

**Nigeria: Publication of Financial Sector Assessment Program Documentation—
Detailed Assessment of Compliance of the Basel Core Principles for
Effective Banking Supervision**

This Detailed Assessment of Compliance of the Basel Core Principles for Effective Banking Supervision for Nigeria was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed in May, 2013. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Nigeria or the Executive Board of the IMF.

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FINANCIAL SECTOR ASSESSMENT PROGRAM

NIGERIA

BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING
SUPERVISION

DETAILED ASSESSMENT OF
OBSERVANCE

MAY 2013

INTERNATIONAL MONETARY FUND
MONETARY AND CAPITAL MARKETS DEPARTMENT

THE WORLD BANK
FINANCIAL SECTOR VICE PRESIDENCY
AFRICA REGION VICE PRESIDENCY

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GLOSSARY

AC	Additional criterion
AMCON	Asset Management Corporation of Nigeria
AML/CTF	Anti-Money Laundering/Combating Financial Terrorism
AT	Assessment team
BCBS	Basel Committee on Banking Supervision
BCP	Basel Core Principles
BDC	Bureaux de Change
BED	Bank Examination Department (NDIC)
BOFI Act	Banks and Other Financial Institutions Act (2004 No 25)
BSD	Banking Supervision Department (CBN)
CAM Act	Companies and Allied Matters Act (2004)
CAR	(Regulatory) Capital Adequacy Ratio
CB	Commercial bank
CrB	Credit bureau
CBN	Central Bank of Nigeria
CBN Act	Central Bank of Nigeria Act, No.7 of 2007
CCO	Chief Compliance Officer
CDD	Customer due diligence
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIA	Chief Internal Auditor
CIBN	Chartered Institute of Banker of Nigeria
CIO	Chief Information Officer
CoG	Committee of Governors (of the CBN)
COO	Chief Operating Officer
CPM	Core Principles Methodology
CRM	Credit risk mitigation
CRMS	Credit risk management systems
CRO	Chief Risk Officer
CSWAMZ	College of Supervisors of West African Monetary Zone
DH	Discount house
DMB	Deposit money bank
EC	Essential criteria
e-FASS	Electronic Financial Analysis and Surveillance System
FATF	Financial Actions Task Force
FC	Finance Company
FDI	Fixed direct investment
FMD	Financial Markets Department (CBN)
FMOF	Federal Ministry of Finance
FOI	Freedom of Information Act
FPRD	Financial Policy and Regulation Department (CBN)
FRCoN	Financial Reporting Council of Nigeria
FSAP	Financial Sector Assessment Program
FSR	Financial Stability Report

FSRCC	Financial Services Regulation Coordinating Committee
FSS	Financial System Stability Directorate (CBN)
FSS 2020	Financial System Strategy 2020
HoldCo	Holding Company
IAASB	International Auditing Assurance Standards Board
ICAAP	Internal Capital Adequacy Assessment Program
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IRRBB	Interest Rate Risk in the Banking Book
ISA	International Standards of Auditing, as issued by IAASB
ISD	Insurance and Surveillance Department (NDIC)
KoB	Knowledge of Business
KYC	Know your customer
LSD	Legal Services Department (CBN)
MFB	Micro-Finance Bank
MoU	Memorandum of Understanding
MPC	Monetary Policy Committee
₦	Naira
NAICOM	National Insurance Commission
NASB	Nigerian Accounting Standards Board
NFIU	Nigeria Financial Intelligence Unit
NGN	Nigerian Naira
NIB	Non-interest bank
NOP	Net open position
NPLs	Nonperforming loans
NSE	Nigerian Stock Exchange
OFI	Other financial institutions
OFISD	Other Financial Institutions Supervision Department (CBN)
PCA	Prompt Corrective Action
PENCOM	National Pensions Commission
PFA	Pension fund administrators
PG	Prudential Guidelines
PMI	Primary mortgage institution
RAS	Risk assessment summary
RBS	Risk-based supervision
SEC	Securities and Exchange Commission
SIID	Special Insured Institutions Department (NDIC)
SME	Small and medium enterprises
SSS	State Security Services
STR	Suspicious transaction reports
UBM	Universal banking model
WAMZ	West African Monetary Zone

I. SUMMARY, KEY FINDINGS AND RECOMMENDATIONS

A. Introduction

1. **The assessment of the current state of the implementation of the Basel Core Principles for Effective Banking Supervision (BCP) in Nigeria, against the BCP methodology issued by the Basel Committee on Banking Supervision (BCBS) in October 2006¹, was completed between August 27 and September 19, 2012, as part of a Financial Sector Assessment Program (FSAP) update, undertaken jointly by the Fund (IMF) and the World Bank, and reflects the regulatory and supervisory framework in place as of the date of the completion of the assessment.** An assessment of the effectiveness of banking supervision requires a review of the legal framework, both generally and as specifically related to the financial sector, and a detailed examination of the policies and practices of the institutions responsible for banking supervision. In line with the BCP methodology, the assessment focused more on the major commercial banks and their regulation and supervision, given their importance to the system. The previous BCP assessment was conducted in 2002, in terms of the 1998 BCP methodology, which is not directly comparable to this assessment.

B. Information and Methodology Used for Assessment

2. **Reaching conclusions required judgment by the assessment team.** Banking systems differ from one country to another, as do their domestic circumstances. The BCPs are capable of application to a wide range of jurisdictions whose banking sectors will inevitably include a broad spectrum of banks. To accommodate this breadth of application, a proportionate approach is adopted within the BCPs, both in terms of expectations on supervisors for the discharge of their own functions and in terms of the standards that supervisors impose on banks. An assessment of a country against the essential criteria must, therefore, recognize that its supervisory practices should be commensurate with the complexity, interconnectedness, size, risk profile and cross-border operation of the banks being supervised. In other words, the assessment must consider the context in which the supervisory practices are applied. The concept of proportionality underpins all assessment criteria. For these reasons, an assessment of one jurisdiction will not be directly comparable to that of another. The assessors take an overarching view of bank regulation and supervision in the country, and the analysis is comprehensive—however, though issues may be identified and recommendations may be proposed, these are not necessarily exhaustive for purposes of achieving full compliance, given the purpose of the BCP assessment, and time and resource constraints.

¹ An updated version of the BCBS's Core Principles for Effective Banking Supervision was issued in September 2012.

3. **The assessment of compliance with each principle is made on a qualitative basis.**

A four-part assessment system is used: compliant; largely compliant; materially non-compliant and non-compliant. To achieve a “compliant” assessment with a principle, all essential criteria (ECs) generally must be met without any significant deficiencies. A “largely compliant” assessment is given if only minor shortcomings are observed, and these are not seen as sufficient to raise serious doubts about the authority’s ability to achieve the objective of that principle. Under the BCP methodology, a “materially non-compliant assessment is given whenever there are severe shortcoming, despite the existence of formal rules, regulations and procedures, and there is evidence that supervision has clearly not been effective, that practical implementation is weak, or that the shortcomings are sufficient to raise doubts about the authority’s ability to achieve compliance. A “non-compliant” assessment is given when no substantive progress toward compliance has been achieved. In interpreting ratings, it is also important to note that for some CPs the assessment takes into account both compliance by banks and compliance of the supervisors. Furthermore, it should provide an overview of the supervisory environment (e.g., the mandate, role and functions of the local regulatory authority, the role of self-regulatory organizations, oversight and regulatory arrangements, legal and institutional framework, transparency, public disclosure, and accountability practices). It should also summarize the capacity, competence, internal controls, integrity of operations, and operational autonomy of the supervisory function.

4. **The assessment team² reviewed the legal framework for banking supervision and held extensive discussions with the staff of the Central Bank of Nigeria (CBN) and the Nigeria Deposit Insurance Corporation (NDIC), which both perform supervision of banks, though the former is the lead supervisor.** The assessors also met with officials of the FMOF, several commercial banks, audit firms and the Chartered Institute of Bankers of Nigeria. The team examined the current practice of on-site and off-site supervision of the CBN and the NDIC.

5. **The assessors appreciated the collaboration and hospitality of the CBN.** The assessment team had the benefit of working with a comprehensive self-assessment completed by the CBN, enjoyed excellent cooperation with its counterparts, and received the information it required. In addition, the assessment team was given access to all documentation and information systems. The team extends its thanks to the staff of the CBN for their participation in the process and their comprehensive self-assessment.

² The BCP assessment was conducted by Carel Oosthuizen (IMF) and Khairul Ibrahim (Consultant; Deputy Director with the Banking Supervision Department of Bank Negara, Malaysia.)

C. Institutional and Macroeconomic Setting, and Market Structure—Overview

6. **Nigeria has a diverse financial sector.** The number of financial institutions as at December 31, 2011 included the following: 21³ commercial banks (CBs) (six banks, including five domestic banks one pan-African bank, dominate the banking sector) five discount houses (DHs), 876 microfinance banks (MFBs), 107 finance companies (FCs), 101 primary mortgage institutions (PMIs), 31 pension fund administrators (PFAs), five pension fund custodians (PFCs), 1,946 bureaux de change (BDCs), 690 securities brokerage firms, five development finance institutions (DFIs), three private credit bureaux, 61 insurance companies, two reinsurance companies, 50 loss adjusters and the Asset Management Corporation of Nigeria (AMCON).

Structure of the Financial System, 2011 (₦billion, unless specified otherwise)

	2006			2010			2011		
	Number	Assets	In percent of total assets	Number	Assets	In percent of total assets	Number	Assets	In percent of total assets
Commercial banks	25	6,738	90.5	24	15,544	94.8	20	18,477	78.7
Private	25	6,738	90.5	24	15,544	94.8	17	17,548	74.7
Domestic	21	6,456	86.7	20	14,217	86.7	13	14,704	62.6
Foreign	4	282	3.8	4	1,327	8.1	4	2,844	12.1
State-owned	0		0.0	0	0	0.0	3	928	4.0
Institutional investors	124	300	4.0	100	565	3.4	91	3,457	14.7
Insurance Companies	107	n.a.		61	565	3.4	61	622	2.6
Pension Funds	13	300	4.0	30	n.a.		21	2,835	12.1
Unit Trusts	8	n.a.		8	n.a.		8	n.a.	
Other Non-Banks Financial Institutions	1,683	409	5.5	1,619	280	1.7	1,403	1,543	6.6
Finance Companies	112	54	0.7	108	31	0.2	n.a.		
Specialized development institutions	6	n.a.	n.a.	6	250	1.5	6	267	1.1
Securities Firms	581	n.a.		580	n.a.		254	n.a.	
Fund Managers							136	1,085	4.6
Mortgage Institutions	90	114	1.5			0.0			
Microfinance Banks	757	55	0.7	800	n.a.		876	191	0.8
Discount Houses	5	186	2.5			0.0	5	n.a.	
Bureaux de Change	126	n.a.		125	n.a.		125	n.a.	
Asset management Companies (AMC)							1	n.a.	
Other	6	n.a.							
Total financial system	1,826	7,447	100.0	16,389	100.0		23,477	100.0	

Source: CBN.

7. **The CBN, as part of its statutory mandate of promoting a sound financial system in Nigeria, licenses and carries out the prudential regulation and supervision of CBs, other financial institutions (OFIs), DHs, Non-interest Banks (NIBs), MFBs, PMIs, FCs, BDCs and AMCON.** NDIC, on the other hand, administers the deposit insurance scheme and also collaborates with the CBN in the onsite and offsite supervision of commercial banks, merchant banks, and insured MFBs and PMIs. The supervisory departments of the CBN and NDIC had 847 supervisors as at end December 2011. Each of the CBN and NDIC,

³ JAIZ Bank Plc, a non-interest bank, was already licensed prior to end-December 2011, but had not commenced operation as of that date.

respectively, separately maintain off-site supervision function in Abuja and on-site examination function in Lagos. Other sector regulators include the Securities and Exchange Commission (SEC), the National Insurance Commission (NAICOM) and the National Pensions Commission (PENCOM) for the securities, insurance and pensions sector respectively

8. **The co-ordination of the activities of the Nigerian banking sector supervisory authorities is conducted under the aegis of the CBN/NDIC Executive Committee on Supervision which should ensure that operations of the two supervisory authorities are coordinated to remove overlaps, avoid gaps and ensure adequate information sharing on issues of supervisory concern.** The Financial Services Regulation Coordinating Committee (FSRCC) provides the platform for the co-ordination among and information sharing with regulatory authorities, inter alia with reference to financial sector stability, and supervision of financial conglomerates, financial holding companies and bank holding companies.

9. **There are also self regulatory organisations that prescribe code of ethics/advocacy for their members.** They include, the Chartered Institute of Bankers of Nigeria (CIBN), Institute of Chartered Accountants, Association of National Accountants, Chartered Institute of Stockbrokers, Association of Stock Broking Houses of Nigeria, Association of Issuing Houses of Nigeria, Association of Capital Market Registrars, Association of Corporate Trustees, Financial Market Association of Nigeria, Capital Market Solicitors Association and the Association of Bureau de Change Operators of Nigeria. They have the powers to sanction erring members in line with their code of ethics.

10. **The CBN and NDIC derive their supervisory powers principally from the Central Bank of Nigeria Act, 2007 (CBN Act), Nigeria Deposit Insurance Corporation Act, 2006 (NDIC Act), and the Banks and Other Financial Institutions Act, 1991 (BOFI Act).** Other legislative instruments that impact on banking supervision include the Failed Banks (Recovery of Debts) and Other Malpractices in Banks Act, 2004, the Companies and Allied Matters Act (CAM Act), 2004, the Economic and Financial Crimes Commission Act 2004 and the Money Laundering Prohibition Act 2011. The CBN and NDIC also issue rules and regulations pursuant to their powers under the above mentioned legislation.

11. **The CBN Act was re-enacted in 2007 to bring the law in tune with developments in the financial system.** New provisions introduced included: enhancement of the security of tenure of the governor and deputy governors of the bank through the Senate's confirmation of appointments and removal of the governor, deputy governors and Board members; operational autonomy of the CBN; establishment of a Monetary Policy Committee (MPC) to drive the implementation of the Bank's monetary policy; expansion of the membership of the FSRCC to include the NDIC; power to regulate Credit Bureaus and the Payment Systems; and enhanced powers for promoting mutual cooperation and exchange of information. At

present, due to the dynamism of the industry, the CBN, BOFI and NDIC Acts are undergoing further review.

12. **Total banking sector assets stood at ₦18.21 trillion⁴ as at end–December 2011, which represented 53.6 percent of GDP.** Of the 21 banks, four are owned by foreign banking organisations while seventeen are domestically controlled. The domestic banks controlled 86.4 percent of industry assets as at end–December 2011 compared with 13.6 percent controlled by foreign institutions. The three domestic banks that were acquired by the AMCON in 2011 controlled 5.0 percent of industry assets.

13. **The banking sector appears relatively sound as at end–December 2011, as shown by soundness indicators, many of which displayed an improving trend.** The ratio of regulatory capital to risk weighted assets increased to 17.8 percent at end–December 2011, representing a 13.6 percentage point increase over the ratio of 4.2 percent recorded at the peak of the banking crisis (end–June 2011). Similarly, the ratio of tier 1 capital to risk weighted assets of 18.1 percent at end–December 2011 was 13.6 percentage points higher than the level of 4.5 percent achieved at end–June 2011. Asset quality indicators also showed a substantial improvement. The ratio of nonperforming loans (NPLs) to total loans of 4.9 percent showed a decline of 22.5 percentage points from its peak of 28.8 percent at end–June 2010. The level of liquidity in the system also displayed an increasing trend—the ratio of core liquid assets to total assets increased to 25.7 percent at end–December 2011 from 17.2 percent at end–June 2010. Similarly, the ratio of liquid assets to short-term liabilities increased by 11.8 percentage points to 31.2 percent between June 2010 and end–December 2011.

14. **The Financial Reporting Council of Nigeria (FRCoN) is a statutory body responsible for auditing and financial reporting standards to be observed in the preparation of financial statements of public interest companies.** The FRCoN developed a roadmap for the adoption of International Financial Reporting Standards (IFRSs) and International Auditing Standards (ISAs) in Nigeria. Currently, the FRCoN and the CBN are collaborating in the adoption of IFRS in the Nigerian banking sector with effect from 2012 (financial statements for financial year ended December 31, 2012 will be the first to be IFRS compliant).

15. **The banking sector has undergone significant change and reform.** After the bank recapitalizations following the 2005–06 banking sector consolidation, Nigeria experienced rapid credit expansion as banks broadened their activities and moved to the untapped retail sector, to borrowers involved in equity market speculation (margin lending collateralized by shares) and acquiring non bank subsidiaries. The 2005–06 banking sector consolidation

⁴ The total assets and other indices do not include JAIZ Bank Plc, which only commenced operation in 2012.

generated capacity for several Nigerian banks to expand internationally, establishing subsidiaries particularly in Africa.

16. **The Nigerian economy has experienced a number of domestic and external shocks in recent years, which impacted the banking sector.** The oil price drop and currency devaluation accompanying the 2008 global financial crisis stressed those banks with heavy concentration in the oil and gas sector, while the NSE downturn adversely affected banks exposed to margin lending. In 2008, the Nigerian stock market lost about two-thirds of its value, following a sharp decline in world oil prices and currency devaluation. Banks with heavy concentration in the oil and gas sector were stressed, while the stock exchange downturn adversely affected banks exposures to margin lending. By 2009, the banking sector was in crisis.

17. **But large buffers, built before the global crisis, and low debt, helped mitigate the impact of the shocks by providing room for expansionary fiscal policy.** Fortunately, the economy continued to grow rapidly at over 7 percent during each year since 2009. Monetary policy was tightened in 2011 after an increase in inflation and a decline in international reserves in 2010. Although the macroeconomic outlook remains positive, substantial risks remain, in view of the fact that oil constitute more than 90 percent of exports and oil receipts generate 75 percent of government revenue, and the recent spate of social unrest in the north of the country continues.

18. **A banking crisis, which involved more than 40 percent of the banking sector assets, came to a head in the second half of 2009.** The authorities identified the following as the main contributing factors, namely:

- Macro-economic instability caused by large and sudden capital inflows.
- Major failures in corporate governance at banks.
- Lack of investor and consumer sophistication.
- Inadequate disclosure and transparency about the financial position of banks.
- Critical gaps in regulatory framework and regulations.
- Uneven supervision and enforcement.
- Unstructured governance and management processes at the CBN/weaknesses within the CBN.
- Weaknesses in the business environment.

19. **A comprehensive set of measures were taken by the authorities to counteract the 2009 banking crisis and, as a result, Nigeria avoided a major economic meltdown, and the economy was stabilized.** The measures adopted in response to the 2009 banking crisis included the following:

- Special examinations were commissioned in respect of all banks and executed by the CBN and NDIC.
- Ten banks were found to be in a “grave situation” and were intervened.
- The CBN removed eight banks’ senior management and replaced them with CBN appointees.
- The CBN provided liquidity support in the amount of ₦620 billion (US\$4.1 billion) in the form of unsecured, subordinated debt. (In essence, this constituted solvency support as well.)
- A blanket guarantee of interbank and foreign credit lines of banks was introduced, and extended (for six-monthly periods) until end-2011.
- The CBN made a public commitment to protect all depositors and foreign creditors against loss and not to permit any bank to fail.
- At the peak of the crisis, the CBN created an expanded discount window which admitted non-federal government securities as eligible securities, while extending the tenure of the facilities to 360 days.
- The FMoF and the CBN established AMCON to support troubled bank resolution, and the banking sector more broadly. AMCON purchased banks’ NPLs in exchange for AMCON three-year zero coupon bonds (which are guaranteed by the Federal Government.) AMCON facilitated mergers and acquisitions of the intervened banks and the creation of bridge banks, which were re-capitalized by AMCON.
- NDIC coverage of insured deposits was recently increased to ₦500,000 for CBs and ₦200,000 for insured community banks.

20. **Important reforms, broadly in line with BCBS pronouncements, were instituted.** These reforms included the following:

- The universal banking model was abolished in favour of a “back-to-basics” banking model, and a new bank license regime was introduced.
- Risk-based supervision was embedded.

- The Corporate Governance Code was implemented.
- A number of regulatory prescriptions were issued covering a range of issues, inter alia by way of circular, code, guideline, prudential guideline, framework and regulation, including capital adequacy, risk and risk management and risk-based supervision, credit risk management, large exposures and related parties, margin lending, cross-border supervision, consolidated supervision (only in draft form), fitness and propriety, internal control, disclosure and AML/CFT.
- Adoption of IFRS in 2012.

21. **The financial sector is large, remains dominated by the banking sector, and has significant international linkages.** The Nigerian banking system has undergone significant change in the recent period, and this process is still ongoing. Although the sector remains dominated by domestic institutions, a few international banks have a presence in Nigeria, with a major regional bank headquartered outside Nigeria and active in 32 countries in Africa, having its largest subsidiary in Nigeria. Overall the number of banks has fallen from 89 in 2005 to 21 in 2012. Six of the banks, of which one is the abovementioned subsidiary, dominate the banking system, with a market share of around 60 percent of total banking sector assets. Three small banks are distressed, the smallest of which is insolvent and the other to being former bridge banks with AMCON being the main owner.

22. **The macroeconomic outlook remains positive, but substantial risks remain.** Like the rest of the Nigerian economy, the financial sector is exposed to the effects of volatility in international markets for commodities and capital. Fortunately, large buffers built before the global crisis, and low debt, helped mitigate the impact of the shocks, by providing room for expansionary fiscal policy.

23. **The Nigerian economy emerged from the banking crisis, and has the potential to enjoy an extended period of strong economic growth.** This could be facilitated by a comprehensive strategy to conclude and exit from the crisis management period; to enhance protection against existing and emerging vulnerabilities; and foster financial deepening that can underpin sustainable growth on an enduring path for the periods ahead.

24. **Although systemic risk has declined since the peak of the recent crisis, the financial system is still exposed to risks from both global and domestic factors.** Though oil prices recovered, a further deterioration in the global environment could result in a sharp drop in oil prices. Also, oil exports could be disrupted. This could impact negatively the current account and fiscal positions, thereby dampening the build up of international reserves and/or increasing public debt, in the absence of fiscal consolidation. The security situation is concerning, arising from terrorist activity in the north of the country.

25. **The bank regulators and supervisors have an extensive reform agenda.** In addition to IFRS, the authorities intend to implement Basel II and Basel III. New

instruments, such as macroprudential, and new techniques, such as stress testing and scenario analysis and analysing financial stability are also important.

D. Preconditions for Effective Banking Supervision

26. Macroeconomic policies have the potential to pose risk to financial stability.

Sound macroeconomic policies are a precondition to and a foundation of a stable financial system. Failure to implement politically difficult fiscal adjustment measures or curb overly ambitious infrastructure spending could pose a risk to the financial system. Fiscal dominance (arising from the imperative to keep monetary policy tight, in order to counteract the deleterious effects of weak fiscal discipline, consequential pressures on the currency, all of which fuels inflation, notwithstanding private credit growth sputtering) is a major contributor to an unfavorable trade-off between inflation and growth. This could also put an undue burden on monetary policy to contain inflation and also fight pressures on the currency and international reserves. At times the markets appear confused, perceiving that the CBN is pursuing multiple objectives. Following the crisis, significant efforts are being made to harmonize the structure for the implementation of monetary policy and prudential regulation. Accordingly, a framework has been developed in Nigeria to align financial system stability goals with broad macroeconomic policy. The key areas that are being addressed progressively by The authorities progressively are addressing key areas, including: policy harmonization and the resolution of the conflict of objectives between the Economic Policy Directorate and the Financial System Stability Directorate of the CBN, the development of a macro prudential toolkit, enhancing the quality of data and consideration of fiscal and monetary policy instruments that have the potential to impact financial stability.

27. The key elements of required public infrastructure are present, though the qualitative dimensions show weaknesses and vulnerabilities.

These key elements include a system of business laws, including corporate, bankruptcy, contract, consumer protection and private property laws; comprehensive and well-defined accounting principles and rules that command wide international acceptance, in the form of IFRS, which banks are required to adopted with effect from 2012; a system of independent audits for listed companies, as well as for banks, independent assurance for users of financial statements that the accounts provide a true and fair view of the financial position of the company; an independent judiciary and self-regulated accounting, auditing and legal professions; supervision of other financial markets and, where appropriate, their participants; a payment and clearing system for the settlement of financial transactions. Concerns regarding the qualitative dimensions of public infrastructure arise, inter alia, from weaknesses in policy making and legislative processes, legal uncertainty on key issues, inability to resolve banks promptly, inability to achieve prompt collection of outstanding debts through legal avenues, inability to execute promptly on collateral, unpredictability of legal outcomes, weak ability to prosecute financial crimes, seeming absence of accountability of external auditors, weaknesses in supervision of other financial institutions and markets, and weaknesses in the payments and clearing system (though the Payment System Vision 2020 aims at significant improvements.)

28. Gaps and weaknesses in market discipline was a material contributor to the 2009 banking crisis. Effective market discipline depends substantially on adequate flows of information to market participants, to enable informed decisions, appropriate financial incentives to reward well-managed institutions, and arrangements that ensure investors are not insulated from the consequences of their decisions. In 2010, the CBN issued a circular on minimum disclosure in the financial statements of banks. The implementation of international standards like IFRS and the relevant part/s of Basel II/III should enhance transparency. Since 2010, the CBN has published a Financial Stability Report on a bi-annual basis, to focus stakeholders' attention on those factors that predispose the financial system to shock as well as the policies to address these concerns. More attention has focused on the data quality of regulatory information submissions by banks. Since 2008, the CBN has not issued an annual bank supervision report. With effect from 2011, a semi-annual Financial Stability Report (FSR), which strives to cover also what previously was covered by the annual bank supervision report, has been issued.

29. The Nigerian framework for crisis management and the financial sector safety net was effective in containing (the contagion from) the crisis, though much needs to be done to benefit from the lessons learnt. The CBN took decisive measures to avert a potential systemic crisis by intervening in troubled banks, injecting liquidity into these banks and providing broad guarantees. These quick measures stabilized the banking system and allowed the authorities time to design a strategy to resolve the intervened banks. The resolution strategy ultimately employed consisted of many elements, including: replacing management in a number of banks; recapitalization subject to shareholders' approval; setting up an asset management company, AMCON, to purchase NPLs of banks in exchange for tradable three-year zero coupon bonds issued by AMCON and guaranteed by the Federal Government; entering into M&A arrangements; and setting up bridge banks that were capitalized by AMCON. All these measures helped the authorities stabilize a banking system that was on the verge of a systemic crisis. The NDIC constitutes an important component of the safety net. Despite the success, the CBN should more fully develop its crisis management and safety net arrangements. Nigeria has taken important steps to facilitate the identification and adoption of a framework for macroprudential policies, with the FSRCC coordinating the supervision of financial institutions and a dedicated department, the Financial Policy and Regulation Department (FPRD), in the CBN having been set up to perform the function of macroprudential supervision. It is necessary to improve bank resolution, inter alia, by specifying preference for depositors and creating a non-judicial/administrative special resolution regime.

E. Main Findings of the BCP Assessment

30. Nigeria has recorded significant improvement in its level of compliance with the BCPs since the last independent assessment by the IMF and the World Bank in 2002. The 2002 independent assessment concluded that Nigeria was compliant with three, largely compliant with eleven, materially non-compliant with nine and non-compliant with two core

principles. Considered against the essential criteria, Nigeria is now compliant with one, largely compliant with seventeen and materially non-compliant with seven CPs.

31. **The improvement in the assessment ratings is attributed to the enhancements of the supervisory capacity of Nigerian banking system supervisors through:** (i) the enactment of new laws and amendment of laws; (ii) issuance of various regulations, circulars and guidelines to address the weaknesses observed during the 2002 assessment; and (iii) reform initiatives embarked upon in the aftermath of the 2009 banking crisis.

