



Pursuant to Article 35, paragraph 1.1 of the Law No. 03/L-209 on Central Bank of the Republic of Kosovo (Official Gazette of the Republic of Kosovo, No.77 / 16 August 2010), and Articles, 16, 46 and 85 of the Law No. 04/L-093 on Banks, Microfinance Institutions and Non-Bank Financial Institutions (Official Gazette of the Republic of Kosovo, No.11 / 11 May 2012) , the Board of the Central Bank of Republic of Kosovo at the meeting held on April 26, 2013 approved as following:

## **REGULATION ON THE CONSOLIDATED SUPERVISION OF BANKING GROUPS**

### **Article 1 Purpose and scope**

1. The purpose of this Regulation is to determine the consolidation supervision of banking groups.
2. The provisions of this Regulation apply to all banks licensed by the CBK to operate in the Republic of Kosovo.

### **Article 2 Definitions**

All terms used in this Regulation are as defined in Article 3 of the Law No. 04/L-093 on Banks, Microfinance Institutions and Non-Bank Financial Institutions (hereafter referred to as: *the Law on Banks*).

### **Article 3 Consolidated supervision of banking groups**

Consolidated Supervision is necessary to protect depositors and other creditors of banks from risks emanating from companies affiliated to banks. The Law on Banks enables the CBK to define a “banking group” to include any companies that the CBK should take account of if it is necessary to ensure that risks to depositors of a bank do not escape supervision. While depositors in a bank may be protected by the limited liability of the bank to an affiliate, in practice no bank can survive damage to its reputation, and thus to its liquidity and solvency, of problems in a closely related entity.

### **Article 4 Approach to consolidated supervision**

1. In order to make an assessment of the strength of a banking group as whole, it is necessary for the CBK to assess the risks in all significant parts of the group. This will be done both on a quantitative basis as well as on a qualitative basis. The CBK will determine which companies in the group involve significant risk and include those in the consolidation. Where a member of a group does not involve significant risk and where the linkages between the companies are weak it may be acceptable not to include such companies within the

consolidation. Non-financial companies may be excluded but only if the linkages are weak or the risks are considered minimal. Where the linkages are close, the CBK may require the bank to reorganize the group so that the financial part is more self-contained.

2. Where a banking group is headed by a bank parent, consolidated supervision is relatively straight-forward and will normally include all the bank's subsidiaries and associated companies. It may also be desirable to supervise a group on a consolidated basis where the parent is a holding company or other entity which is not itself subject to supervision. In such a case a group will be defined to include the bank, its parent and such affiliated companies that in the CBK's opinion pose potential risks to the depositors of the bank. So a banking group will normally be defined as including entities that are all in common control. It also does not exclude the possibility of including companies not in majority share ownership. The CBK will use practical tests to determine whether an entity, even if not majority owned, is nevertheless effectively controlled by a group company, and thus potentially exposing depositors in the bank to risk.
3. Where a bank is a member of a group involving a foreign bank or other foreign regulated company, the CBK will only consolidate the Kosovo bank and any affiliated companies in Kosovo, irrespective of whether they are subsidiaries of the Kosovo bank or subsidiaries of a foreign affiliate of the group. CBK will expect the home supervisor to be responsible for the consolidated supervision of the whole group as stipulated with paragraph 1.8 of Article 7 of Law on Banks. Before licensing such a bank, and continuously thereafter, the CBK will verify that the group continues to be subject to effective consolidated supervision by its home supervisor. If the CBK ceases to be satisfied, it may take steps to ensure that the Kosovo operations are insulated from developments elsewhere. This may involve changes to the shareholding structure of the group.

## **Article 5**

### **Quantitative supervision**

1. The starting point for quantitative supervision of a banking group is the preparation of consolidated financial statements as required by IAS 27. Although the CBK has the power under Article 53.3 of the Law on Banks to prescribe the extent of consolidation for accounting purposes, it will normally rely on the tests in IAS 27 itself. However, the CBK may also include within the scope of its consolidated supervision entities not subject to consolidated accounting. So the fact that an entity is not consolidated for accounting purposes does not necessarily mean it will not be treated as part of the group for consolidated supervision purposes. The CBK may also exclude certain entities, even if consolidated for accounting purposes, if it judges that the risks are not material or significant. For certain quantitative purposes the CBK may exclude the combining of the assets and liabilities of insurance companies with those of other financial entities on a case by case basis when it is considered that they will not impact materially the consolidated financial position. This may apply to capital adequacy calculations, but not to large exposure calculations.
2. Banking groups will also be required to prepare and to submit to the CBK balance sheet and other statistical returns on a consolidated basis. These will enable the calculation of capital adequacy ratios for the group as a whole in order to ensure that no double counting of capital takes place. Intra-group claims and liabilities will in this process be eliminated. In the case of insurance subsidiaries then the investment in the insurance company will be deducted from the parent's capital in order to determine the group's capital. For detailed application of the

capital adequacy requirement for a banking group, banks shall act in accordance with the CBK Regulation on Bank Capital Adequacy.

