131,567
8.	Reserves for active operations of the banks	20,188	48,409	122,433	148,839	157,907	141,319	138,963
	LIABILITIES							
II.	Liabilities, total	599,396	926,086	880,302	942,088	1,054,280	1,127,192	1,212,228
1.	Capital	69,578	119,263	115,175	137,725	155,487	169,320	177,167
1.1	Of it: paid authorized capital	42,873	82,454	119,189	145,857	171,865	175,204	179,310
1.2	Share of the capital in liabilities	11.6	12.9	13.1	14.6	14.7	15.0	14.6
2.	Banks' liabilities	529,818	806,823	765,127	804,363	898,793	957,872	1,035,060
	Of them:							
2.1	funds of economic entities	111,995	143,928	115,204	144,038	186,213	202,550	215,063
2.1.1	Of them: term funds of economic entities	54,189	73,352	50,511	55,276	74,239	92,786	90,532
2.2	funds of individuals	163,482	213,219	210,006	270,733	306,205	364,003	416,205
2.2.1	Of them: term funds of individuals	125,625	175,142	155,201	206,630	237,438	289,129	329,151
	For information:							
1	Regulatory capital	72,265	123,066	135,802	160,897	178,454	178,909	186,046
2	The sufficiency (adequacy) of regulatory capital (H2)	13.92	14.01	18.08	20.83	18.90	18.06	17.88
3	Incomes	68,185	122,580	142,995	136,848	142,778	150,449	106,832
4	Expenditures	61,565	115,276	181,445	149,875	150,486	145,550	104,330
5	Performance results	6,620	7,304	-38,450	-13,027	-7,708	4,899	2,502
6	Return on assets, %	1.50	1.03	-4.38	-1.45	-0.76	0.45	0.32
7	Return on equity, %	12.67	8.51	-32.52	-10.19	-5.27	3.03	2.16
8	Net interest margin, %	5.03	5.30	6.21	5.79	5.32	4.51	4.08
9	Net spread, %	5.31	5.18	5.29	4.84	4.51	3.75	3.47

Findings from the study. Considering the results of studying the basic elements of the banking supervision system we can summarize that the banking supervision system is an integrated complex of multilevel processes of various subject composition. The internal banking supervision covers all mechanisms within the bank, is carried out continuously and at all levels, and is a set of procedures that ensure compliance with the internal and external regulations while carrying out bank operations and the accuracy and completeness of the information. In turn, the external banking supervision is designed to regulate bank operations, and includes the NBU's banking supervision system. It should be noted that the NBU's banking supervision system plays the significant role in exercising the functions of banking regulation and supervision; it functions as a single mechanism within the central apparatus and regional offices of the National Bank. Effective interdependence of all levels of the banking supervision will contribute to meeting requirements of the international environment in the fully realised banking supervision and will have a positive social and economic impact on the economy of Ukraine.

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