Objectives, independence, powers, transparency and co-operation (CP1)

32. **A principal objective of the CBN is to promote financial stability.** The CBN is charged with the primary responsibility of bank supervision and has clear related objectives. The NDIC cooperates with the CBN in discharging the bank supervision responsibility. Though bank supervision is not explicitly clearly stated as an objective of the NDIC, it is implicit. An effective and efficient legislative process through the National Assembly is a necessary precondition to enable congruence and to keep pace with the internationally generally accepted legal and regulatory framework for banking, which is not being achieved currently. It is important to maintain the currency of the legal and regulatory framework, by way of prompt responses (to international policy developments and local needs), through sound policy development and a responsible legislative and regulatory process. (BCP1(1))

33. **The CBN possesses operational independence, transparent processes, sound governance and adequate resources, and is accountable for the discharge of its duties.** The position of the NDIC in relation to independence and to whom it is accountable is less clear. (BCP1(2))

34. **A legal framework for banking supervision, including provisions relating to authorization of banking establishments and their ongoing supervision is in place.** A thorough review and comprehensive updating of the legal and regulatory framework is necessary. (BCP1(3))

35. **The legal framework for banking supervision empowers the supervisor to address compliance with laws.** The law and regulations appear, implicitly, though not necessarily explicitly, to permit the supervisor to apply qualitative judgment in safeguarding the safety and soundness of the banks within its jurisdiction—this should be made explicit. (BCP1(4))

36. **The legal framework for banking supervision makes provision for legal protection for supervisors—however, it does not make provision for their concomitant legal costs.** (BCP1(5))

37. **Arrangements for sharing information between supervisors and protecting the confidentiality of such information are in place, though the coordination between the CBN and the NDIC may require attention.** (BCP1(6))

Licensing and structure (CPs 2-5)

38. **The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined, and the use of the word “bank” in names is controlled as far as possible.** (BCP2)

39. **The licensing authority has the power to set criteria and reject applications for establishments that do not meet the standards set.** The licensing process, at a minimum, consists of an assessment of the ownership structure and governance of the bank and its wider group, including the fitness and propriety of board members and senior management, its strategic and operating plan, internal controls and risk management, and its projected financial condition, including its capital base. Where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor is obtained. Important elements of licensing, including important criteria, and other requirements and process, are implicit and informal—these should be explicitly specified and formalized. The list of prescribed criteria contained in the legal and regulatory framework is incomplete, and the criteria should be focused on outcomes, as opposed to inputs. In addition, the CBN should be required to create a formal audit trail, by the CBN formally and in writing assessing a new bank license application against each and every one of the prescribed criteria. (BCP3)

40. **The supervisor is empowered to review and, if deemed appropriate, to reject any proposals to transfer significant ownership or controlling interest, whether held directly or indirectly in a bank, to other parties.** The supervisor’s flawed powers to review and the supervisor’s weak and inadequate powers to enforce such a rejection should be remedied and bolstered. Furthermore, it is necessary to focus on the beneficial shareholders, as opposed to focusing merely on the registered/nominee shareholders.(BCP4)

41. **The supervisor has the power to review major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and confirming that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.** (BCP5)

Prudential regulation and requirements (CPs 6-18)

42. **The CBN has set prudent and appropriate minimum capital adequacy requirements for banks (though this applies in respect of a bank’s credit risk exposures only) and has defined the components of capital, (largely) bearing in mind its ability to absorb losses.** These requirements, which are applicable to all banks (both local and foreign, and both internationally active and non-internationally active) are mostly in line with those

established in the applicable Basel requirement, apart from some important shortcomings, which need to be rectified. The authorities should develop comprehensive and detailed principles, standards, guidance, prescriptions, statutory returns and supervisory work programs, inter alia based on and aligned with relevant pronouncements of the BCBS, for all key areas, including risk areas, which would enhance effectiveness, efficiency, consistency and transparency of and quality control over supervision, thereby enabling more effective challenging of banks by the supervisor. The authorities should perform overall micro/bottom up and macro/top-down stress testing and simulation exercises in relation to all key areas (including risk areas), as a tool to provide forward-looking assessments of a bank's capacity (in relation to capital, liquidity and earnings) to withstand extreme but plausible macro-financial shocks. Banks should hold capital also against risk exposures other than credit risk, and hold adequate capital where the Basel I capital requirements are not sufficiently prudent. (BCP6)

43. **The CBN's *Guideline for the Development of Risk Management Frameworks for Individual Risk Elements* generally governs a bank's risk taking and risk exposures.** However, it is overarching and generic, and not supplemented with specific and detailed guidance and prescriptions, implying that there are important gaps and shortcomings in the legal, regulatory and supervisory framework relating, inter alia, to a bank's risk management. The CBN applies a risk-based approach to supervision, as provided for in the CBN's *RBS Framework*, including to off-site and on-site supervision. Accordingly, the CBN assesses a bank's risk management (which should be under the oversight of the board of directors and senior management) by gaining an understanding of the risk management policies, strategies, processes and risk appetite/aversion, thereupon assessing the identification, evaluation, monitoring and controlling or mitigating of all material risks, and then assessing the bank's overall capital adequacy in relation to the bank's risk profile. The CBN also assesses whether these processes are commensurate with the size and complexity of the institution. In line with the CBN's HRD plan for specialist career streams, the CBN should engage specialists to support the regulatory and supervisory functions in addressing specialized and complex issues in a range of areas, including corporate governance, capital and capital management, risk management, accounting and auditing, IT and project management, to enable the authorities more effectively to challenge the banks. (BCP7)

44. **The legal and regulatory framework requires that a bank has adequate credit risk management policies, strategies and processes, (including to identify, measure, monitor, and control credit risk, including counterparty risk) commensurate with its credit risk profile.** This includes addressing the granting of loans and making of investments, the evaluation of the quality of such loans and investments, and the ongoing administration and management of the loan and investment portfolios. (BCP8)

45. **In general, the law and regulation provides explicit requirements on how a bank should identify and manage problematic loans and adequately provision.** In addition, the RBS approach entails an appropriate review of banks' significant risky asset portfolios.

However, with the adoption of IFRS by banks with effect from 2012, the provisioning regime prescribed in the *Prudential Guidelines* should be updated concomitantly. (BCP9)

46. **Though supervisors ensure that banks have policies and processes that enable management to identify and manage concentrations within the portfolio, and supervisors set prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties, there are important gaps, shortcomings and vulnerabilities which require attention.** (BCP10)

47. **Abuses, arising from related party transactions and exposures, and conflicts of interest, were identified as major causes of the 2009 banking crisis.** Hopefully the CBN's action in removing executive management in eight banks and sanctioning directors constituted a reality check, instilled necessary discipline and will serve as a deterrent. In general, the law and regulations on related parties are sparse and need to be reviewed and enhanced substantially, to prevent related party abuse again posing a significant threat to financial stability. (BCP11)

48. **The CBN has provided over-arching and generic guidance for banks in managing their risks, including country and transfer risk.** Further, the *RBS Framework* provides CBN supervisors with guidance on how to assess significant activities of banks including cross-border operations. With the increasing internationalization of the banking system, country and transfer risk is an emerging risk requiring increasing attention. (BCP12)

49. **The regulatory and supervisory framework for and supervisory approach to market risk should be improved, inter alia, by adoption of the 1996 Market Risk Amendment, and further strengthening regulatory policies.** (BCP13)

50. **The CBN supervisors (on an ongoing basis) monitor a bank's (day-to-day) liquidity risk management by assessing a bank's compliance with the (somewhat dated) *Guidelines for the Development of Liquidity Management Policies (2003)*, while being cognizant of a bank's risk profile.** In summary, the guidelines require banks to have a proper strategy for managing liquidity risk, with appropriate internal policies and procedures as well as adequate liquidity contingency plans. (BCP14)

51. **The supervisor is satisfied that a bank has in place risk management policies and processes to identify, assess, monitor and control/mitigate operational risk, which policies are commensurate with the size and complexity of the bank.** Detailed guidance on operational risk management is lacking. (BCP15)

52. **IRRBB is not separately and specifically identified in the legal, regulatory or supervisory frameworks as a separate risk.** The IRRBB exposures of banks appear modest, in view of variable interest rates (mostly) applying to both assets and liabilities. Nonetheless, the interest rate profile of the system may change in the future, and it is imperative that the CBN be suitably prepared. (BCP16).

53. **Supervisors are satisfied that banks have in place internal controls that are adequate for the size and complexity of their business.** These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations. Major failures in corporate governance at banks have been identified as one of the main factors which contributed to the 2009 banking crisis. Undoubtedly, there were major gaps and breakdowns of internal controls. Though important regulatory reforms have been undertaken and the supervisory approach and processes were significantly enhanced, at this stage it is too early to come to a conclusive conclusion on whether supervisory effectiveness is at an acceptable and satisfactory level, though the signs are positive. However, fundamental concerns include whether the stakeholders (including the internal auditor, the external auditor and the supervisor) are effectively challenging one another, and whether the supervisors are willing to act proactively, not only in respect of compliance issues, such as relating to breaches of prudential requirements but also in respect of corporate governance, risk management and internal control weaknesses, breaches and excesses. Training of all stakeholders on their duties and responsibilities in relation to all key aspects of banking, and the consequences of breaches and failures of such duties and responsibilities, is necessary. (BCP17).

54. **Though relevant legislation (*The Money Laundering Prohibition Act and the Anti-Terrorism Act*), KYC guidelines and other regulations are in place to control and check the abuse of financial services, there remain fundamental gaps and weaknesses.** The CBN supervisors are equipped with an appropriate supervisory programme and have applied this programme to assess banks' compliance with the relevant law and regulations as well as to determine whether a bank has adequate policies and processes in place which would prevent the bank from being used intentionally and unintentionally for criminal activities. In the light of the 2011 FATF conclusion on Nigeria, the governance breakdowns which contributed to the 2009 banking crisis and the 2011 report by the OCC on a particular bank's CML/CFT failings, there remain grave concerns about the quality of implementation and adherence in relation to AML/CFT. As some of the changes to the legal and regulatory framework were implemented only very recently, it is not as yet appropriate to comment on the quality of implementation thereof. (BCP18).

Methods of ongoing banking supervision (CPs 19-21)

55. **The *RBS Framework* provides an adequate supervisory process, essentially based on the risk profiling of banks, enabling the CBN supervisors to have appropriate understanding of the safety and soundness of banks in the system, and has a forward looking focus.** The framework enables a better evaluation of risks, through the separate assessment of inherent risks and risk management processes, which also requires the CBN

supervisors to understand the effect of the external environment, firstly at the level of the banking system and, secondly at the level of the whole economy. (BCP19)

56. **There is a proper mix of on-site and off-site supervisors to evaluate the condition of banks and their inherent risks.** However, efforts should be in place to increase the quality of the assessment by having an independent quality assurance process in relation to the ratings of banks. More engagement is recommended with the banks' board members, particularly the independent and non-executive members, outside the onsite examination period. (BCP20)

57. **Supervisors are empowered to obtain information from banks, but not from entities related to banks,** and have a means of collecting, reviewing and analyzing prudential reports and statistical returns from banks on a solo, but not (as yet) on a consolidated basis, and a means of independent verification of these reports, through either on-site examinations or use of external experts. (To date, the authorities have not as yet implemented consolidated supervision.) (BCP21)

Accounting and disclosure (CP22)

58. **Generally, the CBN seemingly ensures that each bank maintains adequate records drawn up in accordance with accounting policies and practices that are widely accepted internationally, and publishes, on a regular basis, information that fairly reflects its financial condition and profitability.** However, the 2009 banking crisis came about partly as a result of material failures in this area, and there is a lingering concern that not enough has been done, perhaps, to improve the quality of corporate governance insofar as it relates to and involves the internal audit/auditor or the external audit/auditor, or the quality of the application of accounting, auditing and disclosure. (BCP22).

Corrective and remedial powers of supervisors (CP23)

59. **Supervisors have at their disposal an adequate range of supervisory tools to bring about timely corrective actions.** This includes the ability, where appropriate, to revoke the banking license or to recommend its revocation. These powers were promptly deployed during the 2009 banking crisis. However, there is a concern that the authorities may lack the resolve to fully apply the Intervention Framework and finally resolve a bank which is hopelessly insolvent. The authorities should apply zero tolerance and act promptly, resolutely and forcefully in relation to actions or inactions which put financial stability at risk, as well as in relation to corporate governance transgressions, non-compliance with statutory prescriptions and submission/disclosure of substandard quality of data/information.(BCP23)

Consolidated and cross-border banking supervision (CPs 24-25)

60. **The legal and regulatory framework for consolidated supervision is not yet in**

place. Notwithstanding, the CBN performs some elements of consolidated supervision in relation to the interests of a bank. (The draft *Framework for the Consolidated Supervision of Financial Institutions in Nigeria*, which contains a formal process of evaluating the overall structure of the bank and related parties as well as identifying the risks arising from non-banking activities, should provide largely the necessary regulatory platform for an effective supervisory function on consolidated basis, though a legal foundation is also required. The FSRCC provides a vehicle for coordination among the relevant domestic supervisors and ensures that ongoing supervisory efforts are closely integrated for the local components of a banking group.) (BCP24)

61. **The CBN has in place a *Framework for the Supervision of Cross-Border Institutions* and this document forms the basis of its cross-border supervisory activities.** In addition, CBN has a unit within BSD, dedicated to the supervision of cross-border institutions. There are MoUs in place with other foreign regulatory agencies in jurisdictions where Nigerian banks have presence. In the case of other jurisdictions which have not signed formal information sharing arrangements with the CBN, there are informal arrangements for information sharing, for instance, in the case of the OCC and U.K. FSA. In certain circumstances, the information sharing via informal arrangements is more active than those via the formal arrangements. Foreign banks operating in Nigeria are subjected to the same regulatory and supervisory regimes as applied to domestic banks. (BCP25)

Table 1. Nigeria: Summary Compliance with the Basel Core Principles—Detailed Assessments

Reference Principle	Grading	Comment
1. Objectives, independence, powers, transparency, and cooperation	LC	
1.1. Responsibilities and objectives	LC	<ul style="list-style-type: none"> • The policy development process is (too) ad hoc and event-driven. • The legislative process is not sufficiently responsive to enable an up to date legal and regulatory framework in line with internationally generally accepted standards and principles, thereby to ensure that the banking system is duly enabled to facilitate the required economic development and growth while maintaining financial stability. • No “anchor” has been identified to which any updating of the legal, regulatory and supervisory framework and supervisory approach will be aligned. • The BOFI Act was last amended in 1999 and is dated. • The latest version of the BOFI Act contains clauses which, reportedly, had been amended duly by the National Assembly but, erroneously, had not yet been updated in the legislation itself. • The legal and regulatory framework is not sufficiently logically structured and organized and the internal hierarchy is not clear. • Subsidiary legislation and other pronouncements of the CBN are not well-organized, nor readily accessible • There is uncertainty as to the comprehensive list of circulars, codes, decrees, frameworks, guidelines, prudential guidelines, regulations and rules which are current. • Pronouncements of the Basel Committee on Banking Supervision are not always fully and/or appropriately adopted, sometimes resulting in important deviations, which often have a detrimental effect on the standing of the banking sector. • Currently, banks are seemingly required to be audited by way of Nigerian Auditing Standards. • The question arises whether or not the CBN is incurring liability toward third parties, such as investors and depositors, by its “prior approval” of a bank’s audited financial statements. • The versions of the BOFI Act and the NDIC Act on the websites of the CBN and NDIC, respectively, are not the latest versions of the relevant legislation. • The last annual bank supervision report published by the CBN was in respect of 2008. With effect from 2011, a semi-annual Financial Stability Report, which strives to cover also what previously was covered by the annual bank supervision report, has been issued.
1.2. Independence, accountability, and transparency	LC	<ul style="list-style-type: none"> • The NDIC Act does not contain a mandate and/or objective/s clause. • The NDIC’s “functions” clause does not mention the supervision of banks. • The NDIC Act is not clear on the question of which person or body the NDIC ultimately is accountable to. • Nowhere is it specifically provided for the NDIC to be operationally independent. • BSD staff is permitted to hold and trade shares in banks.

Reference Principle	Grading	Comment
1.3. Legal framework	LC	<ul style="list-style-type: none"> • Important pieces of the legal and regulatory framework has been drafted but not yet finalized and implemented, including: <ul style="list-style-type: none"> - Draft updated Code of Corporate Governance Code. - Draft Bank Holding Company Framework.
1.4. Legal powers	LC	<ul style="list-style-type: none"> • The legal framework does not specifically grant the supervisor full discretion to apply qualitative judgment in coming to a conclusion whether or not a particular situation, circumstance, action of inaction constitutes a threat to financial stability, whether or not a bank is being operated, managed or directed in a safe and sound manner, and in determining whether or not the bank is in a safe and sound condition. • Furthermore, the legal framework does not specifically empower the supervisor where, in the opinion of the supervisor, a bank and/or director and/or management is engaging in unsafe and unsound practices in conducting the business of the bank, to take corrective, enforcement and/or sanctioning actions against such a party/parties. • The legal framework is not explicit and specific that the supervisor has full and unfettered access to all stakeholders involved in a bank, for the purposes of discharging his responsibilities.
1.5. Legal protection	LC	<ul style="list-style-type: none"> • The CBN and NDIC staff not indemnified against legal costs of a legal action arising from the discharging of their duties in good faith.
1.6. Cooperation	LC	<ul style="list-style-type: none"> • The CBN/NDIC Executive Committee on Supervision meets only infrequently.
2. Permissible activities	C	<ul style="list-style-type: none"> • The CBN is not obliged statutorily to maintain and publish a list of licensed banks. • The NDIC is not obliged statutorily to maintain and publish a list of licensed banks.
3. Licensing criteria	LC	<ul style="list-style-type: none"> • The legal and/or regulatory framework essentially is silent on the following: <ul style="list-style-type: none"> - the criteria for issuing a licence; - the desirability and/or license for a shell entity, a shelf company, and a tax haven domiciled entity; - whether the criteria for issuing a license is consistent with those applied in ongoing supervision; - whether it is of concern or not that the proposed legal, managerial, operational and ownership structures of the bank and its wider group will or will not hinder effective supervision, whether on both a solo and a consolidated basis; - whether or not the CBN, when considering a new bank licence application, is required to identify and determine the suitability of major shareholders, including the ultimate beneficial owners, and others who may exert significant influence; - whether or not the CBN, when considering a new bank licence application, is required to consider the transparency of the ownership structure; - whether or not the CBN, when considering a new bank licence application, is required to identify the sources of initial capital; - whether or not the CBN, when considering a new bank licence application, is required to evaluate proposed directors and senior management as to expertise and integrity (fit and proper test), and any potential for conflicts of interest;

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> • whether or not the CBN, when considering a new bank licence application, is required to review and evaluate the proposed strategic and operating plans of the bank, including whether or not an appropriate system of corporate governance, risk management and internal controls, including those related to the detection and prevention of criminal activities, as well as the oversight of outsourced functions, will be in place; • whether or not the CBN, when considering a new bank license application, is required to make a determination whether or not the operational structure reflects and is appropriate for the scope and degree of sophistication of the proposed activities of the proposed bank; • whether or not the CBN, when considering a new bank license application, is required to review pro forma financial statements and projections for the proposed bank, inter alia for purposes of assessing the adequacy of the financial strength to support the proposed strategic plan as well as financial information on the principal shareholder/s of the bank; • whether or not the CBN, when considering a new banking license application, is required to assess whether or not the board, collectively, have a sound knowledge of each of the types of activities the bank intends to pursue and of the associated risks; • whether or not the CBN, when considering a new banking license application, assesses whether or not the shareholder has the ability to supply additional financial support to the proposed bank, as and when needed; • whether or not a license may be obtained on false information; and • whether or not the CBN is required to have policies and processes in place to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that the supervisory requirements outlined in the license approval are being met. • A banking license application is not currently assessed formally against an explicit set of written criteria. • The CBN does not appear formally and comprehensively to document the nature and extent of the work performed in relation to the implicit and informal criteria which it applies when assessing a banking license application. • The legal and regulatory framework does not address the issue of bank's outsourcing activities.
4. Transfer of significant ownership	MNC	<ul style="list-style-type: none"> • Section 7(1) of the BOFI Act is not of much practical use in preventing a change of control of a bank without the CBN's prior approval, as it imposes a duty on a bank in a matter which pertains to shareholders. • The current approach to ensuring that key shareholders are and remain fit and proper is deficient. • Circular BSD/DO/CR/2/2000, dated March 23, 2000, is out of line with the current approach to fit and proper requirements relating to shareholders. • The legal and regulatory framework does not define a beneficial shareholder or distinguish a beneficial shareholder from a nominee shareholder. • A bank is not required to notify the supervisor should it become aware of any material information which negatively affects the suitability of a major shareholder. • Fines prescribed in the BOFI Act are outdated, as they are no longer in line with the gravity of the offence or sufficient deterrent.

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> The components of the legislative framework dealing with this topic are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty
5. Major acquisitions	LC	<ul style="list-style-type: none"> The legal and/or regulatory framework does not prescribe sufficiently comprehensively and clearly how a bank, when considering a (proposed) acquisition or investment, is required to distinguish between cases which are required to be dealt with by way of an ex ante application, an ex post application, an ex ante notification and an ex post notification, and other cases. It is of fundamental and serious concern that a bank is enabled to take large stakes (even controlling stakes, and even full ownership) in agricultural, industrial and venture capital companies. The 2011 change in the banking model, with the removal of the universal banking model, did not affect the above provisions of the BOFI Act.) The components of the legislative framework dealing with this topic are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty
6. Capital adequacy	LC	<ul style="list-style-type: none"> The regulatory capital adequacy requirements are not strictly in line with the Basel I regulatory capital adequacy requirements, as regard both Tier 1 and Tier 2 regulatory eligible elements of capital. A bank from time to time may own an investment in its own capital instruments or in another bank's capital instruments, or provide financing facilities or financing for the purchase of its own shares or the shares of another bank, or provide financing facilities or financing against the security of its own shares or the shares of another bank. The regulatory and/or supervisory framework does not contain any requirements for banks to perform capital management, nor is any guidance given to banks in this regard, nor is any guidance given to supervisors on how to deal with capital management off-site or on-site. No bank holds regulatory capital against any risk other than credit risk A bank is permitted to treat the shortfall in regulatory provisions, constituted by the difference when a bank's regulatory required provisions exceed its IFRS credit impairments, as Tier 1 core capital. To date, the authorities have not consistently and regularly performed overall micro/bottom up and macro/top down stress testing, scenario analyses and simulation exercises in relation to all key areas. The components of the legislative framework dealing with this topic are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty No assessment, seemingly, of the impact of Basel III, has been undertaken.

Reference Principle	Grading	Comment
7. Risk management process	LC	<ul style="list-style-type: none"> • The legal and/or regulatory framework does not contain detailed guidance on all significant existing and emerging risks (e.g., country and transfer risk, market risk, operational risk and IRRBB). • The legal and regulatory framework does not contain a requirement that the approval level of risk exposures be commensurate with the size and risk of the resulting risk exposure, nor that material risk exposures (say, exceeding a prescribed percentage of a bank's capital) should be decided by the bank's senior management or even a higher level body (such as the board risk committee, or even the board itself.) • The CBN does not apply Basel II principles, such as capital management. (ICAAP/SREP), which are fundamental to the safety and soundness of a bank and can be implemented independently of Basel II. • The BSD has limited capacity and capabilities to challenge quantitative models effectively, or to perform stress tests or scenario analyses, or to supervise and challenge Basel II banks and Basel III banks. • No guidance has been developed in respect of internal risk management risk models, stress testing or scenario testing, which implies that one cannot draw much assurance from the outcomes of such models and exercises. • Banks only hold regulatory capital against credit risk, implying that banks do not hold regulatory capital against other significant risks. • The BSD's reform agenda, which includes also Basel II and Basel III constitutes a significant challenge. • The BSD may not have specialists which can effectively challenge the banks and related stakeholders in areas such as capital management and specialist areas of risk management, accounting, auditing, information technology, and project management. • The components of the legislative framework dealing with this topic are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty
8. Credit risk	LC	<ul style="list-style-type: none"> • The CBN requires banks to review their credit risk policies only once in every three years, which may not be frequent enough to capture the dynamic nature of credit risk. • The legal or regulatory framework does not require banks to prescribe that major credit exposures (e.g., exceeding certain level of banks' capital and those beyond the banks' risk appetite) or especially risky credit exposures to be decided by the bank's higher level of senior management. • The legal or regulatory framework does not require a bank to consider the potential future exposure of a counterparty credit risk exposure and to capture the material risks inherent in individual products or transactions.
9. Problem assets, provisions, and reserves	LC	<ul style="list-style-type: none"> • The classification and provisioning of specialized facilities e.g., agricultural finance, project finance, object finance, real estate finance, SME finance and mortgage finance do not take into account qualitative factors. • The CBN is in the midst of capacity building to prepare for full implementation of IFRS. The current supervisory resources have yet to be comfortable with validating banks IFRS models. • The CBN has not leveraged off external expertise in relation to IFRS.
10. Large exposure limits	MNC	<ul style="list-style-type: none"> • The terminology used in relation to large exposures is not consistent and clear.

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> • The definition of a large exposure is not sufficiently comprehensive, as it ignores certain relationships. • The legal and regulatory framework does not prescribe who may be empowered to approve a large exposure. • The large exposure limit as defined constitutes a “soft” limit, in the sense that it may be breached subject to supervisory approval, as opposed to a “hard” limit, which may not be breached. Consequently, also, the excess amount, being the amount of a large exposure which exceeds the 25 percent of a bank’s capital limit, does not constitute an impairment of capital. • The CBN supervisors are not empowered to deem the existence of relationships, outside those defined by law, as constituting part of a large exposure.
11. Exposure to related parties	MNC	<ul style="list-style-type: none"> • The terminology used in relation to large exposures is not consistent and clear. • The definition of a related party may not be sufficiently comprehensive, as it ignores certain relationships. • The legal and regulatory framework does not contain a prescription on which person/s or body/bodies should be empowered to decide matters involving related parties. • The CBN is not empowered to exercise its discretion and, on a case by case basis, deem the existence of relationships, outside those defined by law, as related party relationships. • There is no legal or regulatory provision which prohibits the granting of advances to related parties on more favorable terms than corresponding exposures to non-related counterparties and/or that such transactions should be entered into on an arm’s length basis. • There is no explicit regulatory requirement for monitoring and reporting of related parties’ transactions to be carried out by an independent credit review process. • The 60 percent limit on the maximum credit exposure to all insiders is high, also relative to international norms. • The breach of the 10 percent limit on individual related party exposures or the breach of the limit on aggregated related party exposures do not impact the regulatory capital adequacy computation of a bank.
12. Country and transfer risk	LC	<ul style="list-style-type: none"> • The CBN does not appear to accord priority to country and transfer risk. • Some banking groups have significant exposures to country and transfer risk, yet there is no specific supervisory guidance thereon. • No bank holds regulatory eligible capital against country and transfer risk, not even any bank with significant country and transfer risk exposure.
13. Market risks	MNC	<ul style="list-style-type: none"> • To date, Nigeria has not adopted the 1996 Market Risk Amendment and, consequently, does not impose a market risk requirement or require banks to hold capital against their market risk exposures. • Market risk played an important part in the 2009 banking crisis, yet guidance on market risk is extremely limited and incomplete. • The CBN has not as yet developed comprehensive and detailed standards and guidelines on market risk management. • Supervisory staff does not have access to a satisfactory supervisory program on market risk management which also covers ALCO and treasury operations.

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> • There does not exist any guidance from the CBN on the use of internal models for the valuation of market risk exposures. • Apart from the NOP limit for FX exposures, there are no market risk limits, thresholds and benchmarks. • The supervisory staff may not be comfortable in confronting technical and complex market risk management issues, including valuation of market risk positions, derivatives, stress testing, scenario analysis and back-testing. • No bank holds regulatory eligible capital against market risk, not even any bank with significant market risk exposure.
14. Liquidity risk	LC	<ul style="list-style-type: none"> • The Guidelines for the Development of Liquidity Management Policies, 2003, are somewhat dated. • The calculation method for the regulatory liquidity ratio is not comprehensive and does not cover off-balance sheet obligations. • The CBN has not concluded on the impact of Basel III.
15. Operational risk	LC	<ul style="list-style-type: none"> • There is no specific, comprehensive and detailed guidance on how banks should manage their operational risk profiles (including absence of guidelines on outsourcing). • There is no granular supervisory program to assist the CBN supervisors in specifically assessing operational risk and operational risk management. • No bank holds regulatory eligible capital against operational risk, not even any bank with significant operational risk exposure.
16. Interest rate risk in the banking book (IRRBB)	MNC	<ul style="list-style-type: none"> • There is no is specific regulation addressing IRRBB. • There is no specific supervisory program to guide the CBN supervisors in determining the effectiveness of banks' risk management system in managing IRRBB (including absence of an internal trigger for CBN supervisors to monitor the IRRBB of banks). • There is/are not statutory return/s focused on IRRBB. • The results of the FPRD's top-down stress test exercises have not been shared adequately within BSD. • The BSD does not perform bottom-up stress testing of IRRBB. • No bank holds regulatory eligible capital against market risk, not even any bank with significant market risk exposure.
17. Internal control and audit	LC	<ul style="list-style-type: none"> • It is of grave concern that, notwithstanding the 2006 Corporate Governance Code having alerted everyone and having warned about, essentially all, the factors which led to the 2009 banking crisis, the 2009 banking crisis ensued and the banking system and the country suffered a tremendous loss.
18. Abuse of financial services	MNC	<ul style="list-style-type: none"> • The existing laws and regulations are not adequate in relation to the criminalization of AML/CFT. • The recently issued returns are not in electronic format, which would imply significant human and manual intervention, and there does not appear provision for fixing the accountability, for the quality of the information in the returns, to (a) sufficiently senior person/s. • Major failures in corporate governance at banks were a main contributing factor to the 2009 banking crisis. Some of these activities bordered on, if they were not in fact full-blown, criminal acts and activities. • To date, one thematic examination of banks was performed, which highlighted important problems relating to KYC information at the banks.

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> • Important AML/CFT failings were reported by the OCC in relation to a Nigerian bank's branch in the U.S., which failings had not been picked up by the responsible parties in Nigeria.
19. Supervisory approach	LC	<ul style="list-style-type: none"> • Detailed supervisory programs for inherent risks assessment are not available. • The RBS process does not cater for structured peer comparison (qualitative and quantitative). • Criteria to assess the direction of risk are not granularly stated in the RBS Framework.
20. Supervisory techniques	LC	<ul style="list-style-type: none"> • Structured formal quality assurance process to determine the ratings of banks is not in place. • Engagement with the banks' board members, particularly the independent and non-executive members, is minimal outside the onsite examination period.
21. Supervisory reporting	LC	<ul style="list-style-type: none"> • The e-FASS system does not incorporate a workflow component or an on-site component. • A bank is not required to notify the CBN of all material information regarding the bank's activities, structure or overall condition, or material adverse developments, as soon as possible.
22. Accounting and disclosure	LC	<ul style="list-style-type: none"> • The requirement, provided for by Section 27 of the BOFI Act, for the CBN to approve the draft financial statements, may create the impression that the CBN is responsible for, and therefore legally liable in relation to, the content of the financial statements. • Bank accounting, bank auditing, bank disclosure and corporate governance relating to the roles of bank internal audit/auditors and bank external audit/auditors may not enjoy the required attention, as evidenced by the fact that the CBN does not have specialist capacity and capabilities which are focused on bank accounting, bank auditing, bank disclosure and the corporate governance roles of bank internal and bank external auditors. Accordingly, the CBN may be hamstrung to achieve effective challenge of banks in these areas. So, for example, meetings between supervisors, the external auditors' professional representative body and bank external auditors take place infrequently and the CBN has not been able to discharge its responsibility to develop reporting templates as required, in terms of Section 7.1.4. of the Code of Corporate Governance, which makes provision for the rendering of reports to the CBN on a bank's risk management practices, internal control and level of compliance with regulatory practices. • Banks are not required to have formal internal audit, external audit and disclosure policies. • The CBN does not obtain access to an external auditor's external audit working papers in respect of a problem bank. • An external auditor who complies with Section 29(7) of the BOFI Act and makes a report to the CBN may be held to be in breach of confidentiality requirements. • The BOFI Act does not specifically and explicitly empower the CBN to remove a bank's auditor who does not discharge his responsibilities satisfactorily.
23. Corrective and remedial powers of supervisor	LC	<ul style="list-style-type: none"> • The document titled Supervisory Intervention Framework has been placed in the public domain—the contents of Part 4, titled Supervisory Actions in the Event of Systemic Banking Distress may give rise to moral hazard.