3. Quantitative returns will also enable the calculation of large exposures and foreign exchange positions for the group as a whole. Once the CBK begins to assess bank exposure to other market risks, e.g., interest rate risk and securities investment risks, these will also be assessed on a group basis. CBK Regulation on Large Exposures sets out how the large exposure limits will apply to groups for which the CBK has determined the consolidated supervision arrangements will apply.
4. The limitations on foreign currency exposure, provided for by Article 50, and regulated by CBK Regulation on Foreign Exchange Risk shall be applicable to the group as whole, as well as on a solo basis.

### **Article 6** **Qualitative supervision**

1. In addition to quantitative supervision, the CBK will also consider qualitative aspects. This process will involve ‘mapping’ the connections between different members of a banking group and an understanding and consideration of the management linkages as well as the purely financial linkages. For example, the CBK may require that a bank subsidiary of a group have sufficient independent directors on its board to operate independently of other group companies and thereby ensure sufficient attention is paid to the responsibility of the bank to its depositors. Information gathered in this process will also influence the CBK’s decisions as to which members of a group should be included in the consolidated group for supervisory purposes. Where a group consists of a mixture of financial and other entities, the CBK may seek to ring fence the financial activities and exclude non-financial entities from the scope of consolidated supervision. However, in order to do this, the CBK will wish to ensure that any financial links and managerial links are not such as to vitiate the process. Thus a financial sub-group would be expected to have independent directors and managers and not be excessively influenced by the management of entities outside the consolidation. It may request certain changes to the way a group is structured if it determines that the current structure impedes effective consolidated supervision.
2. The CBK will also use the powers under Article 81 of the Law on Banks where it suspects that a non-licensed entity within a group is carrying on activities prohibited by the Law on Banks or any other relevant laws.
3. The CBK requires that only one firm to be responsible for the external audit of all the companies in a group and not have to rely on the work of several audit firms.

### **Article 7** **Information**

1. The basis for consolidated supervision is the collection of information by the CBK. Article 57 of the Law on Banks gives the CBK powers to obtain information not just from supervised entities within a banking group but also other entities affiliated to a supervised entity in order to determine the extent of the linkages described above. On occasion it also may be necessary for the CBK to examine non-financial entities as also provide for in Article 57. This should not be taken to imply that such entities are thereby supervised by the CBK, especially where such entities are of a non-financial character. Normally, the CBK will rely

on banking members of a banking group for information about the group as whole and about non-supervised entities within the group, but it reserves the right to verify by whatever means are necessary including through on-site examination.

2. Where a banking group includes entities supervised or regulated by another supervisory authority in Kosovo or abroad, the CBK will hold periodic discussions with such supervisory authorities as are necessary to understand the relationship between the Kosovar and foreign companies in the group and to be able to take view on the soundness of the group and its components. Article 79 of the Law on Banks empowers the CBK to exchange information about a Kosovo bank with such other regulatory authorities provided it is satisfied that the information will be used for supervisory purposes and will subject to the same degree of confidentiality as in Kosovo as required under Article 80 of the Law on Banks. The CBK will normally seek to establish a Memorandum of Understanding or other similar agreement with foreign supervisory authorities in such cases.

### **Article 8 Procedure for consolidated supervision**

If the CBK believes that a banking group that requires consolidated supervision exists, it will discuss with the principal bank member of the group and discuss the nature of the linkages. If, on the basis of such discussion it determines that the group does require consolidated supervision CBK will inform the bank in writing, listing the entities that it proposes to include in its consolidated supervision. The determination will also indicate whether any adjustments are necessary to consolidation for accounting purposes. The letter will list the returns that it will expect the group, through the principal bank, to provide on a consolidated basis as well as on solo basis by the banking member of the group. CBK will also notify the bank how it expects the group to observe the capital adequacy requirements and large exposure requirements on a consolidated basis as well as on a solo basis for the bank itself.

### **Article 9 Enforcement, remedial measures and civil penalties**

1. Any enforcement action in respect of breaches of this Regulation or orders given under it will normally be taken against the principal bank member of the group. The CBK may, in certain circumstances, take direct action against other entities within the group if the circumstances require. Where the CBK does not have sufficient powers to correct the weaknesses, the CBK may direct the bank to sever its links with other entities within the group
2. Any violation of this Regulation shall be subject to the remedial measures and penalties provided for in Articles 58, 59, 82, of the Law on Banks.

### **Article 10 Transitory Provision**

Subjects of this Regulation, no later than three (3) months following the entry into force of this Regulation, shall carry out in accordance with the requirements of this Regulation, the review and/or the approval of the internal rules and procedures.

**Article 11**  
**Abrogation**

Upon entry into force of this Regulation, it abrogates the Regulation on Consolidated Supervision of Banking Groups issued by the CBK Board on December 03, 2012.

**Article 12**  
**Entry in to Force**

This Regulation shall enter into force on May 10, 2013, on the day of its publication at the CBK website.

The Chairman of the CBK Board of the Republic of Kosovo.

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Sejdi Rexhepi