

Title:

Toronto Centre Podcast:
Risk-Based Supervision of Cross Border Groups

Speakers:

Paul Wright
Program Leader, Toronto Centre

Chuin Hwei Ng
Program Director, Toronto Centre

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Transcript

Speaker 1: You're listening to a Toronto Center Podcast, welcome. The goal of TC Podcasts is to spread the knowledge and accumulated experience of global leaders, experts, and world-renowned specialists, in financial supervision, and regulation. In each episode, we will delve into some of today's most pressing issues, as it relates to financial supervision and regulation, the financial crisis, climate change, financial inclusion, FinTech, and much more. Enjoy this episode.

Chuin Hwei Ng: Hi everyone. Welcome to TC's Podcast, on the go. I am Chuin Hwei Ng, Program Director from Toronto Center. We have just published a TC Note, entitled *Risk-Based Supervision of Cross-Border Groups*. And I am very pleased today to have the author here with us, Paul Wright, to talk to us about it. So, Paul, thank you for joining us today.

Paul Wright: Well, thank you Joanne, it is a great pleasure.

Chuin Hwei Ng: Paul is a veteran regulator and supervisor, and a long-time program leader with Toronto Center. Paul, you are the best person I know to talk to us about risk-based supervision and the application of that to supervising Cross-Border Groups. So, I wonder, if you could first have you introduce yourself to our listeners, and your experience in risk-based supervision, and cross-border supervision?

Paul Wright: Well, I was a senior supervisor in the UK, for a number of years, and I have also been a program leader with the Toronto Center for almost 10 years now. And I think I was asked to write the note, partly because of my previous experience. So, I was for the supervision of the largest global groups in the UK. And as you can imagine, they have extensive cross-border operations, but many of them also operate across sectors. So, they undertake banking, and securities, and insurance, within the same group. But besides that, in my nearly 10 years of experience with the Toronto center, I've worked with supervisors in many countries. Who are at

different stages in their supervision of international and cross-sector groups? So, it seemed timely, really, to take all that experience, both in the UK and in Toronto Center to take it and put it in one place so that we could share our experience with others.

Chuin Hwei Ng: Thank you, Paul, for that introduction. So, perhaps straight to the TC Note then, what is the TC Note about? Could you give us a broad outline?

Paul Wright: Yes, well, in a sense, the title is self-explanatory. It is about the supervision of cross-border groups. It starts off looking at groups in a single sector, so, firms that are just doing banking or insurance, but have cross-border operations. And then it moves on to the issues in supervising conglomerates, that is to say, firms operating in more than one sector. And the key point really, is a very simple one. And that is whether you are supervising the smallest firm, or the largest global group, you need the same thing. And you need a clear and full oversight of the business, and the risks that are being run. Now, obviously when you are looking at cross-border conglomerates, operating across sectors in multiple jurisdictions, which poses challenges for both the home and the host supervisor.

And there are plenty of examples from history, unfortunately, where no supervisor had a comprehensive or coherent overview of what a group was doing, and that is often led to serious problems. So, the note goes into all of that, and it gives some examples, which are much simplified. But still illustrate the potential complexities of dealing with cross-border and cross-sector groups. So, it draws together existing material from standard sitting bodies, but it also aims to provide some practical advice, on things like colleges, for example, and how to make them work better.

Chuin Hwei Ng: There is already quite a lot out there that is written on risk-based supervision, and the various applications of that, including a series of TC Notes on risk-based supervision, written by yourself. So, why produce this note now? What does it add?

Paul Wright: Yes, so it is a good question. So, as you say, there is quite a lot of existing material, not only on risk-based supervision, but also on consolidated supervision, and the operation of colleges. In the nature of things, some of that is a bit fragmented. So, for instance, it has been produced by several bodies, the Joint Forum, the Basel Committee, and as you rightly say, the Toronto Center itself. And its good stuff, do not get me wrong, it's very valuable, but it seemed to be quite a good idea to try to draw some of that existing material together. But then to add to it, the experience that we had had in dealing with these things in the Toronto Center. And one thing, for instance, that has been clear to me, over the years, is that some supervisors have very little interaction with other relevant supervisors.