Reference Principle	Grading	Comment
		<ul style="list-style-type: none"> • The Supervisory Intervention Framework may not be fully aligned with and grounded in the BOFI Act. • It is of concern that the supervisor in the past may not consistently have acted promptly, resolutely and forcefully in applying corrective, enforcement and sanctioning actions, or in resolving problem banks, especially in instances which hold the potential to imperil financial stability.
24. Consolidated supervision	MNC	<ul style="list-style-type: none"> • The Framework for the Consolidated Supervision of Financial Institutions in Nigeria is still in draft. • The CBN is not (explicitly, directly and unambiguously) empowered to obtain information from or supervise a financial holding company's related entities. • Consolidated supervision is a new area for the CBN supervisors, who may still have only limited capability to supervise banks on a consolidated basis. • The BOFI Act does not empower the CBN to require a bank to close a foreign office or impose limitations on their activities under specified circumstances, namely if the CBN determines that the oversight by the bank and/or supervision by the host supervisor is not adequate relative to the risks the office presents, and/or if it cannot gain access to the information required for the exercise of supervision on a continuous basis.
25. Home-host relationships	LC	<ul style="list-style-type: none"> • Framework for the Supervision of Cross-Border Institutions does not emphasize on the need for CBN to share information with its counterparts, although it stresses the importance of obtaining supervisory information from the overseas authorities. • The CBN has yet to carry out formal comprehensive assessments on the home and host regulators of Nigerian banks, in determining the level of reliance that the CBN can place on these regulators.

Table 2. Nigeria: Recommended Action Plan to Improve Compliance with the Basel Core Principles

Reference Principle	Recommended Action	Priority (H/M/L)
1. Objectives, independence, powers, transparency, and cooperation		
1.1. Responsibilities and objectives	<ul style="list-style-type: none"> • Maintain currency of the legal and regulatory framework, by way of prompt responses (to international policy changes and local developments and needs), through sound policy development and a responsive legislative process. • Perform a BCP self-assessment against the 2012 version of the Basel Core Principles, and align the updating of the legal, regulatory and supervisory framework and supervisory approach with the 2012 version of the Basel Core Principles. • Determine objective/s of the NDIC and incorporate within the NDIC Act. • Review thoroughly, and comprehensively update, the BOFI Act. • Make current consolidated (updated) version of legislation and regulations readily available in logical format in the public domain at all times. • Rationalize the regulatory framework by reviewing thoroughly the subsidiary legislation (subsidiary to the BOFI Act) (which, seemingly, consists of circulars, codes, decrees, frameworks, guidelines, prudential guidelines, regulations and rules), inter alia also to remove ultra vires provisions contained therein (which, if necessary, should be moved to the BOFI Act itself), and thereupon comprehensively update, logically structure in an appropriate hierarchy, and logically reference such subsidiary legislation, and then compile a compendium of such subsidiary legislation, which should be maintained updated. • Specify in the legislation the legal status of and internal hierarchy among the subsidiary legislation (such as a circular, code, decree, framework, guideline, prudential guideline, regulation and rule). • Withdraw annually, with effect from the end of a year, all circulars issued during that year, with effect from the end of that year and, where necessary and appropriate, in relation to issues and prescriptions which remain relevant and continue needing to be dealt with by way of circular, issue duly updated and amended versions of such circulars with effect from the beginning of the next year. • Adopt fully (without cherry picking) and appropriately all relevant pronouncements of the BCBS, to avoid important deviations which undermine certainty and consistency, and which can result in unintended consequences. • Require banks to be audited by means of and in line with International Standards of Auditing (ISAs), and that a formal plan be developed and implemented to ensure a high quality application of ISAs. • The CBN should consider how best to be involved, without incurring liability (whether explicitly or implicitly), in the process of finalization of the audited annual financial statements prior to the publication thereof, while simultaneously ensuring that adequate controls are in place to avoid insider abuses. 	<p>H</p> <p>M</p> <p>M</p> <p>H</p> <p>L</p> <p>M</p> <p>L</p> <p>L</p> <p>L</p> <p>L</p> <p>L</p> <p>L</p>

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> - The CBN is required formally and in writing to assess any new bank license application against the prescribed bank licensed criteria, and that the CBN should document the nature and extent of the work performed and the conclusions reached in relation to each criterion individually, and also overall - The CBN is not empowered to issue a bank license to a shell entity, a shelf company, or a tax haven domiciled entity. - The criteria for issuing a license are consistent with those applied in ongoing supervision - A license obtained based on false information shall be revoked by the CBN; and - That the CBN should have policies and processes in place to monitor the progress of new entrants into the banking sector in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met. • Specify explicitly and formally in the legal and/or regulatory framework that the CBN is required to consider and conclude on whether or not the new bank license application satisfactorily meets at least the following criteria: <ul style="list-style-type: none"> - Evaluate, by review of the (proposed) legal, managerial, operational and ownership structures of a (proposed) bank and its wider group, whether or not such structures would hinder effective supervision on both a solo and a consolidated basis. - Identify and evaluate whether or not the (proposed) major/significant/controlling (ultimate beneficial) shareholders, and others that may exert significant influence, are suitable. - Assess whether the ownership structure of the (proposed) bank is sufficiently transparent. - Identify the (proposed) sources of the (proposed) initial capital for the (proposed) bank, and evaluate whether or not such sources are acceptable. - Evaluate whether or not the (proposed) directors and senior management of the (proposed) bank are suitable, in view of their capacity and capability and integrity (fit and proper test), and in view of any potential for conflicts of interest. - Evaluate whether or not the (proposed) strategic and operating plans of the (proposed) bank, including the system of corporate governance, risk management and internal controls, and including those related to the detection and prevention of criminal activities, as well as the oversight of the proposed outsourced functions, are acceptable. - Evaluate whether or not the (proposed) operational structure reflects and is appropriate for the (proposed) scope and degree of sophistication of the (proposed) activities of the bank. - Evaluate whether or not the pro formal financial statements and projections for the (proposed) bank are adequate for purposes of assessing the adequacy of the financial strength of the (proposed) bank and the capacity of the (proposed) bank to support its strategy. - Evaluate whether or not the board, collectively, has a sound knowledge of each of the types of activities the (proposed) bank intends to pursue, and of the associated risks. 	M

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> - Evaluate whether or not the (proposed) controlling/significant/major shareholders would be in a position to provide the necessary additional financial support to the (proposed) bank to enable it to execute its strategic plan and achieve its strategic aims. - Evaluate whether or not the (proposed) major/significant/controlling shareholders would be in a position to provide the necessary additional financial support to the (proposed) bank in the event of a loss suffered as a result of an extreme but plausible event. 	
4. Transfer of significant ownership	<ul style="list-style-type: none"> • Recast BOFI Act Section 7 to ensure that it can have effect. (For example, the obligation to obtain the prior consent of the governor should be imposed on shareholders, as opposed to the bank itself, as only the shareholders, and not the bank itself, can effect a change of control of the bank or give effect to a disposal of the whole of the business of the bank, or effect an amalgamation or merger of the bank, etc.) In addition, empower the supervisor to stop, neutralize or overturn transactions which proceed without the supervisor's approval or despite the supervisor's approval. • Permit only fit and proper persons to obtain a shareholding exceeding 5 percent, which constitutes a significant shareholding, in a bank. Accordingly, the prior approval of the CBN should be obtained by a (prospective) shareholder prior to the (prospective) shareholder's shareholding in a bank exceeding a 5 percent shareholding in the bank. The CBN should base its assessment of the application on whether the prospective significant shareholder is fit and proper and would be in a position to support the bank in time of stress and need. In the event of a transaction in violation of this provision, the CBN should be empowered to suspend such (beneficial) shareholder's voting rights and dividend rights on all his shares in the bank, until the situation is regularized. Should a significant shareholder in future fail the fit and proper test, the significant shareholder would be required immediately to dispose of his shareholding above 5 percent in the bank. A significant shareholder is required, on an annual basis, to complete and submit to the BSD a form containing his identity, contact details and details of his significant shareholding in a bank. • Prescribe that no person, whether natural or legal may obtain control over a bank without the prior written consent of the CBN. Furthermore, prescribe that where a transaction is concluded which results in breach of (the amended) Section 7(1), the (beneficial) shareholders' voting rights and dividend rights in respect of all such (beneficial) shareholder's shareholding in the bank, at the instance of the CBN, could be suspended until such time as the CBN is satisfied as to the fitness and propriety of the new shareholder and has given its consent to such a transaction. • Consider, in the light of the current approach to fit and proper requirements relating to shareholders, whether Circular BSD/DO/CR/2/2000, dated March 23, 2000, is still relevant and, if not, withdraw it. • Define the concept of a beneficial shareholder (in contradistinction with a nominee shareholder). In addition, wherever the submission of shareholder information is dealt with in the legal and regulatory framework, it should be made clear that it means the submission of information on the beneficial shareholder. (Accordingly, it should be incumbent upon the supervisor to ensure that beneficial shareholders are 	<p>M</p> <p>M</p> <p>M</p> <p>L</p> <p>M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
	<p>and remain fit and proper and in compliance with the legal and regulatory framework.)</p> <ul style="list-style-type: none"> • Require a bank to notify the supervisor as soon as it becomes aware of any material information which may negatively affect the suitability of a significant shareholder. • Review the legal and regulatory framework from time to time and update fines to ensure that they are in line with the gravity of the offence and to constitute a sufficient deterrent. • Consolidate, rationalize, logically organize and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP4. 	<p>M</p> <p>L</p> <p>L</p>
5. Major acquisitions	<ul style="list-style-type: none"> • The legal and/or regulatory framework should prescribe sufficiently comprehensively and clearly how a bank, when considering a (proposed) acquisition or investment, is required to distinguish between cases which are required to be dealt with by way of, respectively, an ex ante application, an ex post application, an ex ante notification and an ex post notification, and other cases. • Consideration should be given to scrapping the provisions which permit a bank to hold shares in agricultural, industrial and venture capital companies. • Consolidate, rationalize, logically order and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP5. 	<p>L</p> <p>M</p> <p>L</p>
6. Capital adequacy	<ul style="list-style-type: none"> • Ensure that the regulatory capital adequacy requirements, at a minimum, are strictly in line with the Basel I, also in relation to Tier 1 and Tier 2 regulatory eligible capital components. • Require a bank, in relation to a capital instrument of the bank or of another bank, to impair its regulatory eligible capital in an amount equal to: <ul style="list-style-type: none"> - its investment therein (whether directly or indirectly, e.g., via a subsidiary); - its financing the purchase thereof (whether directly or indirectly, e.g., via a subsidiary, - its provision of financing facilities for the purchase there for (whether directly or indirectly, e.g., via a subsidiary); - its provision of financing (whether directly or indirectly, e.g., via a subsidiary) against collateral in the form thereof; and - its provision of financing facilities (whether directly or indirectly, e.g., via a subsidiary) against collateral thereof. • Develop and maintain updated comprehensive and detailed principles, standards, guidance, prescriptions, statutory returns and supervisory work programs, inter alia based on and aligned with relevant pronouncements of the BCBS, for all key areas, including corporate governance, capital and capital management, significant existing and emerging risks, which would enhance effectiveness, efficiency, consistency, quality control and transparency of supervision, thus enabling more effective challenging of banks by the supervisor. • Require banks to hold adequate regulatory eligible capital also against significant risk exposures: <ul style="list-style-type: none"> - other than credit risk; and - credit risk exposures not prudently captured by Basel I. 	<p>M</p> <p>H</p> <p>M</p> <p>M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> • Prescribe that the shortfall in regulatory provisions, constituted by the difference when a bank's regulatory required provisions exceed its IFRS credit impairments, does not constitute or qualify as Tier 1 core capital. • Perform, and require banks to perform, overall micro/bottom up and macro/top down stress testing, scenario analyses and simulation exercises in relation to all key areas, including risk areas, as a tool to provide forward-looking assessments of a bank's capacity (as constituted by its capital, liquidity and earnings) to withstand extreme but plausible macro-financial shocks. The results should be taken into account when establishing and reviewing (a bank's) policies, processes, limits, thresholds and benchmarks. • Consolidate, rationalize, logically order and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP6. 	<p>H</p> <p>H</p> <p>L</p>
7. Risk management process	<ul style="list-style-type: none"> • Prescribe that the approval level of risk exposures be commensurate with the size and risk of the resulting risk exposure, and significant risk exposures (say, exceeding a prescribed percentage of a bank's capital) should be decided by the bank's senior management or even a higher level body (such as the board risk committee, or even the board itself.) • Consider the selective implementation, in the interim, of Basel II principles to ensure that the relevant elements of risk and risk management are embedded in banks' capital management. • Develop and issue specific guidance to govern the application of internal risk management models, to ensure that sound principles, practices and controls are applied, and that the measurement and assessment of significant existing and emerging risks yield reasonably prudent outcomes. • Reconsider the quality and quantity of supervisory resources required to enable the regulatory and supervisory authorities to discharge their responsibilities effectively, given also the regulatory reform agenda, including the implementation of IFRS, Basel II and Basel III. • In line with the HRD plan for specialist career streams, engage specialists to support the regulatory and supervisory functions in addressing specialist and complex issues in the areas of capital and capital management, corporate governance, credit risk and credit risk management, country and transfer risk and country and transfer risk management, market risk and market risk management, liquidity risk and liquidity risk management, operational risk and operational risk management, accounting and auditing, information technology and project management, thus enabling the supervisory authority to effectively challenge banks and all related stakeholders, including (boards of) directors, executive management (including the CEO, COO, CFO, CRO, CIA, CIO, CCO, etc) and external auditors. • Consolidate, rationalize, logically arrange and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP7. 	<p>M</p> <p>L</p> <p>L</p> <p>H</p> <p>H</p> <p>L</p>
8. Credit risk	<ul style="list-style-type: none"> • Where relevant, also apply, mutatis mutandis, BCP7's recommendations. • Require that a bank's board regularly reviews the CRM strategy, significant policies and processes, while ensuring that these are consistent with the risk appetite. • Prescribe that the approval level for credit exposures should be commensurate with the size and risk of the resulting credit exposure. 	<p>M</p> <p>M</p> <p>M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
11. Exposure to related parties	<ul style="list-style-type: none"> • Standardize, inter alia through definition, terminology relating to related parties and insiders. • Expand the definition of related party and insiders to include <ul style="list-style-type: none"> - subsidiaries and affiliates of a bank; - parties that are controlled by or have significant influence over related parties of a bank; - parties to whom the related parties of a bank are exposed in terms of transactions which were not arm's length transactions; and - the notion of economic dependency. • Strengthen the definition of related parties by designating, inter alia, also external auditors as related parties. • Prescribe that all matters involving related party exposures should be decided by the bank's board of directors. • Empower CBN to exercise its discretion, where relevant and on a case by case basis, to deem the existence of related party relationships, for purposes of determining the total amount of a bank's exposure to a particular related party or group of connected related parties, in addition to those related party relationships defined in the law. • Prohibit the granting of advances to related parties on more favorable terms than corresponding exposures to non-related counterparties and/or to ensure that such transactions are concluded on an arm's length basis. • Prohibit related parties from being involved in the decision-making process in relation to a related credit or credit facility. • Require that the monitoring and reporting of related party transactions be discharged by way of an independent credit review process. • Adjust substantially downwards the current 60 percent aggregate related party limit. • Amend the legal and regulatory framework to impose a 10 percent single related party limit and an aggregate related parties limit, which limits may not be exceeded and in relation to which the CBN should be prohibited from granting any exception or condonation. • Constitute the total amount of an exposure to a related party as an impairment of capital, which means that such an exposure should be deducted for purposes of determining a bank's regulatory eligible capital. 	<p>M</p> <p>H</p> <p>M</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p> <p>H</p>
12. Country and transfer risk	<ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendation/s. • Manage country and transfer risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, which constitute it as an emerging and, perhaps, even a significant risk exposure in the case of certain banks. • Require a bank to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant country and transfer risk exposure. 	<p>M</p> <p>M</p> <p>M</p>
13. Market risks	<ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendation/s. • Adopt the 1996 Market Risk Amendment. • Manage market risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, which constitute it as an emerging and, perhaps, even a significant risk exposure, in the case of certain banks. Pay particular attention to a bank's treasury and ALCO. 	<p>H</p> <p>H</p> <p>M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> • Require a bank to hold an appropriate (in other words, in relation the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant market risk exposure. • Improve the competencies of supervisory staff in relation to market risk and market risk management. 	<p style="text-align: center;">H</p> <p style="text-align: center;">M</p>
14. Liquidity risk	<ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Update the Guidelines for the Development of Liquidity Management Policies, 2003, in the light of important subsequent reforms relating to liquidity risk management, including the BCBS's Principles for Sound Liquidity Risk Management and Supervision, 2008. For example, the guidelines should be enhanced by considering the following issues: <ul style="list-style-type: none"> - Provide a clear expectation on the roles and functions of the management vis-à-vis Asset-Liability Committee (ALCO). - Require that net funding requirements need to be assessed in the context of a broader review of how other risks could impact the need for funding. - Set limits or ratios to prevent concentration of funding from top depositors, by maturity, and from volatile sources. - Require banks to have separate CFPs for overseas branches or subsidiaries. - Require clear escalation procedures detailing when and how each of the CFP plans can and should be activated, and determine the expected lead time needed to tap additional funds from each of the contingency sources under a stress scenario. - Require the establishment of internal limits or ratios to address diversification and concentration, and identify the party responsible for monitoring and reviewing such limits and ratios. - Require that banks establish internal policies to govern the classification of liquid assets to ensure no over-reliance on illiquid assets. - Incorporate in the liquidity ratio requirement also the potential impact of crystallization of OBS obligations. • Require a bank with significant multiple currency exposures to have proportionate risk management strategies, policies and processes governing its foreign currency operations. Consideration should also be given to imposing separate liquidity ratio requirements in relation to each currency. • Conclude on and respond to the quantitative impact assessment of the liquidity prescriptions (Liquidity Coverage Ratio and Net Stable Funding Ratio) contained in Basel III. 	<p style="text-align: center;">M</p> <p style="text-align: center;">M</p> <p style="text-align: center;">M</p> <p style="text-align: center;">L</p>
15. Operational risk	<ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Manage operational risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, which constitute it as a significant risk exposure. • Require banks to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant operational risk exposure. • Improve the competencies of supervisors in relation to operational risk and operational risk management. • Develop guidance in relation to banks' outsourcing activities. 	<p style="text-align: center;">M</p> <p style="text-align: center;">M</p> <p style="text-align: center;">H</p> <p style="text-align: center;">M</p> <p style="text-align: center;">M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
16. Interest rate risk in the banking book	<ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Manage IRRBB as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, which constitute it as a significant risk exposure. • Require banks to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant IRRBB risk exposure. • Improve the competencies of supervisors in relation to IRRBB and IRRBB management. • FRPD's top-down stress test exercises (including shocks on IRRBB) results should be shared adequately with BSD. 	<p>M</p> <p>M</p> <p>H</p> <p>M</p> <p>M</p>
17. Internal control and audit	<ul style="list-style-type: none"> • Training (in all aspects of banking, including, especially, corporate governance (including the roles and responsibilities of the various stakeholders, such as directors, senior management, CEO, COO, CFO, CRO, CIA, CCO, external auditors and supervisors), capital management, risk management (including key risks such as credit risk, market risk, operational risk, IRRBB, country and transfer risk, and issues such as concentration and large exposures, and related parties) and internal controls) of all stakeholders (including boards of directors, executive management, bank personnel, external auditors and supervisors, including the consequences of breaches and failures of such duties and responsibilities, should be undertaken on an ongoing basis. 	<p>H</p>
18. Abuse of financial services	<ul style="list-style-type: none"> • Amend the relevant laws and regulations to bring them in compliance with international standards. • Require that the AML/CFT statutory returns, to be completed by a bank, are in electronic format, to facilitate effectiveness and efficiency and to minimize human manual intervention. Also, the returns should be signed off by senior personnel who should be held responsible and accountable for the quality of the information submitted. Sound validation, inter alia, by way of on-site verification, and editing controls, should be in place to ensure optimal quality information is uploaded to the relevant database/s. • Launch initiatives to improve the effectiveness of AML/CFT in Nigerian banks, including focused thematic examinations of various aspects of a bank's AML/CFT functions, and perform quality control checks to control and monitor such effectiveness. • Maintain a no-tolerance policy in respect of criminality and corporate governance abuses and breakdowns, react promptly, firmly and forcefully, and impose strong and effective sanctions. 	<p>H</p> <p>M</p> <p>M</p> <p>H</p>
19. Supervisory approach	<ul style="list-style-type: none"> • Include peer comparison among banks with similar risk profiles, to enrich the RBS information and improve the assessment. • Develop specific and granular criteria for assessment of the risk direction. Among others, the CBN may consider the utilization of scenario-based stress testing whereby the CBN supervisors can leverage off the proposed top-down stress test exercises conducted by Financial Regulation & Policy Department. 	<p>M</p> <p>L</p>
20. Supervisory techniques	<ul style="list-style-type: none"> • Develop an independent formal governance process for quality assurance of overall supervisory ratings determined for banks and supervision in general, which may include the involvement of the CBN's risk management and internal audit functions. 	<p>M</p>

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> Ensure regular and timely communication of any supervisory issues with members of a bank's board, even outside the onsite examination process. 	L
21. Supervisory reporting	<ul style="list-style-type: none"> Give consideration to incorporating into the e-FASS system a workflow module (for handling also correspondence and other routine supervisory tasks) and an on-site supervision module (including work programs and work papers), to leverage e-FASS and optimize the efficiency of supervision. Require a bank to notify the CBN of all material information regarding the bank's activities, structure or overall condition, or material adverse developments, as soon as possible. 	L M
22. Accounting and disclosure	<ul style="list-style-type: none"> Reconsider the wisdom of prior approval by the CBN of a bank's draft annual audited financial statements, as provided for by Section 27 of the BOFI Act, as it holds the potential for the CBN to be held (co-) responsible (whether explicitly or implicitly) for the content of the annual audited financial statements upon publication thereof. Establish and maintain a specialist function within the CBN/BSDF/FRPD on bank accounting, bank auditing, bank disclosure and the corporate governance roles of bank internal and bank external auditors. Task this specialist function with ensuring that the legal and regulatory and supervisory framework and the supervisory approach and practices are in line with sound internationally generally accepted standards and practices. The (senior) specialist should be responsible for driving the agenda relating to accounting, auditing, disclosure and corporate governance issues relating to bank internal audit/auditors and bank external audit/auditors, both internal (within the CBN) and externally, in relation, firstly to banks, but, also, in relation to other stakeholders, such as the accounting and auditing profession's representative bodies, the individual accounting and auditing firms and the FRCoN. So, for example, the periodic meetings between bank supervisors and FRCoN to discuss issues of common interest relating to bank audits and bank accounting should be reinstated and the agenda driven by the (senior) specialist. The specialist function should develop a reporting template for, and indicate the frequency of reporting on, the reports to be rendered to the CBN by external auditors of banks on a bank's risk management practices, internal controls and level of compliance, to give effect to the provisions of Section 7.1.4 of the Bank Corporate Governance Code. Require a bank to develop and implement formal policies in relation to internal audit, external audit and disclosure. Amend the legal and/or regulatory framework to require that the CBN may obtain access to an external auditor's external audit working papers in respect of a bank, when a bank becomes a problem bank. Prescribe by way of the BOFI Act that an external auditor who, in good faith, furnishes a report, as provided in Section 29 (7) of the BOFI Act, to the CBN, is protected against claims of having breached any confidentiality. Amend the BOFI Act so that it specifically and explicitly empowers the CBN to remove a bank's auditor who does not discharge his responsibilities satisfactorily. 	L H M M L M
23. Corrective and remedial powers of supervisor	<ul style="list-style-type: none"> Ensure Part 4, titled Supervisory Actions in the Event of a Systemic Banking Distress, of the document titled Supervisory Intervention Framework, is not in the public domain, for avoidance of moral hazard. 	L

Reference Principle	Recommended Action	Priority (H/M/L)
	<ul style="list-style-type: none"> • Review and, if necessary, effect the necessary amendments to ensure that the Supervisory Intervention Framework is fully aligned with and grounded in the provisions of the BOFI Act, and is not open to the charge that it or some of its provisions are ultra vires. • Apply zero tolerance, inter alia in relation to actions or inactions which put financial sector stability or the safety and soundness of a bank at risk, such as corporate governance transgressions and non-compliance with statutory prescriptions. • Supervisors should act promptly, resolutely and forcefully in applying corrective, enforcement and sanctioning actions, and in resolving problem banks, especially in instances which hold the potential to imperil financial stability. 	<p style="text-align: center;">M</p> <p style="text-align: center;">H</p> <p style="text-align: center;">H</p>
24. Consolidated supervision	<ul style="list-style-type: none"> • Ensure the comprehensive incorporation into the BOFI Act of necessary enabling provisions to facilitate the implementation and performance of consolidated supervision. • Expedite the finalization of the draft framework for consolidated supervision and implement it post haste. • Enhance the supervisory capacity and capabilities in relation to consolidated supervision. • Amend the BOFI Act to specifically and clearly empower the CBN to require a bank to close a foreign office or impose limitations on their activities under specified circumstances, namely should the CBN determine that the oversight by the bank and/or supervision by the host supervisor is not adequate relative to the risks the office presents and/or it cannot gain access to the information required for the exercise of supervision on a continuous basis. 	<p style="text-align: center;">H</p> <p style="text-align: center;">H</p> <p style="text-align: center;">H</p> <p style="text-align: center;">M</p>
25. Home-host relationships	<ul style="list-style-type: none"> • Empower the CBN to share information with other supervisory authorities. • Carry-out a one-off review exercise of, and thereafter at regular intervals, review all the host supervisory authorities to assess the nature and quality of the regulatory and supervisory frameworks, supervisory approaches and quality of supervision, including enforcement and resolution. 	<p style="text-align: center;">L</p> <p style="text-align: center;">M</p>

F. Authorities' Response to Assessment

62. The supervisory authorities (Central Bank of Nigeria and the Nigeria Deposit Insurance Corporation) express their appreciation for the comprehensive review of the regulatory and supervisory framework for the Nigerian banking system, carried out by the IMF/World Bank assessment team. The assessment has largely achieved its objective of benchmarking Nigeria's supervisory system against the Basel Core Principles and has also helped in focusing attention on areas where there are gaps and weaknesses that would require more work to further strengthen banking supervision and the overall stability of the Nigerian banking system.

63. Coming at the time it did, it is not unexpected that the outcome of the assessment exercise would be influenced largely by (the run-up to) the banking crisis and the experiences in 2008–2009. The crisis severely tested the resilience of the Nigerian banking system and the capabilities of the supervisors—in response to the crisis, the authorities took unprecedented and extraordinary measures to ameliorate the impact, and also launched reforms which entailed the overhaul of regulations as well as practices underlying supervision. While certain aspects of the reforms had been concluded prior to the commencement of the assessment exercise, other key aspects were either being concluded or were ongoing at the time of the assessment, e.g., Basel II/III and IFRS. The final assessments were not fully reflective of this aspect of the reforms. The continuing and effective implementation of the reforms should result in significant improvement in the level of compliance in the short to medium term. The authorities will not relent on their resolve to ensure that the regulations keep pace with developments in the banking system.

64. The authorities appreciate the recommendations arising from the assessment, including the need to adopt the relevant BCBS pronouncements and ensure their full alignment with local regulations; develop and maintain a well-structured compendium of supervisory regulations; enhance supervisory capacity and capabilities in relation to consolidated supervision; and have in place a more responsive legislative review process, among others. The prospect of significant consequential improvements to the legal, regulatory and supervisory frameworks and processes stiffen the authorities' resolve at ensuring full and effective implementation of the recommendations. Some of the recommendations, especially those that relate to improvement to the legal framework, will require the involvement and cooperation of stakeholders other than the supervisory authorities.

65. Finally, the authorities commend the efforts of the IMF and World Bank in promoting stability and effective supervision of the global financial system and look forward to continued dialogue with the IMF and World Bank, beyond the FSAP exercise.

Table 3. Nigeria: Detailed Self-Assessment of Compliance with the Basel Core Principles

Principle 1	Objectives, autonomy, powers, and resources. An effective system of banking supervision will have clear responsibilities and objectives for each authority involved in the supervision of banks. Each such authority should possess operational independence, transparent processes, sound governance and adequate resources, and be accountable for the discharge of its duties. A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision; powers to address compliance with laws as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Assessment	
Principle 1(1)	Responsibilities and objectives. An effective system of banking supervision will have clear responsibilities and objectives for each authority involved in the supervision of banks.
Essential criteria	
EC1	Laws are in place for banking, and for the authority (each of the authorities) involved in banking supervision. The responsibilities and objectives of each of the authorities are clearly defined and publicly disclosed.
Description and findings re EC1	<p>One of the principal objectives of the CBN is to promote a sound financial system. (CBN Act – Section 2(d))</p> <p>The Banks and Other Financial Institutions Act (1991 No.25) (BOFI Act) regulates banking, banks and other financial institutions and matters connected therewith.</p> <p>The CBN is empowered to issue a bank license, either without conditions or subject to conditions. The CBN is empowered to vary or revoke any condition or impose new conditions. A foreign bank shall not operate a branch or representative office without the prior approval of the CBN. (BOFI Act – Sections 3, 5, and 8)</p> <p>The CBN is required to appoint a Director of Banking Supervision who is empowered to carry out supervisory duties in respect of banks, other financial institutions and specialized banks. (BOFI Act – Section 31)</p> <p>In terms of the BOFI Act, the CBN is empowered to supervise and regulate the activities of other financial institutions and specialized banks. (BOFI Act, Section 61(1)(a))</p> <p>The CBN is a body corporate with perpetual succession and may sue and be sued in its corporate name. The federal government holds a 100 percent ownership interest in the CBN. The CBN's mandate is to promote stability and continuity in economic management. The principal objectives of the CBN include to ensure monetary and price stability and to promote a sound financial system. In order to facilitate the achievement of its mandate, the CBN is required to be an independent body in the discharge of its functions. The principal objects of the CBN shall be to ensure monetary and price stability and to promote a sound financial system. The CBN has regulatory powers as the CBN governor is empowered to make rules and regulations for the operation and control of all institutions under the supervision of the CBN. The Board of Directors of the CBN (CBN Board) is its governing body, as it is responsible for the policy and general administration of the affairs and business of the CBN. The CBN is accountable to the National Assembly, which is manifested in a variety of ways, inter alia by way of the governor's attendance and reporting to the National Assembly, on a semi-annual basis, on efforts, activities, objective and plans of the CBN Board regarding</p>

monetary policy and economic development and prospects for the future. The CBN is also accountable to the president, which is discharged through communications by and from the governor to the president. The CBN is required annually to submit a report and its audited financial statements to the National Assembly and the president. (CBN Act – Sections 1, 2, 4, 6, 8, 33, 49, 50, and 57)

The Nigeria Deposit Insurance Corporation Act (NDIC Act) contains a number of provisions dealing with the regulatory and supervisory duties and responsibilities of the Nigeria Deposit Insurance Corporation (NDIC). The NDIC Act does not contain a mandate and/or objective/s clause, though it does contain a “functions” clause which, however, does not mention the regulation and supervision of banks. “Supervisory authorities” is defined as the NDIC and the CBN. The NDIC is charged with the function of examination of insured institutions. Every insured institution is required to submit to the NDIC such returns and information as may be required from time to time within the stipulated period. The NDIC may require persons having access thereto, at all reasonable times to supply to it information, in such form as the NDIC may from time to time direct, relating to or touching on or concerning matters affecting the interest of depositors of insured institutions. The NDIC is empowered to appoint examiners with powers to examine periodically the books and affairs of every insured institution, be entitled to require and obtain information and explanations from the officers, directors and auditors of an insured institution as they may deem necessary in the performance of their duties, and have access to any accounts, returns and information with respect to any insured institution. (NDIC Act – Sections 7, 27, 28, and 59)

The NDIC is a body corporate with perpetual succession and may sue or be sued in its corporate name. The CBN holds a 60 percent ownership interest and the Ministry of Finance holds a 40 percent ownership interest in the NDIC. The Board of Directors (NDIC Board) of the NDIC is its governing body. The NDIC has regulatory powers as the NDIC Board is empowered to make, alter and revoke rules and regulations for carrying on the business of the NDIC, to appoint officers who are required to carry out the functions of the NDIC, including the examination of insured institutions. The NDIC is required annually to submit a report on its activities to the governor of the CBN, the Auditor-General and the Minister of Finance. (NDIC Act – Sections 1, 7, and 11) Nowhere is it specifically provided for the NDIC to have operational independence.

