RE-ENGINEERING REGULATORY CAPACITY FOR SUSTAINED ECONOMIC DEVELOPMENT

Addressing Operational Challenges in Policy Implementation and Compliance within the Financial Sector

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Introduction

- **Relevance of the Topic**

➢ The Global Financial Crises which started in the US, August 2007 underscored the need for enhancing Regulatory Capacity even in Dev. Countries.

➢ The capital market crash of 2008 in the country also underscores the need for stronger regulatory framework.

➢ Recent takeover of 8 large banks and the injection of a bail out fund of N620 billion by the CBN within the year due largely to failure in Corporate governance is another pointer to the need to re-engineer the regulatory capacity.

➢ The financial sector is central to the moblisation and allocation of resources for sustained economic development, hence the need for its effective regulation.

Objective of Objectives of Building A Resilient Financial System in Nigeria

- The FSS 2020 Strategy Document identified the financial system's objectives to include:

- ➢ Strengthening the domestic financial market
- ➢ Enhancing integration with external markets
- ➢ Building an international financial centre (a bill to that effect has been drafted)

Structure of the Financial System

- Major structural component of the financial system through which sustained development is expected include:

- The Banks and other Credit Institutions
- The Capital Market
- The Insurance Market

Reasons for Strong Bank Regulation/ Supervision

- Banks’ intermediation role
- Banks as channel for monetary policy transmission
- Failure of banks affect virtually all other sectors and businesses.
- Fear of contagion effect within the industry as a result of failure of a single bank.
- Need to safeguard the confidence of depositors.

Types & Objectives of Bank Regulation

- Economic Regulations: Designed to:

➢ Promote monetary stability

➢ Ensure Macro-economic stability

➢ Facilitate prospect of rapid growth

- Prudential Regulations: Classified into three:

➢ Preventive (eg; capital adequacy, liquidity, reserve)

➢ Protective (protection in form of deposit insurance)

➢ Supportive (in form of lender of last resort)

Existing Regulatory/ Supervisory Framework for the Banking Industry

- **Central Bank of Nigeria**

➢ Apex regulatory authority

➢ Derives powers from:

❖ **CBN Act 2007** (which repealed 1991 Act and its amendments) Powers include: autonomy, monetary and price stability, economic management, economic adviser to govt.

Existing Regulatory/ Supervisory Framework for the Banking Industry Cont'd

- **BOFIA 1991 As Ammended.** Powers include licensing of banks, powers to regulate and supervise, power to remove erring directors/ principal officers and powers to revoke operating license of a bank.
- Both the CBN and BOFI Acts are currently undergoing reviews to further empower the regulatory authorities

Existing Regulatory/ Supervisory Framework for the Banking Industry Cont'd

- **Nigeria Deposit Insurance Corporation (NDIC)**

was established by Act No 16 of 2006 (which replaced Decree 22 of 1988) to:

- ➢ Insure eligible deposits of bank
- ➢ Pay guaranteed sum in the event of failure
- ➢ Provide financial and technical assistance to insured ailing bank banks
- ➢ Assist in formulation and implementation of banking policies

Existing Regulatory/ Supervisory Framework for the Banking Industry Cont'd

- **Federal Ministry of Finance**

➢ Oversees regulatory/ supervisory Agencies like NDIC, SEC, Investment and Securities Tribunal (IST) and NICOM

Other Regulatory Agencies in the Financial System

- Securities and Exchange Commission (SEC)

➢ Regulates the capital market.

➢ Protects investors in the capital market.

➢ Registers securities institutions in the market.

➢ Carries out surveillance of the market to ensure compliance with rules and regulation.

Other Regulatory Agencies in the Financial System Cont’d

- **National Insurance Commission**.
  - Established in 1997 to regulate the insurance industry.

- **Financial Services Regulation Coordinating Committee (FSRCC)** provided for under Section 38A (1) of CBN (Amendment) Act No 41 of 1999.
  - Established to facilitate cooperation and coordination of activities of the various regulatory agencies.

Current Major Regulatory Challenges

- Universal banking and the challenge of consolidated supervision
- Risk-based Supervision
- Corporate Governance
- Capacity building

Re-engineering Regulatory Capacity

- Both the NDIC Act of 2006 and the CBN Act of 2007 have significantly improved the regulatory and supervisory capacity of the respective regulatory/ supervisory agencies when compared with the situation before the Acts. In particular, the following improvements, among others, could be observed in the case of NDIC Act:

- Legal protection granted to officials, directors and agents of NDIC for actions taken in good faith;
- Flexibility introduced to deal with coverage and premium assessment with a view to reflecting developments in the industry;
- Appointment as liquidator made less cumbersome; and
- Granting NDIC to establish Bridge Bank.