So, people sometimes say to us, "Well, I have a firm that has operations in a neighboring country, but I've never actually spoken to the supervisor in that country." Or indeed, the firm may have operations in another sector. They may, as I am responsible for banking, but the firm also does insurance or securities.

And there is another supervisor in my country, that deals with those. And I have never had any contact with them, either. And it is always surprising to me when supervisors say, "There are these other relevant supervisors around, but I haven't actually spoke to them." So, we offer lots of practical steps, but the most basic one, really, is when that happens, get in touch, talk to other supervisors, because it is really important.

Chuin Hwei Ng: And I guess that is why you've placed quite a bit of emphasis on colleges of supervisors in the note.

Paul Wright: Well, yes, colleges are of fundamental importance. I remember actually, a long time ago now, when colleges first started happening, we haven't always had colleges. And I can remember some of the very earliest ones. And it is surprising to think now there was suspicion in some quarters about how they would operate. And some supervisors, almost seemed determined to raise obstacles, and there were a number of issues that arose with them. So first of all, confidentiality issues with information sharing, I'll come back to that in a minute. Some supervisors also said, "Well, we can't have a meaningful dialogue with other supervisors because we've got different accounting standards, or different regulatory requirements. So, we can't have a meaningful discussion." There were some supervisors, often, of non-bank parts of groups, which didn't see the need for a college at all. They'd say things like, "Well, I'm responsible for a small part of a group, it's self-contained." That might be, for example, a securities firm, the client money is all segregated.

So, if the firm failed, everyone would be okay, they'd get their money back. It's of no interest to me, what happens in the rest of the group. So, I don't need to take part in the college, I remember quite a few people saying that. And what we've learned over the years about those kinds of concerns, we've learned quite a few lessons over the years. So, first of all, not to get hung up on structures, colleges are not fixed things, the form that they take, and the membership, and the agendas, can be flexible, depending on the issues of the moment. And, they should be flexible, too. So, they shouldn't be fixed structures. Secondly, it is just not the case that the supervisor of any part of a group can be indifferent to what happens to the rest of that group. You may think, well, I'm responsible for supervising a little part of it.

And that little part is insulated from the whole of the rest of the group. So, I don't need to worry about anything else. Well, I've got news for you. And that is, that insulation probably won't work when things go wrong, or if things go wrong. So, you really do, however self-contained you think you, or your part of the group, is. It is not really, and you should be interested, and you should be involved in discussions of the wider group. And then finally, dealing with that question of confidentiality, which was such a barrier in so many cases, it is true, of course, that a lot of supervisory information is confidential. And of course, that confidentiality has to be respected. Of course, it does. But equally, we should not be fixated with it. And if people want to make colleges work, they can find ways around this.

They can find ways to share information, at least on a kind of, need-to-know basis. So, you can have gateways written into your regulations. You can have memorandum of understanding. So, there are all sorts of ways, in which, if there is a will to do it, you can share information, that's relevant, of course, to other supervisors. And you should not be fixated by confidentiality, it shouldn't be a barrier, Although, as I say, it always needs to be respected. But I would make one other point about your question, really. And that is this, even if you think as a supervisor, well, yes, we probably do need a college, but that may be some way down the road, we're not ready to do that yet. There is still a key first step that you can take, and that is just, get in contact with other relevant supervisors. So, if you have a counterparty in another country, responsible for another part of your bank, or your insurance company, or whatever. Pick up the phone or do a Zoom Call, or just say, "Hi, let's just have a talk about this group, we have a shared interest in it."

And for that matter, even if you have another supervisor within your jurisdiction, as I say, if you are responsible for the banking part, but there is someone else looking at the insurance part, or the securities part, get in touch with them, as well. It is really important to do that. It is immeasurably important and more valuable to have some contact than it is to have none. You do not have to have a fully-fledged college, although that's a desirable stage to aim for. And it's surprising how many supervisors haven't got to that stage. You know, I often speak to supervisors in countries, who say, "Well, I know these people are there and I haven't really ever spoken to them." Well, do so, pick up the phone, have a Zoom, do whatever it takes.

Chuin Hwei Ng: Well, thanks for reminding us again, of the value of no supervisory contacts, building those relations. But many host supervisors say it is actually quite difficult to get hearing in the supervisory colleges when they happen. Why do you think that is?