(PS: Sections 1 (1) and 3 (5) of BOFI Act provided that the CBN exercises (certain) functions, powers and duties subject to the oversight of the Minister of Finance. Reportedly, these provisions had been amended to the effect of removing the oversight role of the Minister of Finance, but the BOFI Act was not correctly updated – apparently, this error occurred as a result of the consolidation of the BOFI Act with all its subsequent amendments. In the process of the preparation of LFN 2004, one of the earlier amendments to the BOFI Act, which had been repealed, was inadvertently considered by the National Assembly. This inadvertence has itself been cured by virtue of the provisions of the Revised Edition (Laws of the Federation of Nigeria) Act 2007 which acknowledged the possibility of errors/omissions in the compilation of LFN 2004 and authorizes the discountenancing of such errors/omissions wherever they occur.)

Efforts are on-going to amend both the CBN and BOFI Acts to strengthen financial stability. The NDIC Act is also under-going review.

The CBN Act established the Financial Services Regulation Coordinating Committee (FSRCC) under the Chairmanship of the governor of the CBN. Members of the Committee are the Managing Director, NDIC, the Director-General, Securities and Exchange Commission, the Commissioner for Insurance, the Registrar-General, Corporate Affairs Commission, and a representative of the Federal Ministry of Finance not below the rank of a Director. (BOFI Act – Section 43)

The CBN/NDIC Executive Committee on Supervision aims at coordination, communication and information sharing between the two authorities, and operates at both executive and technical levels. The Committee handles issues of problem banks resolution, supervisory policy formulation and ongoing supervision.

	<p>The CBN issued guidelines for the development of Risk Management Policies for Banks and Discount Houses, Code of Corporate Governance for Banks in Nigeria and a Supervisory Intervention Framework. An updated draft Framework for Consolidated Supervision of Financial Institutions in Nigeria was developed by the FSRCC in May 2011.</p> <p>Pronouncements of the Basel Committee on Banking Supervision are not always fully and/or appropriately adopted, sometimes resulting in important deviations.</p> <p>The versions of the BOFI Act and the NDIC Act on the websites of the CBN and the NDIC, respectively, are not the latest versions of the relevant legislation.</p>
EC2	<p>The laws and supporting regulations provide a framework of minimum prudential standards that banks must meet.</p>
Description and findings re EC2	<p>The BOFI Act and subsidiary supporting regulations prescribe various prudential requirements which banks are required to comply with, such as capital adequacy requirements, liquid asset requirements, reserve fund requirements, large exposure limits and related party limits. (BOFI Act – Section 13, 15, and 16) (Prudential Guidelines for Money Deposit Banks – Section 3)</p> <p>The CBN governor is empowered to make regulations to give full effect to the objects of the BOFI Act, including for the operation and control of all institutions under the supervision of the CBN. (BOFI Act – Section 57)</p> <p>The CBN confirms that banks comply with the various prudential requirements by way of off-site analysis of returns submitted by the banks and monitoring of such information, and on-site examinations, and addresses non-compliance by way of corrective, enforcement and sanctioning actions. (Assessors validated this assertion by way of scrutiny of reports generated by the e-FASS off-site data base system into which the returns of banks are captured, on-site work programs, examination reports and action plans to address breaches.)</p>
EC3	<p>Banking laws and regulations are updated as necessary to ensure that they remain effective and relevant to changing industry and regulatory practices.</p>
Description and findings re EC3	<p>General</p> <p>To date, the policy process has been tortuous, inter alia constrained by capacity and capability limitations, and too ad hoc and event-driven. The legislative process, seemingly, has been functionally impaired, as illustrated by the fact that the last amendment to the BOFI Act is dated 1999, notwithstanding momentous events affecting banking internationally during the intervening period and important consequential changes in the regulatory framework internationally, and numerous attempts to have proposed amending legislation passed. The National Assembly legislative process is not sufficiently responsive to enable a sound, logically structured, modern and up to date legal and regulatory framework in line with internationally generally accepted standards and principles, to ensure that the banking system is duly enabled to facilitate the required economic development and growth while maintaining financial stability.</p> <p>In 2010, the CBN created the Financial Policy and Regulation Department (FRPD), which is responsible for developing financial policy and regulation to ensure that the legal and regulatory framework remains current. To date, the FRPD's agenda has been driven by ad hoc demands which arose mainly from the 2009 banking crisis.</p> <p>Specific</p> <p>The legal framework applicable to the CBN was significantly updated by the enactment of the CBN Act, 2007. Currently, the CBN Act is being reviewed with the aim of further updating thereof.</p> <p>The BOFI Act was originally enacted in 1991, and was (last) subject to amendments during the 1990's. The BOFI Act is dated and no longer able to cope with the demands of the modern era, and needs to be totally reviewed and updated. Despite attempts by the CBN during the intervening period, it has not been possible for the past 13 years to have proposed amendments passed by the National Assembly. Currently, the BOFI Act is being reviewed</p>

	<p>with the aim of comprehensively updating it.</p> <p>Some of the recent flood of amendments to the internationally generally accepted sound framework for bank regulation and supervision has been captured in subsidiary legislation, though, some of these amendments more appropriately should have been captured in the BOFI Act. In some instances, consequently, the subsidiary legislation may be going beyond what the BOFI caters for, posing the danger of ultra vires subsidiary legislation, which undermines legal certainty. An example of the latter may be some of the provisions contained in the Supervisory Intervention Framework.</p> <p>The legal and regulatory framework is not sufficiently logically structured and organized, and the internal hierarchy is not clear. For example, which subsidiary legislation is subsidiary to which other subsidiary legislation? The legal status of some pronouncements of the CBN, such as a circular, code, decree, framework, guideline and prudential guideline is unclear and their position in the hierarchy is not specified. (Authorities' response: All extant regulations, circulars and guidelines are neither hierarchical nor do they conflict with each other. The law gives equal status to circulars, codes, frameworks, guidelines, rules and regulations issued by the supervisory authority. All rules are derived from the primary legislations guiding banking in Nigeria: the CBN Act, BOFI Act, and NDIC Act, etc.)</p> <p>The subsidiary legislation and other pronouncements of the CBN are not properly organized and readily accessible. Furthermore, there is uncertainty as to the comprehensive list of circulars, codes, frameworks, guidelines and prudential guidelines which are current.</p> <p>The NDIC Act was significantly updated by the enactment of the NDIC Act, 2006.</p>
EC4	The supervisor confirms that information on the financial strength and performance of the industry under its jurisdiction is publicly available.
Description and findings re EC4	<p>Banks are required to submit to the CBN, at specified intervals and on specified dates, information on the assets and liabilities of the bank and an analysis of advances and other assets. In addition, a bank is required to submit such other information, documents, statistics or returns as the CBN may deem necessary for the proper understanding of the statements supplied by the bank. The CBN is empowered to carry out supervisory duties in respect of banks and, for that purpose, shall examine periodically the books and affairs of each bank; and have a right of access at all times to the books, accounts and vouchers of banks; and have power to require from directors, managers and officers of banks such information and explanation as he deems necessary for the performance of his duties; and a bank shall produce to the examiner at such times as the examiners may specify, all books, accounts, documents and information which they may require. The CBN is empowered to prepare and publish consolidated statements aggregating the information submitted by the bank (BOFI Act – Section 25, 26, and 31)</p> <p>The CBN is empowered to require persons and institutions having access to information relating to or touching or concerning matters affecting the economy to submit such information as the CBN may direct. (CBN Act – Section 33)</p> <p>The NDIC is empowered to examine the books and affairs of an insured institution; and has right of access at all times to the books, accounts and vouchers of the insured institution, including its management information system; and be entitled to require and obtain information and explanations from the officers, directors and auditors of an insured institution as they may deem necessary in the performance of their duties.; and have access to any accounts, returns, and information with respect to any insured institution which is under the possession of the CBN. (NDIC Act – Section 28)</p> <p>Up until 2008, on an annual basis, the CBN published a bank supervision report.</p> <p>On a semi-annual basis, the CBN's Financial Policy and Regulation Department publishes a Financial Stability Report which contains macroprudential top down information on the</p>

	<p>financial strength and performance of the financial system, with emphasis on the banking sector. To date, three editions have been published.</p> <p>On an annual basis, the College of Supervisors of the West African Monetary Zone (WAMZ), of which the CBN is a member, issues a Financial Stability Report for WAMZ.</p> <p>Banks are required to publish their audited (informally, required to be audited in terms of International Standards of Auditing (ISAs)) financial statements (compiled in terms of International Financial Reporting Standards (IFRS)) within four months of the common bank financial year end of December 31 each year (BOFI Act – Section 27.) The CBN issued <i>Guidelines on Additional Disclosure Requirements in Banks' Financial Statements in Preparation for Full-Scale Adoption of IFRS</i></p> <p>Prior to publication of a bank's audited financial statements, the bank is required to furnish the CBN with a draft copy thereof, which the CBN thereupon scrutinizes—inter alia, the CBN compares the IFRS credit impairments to the on-site examination report's conclusion on the appropriate level of regulatory required credit provisions; the CBN determines whether or not a dividend was being proposed when the bank has made a loss; also, the CBN confirms whether all the contraventions committed by the bank have been disclosed. Upon the CBN being satisfied with the information contained in the draft copy, it issues a "no objection" to the publication thereof. (BOFI Act – Section 27)</p> <p>The question arises whether or not the CBN is incurring liability towards third parties, such as investors and depositors, by its "prior approval" of a bank's annual audited financial statements.</p> <p>The above requirements foster and promote market discipline through the disclosure of relevant, reliable and timely information.</p>
Additional criteria	
AC1	In determining supervisory programs and allocating resources, supervisors take into account the risks posed by individual banks and banking groups and the different approaches available to mitigate those risks.
Description and findings re AC1	The CBN's supervisory approach is a risk-based approach. The supervisory program and allocation of resources is driven by an assessment of the risks to which a bank is exposed. A preliminary risk assessment is performed at the start of the supervisory cycle, which constitutes input to the determination of the annual supervisory program and the allocation of resources. Thereafter, based on the findings of the on-site examination, the risk assessment is updated and finalized. This finalized risk assessment constitutes the starting point for the compilation of the preliminary risk assessment for the next supervisory cycle. (Assessors validated the above assertions by scrutinizing the most recent preliminary risk assessment in respect of a particular bank, the 2012 supervisory program, and the most recent finalized risk assessment for the particular bank.)
Assessment of Principle 1(1)	Largely compliant
Comments	A principal objective of the CBN is to promote financial stability. The CBN is charged with primary responsibility of bank supervision and has clear related objectives. The NDIC cooperates with the CBN in discharging the bank supervision responsibility, though it is not explicitly stated as an NDIC objective. Though bank supervision is not explicitly clearly stated as an objective of the NDIC, it is implicit. An effective and efficient legislative process through the National Assembly is a necessary precondition to enable congruence and to keep pace with the internationally generally accepted legal framework for banking, which is not being achieved currently. It is important to maintain the currency of the legal and regulatory framework, by way of prompt responses (to international policy developments and local needs), through sound policy development and a responsible legislative and regulatory

	<p>process.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Maintain currency of the legal and regulatory framework by way of prompt responses (to international policy developments and local needs), sound policy development, and a responsive legislative process. • Perform a BCP self-assessment against the 2012 version of the Basel Core Principles and align the updating of the legal, regulatory and supervisory frameworks and supervisory approach with the 2012 version of the Basel Core principles. • Determine the objective/s of the NDIC and incorporate within the NDIC Act. • Review thoroughly and comprehensively update the BOFI Act. • Make current consolidated (updated) version of legislation and regulations readily available in logical format in the public domain at all times. • Review thoroughly the subsidiary legislation (subsidiary to the BOFI Act) (which, seemingly, consisting of circulars, codes, decrees, frameworks, guidelines, prudential guidelines, regulations and rules), inter alia also to remove ultra vires provisions (and, if necessary, move relevant provisions to the BOFI Act itself), if any, and thereupon to comprehensively update, rationalize, logically structure in an appropriate hierarchy, logically reference, and then to compile a compendium of such subsidiary legislation, which should be maintained updated. • Specify in legislation the legal status and hierarchy of all types of subsidiary legislation (such as a circular, code, decree, framework, guideline and prudential guideline and regulation and rule.) • Withdraw annually, with effect from the end of a year, all circulars issued during that, and, where necessary and appropriate, in relation to issues and prescriptions which remain relevant and continue needing to be dealt with by way of circular, issue duly updated and amended versions of such circulars with effect from the beginning of the next year. • Adopt fully (without cherry picking) and appropriately all relevant pronouncements of the BCBS, to avoid important deviations which undermine certainty and consistency and can result in unintended consequences. • Require banks to be audited by means of and in line with International Standards of Auditing (ISAs), and that a formal plan be developed and implemented to ensure a high quality application of ISAs. • The CBN to consider how best to be involved, without incurring liability (whether explicitly or implicitly) in the process of finalization of the audited annual financial statements prior to the publication thereof, while simultaneously ensuring that adequate controls are in place to avoid insider abuses. • Ensure that the information disclosed on the websites of the CBN and the NDIC is current, up to date and accurate. • Ensure (in the absence of separate and distinct publications, respectively, covering the macroprudential top down dimension of financial stability, on the one hand, and, on the other hand, covering the microprudential bottom up dimension) that the Financial Stability Report addresses both these dimensions.
Principle 1(2)	Independence, accountability and transparency. Each such authority should possess operational independence, transparent processes, sound governance and adequate resources, and be accountable for the discharge of its duties.
Essential criteria	
EC1	The operational independence, accountability and governance structures of each supervisory authority are prescribed by law and publicly disclosed. There is, in practice, no evidence of government or industry interference which compromises the operational independence of each authority, or in each authority's ability to obtain and deploy the resources needed to carry out its mandate. The head(s) of the supervisory authority can be removed from office during his (their) term only for reasons specified in law. The reason(s) for removal should be publicly disclosed.

Description and findings re EC1	<p>See BCP1 (1) EC1, above.</p> <p>The NDIC Act does not contain a mandate and/or objective/s clause, though it does contain a “functions” clause which, however, does not mention the regulation and supervision of banks. The NDIC Act does not specify to whom the NDIC is ultimately accountable, nor does it mention whether the NDIC is an operationally independent body in the discharge of its functions. The NDIC Act does not spell out the (nature and extent) of rights and powers, one the one hand, and, on the other hand, the duties and responsibilities, of the CBN and the Ministry of Finance, arising from their ownership interest in the NDIC.</p> <p>The appointment of the CBN governor is for a term of five years. The conditions for the removal of the CBN governor include a requirement that the removal must be supported by two-thirds majority of the Senate. (CBN Act – Section 8 and 11)</p> <p>The appointment of the Managing Director of NDIC is for a term of five years. (NDIC Act – Section 8.)</p> <p>(The assessors did not come across evidence suggesting that the CBN's operational independence is limited or tainted by outside interference. Recently, there was an attempt, by way of proposed amendments to the CBN Act, to subjugate the CBN to the ministry of finance. However, this initiative came to naught.)</p>
EC2	The supervisor publishes objectives and is accountable through a transparent framework for the discharge of its duties in relation to those objectives.
Description and findings re EC2	<p>See BCP1 (1) EC1 and EC4.</p> <p>The CBN regularly issues circulars, codes, frameworks, guidelines, prudential guidelines and regulations to the banking industry. Usually, the CBN launches a consultation process prior to finalizing and releasing such documents.</p>
EC3	The supervisory authority and its staff have credibility based on their professionalism and integrity.
Description and findings re EC3	<p>The CBN and the NDIC have human resource policies aimed at ensuring that they are in a position to discharge their mandates effectively, efficiently, credibly, professionally and with integrity. To this end, their respective recruitment processes seeks to employ and retain quality staff. Professional staff is required to be graduates in areas such a general business, economics, law, accounting, risk management, mathematics and statistics. Upon employment, supervisors are required to sign up to a code of business ethics, and conduct and exhibit integrity and professionalism in the discharge of their duties. Staff is encouraged to continue with their studies and to maintain their membership of professional associations in good standing and remain abreast of new developments in their various fields. In addition, the authorities provide opportunities for training, both off-site and on the job, both locally and internationally. Currently, the authorities emphasize training on risk-based supervision. Staff is subject to regular performance measurement and review, and progress in education and training constitutes elements assessed, in addition to quality of work, professionalism and compliance with the code of business conduct and ethics. Staff who attend outside training are required to make the training materials available to the BSD and to schedule a training event where feedback is given on the training undergone. The process of building a central repository of relevant reference and training materials, and to ensure that the authority as a whole benefits from the exposure which staff get to external training opportunities is not satisfactory.</p> <p>The staff of the bank supervisory authorities is not specifically prohibited from holding or trading in shares in banks. The bank supervisory staff interpret this state of affairs as implying that they are permitted to hold and trade in the shares of banks, notwithstanding the contents of the code of conduct to which they all are committed. The bank supervision staff have access to information which is market-sensitive.</p>

EC4	<p>The supervisor is financed in a manner that does not undermine its autonomy or independence and permits it to conduct effective supervision and oversight. This includes:</p> <ul style="list-style-type: none"> • A budget that provides for staff in sufficient numbers and with skills commensurate with the size and complexity of the institutions supervised. • Salary scales that allow it to attract and retain qualified staff • The ability to commission outside experts with the necessary professional skills and independence and subject to necessary confidentiality restrictions to conduct supervisory tasks • A training budget and program that provides regular training opportunities for staff • A budget for computers and other equipment sufficient to equip its staff with the tools needed to review the banking industry and assess individual banks and banking groups; and • A travel budget that allows appropriate on-site work.
Description and findings re EC4	<p>The CBN Board is empowered to consider and approve the annual budget of the CBN and determine its operating surplus after all expenditures have been met. (CBN Act – Section 6)</p> <p>See also BCP1 (2) EC3.</p> <p>The regulators have a travel budget that allows appropriate on-site work. Salaries and allowances approved by the Board are adequate to attract and retain qualified staff. In addition, resources have been devoted to the updating of e-FASS to address shortcomings in information technology and challenges to the rendition of timely and accurate data. Staff has access to adequate information technology. From time to time, the authorities make use of technical assistance rendered by independent consultants.</p> <p>Similar circumstances and conditions, as above, apply in the case of the NDIC.</p>
Additional criteria	
AC1	The head(s) of the supervisory authority is (are) appointed for a minimum term.
Description and findings re AC1	<p>The appointment of the CBN governor is for an initial term of five years and s/he is eligible for a reappointment for another term not exceeding five years—accordingly, a full term limit of 10 years applies. The CBN governor becomes disqualified or his appointment comes to an end under certain specified objectively verifiable circumstances. The president may remove the CBN governor should two thirds of the Senate so vote. (BOFI Act – Section 9 and 11)</p> <p>The appointment of the Managing Director of NDIC is for an initial term of five years and s/he is eligible for a reappointment for another term not exceeding five years—accordingly, a full term limit of 10 years applies. (NDIC Act – Section 8)</p>
Assessment of Principle 1(2)	Largely compliant
Comments	<p>The CBN possess operational independence, transparent processes, sound governance and adequate resources, and are held accountable for the discharge of its duties. The position of the NDIC is somewhat less clear as regards its independence and to whom it is accountable.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Update the NDIC Act, to make provision for a mandate and/or objective/s clause, and spell out clearly and unequivocally to whom or which body the NDIC is accountable. Also, prescribe that the NDIC should have operational independence. • Prohibit all staff of bank supervisory authorities from holding or trading in shares of banks, given their access to price sensitive inside information.
Principle 1(3)	Legal framework. A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision.

Essential criteria	
EC1	The law identifies the authority (or authorities) responsible for granting and withdrawing banking licenses.
Description and findings re EC1	<p>A bank is defined as a bank licensed under the BOFI Act. (CBN Act – Section 60)</p> <p>A banking license is a prerequisite to conducting banking business. The CBN is the sole licensing authority for banks. A person wishing to undertake banking business is required to apply to the CBN for a banking license and comply with all the prescribed requirements. A license may only be issued with the prior approval of the Minister of Finance. A license may be issued subject to conditions and fresh or additional conditions may be imposed. The CBN is empowered to vary or add new conditions and to withdraw a license issued under specified circumstances. A person who fails to comply with and of the conditions of a license is guilty of an offence and liable, on conviction, to a fine. The CBN governor may suspend any license issued or given to any bank which fails to comply with a rule, regulation, guideline, or administrative directives made, given or issued. (BOFI Act – Section 2, 3, 9, 12, 14, 39, 40, 61, and 64)</p> <p>(PS: Sections 1 (1) and 3 (5) of BOFI Act, seemingly erroneously subject the exercise of the functions, powers and duties of CBN to the supervision of the minister of finance. This error has occurred as a result of the consolidation of the BOFI Act with all its subsequent amendments. In the process of the preparation of LFN 2004, one of the earlier amendments to the BOFI Act, which had been repealed, was inadvertently considered by the National Assembly. This inadvertence has itself been cured by virtue of the provisions of the Revised Edition (Laws of the Federation of Nigeria) Act 2007 which acknowledged the possibility of errors/omissions in the compilation of LFN 2004 and authorizes the discountenancing of such errors/omissions wherever they occur.)</p>
EC2	The law empowers the supervisor to set prudential rules (without changing laws). The supervisor consults publicly and in a timely way on proposed changes, as appropriate.
Description and findings re EC2	<p>The CBN is empowered to issue guidelines to any person and any institutions under its supervision. The CBN is empowered by directives by circular to prescribe matters relating to reserve requirements. The CBN is empowered to prescribe rules and regulations for the efficient operation of all clearing and settlement systems. The CBN Board is empowered to make and alter rules and regulations for the good order and management of the CBN. (CBN Act – Section 33, 45, 47, and 51)</p> <p>The CBN is empowered to make rules and regulations for the operation and control of all institutions under its supervision. (BOFI Act – Section 57)</p> <p>See also BCP1 (1) EC2.</p> <p>The CBN had issued numerous circulars and guidelines to banks in view of the changing market conditions in the industry, including Prudential Guidelines, Code of Corporate Governance for Banks in Nigeria, Guidelines for the Development of Risk Management Framework for Individual Risk Elements in Nigerian Banks, an updated draft Framework for Consolidated Supervision of Banks in Nigeria.</p> <p>Important pieces of the legal and regulatory framework has been drafted but not yet finalized and implemented, including:</p> <ul style="list-style-type: none"> • Draft updated Code of Corporate Governance Code. • Draft Bank Holding Company Framework.
EC3	The law or regulations empower the supervisor to obtain information from the banks and banking groups in the form and frequency it deems necessary.
Description and findings re EC3	See BCP1 (1) EC4.

Assessment of Principle 1(3)	Largely compliant
Comments	<p>In general, a suitable legal framework for banking supervision, including provisions relating to authorization of banking establishments and their ongoing supervision, is in place. Both the legal and regulatory framework requires a thorough review and comprehensive updating.</p> <p>The following recommendations are proposed: Finalize promptly and implement the following important pieces of the legal and regulatory framework:</p> <ul style="list-style-type: none"> • Draft updated Code of Corporate Governance Code. • Draft Bank Holding Company Framework.
Principle 1(4)	Legal powers. A suitable legal framework for banking supervision is also necessary, including powers to address compliance with laws as well as safety and soundness concerns.
Essential criteria	
EC1	The law and regulations enable the supervisor to address compliance with laws and the safety and soundness of the banks under its supervision. The law and regulations permit the supervisor to apply qualitative judgment in safeguarding the safety and soundness of the banks within its jurisdiction.
Description and findings re EC1	<p>The BOFI Act contains a substantial number of prescriptions (many of which deal with safety and soundness aspects) which a bank is required to comply with, breach of which constitutes an offence and carries, upon conviction, a fine.(BOFI Act - Section 5, 7, 9, 12, 13, 14, 15, 16, 17, 18, 19, etc.)</p> <p>The CBN Act empowers the CBN to exercise its discretion in coming to a decision by basing its decision on its opinion or conclusion, for example, in relation to whether a bank has properly prepared and kept books of account, or in relation to whether the state of affairs of a bank are dire and not improving. (BOFI Act – Section 17, 27, 33, 35, 36, and 61)</p> <p>The legal framework does not explicitly and specifically grant the supervisor full discretion to apply qualitative judgment in coming to a conclusion whether or not a bank is being operated, managed or directed in a safe and sound manner, and in determining whether or not the bank is in a safe and sound condition.</p> <p>Furthermore, the legal framework does not explicitly and specifically empower the supervisor where, in the opinion of the supervisor, a bank and/or director and/or management is engaging in unsafe and unsound practices in conducting the business of the bank, to take corrective, enforcement and/or sanctioning actions against such a party/parties.</p>
EC2	The supervisor has full access to banks' board, management, staff and records in order to review compliance with internal rules and limits as well as external laws and regulations.
Description and findings re EC2	<p>See BCP 1(1) EC4.</p> <p>Though it is clear that the CBN has full access to all the information in a bank, it is not clear that the supervisor explicitly and specifically has full and unfettered access at all reasonable times to all stakeholders involved in a bank, for purposes of discharging his responsibilities.</p>
EC3	<p>When, in a supervisor's judgment, a bank is not complying with laws or regulations or it is or is likely to be engaged in unsafe and unsound practices, the supervisor has the power to:</p> <ul style="list-style-type: none"> • take (and/or require a bank to take) prompt remedial action; and • Impose a range of sanctions (including the revocation of the banking license).

Description and findings re EC3	<p>See BCP23</p> <p>Where the CBN is satisfied that it is in the public interest to do so, or that a bank has been carrying on its business in a manner detrimental to the interest of depositors and creditors, or that a bank has insufficient assets to cover its liabilities to the public, or that a bank has been contravening the law, the CBN has the power to order a special examination of the books and affairs of the bank. Where a bank informs the CBN that it is likely to become unable to meet its obligations under the law; or that it is about to suspend payment to any extent; or that it is insolvent; or where, after a special examination or otherwise howsoever, the CBN is satisfied that a bank is in a grave situation; the CBN may by written order require the bank to take such steps or action which the CBN may consider necessary. If the state of affairs of the bank thereupon does not improve, the CBN may turn over the control of the bank to the NDIC on such terms and conditions as it may stipulate. (BOFI Act – Section 32 and 35)</p> <p>Where an examination of an insured institution revealed that the insured institution or directors or staff have engaged or are engaging in unsafe and unsound practices in conducting the business of the institution or are in violation of the law which may lead to dissipation of the assets or insolvency of the insured institution, the NDIC is empowered to issue specific directives to the management to address the situation by taking corrective measures. (NDIC Act – Section 32)</p>
Assessment of Principle 1(4)	Largely compliant
Comments	<p>The legal framework for banking supervision empowers the supervisor to address compliance with laws. The law and regulations appear, implicitly, though not necessarily explicitly, to permit the supervisor to apply qualitative judgment in safeguarding the safety and soundness of the banks within its jurisdiction.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Update the BOFI Act specifically and explicitly to authorize the CBN to exercise its discretion and judgment to consider whether or not: <ul style="list-style-type: none"> - a particular situation, circumstance, action or inaction constitutes a threat to financial stability; - a bank is being operated, managed or directed in a safe and sound manner; and - a bank is in a safe and sound condition. (The NDIC Act should contain a corresponding provision.) • Update the BOFI Act specifically and explicitly to empower the CBN to take corrective, enforcement and/or sanctioning actions or undertake the resolution of a bank, where, in the opinion of the supervisor: <ul style="list-style-type: none"> - a situation, circumstance, action or inaction in relation to that bank constitutes a threat to financial stability; - a bank and/or director and/or management is engaging in unsafe and unsound practices in conducting the business of the bank. (The NDIC Act should contain a corresponding provision.) • Provide in the BOFI Act that the CBN has full and unfettered access at all reasonable times to all stakeholders involved in a bank, for purposes of discharging its responsibilities. (The NDIC Act should contain a corresponding provision.)
Principle 1(5)	Legal protection. A suitable legal framework for banking supervision is also necessary, including legal protection for supervisors.