Re-engineering Regulatory Capacity

- The NDIC Act is currently being reviewed so as to enhance the effectiveness of the Corporation. Some of the areas of review include:

➢ Granting powers to NDIC to pay insured amount to depositors in the event of imminent or actual suspension of payment by an insured institution even before licence revocation;

➢ Having powers to review the books of subsidiaries;

➢ Seeking independent enforcement powers to deal with erring banks and their directors/officials;

➢ Protection of Corporation's assets against creditors who obtain judgement against closed insured institutions;

Re-engineering Regulatory Capacity cont'd

- However, there are still areas that need strengthening and continuous improvement:

➢ **Supervisory Capacity**

❖ Continuous skill acquisition and update to be ahead of the operators especially in the light of the adoption of risk-based supervision as well as universal and cross-border banking.

❖ Closer collaboration and cooperation amongst the various regulatory agencies to facilitate consolidated supervision in the light of the universal banking being operated.

Re-engineering Regulatory Capacity cont’d

- The proposed establishment of a training centre by all the regulatory authorities so as to promote uniform standard for all supervisors is a welcome development.
- The Solo-plus approach being prposed for consolidated supervision will further enhance the effectiveness of supervision.
- In the same vein, another step taken to strengthen regulatory/supervisory framework is the agreed joint examination of banks by CBN and NDIC.

Re-engineering Regulatory Capacity cont'd

- In order to further strengthen collaboration/cooperation amongst regulatory authorities, the following steps have been taken:
  - Establishment of FSRCC Web site to facilitate information-sharing as well as ease access to vital information by members of the public;
  - The Relevant Regulatory Authorities have been directed to draft a bill for the formulation of holding companies as they exist in the USA for ease of regulation and transparency
  - The proposed Code of Conduct for all the members of the FSRCC that will complement individual member's Codes of Conduct will enhance the integrity and credibility of the regulatory apparatus in the country.

Re-engineering Regulatory Capacity cont'd

- Although there is cordial relationship between the CBN and the NDIC, there is still need to amend the NDIC to give it powers to implement its recommendations and apply sanctions. This will facilitate early redress of potential crises.

- Capacity building to effectively adopt the International Financial Reporting Standard in the light of increasing reach out of our banks into other countries (cross-border banking). The primary objective is to have the same set of rules/parameters for reporting our financial statement to ensure comparability with international standards. This has become imperative for many of our banks that are listed in foreign stock exchanges.

- Zero tolerance to operational abuses especially in such areas as disclosures and misrepresentation of financial statement

Re-engineering Regulatory Capacity Cont'd

- **Legal Capacity**
- Need to amend CBN Act to enable it provide financial support by way of capital injection for systemic financial sector crises.
- Need to put in place regulation regarding margin trading so as to forestall a repeat of the current ugly developments.
- Need to review fines and other financial penalties in the existing relevant Acts for infraction of rules to serve as true deterrent.
- Need for more effective legal provision that will facilitate the enforcement of financial contracts, loan recovery and realization of collaterals.

Re-engineering Regulatory Capacity Cont'd

- **Funding**

❖ Adequate funding is critical for the effectiveness of a deposit insurance system.

❖ As At June 30, 2009:

➢ NDIC's DIF was N235.77 B

➢ Insured Deposits Of the Industry was N1,373.6 B

➢ Ratio of DIF To Insured Deposits was 16.42%

➢ Insured Deposits Of Distressed Banks was N666.61 B

➢ One of the banks had insured deposits of N416.88 Billion

Re-engineering Regulatory Capacity Cont’d

- **Funding Cont’d**
- From the statistics above, given the level of DIF and the risk exposure of the funds to the banking system, increased coverage level, the adoption of DPAS coupled with the fact that the Corporation does not receive annual subvention from government, there is the need to pay attention to the growth of the DIF for it to adequately meet its obligations in the country.
- However, the Fiscal Responsibility Act (FRA) of 2007 requires the NDIC and other Government organizations listed in the Act to pay 80% of their operating surplus to the consolidated Revenue Fund of the Federal Government.

Re-engineering Regulatory Capacity Cont’d

- **Funding Cont’d**
- That requirement impairs the pace of rapidly building up of the DIF to meet its obligations.
- There is therefore the need to de-list NDIC from the list of affected Government organizations listed under the Act in order for the NDIC to have a robust funding base and be further strengthened to discharge its mandate.

Re-engineering Regulatory Capacity Cont'd

- **Corporate Governance**

  - The concept of "proper & fit" should be employed effectively and periodically reviewed for appointment of Board members at the level of both the operators and regulators.

Conclusion

- Recent global financial crisis and the developments within the domestic capital and banking sub-sectors further underscore the need for stronger regulation/supervision.
- Areas that will require fine-tuning to enhance the regulatory/supervisory framework include:

➢ Review of relevant laws to grant more powers to the regulatory/supervisory agencies

➢ Enhanced capacity building; and

➢ Closer cooperation/collaboration amongst various regulatory agencies

Thank you for your attention!