Paul Wright: Well, it is an issue, and it is especially an issue, I think, when you have large groups that have operations in many countries. And it is very common to hear that a branch or a subsidiary, it may be very important in a host jurisdiction. It might have high impact there, but to be honest, it may be only a small part of a group's total operations. And when that happens, it gives rise to what, in the note, I call an asymmetry of impact. So, in other words, a branch or a subsidiary, may loom much larger in the mind of a host supervisor, than it does in the mind of the home supervisor. Or for that matter, the parent's firm. And that can be very frustrating for hosts, who feel, you know, "I've got this firm, which is of great importance to me, and I keep trying to get a hearing by having a dialogue about it." But the home supervisors not really interested because they always feel they have bigger, more important things to worry about.

Chuin Hwei Ng: Yes, I like the term that you use the asymmetry of impact, but what can we actually do about this? Is there a solution to this?

Paul Wright:

Well, there is not a magic solution, no. Because obviously, frankly, there is going to be that asymmetry, and people must be realistic about that. So, there is no magic solution, but we do offer some advice in the note and above all, hosts should speak up. I mean, I often hear people complaining about the fact they cannot really get much of a hearing, but I am not often sure how hard they try really, and hosts should speak up. And I can think of two cases, people might want to think about. So, the first one is, supposing you are a host supervisor, and you are seeking some reassurance from the home supervisor. So, you might say, "Well, can we be sure that this group is basically sound? Or can we be sure that the controls in the parent firm are adequate or sufficiently strong?"

Well, that is something I need to know as a host. I cannot find that out directly, by definition, because it is about the home country or about the parent. I cannot find it out. I need to ask you, the home supervisor. Now, my advice there is, if you have a concern like that, raise it well in advance of a college. Do not wait for the college but raise it well in advance. And then even if it turns out that it does not warrant an agenda item on the college itself, it still gives the home an opportunity to respond. They might find an alternative way of doing it. They might get in touch with you bilaterally or create some sort of parallel structure to the college, which can deal with issues like that. So, raise the issue, do not hesitate to do so, and do it well in advance.

And there is another kind of issue, which is where the host may observe something, which they think might be of wider significance. So, supposing you are a host supervisor, and you say, "It seems to me, a lot of the control procedures in the branch, or the subsidiary that I am responsible for, look a bit weak, and I'm not really convinced they're very effective. But when I challenge the firm about it, they say, "Well, no, this is our firm-wide standard, and the home supervisor's perfectly happy with them. So, you should be as well. Now that is something where the host may have a concern about that, and want to check that with the home supervisor, but it may be of interest to others as well, who may have observed similar issues, as host supervisors. So again, raise it with a home. It may warrant an agenda item in the college if it is a wide enough significance. But even if it does not, you can seek a bilateral response.

As I said, the home supervisor may choose then, to set up some complimentary, or parallel structure, to the college proper, in which issues like that can be addressed. So, speak up. And the third point, I think we say, we make in the note is home supervisors are always going to be much more willing to talk to you if you have something to offer. So, if you say, "Look, I have got some insights into how this firm's cross-border operations work, because I see those as the host supervisor. So, I have got something to tell you, which is of relevance in interest and in return, I hope you will be open with me. So, you know, speak up.

Chuin Hwei Ng:

Yes, those are, indeed, some of the common scenarios faced by host and home supervisors, in their interaction. So, thank you again, Paul, for bringing us through the highlights of the note, and the motivation for this TC note. So, just bringing

this session to a close, is there one piece of advice that you would give to our listeners based on this work?

Paul Wright:

Well, there is, and my advice would be, read the note. Because it is a complex area, potentially, and obviously we cannot really do justice to it in a short discussion like this. So, we have talked about some of the issues, and some of the highlights, but do, please, read the note because it draws on a wealth of experience that I, as the author, but also the Toronto Center have amassed over the years. And as I say, it aims be a combination of standard setting material, but also real-world advice, which we hope people will find useful.

Chuin Hwei Ng:

Yes, I would certainly recommend the note to everyone who is listening to the podcast. So, I am here today with Paul Wright. Paul, thank you again. And you have been listening to a Toronto Center Podcast, on the go. Thank you for the joining us.