Essential criteria	
EC1	The law provides protection to the supervisory authority and its staff against lawsuits for actions taken and/or omissions made while discharging their duties in good faith.
Description and findings re EC1	<p>The Federal Government, the Bank and any of their staff are protected from any claim, demand or liability in respect of anything done or omitted to be done in good faith in pursuance or execution of the provisions of the Act. (CBN Act – Section 52; BOFI Act – Section 53).</p> <p>The NDIC or any of its directors, officers or agents are not to be subjected to any action, claim or demand by or liability to any person in respect of anything done or omitted to be done in good faith in pursuance or in execution of or in connection with the execution of any power conferred upon the NDIC, director officer or agent. (NDIC Act – Section 55).</p> <p>The import of the provisions on legal protection appears to be well grounded having been judicially pronounced upon in the case of Peak Merchant Bank Limited verses the CBN and two others. FHC/L/CS/229/2003.</p>
EC2	The supervisory authority and its staff are adequately protected against the costs of defending their actions and/or omissions made while discharging their duties in good faith.
Description and findings re EC2	<p>None of the relevant legal instruments, being the BOFI Act, the CBN Act or the NDIC Act, addresses the issue of the responsibility for the legal costs of any action, claim or demand, as mentioned above.</p> <p>As a matter of course, to date, the supervisory authorities reportedly have covered the legal costs of their staff in defending themselves in lawsuits instituted against them arising from their execution of their official duties.</p>
Assessment of Principle 1(5)	Largely compliant.
Comments	<p>The legal framework for banking supervision makes provision for legal protection for supervisors—however, it does not make provision for their legal costs.</p> <p>The following recommendations are proposed: Provide for the indemnification, by way of an amendment to the law, of staff of the supervisory authority against the costs of defending their actions and/or omissions made while discharging their duties in good faith.</p>
Principle 1(6)	Cooperation. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Essential criteria	
EC1	Arrangements, formal or informal, are in place for cooperation and information sharing between all domestic authorities with responsibility for the soundness of the financial system, and there is evidence that these arrangements work in practice, where necessary.
Description and findings re EC1	<p>The CNB is empowered , in the exercise of its powers and on the basis of reciprocity, to enter into agreement and arrangements with other regulatory authorities, whether domestic or in other countries exercising similar responsibilities for the promotion of mutual cooperation and the exchange of information for purposes of enhancing the regulation and supervision of financial institutions. Such exchange of information is required to be conditional upon assurances o confidential treatment of the information so given and received. (CBN Act – Section 33)</p> <p>The CBN Act enabled the establishment of The Financial Services Regulation Coordinating Committee (FSRCC) under the chairmanship of the governor of the CBN. Members of the Committee are the Managing Director, NDIC, the Director-General, Securities and Exchange</p>

	<p>Commission, the Commissioner for Insurance, the Registrar-General, Corporate Affairs Commission, and a representative of the Federal Ministry of Finance not below the rank of a Director. The Committee was set up to, <i>inter alia</i>, co-ordinate the supervision of financial institutions, including conglomerates; cause reduction of arbitrage opportunities usually created by differing regulation and supervision standards amongst supervisory authorities; eliminate information gaps between regulatory agencies; and articulate the strategies for the promotion of safe, sound and efficient practices by financial intermediaries. The FSRCC provides a formal interface for coordination and sharing of information amongst domestic authorities with a stake in the soundness of the financial system. (CBN Act – Section 43) Such arrangements for joint coordination of regulatory/supervisory efforts in the financial system have recently resulted in: implementation of reforms by the various regulatory agencies in their respective sub-sectors; the establishment of AMCON; emergence of a New Banking Model; joint issuance of Margin Lending Rules by CBN/SEC; execution of an MOU by the members of the FSRCC and preparation of various financial sector legislation under the Financial System Strategy (FSS) 2020 framework.</p> <p>The NDIC is empowered to obtain the CBN's (bank) examination report. The CBN is obliged to make available to the NDIC relevant information on insured institutions licensed by it, including contraventions committed by any insured institution licensed by it. The NDIC is obliged to make NDIC (insured institution) examination reports available to the CBN. The NDIC is required to cooperate with the CNB on matters affecting any insured institution. (NDIC Act – Section 53)</p> <p>The CBN/NDIC Executive Committee on Supervision operates at both executive and technical levels. The Committee attends to supervisory policy formulation and problem banks resolution. The CBN/NDIC Executive Committee on Supervision does not meet regularly.</p> <p>The CBN and NDIC use the same reporting system, the e-FASS system, to gather information from banks, store such information in a data base, manipulate such data and produce reports. Examination reports are routinely shared between CBN and NDIC.</p> <p>Information sharing among members of the FSRCC is well established both in law and in practice.</p>
EC2	<p>Arrangements, formal or informal, are in place, where relevant, for cooperation and information sharing with foreign financial sector supervisors of banks and banking groups of material interest to the home or host supervisor, and there is evidence that these arrangements work in practice, where necessary.</p>
Description and findings re EC2	<p>The CBN has entered into a number of MOUs with jurisdictions where Nigerian banks are operating and is working on arrangements to collaborate with all foreign supervisors where Nigerian banks have a presence to engage with them, both formally and informally, in line with the home-host framework, to enable the supervisory authorities fulfill their obligations. Most Nigerian banks' foreign subsidiaries are in the West African Sub-region, and the CBN has signed MOUs with all the English-speaking West African countries. Also, the College of Supervisors of the West African Monetary Zone (CSWAMZ) has been collaborating in the supervision of banks. The objectives of the college are to facilitate the exchange of information, among supervisors in the WAMZ area and to enable supervisors to develop a common understanding of the risk profile of a banking group, as a starting point for risk-based supervision at both the solo and consolidated levels. The college meets once every quarter. The CBN and, respectively, each host country's central bank, have commenced joint examination of Nigerian banks in West African countries. To date, the challenges to cooperation/cooperation/information-sharing arrangements have included language (French), resource and technology limitations. (Assessors validated the assertions by way of scrutiny of the CSWAMZ report and an inspection report of a Nigerian bank's subsidiary in a WAMZ member country.)</p>
EC3	<p>The supervisor may provide confidential information to another domestic or foreign financial sector supervisor. The supervisor is required to take reasonable steps to ensure that any</p>

	confidential information released to another supervisor will be used only for supervisory purposes and will be treated as confidential by the receiving party. The supervisor receiving confidential information from other supervisors is also required to take reasonable steps to ensure that the confidential information will be used only for supervisory purposes and will be treated as confidential.
Description and findings re EC3	The CBN, in the exercise of its powers and on the basis of reciprocity, is empowered to enter into agreement or arrangements with other regulatory authorities in Nigeria or in other countries exercising similar responsibilities for the promotion of mutual co-operation and the exchange of information for the purposes of enhancing the supervision and regulation of financial institutions. The above prescriptions also contain a proviso that the exchange of such information shall be conditional upon assurances of confidentiality. (CBN Act – Section 33)
EC4	The supervisor is able to deny any demand (other than a court order or mandate from a legislative body) for confidential information in its possession.
Description and findings re EC4	The CBN is committed to treating information received with utmost confidentiality. Such information may only be divulged by the CBN where it is satisfied that it is in the best national interest to do so or that the person supplying the information does not object to its publication or the authorities have been ordered to do so by a court of competent jurisdiction. In addition, the authorities may also divulge information of a confidential nature if it is in fulfillment of the requirements of the Freedom of Information Act. (CBN Act – Section 33)
Assessment of Principle 1(6)	Largely compliant.
Comments	<p>Arrangements for sharing information between supervisors and protecting the confidentiality of such information are in place, though the coordination between the CBN and the NDIC may require attention.</p> <p>The following recommendations are proposed: Reconsider the raison d'être of the CBN/NDIC Executive Committee of Supervision and, if this committee be found to be necessary and indispensable, update its mandate, objectives and functions to ensure its optimal relevance, and fix the responsibility for its agenda.</p>
Principle 2	Permissible activities. The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined and the use of the word “bank” in names should be controlled as far as possible.
Essential criteria	
EC1	The term “bank” is clearly defined in laws or regulations.
Description and findings re EC1	The term “bank” is clearly and consistently defined in the CBN Act and the BOFI Act, as a bank licensed under the BOFI Act. The NDIC Act defines the term “bank” to mean “any person who carries on the business of banking which includes the acceptance of deposits.” No person is permitted to carry on any banking business except a duly incorporated company which holds a valid banking license. (CBN Act – Section 60) (BOFI Act – Section 2 and 66) (NDIC Act – Section 59)
EC2	The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined either by supervisors, or in laws or regulations.
Description and findings re EC2	<p>See also BCP5.</p> <p>On the one hand, restrictions are placed on certain banking activities. For example, large exposures, related party transactions and credit concentration is restricted. On the other hand, banks are prohibited from undertaking other specified activities, including illegal AML/CFT transactions. (BOFI Act – Section 20, 21, and 22s) (CBN Regulation No. 3 titled Prudential Guidelines for Deposit Money Banks – Section 3.2-3.5)</p> <p>A bank is not permitted to provide financing for the investment in a primary issue of bank</p>

	shares. (CBN regulation on Scope of Banking Activities and Ancillary Matters – Section 5)
EC3	The use of the word “bank” and any derivations such as “banking” in a name is limited to licensed and supervised institutions in all circumstances where the general public might otherwise be misled.
Description and findings re EC3	No person, other than a bank licensed under the BOFI Act, shall or continue to use the word “bank” or any of its derivatives, either in English or any other language in the description or title under which it carries on business in Nigeria. On the other hand, a bank is required to use as part of its description or title the word “bank.” (BOFI Act – Section 43)
EC4	The taking of deposits from the public is generally reserved for institutions that are licensed and subject to supervision as banks.
Description and findings re EC4	The definition of “banking business” includes the receiving of deposits, and also defines “deposit” as meaning money lodged with any person. No person other than a bank (or other person authorized to take deposits) shall issue any advertisement inviting the public to deposit money with it. Certain activities are deemed to constitute receiving money as deposits. Only a Nigerian company holding a banking license is permitted to carry out banking business. A person who transacts banking business without a banking license is guilty of an offence and liable, upon conviction, to imprisonment up to 10 years or a fine (BOFI Act – Section 1, 2, and 66)
EC5	The supervisory or licensing authority publishes, and keeps current, a list of licensed banks and branches of foreign banks operating within its jurisdiction.
Description and findings re EC5	Though there is no statutory requirement to this effect, the CBN of its own volition maintains a list of licensed banks on its website. (http://www.cenbank.org/Supervision/Inst-DM.asp) Though there is not statutory requirement to this effect, the NDIC of its own volition maintains a list of insured banks. (http://ndic.org.ng/list-of—banks-and-their-directors.html)
Assessment of Principle 2	Compliant
Comments	The permissible activities of institutions that are licensed and subject to supervision as banks is clearly defined and the use of the word “bank” in names is controlled as far as possible. The following recommendations are proposed: <ul style="list-style-type: none"> • Formally require the CBN to maintain and publish a list of licensed banks. • Formally require the NDIC to maintain and publish a list of insured institutions.
Principle 3	Licensing criteria. The licensing authority must have the power to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the ownership structure and governance of the bank and its wider group, including the fitness and propriety of Board members and senior management, its strategic and operating plan, internal controls and risk management, and its projected financial condition, including its capital base. Where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.
Essential criteria	
EC1	The licensing authority could be the banking supervisor or another competent authority. If the licensing authority and the supervisory authority are not the same, the supervisor has the right to have its views considered on each specific application. In addition, the licensing authority provides the supervisor with any information that may be material to the supervision of the licensed institution.
Description and findings re EC1	The CBN is both the licensing and bank supervisory authority. (BOFI Act – Section 2, 3, 5, 12, 31, 39, 57, and 62)

EC2	The licensing authority has the power to set criteria for licensing banks. These may be based on criteria set in laws or regulations.
Description and findings re EC2	<p>The CBN is empowered to make regulations to give full effect to the objects of the BOFI Act. (BOFI Act – Section 57) Accordingly, the CBN is empowered to set criteria for licensing banks.</p> <p>An application for a bank license is required to be lodged with the CBN and to be accompanied by a feasibility report of the proposed bank, a draft memorandum and articles of association of the proposed bank, a list of the shareholders, director and principal officers of the proposed bank and their particulars, and such other information, documents and reports and the CBN may, from time to time, specify. The CBN is empowered to issue a banking license with or without conditions, and to vary or revoke any condition subject to which a license was granted or may impose additional conditions to the grant of a license, or to reject an application. Where the grant of a license is subject to conditions, the bank is required to comply with those conditions to the satisfaction of the CBN within such period as the CBN may deem appropriate in the circumstances. Non-compliance by the bank with any of the conditions of the license constitutes an offence and, upon conviction the bank may be liable to a fine. The BOFI Act contains minimum requirements which an applicant for a bank license is required to comply with prior to being issued with a banking license, such as minimum amount of paid-up share capital. A bank's license may be revoked if the bank fails to fulfill or comply with any condition subject to which the license was granted. The CBN is empowered to issue a license for off-shore banking. (BOFI Act – Section 3, 5, 8, 9, and 12). As a matter of (unwritten) policy, the CBN does not license shell banks.</p> <p>The <i>CBN Guidelines for Obtaining a Commercial Banking License in Nigeria</i>, dated September 2010, specifies the information and documents required for purposes of making application for a commercial banking license.</p> <p>Though the legal and regulatory framework specifies a list of documents and information which are required to accompany a bank license application, it does not explicitly and formally specify a complete list of the criteria for issuing a license or that such criteria should be consistent with those applied in ongoing supervision, (BOFI Act – Section 3), though much of this is implicit. As a consequence, seemingly, the CBN does not appear formally and comprehensively to document the nature and extent of the work performed in relation to the (often implicit and informal) criteria which it applies when assessing a banking license application.</p> <p>(The CBN licensing appraisal process includes reliance on third party opinion. For example, the vetting of potential board members/top management and significant shareholders must go through the various agencies of the State such as the State Security Service (SSS), SEC, NDIC, NAICOM, Credit Bureau (CRMS) and reference to CBN's black book maintained by the Bankers Committee Secretariat.)</p> <p>The <i>CBN Regulation on the Scope of Banking Activities & Ancillary Matters, No. 3, 2010</i> sets the criteria for licensing banks under the new Banking Model based on the criteria set in Section 3 of BOFI Act.</p> <p>Other relevant components of the legal and regulatory framework include "Requirements for Opening Representative Office in Nigeria by Foreign Banks," CBN Scope, Conditions & Minimum Standards for Commercial Banks," Regulation No. 1 of 2010, "CBN Scope, Conditions & Minimum Standards for Merchant Banks," Regulation No. 2 of 2010.</p> <p>In processing an application for a banking license submitted recently, an Approval in Principle was granted to the bank. However, before the final license could be issued to the bank, the CBN, in the exercise of the powers conferred on it by Section 9 of BOFI Act, increased the minimum capital requirement of banks, which development delayed the licensing of the bank until it was able to meet the new minimum capital requirement.</p> <p>The assessors were informed that in the past the CBN has rejected applications for bank licenses.</p>

EC3	The criteria for issuing licenses are consistent with those applied in ongoing supervision.
Description and findings re EC3	<p>The legal and/or regulatory framework does not explicitly and formally specify that the criteria for issuing a license should be consistent with those applied in ongoing supervision.</p> <p>The CBN representatives indicated that implicitly and informally the objectives of the licensing process include ensuring that the applicant has the capacity, capabilities and resources both to start off as a safe and sound bank and to maintain that status on a sustainable basis. In the light of the foregoing, the criteria for issuing a bank license are consistent with those applied in ongoing supervision. (The above assertion was made during a discussion between responsible the CBN staff and the assessors—however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>
EC4	The licensing authority has the power to reject an application if the criteria are not fulfilled or if the information provided is inadequate.
Description and findings re EC4	<p>See BCP3 EC2.</p> <p>Newly licensed banks are subject to intensive supervisory attention and scrutiny. The maiden on-site examination is undertaken within six months of a new bank license being issued.</p>
EC5	The licensing authority determines that the proposed legal, managerial, operational and ownership structures of the bank and its wider group will not hinder effective supervision on both a solo and a consolidated basis.
Description and findings re EC5	<p>The legal and/or regulatory framework does not explicitly and specifically specify that the CBN, when considering a new bank license application, should assess whether or not proposed legal, managerial, operational and ownership structures of a bank and its wider group will hinder effective supervision on both a solo and a consolidated basis.</p> <p>The CBN representatives indicated that implicitly and informally the abovementioned condition does constitute a requirement of the licensing process as the CBN, inter alia, reviews a proposed bank's organogram, to determine reporting relationships, lines of authority and responsibility. The CBN does not license shell banks. (The above assertion was made during a discussion between responsible CBN staff and the assessors—however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p> <p>The updated draft <i>Framework for of Financial Institutions in Nigeria</i> dated May 2011 requires that the CBN and NDIC supervise banks and their subsidiaries on a solo and consolidated basis.</p>
EC6	The licensing authority identifies and determines the suitability of major shareholders, including the ultimate beneficial owners, and others that may exert significant influence. It also assesses the transparency of the ownership structure and the sources of initial capital.
Description and findings re EC6	<p>The legal and/or regulatory framework does not explicitly and specifically prescribe that the CBN, when considering a new bank license application, should identify and determine the suitability of major shareholders, including the ultimate beneficial owners, and others that may exert significant influence.</p> <p>A bank is prohibited from employing a person who is or at any time was adjudged bankrupt or has suspended payment to or has compounded with his creditors or who is or has been convicted by a court for an offence involving fraud or dishonesty or professional conduct. Prior to the appointment of a director or CEO, a bank is required to seek and obtain the CBN's written approval for the proposed appointment. No person shall be appointed or remain a director, secretary or an officer of a bank who is of unsound mind or as a result of ill health is incapable of carrying out his duties, is declared bankrupt or suspends payments or compounds with his creditors, or is convicted of any offence involving dishonesty or fraud, or is guilty of serious misconduct in relation to his duties, or in the case of a person possessed of professional qualification, is disqualified or suspended from practicing his profession by the</p>

	<p>order of any competent authority. Any person whose appointment with a bank has been terminated or who has been dismissed for reasons of fraud, dishonesty or conviction of an offence involving dishonesty or fraud shall not be employed by any bank. (BOFI Act – Section 19 and 48)</p> <p>The <i>CBN Guidelines for Obtaining a Commercial Banking License in Nigeria</i>, dated September 2010, specifies that, as part of the documentation accompanying an application for a commercial banking license, signed fitness and propriety questionnaire and declaration should be submitted in respect of each proposed shareholder, director and manager. The CBN representatives indicated that implicitly and informally the abovementioned considerations do constitute key issues when coming to a decision whether or not to issue a banking license. A key requirement for a new banking license is a feasibility report on the proposed deposit-taking financial institution, which provides information on the ownership structure detailing names of proposed investor(s), profession/business and percentage shareholding. As part of the license application evaluation process, the CBN conducts background checks (fit and proper tests) on major shareholders and others that could exert significant influence to determine their suitability, and the CBN rejects the shareholding of anyone that is considered not suitable. The CBN conducts capital verification exercise to ascertain the sources of the initial and additional capital injection into banks. In the process of the 2004/2005 banking sector consolidation exercise, ₦406.4 billion was raised by banks from the capital market but only ₦360 billion was accepted by the CBN after verification. The recapitalization exercise and capital verification process also led to the inflow of Foreign Direct Investment (FDI) of US\$652 million and GBP162,000. (The above assertion was made during a discussion between responsible CBN staff and the assessors— written records confirming the fact that the CBN conducts background checks were found in the license application file scrutinized by the assessors.)</p> <p>Other relevant components of the legal and regulatory framework include the “Approved Persons Guidelines,” “Requirements for a New Banking License” Ref BSD/BLR/05, “CBN Guidelines for Obtaining a Commercial Banking License” and “Code of Corporate Governance.”</p> <p>The CBN representatives indicated that capital verification is an integral part of the licensing process and is always carried out by the CBN in order to ascertain the sources of capital provided by investors and to ensure transparency of the ownership structure of a bank. (See also the “CBN Guidelines for Obtaining a Commercial Banking License” – Section 3.1.1.2(e) and Section 1(II) of BSD/BLR/05, dated 2005 03 01)</p>
EC7	A minimum initial capital amount is stipulated for all banks.
Description and findings re EC7	<p>See also BCP6.</p> <p>The CBN is empowered to stipulate the prescribed minimum paid-up share capital for all categories of banks and the prescribed minimum percentage of regulatory eligible capital to risk weighted assets. A bank is required to maintain at all times the prescribed minimum amount of paid-up share capital and the prescribed minimum percentage of regulatory eligible capital to risk weighted assets.</p>
EC8	The licensing authority, at authorization, evaluates proposed directors and senior management as to expertise and integrity (fit and proper test), and any potential for conflicts of interest. The fit and proper criteria include: (i) skills and experience in relevant financial operations commensurate with the intended activities of the bank; and (ii) no record of criminal activities or adverse regulatory judgments that make a person unfit to uphold important positions in a bank.
Description and findings re EC8	<p>The legal and/or regulatory framework does not explicitly and specifically prescribe that the CBN, when considering a new bank license application, is required, to evaluate proposed directors and senior management as to expertise and integrity (fit and proper test), and any potential for conflicts of interest.</p> <p>The <i>CBN Guidelines for Obtaining a Commercial Banking License in Nigeria</i>, dated September 2010, specifies that, as part of the documentation accompanying an application for</p>

	<p>a commercial banking license, a signed fitness and propriety questionnaire and declaration should be submitted in respect of each proposed shareholder, director and manager.</p> <p>The <i>Circular on Approved Persons Regime</i>, dated 21 June 2011, aims at ensuring that only fit and proper persons are considered for appointment to top management positions in banks as well as serve as significant shareholders (shareholding of 5 percent and above.) The fit and proper criteria include prescriptions regarding: (i) skills and experience in relevant financial operations commensurate with the intended activities of the bank; and (ii) no record of criminal activities or adverse regulatory judgments that make a person unfit to uphold important positions in a bank. The CBN also issued the <i>Code of Corporate Governance for Bank in Nigeria</i>. A banking license application is required to be accompanied by a list of the shareholders, directors and principal officers of the proposed bank and their particulars. (BOFI Act – Section 3)</p> <p>As part of the CBN's new license application assessment procedures, the CBN assesses the fitness and propriety of the promoters, proposed shareholders, directors and senior management. This is done through the review of academic and professional qualifications, skills, experience, reference letters from past employers and credible persons, security screening and status enquiry from SSS, SEC, NDIC, NAICOM, Credit Bureau (CRMS) and reference to CBN's black book maintained by the Bankers Committee Secretariat. (The above assertion was made during a discussion between responsible CBN staff and the assessors— however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p> <p>The CBN reviews the CVs of each of the proposed directors and top management to determine their qualifications, experience, and technical competence vis-s-vis the business of the proposed bank. (Code of Corporate Governance – Section 4.11)</p>
EC9	<p>The licensing authority reviews the proposed strategic and operating plans of the bank. This includes determining that an appropriate system of corporate governance, risk management and internal controls, including those related to the detection and prevention of criminal activities, as well as the oversight of proposed outsourced functions, will be in place. The operational structure is required to reflect the scope and degree of sophistication of the proposed activities of the bank.</p>
Description and findings re EC9	<p>The legal and/or regulatory framework does not explicitly and specifically prescribe that the CBN, when considering a new bank license application, is required, to review and evaluate the proposed strategic and operating plans of the bank, including that an appropriate system of corporate governance, risk management and internal controls, including those related to the detection and prevention of criminal activities, as well as the oversight of the proposed outsourced functions, will be in place. Nor is the CBN required to make a determination whether or not the operational structure is required to reflect the scope and degree of sophistication of the proposed activities of the bank.</p> <p>A banking license application is required to be accompanied by a feasibility report and such other information, documents and reports as the CBN may specify. (BOFI Act – Section 3)</p> <p>As part of the CBN's new license application assessment procedures, the CBN asserts that it reviews the assumptions underlying the feasibility report, the bank's organogram detailing board and management structure, framework for risk management and internal controls. The CBN asserts that it ensures that the organogram reflects the scope, complexity and degree of sophistication of the bank's proposed operations. A regulatory policy on banks' outsourcing activities is however yet to be issued to the industry. (The above assertion was made during a discussion between responsible CBN staff and the assessors. However, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>

	<p>The CBN asserts that critical (proposed) policies, such as in relation to risk management, credit, corporate governance and operations are reviewed during the assessment of a licensing application. (See also “CBN Guidelines for Obtaining a Commercial Banking License”)</p>
EC10	<p>The licensing authority reviews pro forma financial statements and projections for the proposed bank. This includes an assessment of the adequacy of the financial strength to support the proposed strategic plan as well as financial information on the principal shareholder of the bank.</p>
Description and findings re EC10	<p>The legal and/or regulatory framework does not explicitly and formally require the CBN, when considering a new bank license application, to review pro formal financial statements and projections for the proposed bank, inter alia, for purposes of assessing the adequacy of the financial strength to support the proposed strategic plan as well as financial information on the principal shareholder/s of the bank.</p> <p>A banking license application is required to be accompanied by a feasibility report and such other information, documents and reports as the CBN may specify. (BOFI Act – Section 3)</p> <p>The <i>CBN Guidelines for Obtaining a Commercial Banking License in Nigeria</i>, dated September 2010, specifies that, as part of the documentation accompanying an application for a commercial banking license, a statement of intent to invest in the bank should be submitted and a five year financial projection of the proposed bank.</p> <p>As part of the CBN’s new license application assessment procedures, the CBN reviews the feasibility report on the proposed deposit-taking financial institution which provides information on financial projections and the underlying assumptions. The review includes detailed assessment of capacity of the bank to effectively finance and achieve its proposed strategic plan. The capital verification exercise conducted by the CBN to ascertain the source and stability of initial capital injection into a new bank also covers information on the financial strength of the principal shareholders of the bank. (The above assertion was made during a discussion between responsible CBN staff and the assessors—however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>
EC11	<p>In the case of foreign banks establishing a branch or subsidiary, before issuing a license, the host supervisor establishes that no objection (or a statement of no objection) from the home supervisor has been received. For purposes of the licensing process, as well as ongoing supervision of cross-border banking operations in its country, the host supervisor assesses whether the home supervisor practices global consolidated supervision.</p>
Description and findings re EC11	<p>The <i>CBN Guidelines for Obtaining a Commercial Banking License in Nigeria</i>, dated September 2010, specifies that, as part of the documentation accompanying an application for a commercial banking license, a statement of no objection from the home supervisor should be attached.</p> <p>For purposes of the licensing process, as well as ongoing supervision of cross-border banking operations in its country, the CBN as host supervisor should be required to assess whether the home supervisor practices global consolidated supervision, which is not currently an explicit and specific criterion.</p> <p>No foreign bank is permitted to open a branch locally, except with the prior approval of the CBN. (BOFI Act – Section 8) The <i>Framework for Cross-Border Supervision of Banks</i> provides for on-going supervision of cross-border banking. The Framework requires among other things, that a statement of no objection from the home supervisor should be obtained in the case of foreign banks establishing a branch or subsidiary in Nigeria.</p> <p>One of the key considerations by the CBN in signing an MOU with other jurisdictions with</p>

	<p>respect to ongoing supervision of cross-border banking institutions is the ability of the home supervisor to carry out global consolidated supervision. (The above assertion was made during a discussion between responsible CBN staff and the assessors. However, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>
EC12	<p>If the licensing, or supervisory, authority determines that the license was based on false information, the license can be revoked.</p>
Description and findings re EC12	<p>The legal and/or regulatory framework does not explicitly and formally specify that a license obtained based on false information can be revoked by the CBN.</p> <p>See also BCP3 EC2.</p> <p>The CBN is empowered to revoke a license under certain circumstances, including if the bank ceases the carry on the type of banking business for which the license was issued, goes into liquidation or is wound up or otherwise dissolved, fails to comply with any condition subject to which the license was granted, has insufficient assets to meet its obligations or fails to comply with any obligation imposed upon it by or under the BOFI Act or the CBN Act. Breach of the regulatory required minimum capital adequacy requirement constitutes grounds for revocation of the bank's license. Where a bank over which the NDIC has assumed control cannot be rehabilitated, the NDIC may recommend to the CBN that other resolution measures may include the revocation of the bank's license. Where the license of a bank has been revoked, the NDIC shall apply to the Federal High Court for a winding up order of the affairs of the bank. If any book, document or information which the a bank produces to an examiner is false in any material particular, the bank would be guilty of an offence and liable on conviction to a fine.(BOFI Act – Section 9, 12, 39 and 40)</p> <p>As part of the CBN's new license application assessment procedures, the CBN assesses the nature and quality of the information it received from the applicant. (The above assertion was made during a discussion between responsible CBN staff and the assessors. However, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p> <p>The CBN normally includes in a license approval letter a statement to the effect that "any false claims on the basis of which the license was issued will render the license invalid"</p>
EC13	<p>The board, collectively, must have a sound knowledge of each of the types of activities the bank intends to pursue and the associated risks.</p>
Description and findings re EC13	<p>The legal and/or regulatory framework does not explicitly and formally specify that the CBN, when considering a new bank license application, should assess whether or not the board, collectively, have a sound knowledge of each of the types of activities the bank intends to pursue and of the associated risks.</p> <p>See also BCP3 EC2</p> <p>The <i>Code of Corporate Governance for Banks</i> requires that only people of proven integrity and who are knowledgeable in business and financial matters should be on the board of a bank. (See paragraph 5).</p> <p>As part of the CBN's new license application assessment procedures, the CBN assesses whether or not the board, collectively, have a sound knowledge of each of the types of activities the bank intends to pursue and of the associated risks. (The above assertion was made during a discussion between responsible CBN staff and the assessors—however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>

Additional criteria	
AC1	The assessment of the application includes the ability of the shareholder to supply additional financial support, if needed.
Description and findings re AC1	<p>The legal and/or regulatory framework does not explicitly and formally specify that the CBN, when considering a new bank license application, should assess whether or not the shareholder has the ability to supply additional financial support to the proposed bank, as and when needed.</p> <p>As part of the CBN's new license application assessment procedures, the CBN assesses whether or not the principal shareholders have the ability to supply additional financial support to the proposed bank, as and when needed. (The above assertion was made during a discussion between responsible CBN staff and the assessors—however, no written record confirming this assertion was found in the license application file scrutinized by the assessors.)</p>
AC2	The licensing or supervisory authority has policies and processes in place to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met.
Description and findings re AC2	<p>The legal and/or regulatory framework does not explicitly and formally specify that the CBN should have policies and processes in place to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met.</p> <p>As part of the CBN's new license application assessment procedures, the CBN conducts maiden examination of all new banks within six months after the commencement of operation. The off-site analysis of the mandatory returns rendered to the supervisory authorities which is followed by the maiden examination of a new bank enables the CBN and NDIC to monitor the progress of new entrants in meeting their business and strategic goals, and to determine that supervisory requirements in the license approval are being met. (Assessors confirmed these assertions during discussion with two counterparties.)</p>
Assessment of Principle 3	Largely compliant.
Comments	<p>The licensing authority has the power to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, consists of an assessment of the ownership structure and governance of the bank and its wider group, including the fitness and propriety of Board members and senior management, its strategic and operating plan, internal controls and risk management, and its projected financial condition, including its capital base. Where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor is obtained. Important elements of licensing, including important criteria, other requirements and process are implicit and informal, and require to be specified explicitly and to be formalized. The list of prescribed criteria contained in the legal and regulatory framework is incomplete and the criteria should focus on outcomes, as opposed to inputs. In addition, the CBN should be required to maintain a formal audit trail, by the CBN formally and in writing assessing a new bank license application against each and every one of the prescribed criteria</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Specify explicitly and formally in the legal and/or regulatory framework: <ul style="list-style-type: none"> - the criteria for issuing a licence; - that the CBN is required formally and in writing to assess any new bank license application against the criteria and to document the nature and extent of the work performed and the conclusions reached in relation to each criterion individually, and also overall; - that the CBN is not empowered to issue a bank licence for a shell entity, a shelf

	<p>company, or a tax haven domiciled entity;</p> <ul style="list-style-type: none"> - that the criteria for issuing a licence are consistent with those applied in ongoing supervision; - that a licence obtained based on false information shall be revoked by the CBN; and - that the CBN should have policies and processes in place to monitor the progress of new entrants into the banking sector in meeting their business and strategic goals, and to determine that supervisory requirements outlined in the license approval are being met. <ul style="list-style-type: none"> • Specify explicitly and formally in the legal and/or legal framework that the CBN is required to base its decision whether or not to approve an application for a new bank license on the following criteria: <ul style="list-style-type: none"> - evaluate, by review of the proposed legal, managerial, operational and ownership structures of a (proposed) bank and its wider group, whether or not such structures would hinder effective supervision on both a solo and a consolidated basis; - identify and evaluate whether or not the (proposed) major/significant/controlling (ultimate beneficial) shareholders and others that may exert significant influence, are suitable; - assess whether or not the (proposed) ownership structure of the (proposed) bank is sufficiently transparent; - identify the (proposed) sources of initial capital for the (proposed) bank and evaluate whether or not such sources are acceptable; - evaluate whether or not (proposed) directors and senior management of the (proposed) bank are suitable, in view of their capacity and capability, and integrity (fit and proper test), and in view of any potential for conflicts of interest; - evaluate whether or not the (proposed) strategic and operating plans of the (proposed) bank, including the system of corporate governance, risk management and internal controls, and including those related to the detection and prevention of criminal activities, as well as the oversight of the proposed outsourced functions, are acceptable; - evaluate whether or not the (proposed) operational structure of the (proposed) bank reflects and is appropriate for the scope and degree of sophistication of the proposed activities of that bank; - evaluate whether or not pro formal financial statements and projections for the (proposed) bank are adequate for purposes of assessing the adequacy of the financial strength of the (proposed) bank and the capacity of the (proposed) bank to support its strategy; - evaluate whether or not the board, collectively, has a sound knowledge of each of the types of activities the (proposed) bank intends to pursue and of the associated risks; - evaluate whether or not the (proposed) major/significant/controlling shareholder/s would be in a position to provide the necessary additional financial support to the (proposed) bank to enable it to execute its strategic plan and achieve its strategic aims; and - evaluate whether or not the (proposed) major/significant/controlling shareholder/s would be in a position to provide the necessary additional financial support to the (proposed) bank in the event of a loss suffered as a result of an extreme but plausible event.
Principle 4	Transfer of significant ownership. The supervisor has the power to review and reject any proposals to transfer significant ownership or controlling interests held directly or indirectly in existing banks to other parties.
Essential criteria	
EC1	Laws or regulations contain clear definitions of “significant” ownership and “controlling interest.”
Description and findings re EC1	An application for a bank license is required to be accompanied by a list of shareholders. (BOFI Act – Section 3) “Significant shareholding” is defined as a holding of at least 5 percent (individually or aggregate) of a bank’s equity. (<i>Prudential Guidelines for Deposit Money Banks</i>

	<p><i>in Nigeria, June 2010 – Section 3.4</i>) “Significant influence,” a closely related term, is defined in the as “the ability to exercise significant influence over the operating, financial, or accounting policies of another entity. (<i>Regulation on the Scope of Banking Activities & Ancillary Matters, No. 3, 201.</i>)</p> <p>The term “controlling interest” is not defined in the CBN Act, the BOFI Act, or the NDIC Act.</p> <p>PS: The components of the legislative framework dealing with this topic (transfer of significant ownership) are scattered, seemingly somewhat randomly throughout the legislative framework, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty.</p>
EC2	There are requirements to obtain supervisory approval or provide immediate notification of proposed changes that would result in a change in ownership, including beneficial ownership, or the exercise of voting rights over a particular threshold or change in controlling interest.
Description and findings re EC2	<p>Except with the prior consent of the CBN, no bank shall enter into an agreement or arrangement which results in a change in the control of the bank; for the sale, disposal or transfer howsoever, of the whole or any part of the business of the bank; for the amalgamation or merger of the bank with any other person; for the reconstruction of the bank; to employ a management agent or to transfer its business to any such business. (BOFI Act – Section 7) An equity holding above 10 percent by any investor is subject to CBN’s prior approval. (<i>CBN Code of Corporate Governance – Section 5.1.3</i>) Information is required to be filed with the Securities Exchange Commission (SEC) by a company’s share registrar on any transaction that results in the beneficial ownership holding of shares in a company crossing the 5 percent threshold. (SEC rules on Securities Ownership – Rule 386) In terms of a mutual MoU, the SEC is required to inform the CBN of such a filing.</p> <p>Section 7(1) of the BOFI Act states that no bank shall enter into an agreement or arrangement which results in a change in the control of the bank without the consent of the CBN. However, this provision is of no practical use, as the bank itself does not have any say in who controls the bank or whether or not control in the bank changes.</p>
EC3	The supervisor has the power to reject any proposal for a change in significant ownership, including beneficial ownership, or controlling interest, or prevent the exercise of voting rights in respect of such investments, if they do not meet criteria comparable to those used for approving new banks.
Description and findings re EC3	<p>See BCP4 EC2.</p> <p>Accordingly, insofar as Section 7 of the BOFI Act imposes an obligation or prohibition on a bank in respect of something which is within the powers of the bank, the supervisor has the power to reject such proposal. On the other hand, insofar as Section 7 of the BOFI Act imposes an obligation or prohibition on a bank in respect of something which is not within the powers of the bank, such provision is of no force and effect.</p> <p>CBN Circular BSD/DO/CR/2/2000, dated March 23, 2000, needs to be revisited as it is no longer appropriate in the light of the current approach to fit and proper requirements in relation to shareholders.</p>
EC4	The supervisor obtains from banks, through periodic reporting or on-site examinations, the names and holdings of all significant shareholders or those that exert controlling influence, including the identities of beneficial owners of shares being held by nominees, custodians and through vehicles which might be used to disguise ownership.
Description and findings re EC4	Banks are required to submit returns on their shareholders to the CBN. (BOFI Act – Section 25) Only shareholders which are fit and proper are permitted to hold a significant shareholding, being a shareholding of 5 percent or more, in a bank. (<i>CBN circular on Approved Persons Regime – Section 5</i>)

	<p>As part of continuous supervision, the CBN investigates shareholders with holdings of 5 percent or more to determine their fitness and propriety. Data integrity of such information constitutes a challenge, for example, in ensuring that information on beneficial shareholders as opposed to registered shareholders is obtained. (Assessors verified the validity of these assertions during a scrutiny of an application for a bank license.)</p> <p>The legal and regulatory framework does not appear to contain a reference to “beneficial owners of shares” or “beneficial” shareholders, as opposed to (nominee) shareholders in name only. Consequently, where the beneficial shareholder differs from the nominee shareholder, the supervisor is not required to identify the beneficial shareholder and ensure that the beneficial shareholders are fit and proper and comply with the legal and/or regulatory framework.</p>
EC5	The supervisor has the power to take appropriate action to modify, reverse or otherwise address a change of control that has taken place without the necessary notification to or approval from the supervisor.
Description and findings re EC5	<p>CBN is empowered to impose a fine (not exceeding ₦1 million and in the case of a continuing offence an additional fine of ₦10,000 for each day during which the offence continues) in the event that prior consent of the CBN is not obtained for specified transactions, such as transactions which results in a change in the control of the bank; for the sale, disposal or transfer howsoever, of the whole or any part of the business of the bank; for the amalgamation or merger of the bank with any other person; for the reconstruction of the bank; to employ a management agent or to transfer its business to any such business. (BOFI Act – Section 7)</p> <p>The fines indicated in Section 7 of the BOFI Act are small, not in line with the gravity of the offence and, consequently, not a sufficient deterrent. As it would simply be unacceptable for an unfit party to obtain control over a bank, there is a need also for measures to reverse or neutralize such transactions.</p>
Additional criteria	
AC1	Laws and regulations provide, or the supervisor ensures, that banks must notify the supervisor as soon as they become aware of any material information which may negatively affect the suitability of a major shareholder.
Description and findings re AC1	<p>The audited annual financial statements are required to disclose in detail penalties paid as a result of contravention of the provisions of the BOFI Act and provisions of any policy guidelines, and the auditor’s report shall reflect such contravention. If the auditor is satisfied that there has been a contravention of the BOFI Act or an offence under any other law has been committed by the bank or any other person; or losses have been incurred by the bank which substantially reduce the bank’s capital’ or any irregularity has occurred; or he is unable to confirm that the claims of depositors or creditors are covered by the assets of the bank, he is required immediately to report the matter to the CBN. (BOFI Act – Section 27 and 29)</p> <p>Banks are required to establish “whistle blowing” procedures which encourage (including by assurances of confidentiality) all stakeholders (including shareholders, directors, management, staff, customers, suppliers, applicants, external auditors) to report any unethical activity or breach of the corporate governance code using, among others, a special email or hotline to both the bank and the CBN. (Code of Corporate Governance for Banks – Section 6.1.12)</p> <p>There is no specific and explicit provision in the legal and/or regulatory framework which requires a bank to notify the supervisor as soon as it becomes aware of any material information which may negatively affect the suitability of a major shareholder.</p>
Assessment of Principle 4	Materially non-compliant

Comments	<p>The supervisor is empowered to review and, if deemed appropriate, to reject any proposals to transfer significant ownership or controlling interests held directly or indirectly in existing banks to other parties. However, the supervisor's powers to review are flawed, and the supervisor's powers to enforce such as rejection are weak and inadequate. Furthermore, it is necessary to focus on the beneficial shareholders, as opposed to focusing merely on the registered/nominee shareholders.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Recast BOFI Act – Section 7 to ensure that it can have effect. (For example, the obligation to obtain the prior consent of the governor should be imposed on shareholders, as opposed to the bank itself, as only the shareholders, and not the bank itself, can effect a change of control of the bank or give effect to a disposal of the whole of the business of the bank, or effect an amalgamation or merger of the bank, etcetera.) In addition, empower the supervisor to stop, neutralize or overturn transactions which proceed without the supervisor's approval or despite the supervisor's disapproval. • Permit only fit and proper persons to obtain or hold a shareholding exceeding 5 percent, which constitutes a significant shareholding, in a bank. Accordingly, the prior approval of the CBN should be obtained by a (prospective) shareholder prior to the (prospective) shareholder's shareholding in the bank exceeding a 5 percent shareholding in the bank. The CBN should base its assessment of the application on whether the prospective significant shareholder is fit and proper and would be in a position to support the bank in time of stress and need. In the event of a transaction in violation of this provision, the CBN should be empowered to suspend such (beneficial) shareholder's voting rights and dividend rights on this total shareholding in the bank until the situation is regularized. Should the significant shareholder in future fail the fit and proper test, the significant shareholder would be required immediately to dispose of his shareholding above 5 percent in the bank. A significant shareholder is required, on an annual basis, to complete and submit to the CBN a form requesting his identity, contact details and details of his significant shareholding in a bank. • Prescribe that no person or group of related persons, whether natural or legal, may obtain control over a bank without the prior written consent of the CBN. Furthermore, prescribe that where a transaction is concluded which results in breach of (the amended) Section 7(1), the (beneficial) shareholders' voting rights and dividend rights in respect of all such (beneficial) shareholder's shareholding in the bank, at the instance of the CBN, could be suspended until such time as he CBN is satisfied as to the fitness and propriety of the new shareholder and has given its consent to such a transaction. • Consider, in the light of the current approach to fit and proper requirements relating to shareholders, whether Circular BSD/DO/CR/2/2000, dated March 23, 2000, is still relevant and, if not, withdraw it. • Define the concept of a beneficial shareholder (in contradistinction with a nominee shareholder). In addition, wherever the submission of shareholder information is dealt with in the legal and regulatory framework, it should be made clear that it means the submission of information on the beneficial shareholder. (Accordingly, it should be incumbent upon the supervisor to ensure that beneficial shareholders are and remain fit and proper and in compliance with the legal and regulatory framework.) • Require a bank to notify the supervisor as soon as it becomes aware of any material information which may negatively affect the suitability of a significant shareholder. • Review the fines stipulated in the legal and regulatory framework and update such fines in line with the gravity of the offence and to constitute a sufficient deterrent • Consolidated, rationalize, logically arrange and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP4.
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Principle 5	Major acquisitions. The supervisor has the power to review major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and confirming that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Essential criteria	
EC1	Laws or regulations clearly define what types and amounts (absolute and/or in relation to a bank's capital) of acquisitions and investments need prior supervisory approval.
Description and findings re EC1	<p>Banking model A bank is permitted to acquire or hold shares in an agricultural, industrial or venture capital company, subject to certain conditions, including the limitation that any such individual investment may not exceed 10 percent of the bank's shareholders' funds and the aggregated of all such investments do not exceed 20 percent of the bank's shareholders' funds. Except for the foregoing, as a general rule, a bank is prohibited from acquiring or holding shares in any entity, and then only with the approval of the CBN. (BOFI Act – Section 20 and 21)</p> <p>The assessors have a fundamental and serious concern regarding these provisions, as they enable a bank to take large stakes (even controlling stakes, and even full ownership) of agricultural, industrial and venture capital companies. In addition to exposing a bank to equity investment risk, for which a bank is not the appropriate vehicle and may well not be appropriately capitalized, and it may result in bank management's attention being diverted from banking business. (The 2011 change in the banking model, with the removal of the universal banking model, did not affect the above provisions of the BOFI Act.) (The CBN noted that "such investments would be deducted from a bank's capital for calculation of capital adequacy purposes, thus depositors funds would not be at risk." Though such an approach would be conservative and therefore commendable, in itself it will not address all the risks arising from these investments, such as liquidity risk.)</p> <p>During the period 2000 to 2010, the CBN's exercise of its abovementioned approval was guided by the so-called Universal Banking Guidelines, which enabled the use of a universal banking model by banks and provided for a single universal banking license. The Universal Banking Guidelines were withdrawn by way of the 2010 regulation titled Scope of Banking Activities and Ancillary Matters (BAAM regulation), which came into effect on 15 November 2010. The BAAM regulation restricts banks to banking business, as defined, and makes provision for three types of banking licenses, namely as a commercial bank, a merchant bank or a specialized bank.</p> <p>A bank is no longer permitted to acquire or hold an equity investment, as, in terms of the BAAM regulation, no bank shall establish, acquire or maintain any Related Enterprise, as defined (with limited exceptions, such as a (proposed) bank incorporated outside Nigeria subject to and with CBN approval.) A Related Enterprise is widely defined as any entity in which the bank holds any equity interest. In addition, no bank is permitted to acquire and hold immovable property, other than for own-use in the business.</p> <p>A bank wishing to undertake expansion abroad is required to submit a formal application (in line with the prescriptions contained in CBN circular on Offshore Expansion, ref BSD/DIR/CIR/GEN/02/014) to the CBN. A parent bank's aggregate investment in all its subsidiaries is subject to a limit of 25 percent of the bank's paid-up capital and statutory reserve.</p> <p>Other relevant prescriptions No bank may open a branch office without the prior consent of the CBN. No bank is permitted to enter into an agreement or arrangement relating to the restructuring, re-organization, merger and disposal, etc, of the bank, without the prior approval of the CBN. No bank is permitted to acquire or hold shares in any financial, commercial or other undertaking unless it</p>

	<p>complies with specified conditions. (BOFI Act – Section 6, 7, and 20) Limits are placed on exposures to a single obligor/connected lending. (Prudential Guidelines for Deposit Money Banks)</p> <p>PS: The components of the legislative framework dealing with this topic (major acquisitions) are scattered, seemingly somewhat randomly throughout the legislative framework, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty.</p>
EC2	Laws or regulations provide criteria by which to judge individual proposals.
Description and findings re EC2	See BCP5 EC1.
EC3	Consistent with licensing requirements, among the objective criteria that the supervisor uses is that any new acquisitions and investments do not expose the bank to undue risks or hinder effective supervision. The supervisor can prohibit banks from making major acquisitions/investments (including the establishment of foreign branches or subsidiaries) in countries with secrecy laws or other regulations prohibiting information flows deemed necessary for adequate consolidated supervision.
Description and findings re EC3	<p>See also BCP5 EC1</p> <p>General The safety and long term soundness of a bank constituted an overriding consideration for abandoning the universal banking model and reverting back to basics, as regulated in the 2010 regulation titled Scope of Banking Activities and Ancillary Matters (BAAM regulation), which came into effect on November 15, 2010.</p> <p>As a bank wishing to undertake expansion abroad is required to submit a formal application (in line with the prescriptions contained in CBN circular on Offshore Expansion, ref BSD/DIR/CIR/GEN/02/014) to the CBN, the CBN is in a position fully to control the process.</p> <p>Accordingly, the CBN can prevent and prohibit banks from making major acquisitions/investments (including the establishment of foreign branches or subsidiaries) in countries with secrecy laws or other regulations prohibit information flows deemed necessary for adequate consolidated supervision, and ensure that any new acquisition or investment does not expose the bank to undue risks or hinder effective supervision.</p> <p>The CBN has rejected applications by banks to open branches/subsidiaries in some tax haven countries as well as other jurisdictions which prohibit information flows deemed necessary for effective consolidated Supervision. (Assessors verified the validity of these assertions during a scrutiny of an application for offshore expansion.)</p>
EC4	The supervisor determines that the bank has, from the outset, adequate financial and organizational resources to handle the acquisition/investment.
Description and findings re EC4	The CBN, in the processing of a bank's request for approval to undertake an acquisition/investment, takes into consideration an extensive range of factors and information, including the bank's capital adequacy, liquidity ratio position, adequacy of risk management processes, investment in fixed assets in relation to the bank's shareholders' fund and long term loans. The bank's free fund is usually computed to ascertain that it has adequate financial and organizational resources to carry out the acquisition/investment. (Assessors verified the validity of these assertions during a scrutiny of a file dealing with an application by a bank relating to an off-share expansion application.)
EC5	Laws and regulations clearly define for which cases notification after the acquisition or investment is sufficient. Such cases should primarily refer to activities closely related to banking and the investment being small relative to the bank's capital.

Description and findings re EC5	<p>The legal and/or regulatory framework does not prescribe sufficiently comprehensively and clearly how a bank, when considering a (proposed) acquisition or investment, is required to distinguish between cases which are required to be dealt with by way of an ex ante application, an ex post application, an ex ante notification and an ex post notification, and other cases.</p> <p>In the case of the acquisition by a bank of shares in SMEs, agricultural enterprises and venture capital companies, the bank is required to furnish full particulars of the acquisition within 21 days. Breach of this prescription would constitute an offence and upon conviction, the bank would be liable to a fine. (BOFI ACT – Section 21)</p>
EC6	The supervisor is aware of the risks that non-banking activities can pose to a banking group, and has the means to take action to mitigate those risks.
Description and findings re EC6	<p>See BCP5 EC1</p> <p>The CBN applies a risk-based approach to supervision, which entails, inter alia, that the supervisor performs a risk assessment of a bank.</p> <p>The supervisor has the power to impose a specific capital charge on all material risk exposures. (See BOFI Act – Section 13)</p> <p>The Intervention Framework contains a number of prescriptions which could be used to address problem situations and a problem bank.</p>
Additional criteria	
AC1	When a bank wishes to acquire a significant holding in a financial institution in another country, the supervisor should take into consideration the quality of supervision in that country and its own ability to exercise supervision on a consolidated basis.
Description and findings re EC1	See BCP5 EC3 and BCP25.
Assessment re Principle 5	Largely compliant
Comments	<p>The supervisor has the power to review major acquisitions or investments by a bank, against prescribed criteria, including the establishment of cross-border operations, and confirming that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Prescribe sufficiently comprehensively and clearly how a bank, when considering a (proposed) acquisition or investment, is required to distinguish between cases which need to be dealt with by way of, respectively, an ex ante application, an ex post application, an ex ante notification and an ex post notification, and other cases. • Consolidated, rationalize, logically order and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP5.
Principle 6	Capital adequacy. Supervisors must set prudent and appropriate minimum capital adequacy requirements for banks that reflect the risks that the bank undertake, and must define the components of capital, bearing in mind its ability to absorb losses. At least for internationally active banks, these requirements must not be less than those established in the applicable Basel requirement.

Essential criteria	
EC1	Laws and regulations require all banks to calculate and consistently maintain a minimum capital adequacy ratio. Laws, regulations or the supervisor define the components of capital, ensuring that emphasis is given to those elements of capital available to absorb losses.
Description and findings re EC1	<p>Banks are required consistently to maintain capital funds unimpaired by losses in such a ratio to all assets or to all or any liabilities or to both assets and liabilities of the bank and all its offices in and outside Nigeria as may be specified by the CBN. (BOFI Act – Section 13)</p> <p>The minimum CAR ratio is set at 10 percent, which is higher than the prescribed CAR ratio of 8 percent (under Basel1). (<i>CBN Circular BSD/11/2003, dated August 4, 2003</i>) (<i>Prudential Guideline for Deposit Money Banks, Effective July 1, 2010 – Section 3.17</i>) A regulatory CAR of 15 percent applies to Nigerian banks with international authorization.</p> <p>Regulatory eligible capital is divided into two components, namely Tier 1 capital and Tier 2 capital. Tier 1 capital is defined to include paid up capital, statutory reserves (See <i>Prudential Guideline for Deposit Money Banks, Effective July 1, 2010 – Section 3.14</i>), share premium, general reserves, reserves for small and medium enterprises and other reserves. Tier 2 capital is defined to include fixed assets revaluation reserves, forex revaluation reserves, general provisions, minority interest, hybrid capital instruments, preference shares and debenture stock. Goodwill and intangible assets, unpublished losses of the current year, under provisioning and investments in unconsolidated subsidiaries and associates are required to be deducted from total capital and reserves in computing capital adequacy ratio. (CBN Circular BSD/DO/CIR/GEN/VOL02/044, dated January 29, 2009.)</p> <p>At least 50 percent of a bank's capital is required to comprise of paid up capital and reserves. Total Tier 2 capital is limited to 100 percent of Tier 1 capital while general provisions that form part of Tier 2 capital is limited to 1.25 percent of risk weighted assets as contained in Section 3.16 (d) of the PG.</p> <p>Though the requirements pertaining to regulatory eligible capital and regulatory capital adequacy requirements are mostly in line with those established in the applicable Basel requirements, there are certain important shortcomings which require rectification.</p> <p>The Tier 1 elements of regulatory eligible capital are not strictly in line with Basel I. For example, statutory reserves (which constitute reserves raised in compliance with statutory prescription to cater for (a) specific risk/s or loss/es, as opposed to the statutory reserves raise in compliance with Section 3.14 of the <i>Prudential Guideline for Deposit Money banks, effective July 1, 2010</i>) and reserves for small and medium enterprises (conceivably constituting reserves raised to cater for (a) specific risk/s or loss/es) do not meet the requirement of being available immediately to absorb losses.</p> <p>The Tier 2 elements of regulatory eligible capital also are not strictly in line with Basel I. For example, a maximum of only 45 percent of revaluation reserves arising from investment in equities qualify; hybrid debt instruments qualify only subject to the specified conditions (namely, they are unsecured, subordinated and fully paid up; they are not redeemable at the initiative of the holder or without the prior consent of the supervisory authority; they are available to participate in losses without the bank being obliged to cease trading; and, although the capital instrument may carry an obligation to pay interest that cannot permanently be reduced or waived, it should allow service obligations to be deferred where the bank could not support payment.)</p> <p>A bank is not required to impair its regulatory eligible capital in an amount equal to the amount of its holding (whether directly or indirectly, e.g., via a subsidiary) of its own shares or the shares of another bank, nor of the financing facilities or financing provided (whether directly or indirectly, e.g., via a subsidiary) for the purchase of its own shares or the shares of another</p>

	<p>bank, nor of the financing facilities or financing provided (whether directly or indirectly, e.g., via a subsidiary) against the security of its own shares or the shares of another bank.</p> <p>The regulatory and/or supervisory framework does not contain any requirements for banks to perform capital management, nor is any guidance given to banks in this regard, nor is any guidance given to supervisors on how to deal with capital management off-site or on-site.</p> <p>Banks are required to adopt IFRS with effect from financial year ended 2012. In terms of the guidance issued by the CBN for the provisioning process, a bank is permitted to treat the shortfall, constituted by the difference, when a bank's regulatory required provisions exceed its IFRS credit impairments, as Tier 1 core capital—we do not agree with this treatment. (The authorities stated that this issue will be resolved in due course.)</p> <p>The 2008 Bank Supervision Annual Report noted that the average regulatory capital adequacy, of 21.9 percent for the banking sector at the end of December 2008, was satisfactory, when compared with the regulatory minimum of 10 percent. A few months later, it was determined that the regulatory capital adequacy was of the order of only 5 percent. This raises serious concerns about a range of fundamental issues, including capital management, accounting, auditing, internal audit, risk management, credit risk management, and governance. Though significant improvements were effected in the interim, it is too early to conclude whether all these aspects have achieved, and are being maintained at, a satisfactory level.</p> <p>PS: The components of the legislative framework dealing with this topic (capital adequacy) are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty.</p>
EC2	At least for internationally active bank, the definition of capital, the method of calculation and the ratio required are not lower than those established in the applicable Basel requirement.
Description and findings re EC2	The capital adequacy regime applies to all banks equally, whether internationally active or otherwise, in that the definition of capital, the method of calculation and the required CAR ratio (of 10 percent, as opposed to the Basel I CAR ratio of 8 percent) applies to all banks. (Since recently, internationally active banks are required to maintain a 15 percent CAR.)
EC3	The supervisor has the power to impose a specific capital charge and/or limits on all material risk exposures.
Description and findings re EC3	<p>A bank is required at all times to maintain regulatory capital in such ratio to all or any such assets as may be specified by the CBN. Accordingly, the supervisory has the power to impose a specific capital charge on all material risk exposures. (See BOFI Act – Section 13)</p> <p>CBN imposed an additional capital charge on all banks above the minimum regulatory capital adequacy requirements, when it raised the CAR ratio from 8 percent to 10 percent.</p> <p>Seemingly, the CBN is implicitly empowered, where and when deemed necessary, to vary a bank's CAR upwards as a function of banks' size, complexity of operations and risk profile. (<i>Supervisory Intervention Framework.</i>)</p>
EC4	The required capital ratio reflects the risk profile of individual banks. Both on-balance sheet and off-balance sheet risks are included.
Description and findings re EC4	<p>The capital adequacy requirements are based on and take account of both on and off balance sheet risks of banks. (BOFI Act – Section 13) (PG – Section 3.16) (Circular ref BSD DO CIR GEN VOL 02 044)</p> <p>None of the banks hold regulatory capital against any risk other than credit risk.</p>

EC5	Capital adequacy requirements take into account the conditions under which the banking system operates. Consequently, laws and regulations in a particular jurisdiction may set higher capital adequacy standards than the applicable Basel requirements.
Description and findings re EC5	The minimum regulatory capital adequacy requirement is set at 10 percent, which is above the minimum Basel I requirement of 8 percent—this higher CAR ratio is motivated based on the peculiarities of the local environment. (CBN Circular BSD/II/2003 of August 4, 2003.) (Prudential Guideline – Section 3.16)
EC6	Laws or regulations clearly give the supervisor authority the power to take measures should a bank fall below the minimum capital ratio.
Description and findings re EC6	Nigerian banking laws and regulations empower the CBN to take definite measures when banks fail to meet the minimum capital adequacy ratio requirement, including prompt corrective measures. Failure to meet the capital adequacy requirement is a sufficient ground for the revocation of the license of a bank and getting the NDIC involved in the bank resolution. (BOFI Act – Section 14 and 37) (<i>Supervisory Intervention Framework</i>) The PCA measures to be taken by the CBN and NDIC under various scenarios are stated in the <i>Supervisory Intervention Framework</i> .
EC7	Where the supervisor permits banks to use internal assessments of risk as inputs to the calculation of regulatory capital, such assessments must adhere to rigorous qualifying standards and be subject to the approval of the supervisor. If banks do not continue to meet these qualifying standards on an ongoing basis, the supervisor may revoke its approval of the internal assessments.
Description and findings re EC7	Currently, banks are not required to use internal assessments of risks as inputs to the calculation of regulatory required capital. Also, it is not envisaged that banks would be obliged in future to use internal assessments of risks as inputs to the calculation of regulatory required capital. As the requirements of Pillars 1 and 2 of Basel II are yet to become mandatory in Nigeria, there are neither standards for the assessment of banks' internal models nor a requirement for CBN's prior approval for the use of the models. Though the CBN's RBS Methodology could be interpreted as incorporating key aspects of Pillar 2 of Basel II, in practice no bank is required to hold capital against any risk other than in terms of the Basel I in respect of credit risk. (Nigeria is in the process of preparing for Basel II implementation.)
Additional criteria	
AC1	For non-internationally active banks, the definition of capital, the method of calculation and the capital required are broadly consistent with the principles of applicable Basel requirements relevant to internationally active banks.
Description and findings re AC1	Foreign banks and local banks are expected to meet the same minimum regulatory capital requirements, and a minimum CAR ratio of 10 percent applies, as opposed to the Basel I minimum of 8 percent. The 1996 Market Risk Amendment. (CBN Scope, Conditions & Minimum Standards for Commercial Banks Regulation 01 of 2010) has not as yet been implemented. Basel II, when implemented, should result in better calibration of capital in relation to risk.
AC2	For non-internationally active banks and their holding companies, capital adequacy ratios are calculated and applied in a manner generally consistent with the applicable Basel requirement, as set forth in the footnote to the Principle.

Description and findings re EC2	See BCP22 AC1.
AC3	The supervisor has the power to require banks to adopt a forward-looking approach to capital management and set capital levels in anticipation of possible events or changes in market conditions that could have an adverse effect.
Description and findings re EC3	As contemplated in the Supervisory Intervention Framework for Banks and Other Financial Institutions, supervisors evaluate banks' capital management policies and practices in assessing capital adequacy. The supervisor's review entails the assessment of the adequacy of the level of capital to support planned business Activities and possible future market conditions. The CBN Regulation 03 requires banks in Nigeria to operate as commercial (international, national or regional), merchant or specialized banks.
AC4	The supervisor requires adequate distribution of capital within different entities of the banking group according to the allocation of risks.
Description and findings re EC4	To date, the CBN has not yet implemented consolidated supervision. Once consolidated supervision is implemented, capital adequacy for banking groups would be assessed on a group wide basis to detect cases of multiple gearing, excessive leverage, contagion from intra group transactions, etc. The CBN's draft Consolidated Supervisory Framework is aimed at ensuring that banking groups maintain adequate capital resources commensurate with their risk, no matter where they are domiciled.
AC5	The supervisor may require an individual bank or banking group to maintain capital above the minimum to ensure that individual banks or banking groups are operating with the appropriate level of capital.
Description and findings re EC5	A bank or banking group may be required to maintain capital above the minimum regulatory requirement as a function of size, complexity of operations and risk profile, if deemed necessary by the CBN. To date, neither the CBN, nor the NDIC, have required a bank or banking group to maintain capital above the regulatory requirement, other than as was specified above.
Assessment re Principle 6	Largely compliant
Comments	<p>The CBN has set prudent and appropriate minimum capital adequacy requirements for banks (though this applies in respect of a bank's credit risk exposures only) and has defined the components of capital, (largely) bearing in mind its ability to absorb losses. These requirements, which are applicable to all banks (both local and foreign, and both internationally active and non-internationally active) are mostly in line with those established in the applicable Basel requirement, apart from some important shortcomings, which need to be rectified. The authorities should develop comprehensive and detailed principles, standards, guidance, prescriptions, statutory returns and supervisory work programs, inter alia based on and aligned with relevant pronouncements of the BCBS, for all key areas, including risk areas, which would enhance effectiveness, efficiency, consistency and transparency of and quality control over supervision, thereby enabling more effective challenging of banks by the supervisor. The authorities should perform overall micro/bottom up and macro/top down stress testing and simulation exercises, also in relation to all key areas, including risk areas, as a tool to provide forward-looking assessments of a bank's capacity (in relation to capital, liquidity and earnings) to withstand extreme but plausible macro-financial shocks. Banks should hold capital also against risk exposures other than credit risk, and should hold adequate capital where the Basel I capital requirements are not sufficiently prudent.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Ensure that the regulatory capital adequacy requirements, at a minimum, are strictly in line with the Basel I, also in relation to Tier 1 and Tier 2 regulatory eligible capital components,

	<p>inter alia, to avoid being classified as being sub-standard or non-compliant relative to Basel I.</p> <p>(For example, regarding regulatory eligible Tier 1: Statutory reserves (insofar as they constitute reserves raised in compliance with statutory prescriptions to cater for (a) specific risk/s or loss/es) and reserves for small and medium enterprises (seemingly constituting reserves raised to cater for (a) specific risk/s or loss/es pertaining to exposures to small and medium enterprises) would not meet the Tier 1 qualifying requirements, inter alia, in that it should be available immediately to absorb losses, (which it cannot be if it was raised to cater for (a) specific risk/s or losses), and should be excluded from Tier 1 regulatory eligible capital.)</p> <p>(For example, regarding regulatory eligible Tier 2: Only a maximum of 45 percent of revaluation reserves arising from investment in equities, and only such hybrid debt instruments which meet specifies conditions (namely, they are unsecured, subordinated and fully paid up; they are not redeemable at the initiative of the holder or without the prior consent of the supervisory authority; they are available to participate in losses without the bank being obliged to cease trading; and, although the capital instrument may carry an obligation to pay interest that cannot permanently be reduced or waived, it should allow service obligations to be deferred where the bank could not support payment.) should qualify as Tier 2 regulatory eligible capital.)</p> <ul style="list-style-type: none"> • Require a bank, in relation to a capital instrument of the bank or of another bank, to impair its regulatory eligible capital in an amount equal to: <ul style="list-style-type: none"> - its investment therein (whether directly or indirectly, e.g., via a subsidiary); - its financing the purchase thereof (whether held directly or indirectly, e.g., via a subsidiary); - its provision of financing facilities for the purchase there for (whether directly or indirectly, e.g., via a subsidiary); - its provision of financing (whether directly or indirectly, e.g., via a subsidiary) against collateral thereof; or - its provision of financing facilities (whether directly or indirectly, e.g., via a subsidiary) against collateral thereof. • Develop and maintain updated, comprehensive and detailed principles, standards, guidance, prescriptions, statutory returns and supervisory work programs, inter alia based on and aligned with relevant pronouncements of the BCBS, for all key areas, including corporate governance, capital and capital management, and risk areas, which would enhance effectiveness, efficiency, consistency, and transparency of, and quality control over, supervision, thereby also enabling more effective challenging of banks by the supervisor. • Require banks to hold adequate regulatory eligible capital also against significant risk exposures: <ul style="list-style-type: none"> - other than credit risk; and - credit risk exposures which are not prudently captured by Basel I. • Prescribe that the shortfall in regulatory provisions, constituted by the difference, when a bank's regulatory required provisions exceed its IFRS credit impairment, does not constitute or qualify as Tier 1 core capital. • Perform, and require banks to perform, overall micro/bottom up and macro/top down stress testing, scenario analyses and simulation exercises in relation to all key areas, including risk areas, as a tool to provide forward-looking assessments of a bank's capacity (as constituted by its capital, liquidity and earnings) to withstand extreme but plausible macro-financial shocks. The results should be taken into account when establishing and reviewing (a bank's) policies, processes, limits, thresholds and benchmarks.
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	<ul style="list-style-type: none"> Consolidated, rationalize, logically order and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP6.
Principle 7	Risk management process. Supervisors must be satisfied that banks and banking groups have in place a comprehensive risk management process (including Board and senior management oversight) to identify, evaluate, monitor and control or mitigate all material risks and to assess their overall capital adequacy in relation to their risk profile. These processes should be commensurate with the size and complexity of the institution.
Essential criteria	
EC1	Individual banks and banking groups are required to have in place comprehensive risk management policies and processes to identify, evaluate, monitor and control or mitigate material risks. The supervisor determines that these processes are adequate for the size and nature of the activities of the bank and the banking group and are periodically adjusted in the light of the changing risk profile of the bank or banking group and external market developments. If the supervisor determines that the risk management processes are inadequate, it has the power to require a bank or banking group to strengthen them.
Description and findings re EC1	<p>The CBN's <i>Guideline for the Development of Risk Management Frameworks for Individual Risk Elements</i> (Ref BSD/DIR/CIR/VI/011) requires all banks to have adequate policies, approved by the board of directors, to manage and mitigate their risk exposures. The banks are also required to develop and implement appropriate systems and procedures to manage and control the risks in line with their risk profile.</p> <p>The banks' risk management frameworks have been assessed by CBN supervisors to ensure they are adequate for the size and nature of the banks' respective activities. In the course of onsite reviews, CBN supervisors evaluate risk management as part of the review of the control functions to confirm that policies are in place and are effective in managing and mitigating the institution's risk exposures. The assessment of banks' risk management frameworks is explained in section notes (both track 1 section notes, for the various significant activities, and track 2 section notes, on overall risk management). The assessors noted that the assessments contained in the section notes reflect CBN supervisors' view, which was driven by the supervisory process in reviewing banks' risk management policies and discussions with the risk management units/departments of banks to conclude the assessment. Where risk management policies are found to be ineffective, banks are recommended to implement remedial actions via supervisory letters. The assessors noted that supervisory letters addressed the issues and recommendations accordingly. From time to time, the CBN engages outside consultants, also in relation to bank regulation and supervision. Typically, such consultants are tasked also with capacity development of CBN staff.</p> <p>PS: The components of the legislative framework dealing with this topic (risk management) are scattered throughout the legislative framework, seemingly somewhat randomly, in different (types) of documents, while the relevant provisions do not all easily and logically fit together, thereby impeding legal certainty.</p>
EC2	The supervisor confirms that banks and banking groups have appropriate risk management strategies that have been approved by the board. The supervisor also confirms that the board ensures that policies and processes for risk-taking are developed, appropriate limits are established, and senior management takes steps necessary to monitor and control all material risks consistent with the approved strategies.
Description and findings re EC2	<p>Banks have been required to submit their risk management frameworks, which include risk appetite and risk management policies to their Boards for approval.</p> <p>During onsite examinations, CBN supervisors confirm that appropriate limits are established with emphasis on both the characteristics and performance of the risk management control functions including the effectiveness of the board and senior management. The assessment process involves reviews over the policies and limits on risk taking activities as well as boards' papers and discussion minutes. The assessment would then be reflected in the section notes on risk management (both track 1 and track 2). The selected sample of track 1 review notes</p>

	(e.g., on lending activities and cross-border activities of two banks) reflected an explicit assessment of the appropriateness of risk policies and limits. Further discussion with CBN supervisors responsible for generating the review notes confirmed that the assessment was based on CBN supervisors' engagement with the board members, to understand the risk appetites set for the banks to ensure the policies developed and limits set are consistent with the appetites.
EC3	The supervisor determines that risk management strategies, policies, processes and limits are properly documented, reviewed and updated, communicated within the bank and banking group, and adhered to in practice. The supervisor determines that exceptions to established policies, processes and limits receive the prompt attention of and authorization by the appropriate level of management and the Board where necessary.
Description and findings re EC3	<p><i>The Risk Management Assessment Criteria Guide</i> which forms part of the <i>RBS Framework</i> details some of the factors used by the CBN supervisors in assessing both the characteristics and performance of the risk management control functions including the board and senior management oversight, and make appropriate recommendations, with respect to:</p> <ul style="list-style-type: none"> • the adequacy of the mandate of the risk management function and the extent to which the function's mandate is communicated within the institutions; • the appropriateness of the organizational structure of the function in terms of status and authority of the function and the extent to which the function is independent of day-to-day management of risks; • adequacy of the function's resources and appropriateness of its collective qualifications and competencies for carrying out its mandate; • adequacy of risk management's methodology and practices; • adequacy of policies and practices used to report identified weaknesses and to monitor and follow up on their resolution; and • The effectiveness of senior management and board oversight. <p>In the course of onsite examinations, CBN supervisors review the terms of reference of risk management functions, the organization charts, background of the risk management staff and documents on the risk management methodology used to derive conclusion to the above questions. The review was based on relevant documents, such as the organization chart and CVs of the staff, and such documents were included in the CBN supervisors' working papers (as observed by the assessors). The working papers also included notes on CBN supervisors' discussions with the board members (which were filed with the relevant section notes), in addition to reviewing the boards' papers and minutes, to support the assessments. The legal and regulatory framework does not impose a requirement that the approval level for risk exposures should be commensurate with the size and risk of the resulting exposure, nor that material risk exposures (say, exceeding a prescribed percentage of a bank's capital) should be decided by the bank's senior management or even a higher level body (such as the board risk committee or the board itself.)</p>
EC4	The supervisor determines that senior management and the board understand the nature and level of risk being taken by the bank and how this risk relates to adequate capital levels. The supervisor also determines that senior management ensure that the risk management policies and processes are appropriate in the light of the bank's risk profile and business plan and that they are implemented effectively. This includes a requirement that senior management regularly reviews and understand the implications (and limitations) of the risk management information that it receives. The same requirement applies to the board in relation to risk management information presented to it in a format suitable for board oversight.
Description and findings re EC4	<p>The CBN supervisors are required to assess the effectiveness of the banks' board and senior management oversight functions in order to determine whether:</p> <ul style="list-style-type: none"> • Policies and limits are proactively updated in response to changes in the industry and in the banks' strategies, business activities and risk tolerance; • Risk policies and limits are integrated into day-to-day business activities and with the

	<p>institution's strategies, capital and liquidity management policies;</p> <ul style="list-style-type: none"> • The risk management functions monitor risk positions against approved limits and ensure that material breaches are addressed on a timely basis; • The risk management functions use risk measurement and monitoring tools that are appropriate to provide early warning indicators of adverse trends and conditions, proactively analyses these trends and conditions, and follows up to ensure that they are addressed on a timely basis; • The risk management functions proactively and effectively address risk management weaknesses identified as a result of internal or external events, or by other control functions; and • the risk management functions provide regular and comprehensive reports to the board (or its committee) and senior management on the effectiveness of the banks' risk management processes and ensures that significant issues are escalated to senior management and the board on a timely basis. As mentioned in BCP7 EC3, above, in the course of onsite examinations, CBN supervisors review the terms of reference of risk management functions, the organization charts, background of the risk management staff and documents on the risk management methodology used to derive conclusion to the above questions. CBN supervisors also engage with the board members, in addition to reviewing the boards' papers and minutes, to support the assessments.
EC5	<p>The supervisor determines that the banks have an internal process for assessing their overall capital adequacy in relation to their risk profile, and reviews and evaluates bank's internal capital adequacy assessments and strategies. The nature of the specific methodology used for this assessment will depend on the size, complexity and business strategy of a bank. Non-complex banks may opt for a more qualitative approach to capital planning.</p>
Description and findings re EC5	<p>To date the CBN has not implemented the Basel II capital accord (with its Pillar II requirements for banks to have in place an Internal Capital Adequacy Assessment Process – ICAAP, in relation to its risk profile), though it is planning to do so in the foreseeable future. However, under the <i>RBS Framework</i>, banks' capital and earnings are assessed in arriving at a bank's overall composite risk rating. In assessing capital, consideration is given to its adequacy, capital management and board/management oversight functions. Factors that are considered, among others, include:</p> <ul style="list-style-type: none"> • level of capital relative to required regulatory minimum, and banks' risk profile; • adequacy of capital relative to planned business activities; • extent to which capital management is enterprise-wide and supported by sufficient authorities; and • extent to which capital planning is integrated into strategic and business plans. <p>In assessing the capital adequacy during on-site examination, CBN supervisors run through the capital calculation and check against the respective minimum regulatory capital levels i.e., either 10 percent or 15 percent (checking of the capital calculation is normally done offsite using the data submitted via e-FASS). The assessors confirmed, in discussions with CBN supervisors, that the monitoring of the regulatory submission of capital positions is carried out on a monthly basis, as the banks' submit monthly capital numbers via e-FASS. CBN supervisors also review the capital management documents (e.g., banks' internal capital policy) to determine whether the capital management is a bank-wide activity, and review the boards' and senior managements' minutes and discussion notes on business strategies to see that capital considerations are in place when developing the strategies. The assessors noted that discussion notes and minutes of the meetings with the banks' boards and senior management on the capital position formed part of working papers, together with copies of capital management policies. For three banks, these documents were filed together with section notes on capital adequacy review notes.</p> <p>CBN should consider the selective implementation, in the interim, of Basel II principles in order to strengthen risk and capital management framework of the Nigerian banks.</p>

	To ensure effective implementation of the principles, CBN needs to re-look at its supervisory resources to ensure competent set of supervisors are in place.
EC6	Where banks and banking groups use models to measure components of risk, the supervisor determines that banks perform periodic and independent validation and testing of the models and systems.
Description and findings re EC6	<p>Although, the use of risk models (to provide early warning indicators of adverse risk trends) is not mandatory, some banks (particularly the foreign banks) use them. There are no supervisory requirements for independent validation and testing of these models. Furthermore, the CBN has not built enough expertise to review banks' validation of the models.</p> <p>Moving forward, CBN should start preparing itself and the supervisors for the use of models to measure components of risk by obtaining or developing the capacity and capabilities to develop guidance on minimum standards for the use of such models. Emphasis should be given to the need for independent validation and back-testing while the CBN supervisors need to have the capacity and capabilities effectively to challenge the output generated by such the models.</p>
EC7	The supervisor determines that bank and banking groups have adequate information systems for measuring, assessing and reporting on the size, composition and quality of exposures. It is satisfied that these reports are provided on a timely basis to the board or senior management and reflect the bank's risk profile and capital needs.
Description and findings re EC7	<p>As per CBN's <i>Guideline for the Development of Risk Management Frameworks for Individual Risk Elements</i>, banks are required to develop and implement appropriate and effective information systems for reporting and procedures to manage and control risks in line with risk management policies. Banks are also required to submit reports on the size and quality of their exposures for board and senior management consideration.</p> <p>While assessing the effectiveness of the risk management functions, CBN supervisors assess the adequacy of the information systems and ensure that significant weaknesses are escalated to senior management and the board on a timely basis at exit discussions and via the supervisory letter issued to banks following on-site examinations. The recommendations would then be monitored by CBN supervisors on an on-going basis. In assessing the adequacy of the risk information being escalated to the banks' boards and senior managements, CBN supervisors review boards' and senior managements' information pack. CBN supervisors then determine whether the information contents are sufficient or not for boards and senior managements to make informed decisions. Any shortfalls are discussed with the banks and serious gaps are highlighted in the supervisory letters. In a particular case, the assessors found that the issue of information flow regarding overseas operations was highlighted in one of the section notes—from a discussion with the relevant CBN supervisors it transpired that the issues were resolved after several follow-ups and after a supervisory letter had been issued.</p>
EC8	The supervisor determines that banks have policies and processes in place to ensure that new products and major risk management initiatives are approved by the board or a specific committee of the board.
Description and findings re EC8	CBN supervisors determine whether the risk management framework deals appropriately with the issues of new products and major risk initiatives, which should require approval by the banks' boards or their relevant committees. This process is done via reviews of banks' policies on new products and banks' board papers to see appropriate deliberations take place during the approval process of the new products by banks' boards. Notwithstanding, CBN must be notified of the introduction of new products and CBN has the right to disallow any new products to be introduced in the market if in the CBN supervisors' opinion, the banks do not have sufficient risk management capabilities to manage the products or CBN supervisors themselves are not fully familiar with the potential risks emanating from these products. The assessments of the banks' notifications for new products are conducted offsite. CBN offsite teams assess the capabilities via the risk management section notes prepared by the onsite examiners and further discussions with onsite examiners are carried out, if the offsite analysts

	<p>feel that further clarifications are needed. If the offsite analysts are of the view that the banks' risk management capabilities are not able to manage the new products, banks are advised to reconsider introducing the products. The assessors reviewed a sample of notifications of new products by banks, and noted several instances where CBN supervisors required banks not to introduce proposed new products, all of which related to derivative products.</p>
EC9	<p>The supervisor determines that banks and banking groups have risk evaluation, monitoring and control or mitigation functions with duties clearly segregated from risk-taking functions in the bank, and which report on risk exposures directly to senior management and the board.</p>
Description and findings re EC9	<p>As per CBN's <i>Guideline for the Development of Risk Management Frameworks for Individual Risk Elements</i>, banks are required to set-up a dedicated units to take-up the risk management functions and should be led by a chief risk officer.</p> <p>In the course of supervisory assessment, CBN supervisors assess the appropriateness of the organizational structure of the risk management functions in terms of status and authority, and the extent to which the functions are independent of day-to-day risk taking activities. The reporting lines are also assessed to determine that the risk management reports are channeled to the board via board risk committees. The process involves reviewing the banks' organizational charts and tracing the reporting lines of the risk management functions. From the organization charts, CBN also determines the level of the chief risk officers among the senior management teams to determine their status and hence, conclude on their stature vis-à-vis risk taking units. A review of a sample of Knowledge of Business (KoB) documents for two banks revealed notes on the organizational structure—the assessors' subsequent discussion with the relevant CBN supervisors on the matter indicated that the notes on the organizational chart related to a determination of the reporting line (in assessing independence) as well as the status of the risk management head and the risk management department.</p>
EC10	<p>The supervisor issues standards related to, in particular, credit risk, market risk, liquidity risk, interest rate risk in the banking book and operational risk.</p>
Description and findings re EC10	<p>The CBN issued the <i>Guidelines for the Development of Risk Management Framework for Individual Risk Elements in Nigerian Banks</i> in 2007. The Guidelines addressed the key elements of the risk management process, risk management structure, monitoring and control of risks, risk management system review mechanism and supervisory framework.</p> <p>The <i>Guidelines</i> do not address in sufficient detail some of the critical risk categories in the CBN Risk Based Supervisory Framework, such as country and transfer risk, market risks, operational risk and IRRBB. In the absence of comprehensive and detailed prudential principles, standards and guidance, assessment of bank's risk exposures and risk management is largely dependent on the professional judgment of examiners.</p>
Additional criteria	
AC1	<p>The supervisor requires larger and more complex banks to have a dedicated unit(s) responsible for risk evaluation, monitoring and control or mitigation for material risk areas. The supervisor confirms that this unit (these units) is (are) subject to periodic review by the internal audit function.</p>
Description and findings re AC1	<p>The CBN's <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements</i> stipulates that the risk management structure in banks should contain at least the board of directors, the board risk management committee, senior management, and the risk management functions. The risk management function ensures effective management of significant risks inherent in the operations of banks. As mentioned earlier, the Guidelines also require banks to have a dedicated unit responsible for risk management functions. As with other units, it is mandatory that the risk management function is periodically reviewed by internal audit. These requirements are imposed on all banks, regardless of their sizes and complexities.</p> <p>During on-site examinations, CBN supervisors assess and determine that the guidelines' expectations are implemented. The process of validation involves review of the reporting lines for risk management functions (via organization charts – as per review explained in EC9). It</p>

	also involves reviews of the terms and references of the board risk management committees, executive risk management committees and the risk management units/departments themselves (as explained in EC3)
AC2	The supervisor requires banks to conduct rigorous, forward-looking testing that identifies possible events or changes in market conditions that could adversely impact on the bank.
Description and findings re AC2	Starting from June 2012, CBN has provided standards stress test templates (developed by IMF) to be run by banks (the shocks applied on credit, market and liquidity risks) and banks are required to submit the results of these exercises on six-monthly basis. Currently, the submissions are to the Financial Surveillance Division (FSD) of Financial Policy & Regulation Department for macro surveillance purpose. Moving forward, FSD plans to share the information on the results of individual banks with CBN supervisors as supervisory tools to challenge the robustness of banks risk identification, measurement, control and monitoring functions. On a bi-monthly basis, the Director of Bank Supervision makes a presentation on the financial stability of the banking system (based on the results of the stress tests performed by the FPRD) to the Monetary Policy Committee.
AC3	The supervisor requires banks and banking groups to have in place appropriate policies and processes for assessing other material risks not directly addressed in the subsequent CPs, such as reputational and strategic risks.
Description and findings re AC3	Starting from June 2012, CBN has provided standards stress test templates to be run by banks (the shocks applied on credit, market and liquidity risks) and banks are required to submit the results of these exercises on six-monthly basis. CBN's supervisors will use these results to identify sources of vulnerabilities for any particular banks.
Assessment of Principle 7	Largely Compliant
Comments	<p>The CBN's <i>Guideline for the Development of Risk Management Frameworks for Individual Risk Elements</i> generally governs a bank's risk taking and risk exposures—however, it is overarching and generic, and not specific and detailed, implying that there are important gaps and shortcomings in the legal, regulatory and supervisory framework relating to a bank's risk management. The CBN applies a risk-based approach to supervision, as provided for in the CBN's <i>RBS Framework</i>, including to off-site and on-site supervision. Accordingly, the CBN assesses a bank's risk management (which should be under the oversight of the board of directors and senior management) by gaining an understanding of the risk management policies, strategies, processes and risk appetite/aversion, thereupon assesses the identification, evaluation, monitoring and controlling or mitigating of all material risks, and then assesses the bank's overall capital adequacy in relation to the bank's risk profile. The CBN also assesses whether these processes are commensurate with the size and complexity of the institution.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Develop and maintain updated comprehensive and detailed principles, standards, guidance, prescriptions, statutory returns, supervisory work programs, inter alia based on and aligned with relevant pronouncements of the BCBS, for all significant existing and emerging risks (for example, country and transfer risk, market risk, operational risk and IRRBB), which would enhance effectiveness, efficiency, consistency, and transparency of, and quality control over supervision, thereby also enabling more effective challenging of banks by the supervisor. • Prescribe that the approval level for risk exposures should be commensurate with the size and risk of the resulting exposure, and significant risk exposures (say, exceeding a prescribed percentage of a bank's capital) should be decided by the bank's senior management or even a higher level body (such as the board risk committee or the board itself.) • Consider the selective implementation, in the interim, of Basel II principles to ensure the elements of risk and risk management are embedded in banks' capital management

	<ul style="list-style-type: none"> • Develop and issue guidance to govern the application of internal risk management model/s, to ensure that sound principles and practices are applied, and that the measurement and assessment of significant existing and emerging risks yield reasonably prudent outcomes. • Perform, and require banks to perform, (bottom up) stress testing and scenario analysis of all significant existing and emerging risks, to monitor the impact of extreme but plausible shocks on a bank's earnings and capital. Consider, and require banks to consider, these results when establishing and reviewing (the bank's) policies, processes, limits, thresholds and benchmarks. • Require a bank with significant existing risk exposure to hold an appropriate (in other words, in relation to the threat which a bank's significant existing risk exposure poses to economic value) amount of regulatory eligible capital against such a significant exposure. • Reconsider the quality and quantity of supervisory resources required to enable the regulatory and supervisory authorities to discharge their responsibilities effectively, given also the regulatory reform agenda, such as the implementation of IFRS, Basel II and Basel III. • In line with the HRD plan for specialist career streams, engage specialists to support the regulatory and supervisory functions in addressing specialist and complex issues in the areas of capital and capital management, corporate governance, risk and risk management, credit risk and credit risk management, country and transfer risk and country and transfer risk management, market risk and market risk management, liquidity risk and liquidity risk management, operational risk and operational risk management, accounting and auditing, information technology, and project management, thus enabling the supervisory authority more effectively to challenge the banks and all related stakeholders, including (boards of) directors, executive management (including the CEO, COO, CFO, CRO, CIA, CIO, CCO, etc) and external auditors. (Effective challenge by the supervisor implies that the decision-making in the banking system consequently is improved. Inability by the bank supervisor effectively to challenge banks, and all related stakeholders, would imply inability by the bank supervisor to add value by means of bank supervision, which, in turn, would imply that the bank supervisor detracts value from the system and is superfluous.) • Consolidated, rationalize, logically arrange and simplify components of the legal and/or regulatory framework which deal with issues pertinent to BCP7.
Principle 8	Credit risk. Supervisors must be satisfied that banks have a credit risk management process that takes into account the risk profile of the institution, with prudent policies and processes to identify, measure, monitor and control credit risk (including counterparty risk). This would include the granting of loans and making of investments, the evaluation of the quality of such loans and investments, and the ongoing management of the loan and investment portfolios.
Essential criteria	
EC1	The supervisor determines, and periodically confirms, that a bank's Board approves, and periodically reviews, the credit risk management strategy and significant policies and processes for assuming, identifying, measuring, controlling and reporting on credit risk (including counterparty risk). The supervisor also determines, and periodically confirms, that senior management implements the credit risk strategy approved by the Board and develops the aforementioned policies and processes.
Description and findings re EC1	The credit policies of banks are required to be duly approved by their board and should be reviewed at least every three years (as per <i>Section 3.1 of the Prudential Guidelines</i>). Banks are also expected to have credit risk management procedures that are holistic. At the minimum, they should cover formulation of overall credit strategies, credit originations, administration, analyses, measurement and controls. They should also include the risk review processes and procedures for managing problem credits (requirement under <i>Section 5.1.1 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>). In addition, the responsibilities of the senior management,

	<p>amongst others, are highlighted in the <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>:</p> <ul style="list-style-type: none"> • <i>Section 4.4.1</i>: Senior managements are responsible for the implementation of risk policies and procedures in line with the strategic directions and risk appetite specified by the boards; and • <i>Section 4.2.3.2</i>: Senior managements are responsible for the development and implementation of procedures and practices that translate the boards' goals, objectives and risk tolerances into operating standards that are well understood by across the banks. <p>Banks also generate regular reports which cover, amongst others, the compliance with policies and the limit set by the Board and senior management (as required under <i>Section 6.3 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>).</p> <p>As part of the review of the effectiveness of the control functions, CBN supervisors determine during on-site examinations that banks' boards approve and periodically review the credit policies. CBN supervisors indicated to the assessors that the latest version of a bank's credit policies was obtained, and the dates of the documents were noted when reviewing the documents. CBN supervisors also confirm during on-site examinations that senior managements implement the policies as approved by the boards. The assessments were then reflected in the section notes (both track 1 and track 2)—the assessors confirmed these assessments during a scrutiny of two samples of section notes of two banks (both samples related to track 1 and dealt with, respectively, treasury and lending.)</p> <p>The requirement on frequency of credit risk policies reviews (once in every three years) may not be frequent enough, given that credit risk is the most significant risk element in most of the banks in Nigeria and the current rapid changes in surrounding risk environment. CBN should also prescribe the minimum frequency of reporting by banks and to whom the report should be submitted to ensure credit risks are contained within the bank's risk appetite at all times.</p>
EC2	<p>The supervisor requires, and periodically confirms, that such policies and processes establish an appropriate and properly controlled credit risk environment, including:</p> <ul style="list-style-type: none"> • a well documented strategy and sound policies and processes for assuming credit risk; • well defined criteria and policies and processes for approving new exposures as well as renewing and refinancing existing exposures, identifying the appropriate approval authority for the size and complexity of the exposures; • effective credit administration policies and processes, including continued analysis of a borrower's ability and willingness to repay under the terms of the debt, monitoring of documentation, legal covenants, contractual requirements and collateral, and a classification system that is consistent with the nature, size and complexity of the bank's activities or, at the least, with the asset grading system prescribed by the supervisor; • comprehensive policies and processes for reporting exposures on an ongoing basis; • comprehensive policies and processes for identifying problem assets; and • prudent lending controls and limits, including policies and processes for monitoring exposures in relation to limits, approvals and exceptions to limits.
Description and findings re EC2	<p>The senior managements of banks are responsible to ensure those banks' risk policies, appetites, and tolerances are well documented (as required under <i>Section 4.2.3.2 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>). Banks are also required to have a documented framework for defining and managing credit risk concentrations in relation to capital and total assets (<i>Section 3.3 (b) of Prudential Guideline</i>). In addition, banks are also required to ensure that the credit policies address the different types of credit facilities offered by the banks e.g., project financing, real estate financing, agricultural financing and SME financing. The policies should include loan administration, disbursement and appropriate monitoring mechanism (<i>Sections 3.1, 6.1, 7.1, 8.1, 9.1 and 11.1 of Prudential Guidelines</i>). Banks are also required to put in place policies on credit portfolio plan as part of their credit risk management to be approved</p>

	<p>by their boards. The policies are required to be in line with the <i>Standard Industry Classification (SIC)</i>, released by CBN and must specify the target portfolio size as well as portfolio distribution by industry, economic sectors and business units (<i>Section 3.3 (c), (d), (e) & (f) of the Prudential Guidelines</i>). On the other hand, the credit administration functions are expected to perform the functions of credit documentation, monitoring and maintenance of credit files, collateral and security documents as well as ensuring that loan disbursement and repayment adheres to banks' internal policies. (<i>Section 5.1.4.1 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>) Banks are also required to put in place an internal rating policy/model and conduct internal credit ratings for all counter parties/obligors and sectors. Factors to be considered include character and capacity of the obligor to pay or meet contractual obligations, current exposures to the counter party/obligor and its likely future developments, credit history of the counter party/obligor and the likely recovery ratio in case of default obligations (<i>Section 3.17 of Prudential Guidelines</i>). <i>Section 6.1, 6.2 and 6.3 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i> require banks to establish risk monitoring processes to evaluate the performance of the banks' risk strategies, policies and procedures in mitigating individual risks being encountered. The monitoring processes are expected to cover the banks' exposure to individual risk elements, ensuring and assessing the adequacy of each risk measurement systems. At minimum, the following reports are expected to be generated on a regular basis:</p> <ul style="list-style-type: none"> • summaries of banks' exposure to individual risk elements; • report of compliances with policies and limits set by boards and management as well as regulatory requirements; and • summaries of findings of risk reviews of policies and procedures relating to individual risk elements as well as the adequacy of risk measurement systems, including any findings of internal/external auditors or consultants. <p>Banks are also expected to establish a system that helps identifying problem loans ahead of time when there may be more options available for remedial measures. (<i>Section 5.1.6.1 of The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i>) In addition, <i>The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Bank</i> prescribe that:</p> <ul style="list-style-type: none"> • the banks' internal control structure should ensure the effectiveness of the processes relating to the management of individual risk elements. (<i>Section 7.1</i>); • the control processes should include determining and adhering with banks' overall risk appetites and exposure limits in relation to the risk strategies. (<i>Section 7.5</i>); • risk limits for business units should be compatible with banks' strategies, risk management systems and risk tolerance. (<i>Section 7.6</i>); and • breaches or exceptions to limits should be promptly reported to appropriate authorities, using appropriately set of policies on reporting procedure for breaches and actions to be taken. (<i>Section 6.5</i>). <p>During the onsite review of significant lending operations, CBN supervisors assess boards and senior management oversight of credit risk management systems vis-à-vis the above requirements, which form the basis of the risk rating accorded. Assessors scrutinized such an assessment during a review of a sample of section notes on lending activity of a local bank.</p>
EC3	The supervisor requires, and periodically confirms, that banks make credit decisions free of conflicts of interest and on an arm's length basis.
Description and findings re EC3	<p><i>Section 18 of BOFI Act</i> stipulates that:</p> <ul style="list-style-type: none"> • managers and officers of banks are prohibited from having personal interest in any credit facility unless such interest is declared; grant credit facilities unless authorized in line with the policies of the bank; and benefit as a result of a credit facility granted by the bank; and • a director of any bank who either directly or indirectly has an interest in the grant of a credit facility is required to declare the nature of his interest.

	<p>(The draft <i>Revised Codes of Corporate Governance</i> also requires banks' board members that have interest in the credit facilities to abstain from any decision making process with regard to those facilities. Such legal requirement ensures appropriate financial system that is free of conflict of interest. However, the code is still at a draft stage.)</p> <p>During onsite examinations, CBN supervisors determine whether banks comply with the above requirements—assessors confirmed this during a discussion with CBN supervisors.</p>
EC4	The supervisor has full access to information in the credit and investment portfolios and to the bank officers involved in assuming, managing, controlling and reporting on credit risk.
Description and findings re EC4	<i>Section 33 of CBN Act 2007</i> and <i>Section 31(2) (b) (c) of BOFI Act</i> provide the legal basis for CBN supervisors' access to information on banks' credit and investment portfolios.
Additional criteria	
AC1	The supervisor requires that the credit policy prescribes that major credit risk exposures exceeding a certain amount or percentage of the bank's capital are to be decided by the bank's senior management. The same applies to credit risk exposures that are especially risky or otherwise not in line with the mainstream of the bank's activities.
Description and findings re AC1	<p>There is no specific provision in law or regulation requiring banks requiring the following credits to be decided by the bank's senior management:</p> <ul style="list-style-type: none"> • major credit risk exposures exceeding a certain amount or percentage of the bank's capital; and/or • credit risk exposures that are especially risky or not in line with the mainstream of the bank's activities.
AC2	The supervisor determines that banks have in place policies and processes to identify, measure, monitor and control counterparty credit risk exposure, including potential future exposure sufficient to capture the material risks inherent in individual products or transactions. These processes should be commensurate with the size or complexity of the individual bank.
Description and findings re AC2	<p><i>Section 3.3 of Prudential Guideline</i> spells out that banks are required to put in place policies, systems and controls approved by their boards to identify, measure, monitor and control credit risk exposures such as:</p> <ul style="list-style-type: none"> • significant exposures to an individual counterparty or group of related counterparties; • credit exposures to counterparties in the same economic sectors or geographies; • credit exposures to counterparties whose financial performance is dependent on the same activities or commodities; and • indirect credit exposures arising from a bank's credit risk mitigation activities (e.g., exposure to a single collateral type or to credit protection provided by a single counterparty). <p>There is no specific provision in the law or regulations, which requires a bank to consider the potential future exposure of a counterparty credit risk exposure to capture the material risks inherent in individual products or transactions.</p>
AC3	The supervisor determines that banks have policies and processes to monitor the total indebtedness of entities to which they extend credit.
Description and findings re AC3	<p>In the credit assessment process for granting of credit facilities, banks are required to check the prospective credit counter parties' exposures with other banks against credit bureau information (currently CBN and three other private operators provide such services). At minimum, banks are required to check against CRMS (credit bureau system operated by CBN) and two of the three privately-run systems.</p> <p>In the course of on-site examination, CBN supervisors assess banks' compliance against the above requirement to ensure banks have total information on the potential counter parties' credit exposures before any credit decision is made.</p>

Assessment of Principle 8	Largely compliant
Comments	<p>The legal and regulatory framework provides that a bank has adequate credit risk management policies, strategies and processes, (including to identify, measure, monitor, and control credit risk, including counterparty risk) commensurate with its credit risk profile. This includes the granting of loans and making of investments, the evaluation of the quality of such loans and investments, and the ongoing management of the loan and investment portfolios.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Require that a bank’s board regularly reviews the CRM strategy, significant policies and processes, while ensuring that these are consistent with the risk appetite. • Prescribe that the approval level for credit exposures should be commensurate with the size and risk of the resulting credit exposure. • Prescribe that major credit risk exposures exceeding a certain amount or percentage of a bank’s capital and especially risky credit risk exposures should be decided by the bank’s senior management or even a higher level body (such as the board credit committee, or even the board itself.) • Prescribe that a bank should consider the potential future exposure of a counterparty credit risk exposure to capture the material risks inherent in individual products or transactions. <p>See BCP6 and BCP7 for related generic recommendation/s.</p>
Principle 9	Problem assets, provisions and reserves. Supervisors must be satisfied that banks establish and adhere to adequate policies and processes for managing problem assets and evaluating the adequacy of provisions and reserves.
Essential criteria	
EC1	Laws, regulations or the supervisor require banks to formulate specific policies and processes for identifying and managing problem assets. In addition, laws, regulations or the supervisor require periodic review by banks of their problem assets (at an individual level or at a portfolio level for credits with homogenous characteristics) and asset classification, provisioning and write-offs.
Description and findings re EC1	<p>Banks are required to have policies approved by the boards for the management of credit risks and adequate credit administration procedures to ensure the timely detection and management of problem assets and recovery of past due loans. Banks are required to review their credit portfolio continuously (at least on quarterly basis) with a view of identifying any problem assets. The reviews should systematically and realistically classify banks’ credit exposures based on the perceived risks of default. The assessment is based on criteria, which include repayment performance, borrowers’ repayment capacity on the basis of current financial condition and net realisable value of collateral. A credit facility is deemed to be nonperforming when interest or principal is due and unpaid for 90 days or more. An NPL is classified as:</p> <ul style="list-style-type: none"> • Substandard—when, inter alia, unpaid principal and/or interest remain outstanding for more than 90 days, but less than 180 days. Interest is required to be suspended and a 10 percent provision is required to be raised. • Doubtful— when, inter alia, unpaid principal and/or interest remain outstanding for more than 180 days, but less than 360 days. Interest is required to be suspended and a 50 percent provision is required to be raised. • Loss— when, inter alia, unpaid principal and/or interest remain outstanding for more than 360 days. Interest is required to be suspended and a 100 percent provision is required to be raised. <p>(Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3 and 12)</p>

	<p>CBN supervisor also periodically reviews (via on-site examinations) bank's classification of credits, and reserves the right to object to the classification of any credit facility and to prescribe the classification it considers appropriate. Assessors noted in a supervisory letter an instance where the CBN supervisors were not satisfied with the provisioning level for a loan and required the bank to increase the provisions.</p>
EC2	<p>The supervisor confirms the adequacy of the classification and provisioning policies and processes of a bank and their implementation; the reviews supporting this opinion may be conducted by external experts.</p>
Description and findings re EC2	<p>During on-site examinations of banks, the CBN supervisors assess the adequacy of the classification and provisioning policies as well as the relevant processes of banks. (See also BCP9 EC1, above.)</p> <p><i>Section 12.14 of Prudential Guidelines</i> empowers CBN supervisors to require banks to require additional provision when they believe that there are excessive concentration risks, or has industry knowledge of a delinquent obligor and other subjective factors. Some of the conditions that CBN considers to require banks to make additional provision include:</p> <ul style="list-style-type: none"> • huge concentration in banks' credit portfolios; • high number of NPLs or watch list; • adverse macro-economic developments affecting the industry to which the bank is exposed; and • poor board oversight and insider dealings. <p>Upon discovery of such scenario, CBN supervisors will raise the issue via supervisory letters and in the examination reports and expect the banks to increase the level of provisions for those particular cases. (See BCP9 EC1, above)</p> <p>Up to now, CBN supervisors have not yet relied on the work of external experts in assessing the level of additional provisions to be imposed on banks.</p>
EC3	<p>The system for classification and provisioning takes into account off-balance sheet exposures.</p>
Description and findings re EC3	<p>Off balance sheet exposures are taken into full consideration in the classification and provisioning of banks' assets, as prescribed in the Prudential Guidelines. A CBN supervisor explained that the off-site surveillance team analyze, by means of e-FASS, monthly submissions of provisioning information and specifically determine whether off-balance sheet exposures were considered.</p> <p><i>Section 12.11 of the Prudential Guidelines</i> requires banks to carry out periodic appraisal of off-balance-sheet with a view to determining the extent of loss a bank may likely sustain. The Prudential Guidelines indicate that the factors to be considered include the date the liability was incurred, expiry date, security pledged, performance of other facilities underwritten by the customer, e.g., loan and advances and their perceived risks.</p>
EC4	<p>The supervisor determines that banks have appropriate policies and processes to ensure that provisions and write-offs reflect realistic repayment and recovery expectations.</p>
Description and findings re EC4	<p><i>Section 3.1 of Prudential Guideline</i> requires banks to have policies, approved by the boards, for the management of credit risks as well as adequate credit administration procedures to ensure the timely detection and management of problem assets, and recovery of past due loans. Meanwhile, <i>Section 12.1 and 12.2 of Prudential Guideline</i> require banks to use objective and subjective criteria contained in the guideline to classify credits as performing or nonperforming in order to identify deteriorating assets for subsequent monitoring.</p> <p>During onsite examinations, CBN supervisors review banks' classification of risky assets to confirm the adequacy of the provision for loan losses at least meets the regulatory requirements as prescribed by the guideline. The assessors' review of a sample of section notes on lending activity of a local bank revealed that the review included a conclusion. The assessment is based on factors such as repayment performances, borrowers' repayment capacities on the basis of current financial conditions and net realisable values of collaterals.</p>

	The supervisory review process involves reviewing samples of credit files for problematic exposures and based on the information from the files (complemented by the supervisory knowledge), CBN supervisors determine the adequacy of provisions. If the CBN supervisors are of the view that the provisioning is not sufficient, banks are required to provide additional provisions on those particular exposures. Further evidentiary support of the existence of process was found in the fact that the conclusion was supported by a list (in an appendix) of the top risky assets which had been sampled by the CBN supervisors.
EC5	The supervisor determines that banks have appropriate policies and processes, and organizational resources for the early identification of deteriorating assets, for ongoing oversight of problem assets, and for collecting on past due obligations.
Description and findings re EC5	During onsite examinations, CBN supervisors review banks' policies, processes and organisational resources to determine the appropriateness of the processes for early identification of deteriorating assets, ongoing oversight of problem assets, and collections/recoveries activities of problematic exposures. The assessors noted that the working papers, supporting the section notes on the lending activities of a local bank, contained a description of the credit process (which included the risk identification process of problematic loans). Also included in the documentation was an analysis on the strength of the human resources in the lending activities, including those in charge of identification of problematic loans.
EC6	The supervisor is informed on a periodic basis, and in relevant detail, or has access to information concerning the classification of credits and assets and provisioning.
Description and findings re EC6	In terms of <i>Circular on Monthly Submission of Credit Portfolio Classification</i> , banks are required to submit, on a monthly basis, information on classification of credit exposures. The information is provided in detail and analyses classifications on several bases e.g., customers, loan types, sectors, regions, top 50 borrowers, location and business lines. Banks are also statutorily required to submit quarterly return on classification of credits.
EC7	The supervisor has the power to require a bank to increase its levels of provisions and reserves and/or overall financial strength if it deems the level of problem assets to be of concern.
Description and findings re EC7	<i>Section 12.14 of the Prudential Guidelines</i> requires banks to increase their level of provisioning if the existing provisioning amount is deemed to be inadequate, following onsite examination of banks or when CBN supervisors are of the opinion that based on the banks' portfolio analysis, there is excessive concentration risks, or has industry knowledge of a delinquent obligor and other subjective factors. CBN supervisors have, on several occasions, required banks to beef up their provisions to acceptable levels. Where there are concerns on banks' asset quality, the PCA measures detailed in <i>The Supervisory Intervention Framework</i> spell out the regulatory actions to be taken.
EC8	The supervisor assesses whether the classification of the credits and assets and the provisioning is adequate for prudential purposes. If provisions are deemed to be inadequate, the supervisor has the power to require additional provisions or to impose other remedial measures.
Description and findings re EC8	As explained earlier, <i>Section 12.14 of the Prudential Guidelines</i> allow CBN supervisors to require that additional provisions be raised by banks. CBN supervisors conduct regular review on the credit portfolio of banks to ensure that the classification of the loans and the provisioning is adequate for prudential purposes and there are occasions where CBN supervisors exercise this power. If, during supervisory review process of samples of credit files for problematic exposures, the CBN supervisors are of the view that the provisioning is not sufficient, banks are required to provide additional provisions on those particular exposures. (See also BCP9 EC1, above)
EC9	The supervisor requires banks to have appropriate mechanisms in place for periodically assessing the value of risk mitigants, including guarantees and collateral. The valuation of collateral is required to reflect the net realizable value.
Description and findings re EC9	<i>Section 12.13 of the Prudential Guidelines</i> provides for process of credit adjustment in loan provisioning to encourage banks to utilise more credit enhancement and mitigation strategies.

	<p>Due consideration is given to the quality and realizability of underlying collaterals pledged. Among others, collateral is expected to display the following characteristics to be considered:</p> <ul style="list-style-type: none"> • must be perfected; • must be realisable with no restrictions on sale; • must be regularly valued by way of a transparent method of valuation; and • all documentation used in collateralised transactions must be binding on all parties and legally enforceable in all jurisdictions.
EC10	Laws, regulations or the supervisor establish criteria for assets to be identified as impaired, e.g., loans are identified as impaired when there is reason to believe that all amounts due (including principal and interest) will not be collected in accordance with the contractual terms of the loan agreement.
Description and findings re EC10	<p><i>Section 12.1 (b)[2] of the Prudential Guidelines</i> provides the criteria for classification of normal credit exposures, i.e., consideration for non performing or impaired as follows:</p> <ul style="list-style-type: none"> • interest or principal is due and unpaid for 90 days or more; and • interest payments equal to 90 days interest or more have been capitalised, rescheduled or rolled over into a new loan. <p>For specialized facilities e.g., agricultural finance, project finance, object finance, real estate finance, SME finance and mortgage finance, <i>Annexure 2-6 of the Prudential Guidelines</i> specify the rules for their classification and provisioning. Generally, the banks are required to classify loans as impaired based only on the days past due. Accordingly, qualitative factors are not taken into account in this regard.</p> <p>CBN is in the midst of capacity building to prepare for full implementation of IFRS, including IFRS39. The current supervisory resources have yet to be comfortable in validating banks IFRS39 models. A number of capacity building initiatives to equip examiners to carry out supervision of banks in the IFRS environment have been undertaken or are ongoing. For example, Ernst & Young is currently carrying out an intensive capacity building for bank supervisors, which will stretch over two years.</p>
EC11	The supervisor determines that the Board receives timely and appropriate information on the condition of the bank's asset portfolio, including classification of credits, the level of provisioning and major problem assets.
Description and findings re EC11	Supervisors confirm that banks have appropriate management information systems that update the boards regularly on the condition of the risky assets portfolio, level of NPLs, provisioning levels and recovery efforts on past due loans. Bank are required to have board credit committees, which are expected to meet at least quarterly to consider and approve credit above certain threshold, and consider the classification of credits and the level of provisioning for major problem assets. The on-site appraisal of the level of information available to boards on bank's risk asset portfolio determines the rating given to the board in the assessment of the control function. The assessors noted that the working papers supporting the section notes on the lending activities of a local bank also contained the terms of reference of the board credit committee. The assessors also noted that the section notes contained the CBN supervisors' assessment of the board credit committee minutes.
EC12	The supervisor requires that valuation, classification and provisioning for large exposures are conducted on an individual item basis.
Description and findings re EC12	<p>There is no such legal or regulatory requirement on banks. However, in reviewing banks' risky assets and classification of NPLs, emphasis is placed on large exposures, which are reviewed on an individual item basis. (See also BCP9 EC4, above.)</p> <p>As per issue raised in EC10 (above), it is anticipated that the CBN will develop comprehensive provisioning and classification requirements and expectations to ensure full adoption of the IFRS 39. This way, specific requirements for large credit exposures to be assessed on individual basis (as per IFRS requirements) will be enforced.</p>

Additional criteria	
AC1	Loans are required to be classified when payments are contractually a minimum number of days in arrears (e.g., 30, 60, 90 days). Refinancing of loans that would otherwise fall into arrears does not lead to improved classification for such loans.
Description and findings re AC1	<p>Under <i>Section 12.1 of Prudential Guidelines</i>, a normal credit facility should be deemed as nonperforming when any of the following conditions exists:</p> <ul style="list-style-type: none"> • Interest or principal is due and unpaid for 90 days or more; and/or • Interest payments equal to 90 days interest or more have been capitalised rescheduled or rolled over into a new loan. <p>Under <i>Section 12.2 of Prudential Guideline</i>, for specialised facilities e.g., agricultural finance, project finance, object finance, real estate finance, SME finance and mortgage finance, <i>Annexure 2-6</i> specify the rules for their classification and provisioning. In addition, it is also required that for rescheduled facilities, the provisioning continues until it is clear that rescheduling is working at a minimum, for a period of 90 days.</p>
Assessment of Principle 9	Largely compliant
Comment	<p>In general, the law and regulation provides explicit requirements on how the banks should identify and manage problematic loans and adequately provision. In addition, The RBS approach entails an appropriate review of banks' significant risky asset portfolios. However, with the adoption of IFRS in Nigeria by 2012, the provisioning regime prescribed in the <i>Prudential Guidelines</i> should be updated concomitantly.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Require that the classification and provisioning of specialized facilities e.g., agricultural finance, project finance, object finance, real estate finance, SME finance and mortgage finance also take into account qualitative factors. • Build up expertise in IFRS, especially in the validation of banks' impairment provisioning models. • Leverage off external auditors' expertise, as an interim measures, in relation to assessing the reasonableness of the classification and provisioning process and outcomes. <p>See BCP6 and BCP7 for related generic recommendation/s.</p>
Principle 10	Large exposure limits. Supervisors must be satisfied that banks have policies and processes that enable management to identify and manage concentrations within the portfolio, and supervisors must set prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties.
Essential criteria	
EC1	Laws or regulations explicitly define, or the supervisor has the power to define, a "group of connected counterparties" to reflect actual risk exposure. The supervisor may exercise discretion in applying this definition on a case by case basis.
Description and findings re EC1	<p>The concepts of large exposure or connected exposures or connected counterparties are not defined in the BOFI Act, though they are dealt with in Section 20 of the BOFI Act.</p> <p>Circular 9 of 2004, dealing with "Large Exposures and Connected Lending" defines a large exposure as "any credit to a customer or a group of related borrowers that is at least 10 percent of the bank's shareholders funds unimpaired by losses." The concept of "related borrowers" is not defined. (See also Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2)</p> <p>The above definition of a large exposure is inadequate as it is not comprehensive and clear as</p>

	to what types of exposures should be included (for example, should transactions relating to off-balance sheet items such as credit facilities or derivatives be included) or which borrowers are considered to be connected (for example, what about a customer's subsidiaries and affiliates, or parties controlled by or which have a significant influence over counterparties, or the notion of economic dependency.) Also, the CBN supervisors are not empowered to deem the existence of connected party relationship beyond the legal definition.
EC2	Laws, regulations or the supervisor set prudent limits on large exposures to a single counterparty or a group of connected counterparties. "Exposures" include all claims and transactions, on-balance sheet as well as off-balance sheet. The supervisor confirms that senior management monitors these limits and that they are not exceeded on a solo or consolidated basis.
Description and findings re EC2	<p>See BCP10 AC1.</p> <p>For purposes of determining the total amount of a large exposure, 33.3 percent of off balance sheet engagements shall be taken into account. (Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2) It is not clear what the basis of or source for the figure of 33.3 percent is, nor whether it has been tested to determine whether it is appropriate.</p> <p>Penalties are levied on banks for the contravention of this requirement.</p> <p>Banks are required to report on compliance with regulatory requirements regularly. ((Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 6.3) For example, a bank was sanctioned in 2008 when an onsite examination discovered violation of single obligor limit.</p> <p>CBN has the authority to apply forbearance from complying with the 20 percent regulatory limit, with lowest approving authority residing with the deputy governor. Hence, it is critical for CBN to ensure prudent internal governance process to ensure forbearance is granted on only highly exceptional basis.</p>
EC3	The supervisor determines that a bank's management information systems identify and aggregate on a timely basis exposure to individual counterparties and groups of connected counterparties.
Description and findings re EC3	<p><i>Section 3.3 of the Prudential Guideline</i> requires banks to put in place effective internal policies, systems and controls (duly approved by the boards), to identify, measure, monitor, and control their risk concentrations such as:</p> <ul style="list-style-type: none"> • significant exposures to an individual counterparty or group of related counterparties; • credit exposures to counterparties in the same economic sector or geographic region; • credit exposures to counterparties whose financial performance is dependent on the same activity or commodity; and • indirect credit exposures arising from banks' credit risk mitigation (CRM) activities (e.g., exposure to a single collateral type or to credit protection provided by a single counterparty). <p>Total outstanding exposure (on and off balance sheet) by a bank to all tiers of government and their agencies shall not at any point in time exceed 10 percent of the total credit portfolio. (Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2)</p>
EC4	The supervisor confirms that a bank's risk management policies and processes establish thresholds for acceptable concentrations of credit and require that all material concentrations be reviewed and reported periodically to the Board.
Description and findings re EC4	During on-site examinations, CBN supervisors assess banks' risk management practices are effective in managing banks' risk exposures including concentration risks. CBN supervisors also assess banks' adherence to their internal risk concentration limits and that exceptions are promptly reported to the board and rectified on a timely basis. The assessors noted references to a bank's internal limits in a sample of section notes on the lending activity of a

	local bank.
EC5	The supervisor regularly obtains information that enables concentrations within a bank's portfolio, including sectoral, geographical and currency exposures, to be reviewed. The supervisor has the power to require banks to take remedial actions in cases where concentrations appear to present significant risks.
Description and findings re EC5	<p>Banks are required to submit monthly reports to CBN, highlighting sectoral and geographical concentrations within their portfolio, as part of reports based on <i>Standard Industry Classification (SIC)</i>. Supervisors monitor concentration risks on bank-by-bank basis as well as on an industry wide basis.</p> <p>Where a bank exceeds prudential concentration limits, penalties are imposed and the bank is given a time frame to regularise its position. Where the concentrations appear to pose significant risk, CBN supervisors could request such banks to increase the level of provisioning or beef up capital when the earnings and existing provisions are insufficient to absorb additional required provisioning. The assessors came across an instance where CBN supervisors, by way of a supervisory letter, required a local bank to include a particular exposure in a group of exposures.</p>
Additional criteria	
AC1	<p>Banks are required to adhere to the following definitions:</p> <ul style="list-style-type: none"> • 10 percent or more of a bank's capital is defined as a large exposure; and • 25 percent of a bank's capital is the limit for an individual large exposure to a private sector non-bank counterparty or a group of connected counterparties. <p>Minor deviations from these limits may be acceptable, especially if explicitly temporary or related to very small or specialized banks.</p>
Description and findings re AC1	<p>Circular 9 of 2004, dealing with "Large Exposures and Connected Lending" defines a large exposure as "any credit to a customer or a group of related borrowers that is at least 10 percent of the bank's shareholders funds unimpaired by losses." The concept of "related borrowers" is not defined. (See also Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2)</p> <p>Except with the prior approval of the CBN, a (commercial) bank is not permitted to incur an exposure to a counterparty (including its subsidiaries and associates) of in excess of 20 percent of its shareholders funds, while a merchant bank has a corresponding limited of 50 percent. (BOFI Act – Section 20(1)) (Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2)</p> <p>The aggregate of large exposures in a bank should not exceed eight times (800 percent) the shareholders fund unimpaired by losses. (Prudential Guidelines for Deposit Money Banks in Nigeria, dated July 1, 2010 – Section 3.2)</p> <p>The excess amount, being the amount of a large exposure which exceeds the 25 percent of a bank's capital limit, does not constitute an impairment of capital.</p> <p>The legal and regulatory framework does not prescribe which person/s or body/bodies should be empowered to decide on large exposures.</p>
Assessment of Principle 10	Materially Non-compliant
Comments	Though supervisors ensure that banks have policies and processes that enable management to identify and manage concentrations within the portfolio, and supervisors set prudential limits to restrict bank exposures to single counterparties or groups of connected counterparties, there are important gaps, shortcomings and vulnerabilities which require attention.

	<p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Standardize, inter alia through definition, terminology relating to large exposures, whether single entities or groups of connected entities. • Expand the definition of large exposures to include: <ul style="list-style-type: none"> - Subsidiaries and affiliates of a counterparty of a bank; - Parties that are controlled by or have significant influence over a counterparty of a bank; - Parties to whom a counterparty of a bank is exposed in terms of transactions which were not arm's length transactions; and - The notion of economic dependency • Prescribe that all large exposures (being exposures exceeding 10 percent of a bank's capital) should be decided by the bank's senior management or even a higher level body (such as the board's credit committee, or even the board itself.) • Amend the legal and regulatory framework to impose a (maximum) 25 percent large exposure limit which may not be exceeded and in relation to which the CBN should be prohibited from granting any exception or condonation. • Prescribe that any amount of an exposure in excess of the large exposure limit (of a (maximum) of 25 percent of capital) constitutes an impairment of capital for purposes of computing regulatory eligible capital. • Prescribe that the total outstanding exposure (on and off balance sheet) by a bank to all tiers of government (other than the sovereign itself), and their agencies shall not at any point in time exceed 10 percent of the total credit portfolio, and that any excess amount above 10 percent of the total credit portfolio limit shall constitute an impairment of capital for purposes of computing regulatory eligible capital • Develop and impose limits for sectoral exposures of banks, especially in relation to the oil and gas sector and the telecommunications sector. • Empower CBN supervisors to exercise their discretion, where relevant and on a case by case basis, deem the existence of large exposure relationships for purposes of determining the total amount of a bank's exposure to a particular counterparty or group of connected counterparties, in addition to those connected counterparty relationships defined in the law. <p>See BCP6 and BCP7 for related generic recommendation/s.</p>
Principle 11	Exposures to related parties. In order to prevent abuses arising from exposures (both on balance sheet and off balance sheet) to related parties and to address conflict of interest, supervisors must have in place requirements that banks extend exposures to related companies and individuals on an arm's length basis; these exposures are effectively monitored; appropriate steps are taken to control or mitigate the risks; and write-offs of such exposures are made according to standard policies and processes.
Essential criteria	
EC 1	Laws or regulations explicitly provide, or the supervisor has the power to provide, a comprehensive definition of "related parties." This should consider the parties identified in the footnote to the Principle. The supervisor may exercise discretion in applying this definition on a case by case basis.
Description and findings re EC1	<p>The terms related party, related counterparty or insider are not defined in the BOFI Act. The term "relation of person" is defined and includes shareholders, directors, employees, and their relations' interests, e.g., director's wife/husband, parents, siblings, children, uncle/aunt, and their spouses. (BOFI Act – Section 66). However, that term is not used in the BOFI Act.</p> <p>CBN's Circular (<i>BSD/1/2004</i> released on February 18, 2004 on <i>Disclosure of Insider Facilities</i>) defines "insider transactions" to include transactions involving shareholders (holding more than a 5 percent shareholding in the bank—defined as a "significant shareholding),"</p>

	<p>employees, directors and their related interests. Director is defined to include the director's wife, husband, father, mother, brother, sister, son, daughter and their spouses. (BOFI Act – Section 20)</p> <p>CBN supervisors are not empowered to deem the existence of related parties outside those defined in the law.</p> <p>The concept of related party does not include subsidiaries and affiliates of a bank, of the shareholders, directors, employees of such subsidiaries and affiliates, or parties that are controlled by or have significant influence over related parties of a bank, or parties to whom the related parties of a bank are exposed in terms of transactions which were not arm's length transactions, or the notion of economic dependency.</p>
EC2	Laws, regulations or the supervisor require that exposures to related parties may not be granted on more favorable terms (i.e., for credit assessment, tenor, interest rates, collateralize schedules, requirement for collateral) than corresponding exposures to non-related counterparties.
Description and findings re EC2	<p>Under <i>Section 20 (2) of BOFI Act</i>, banks are prohibited from carrying out the following without the CBN's prior approval:</p> <ul style="list-style-type: none"> • granting unsecured advances to directors or their related (business) interests in an amount in excess of ₦50,000; • granting unsecured advances to officers and employees, which in aggregate exceeds one year emolument of the employee; and • remit, either in whole or part the debt owed it by any of its directors, whether present or past. <p>There is no legal or regulatory provision that prohibits the granting of advances to related parties on more favorable terms than corresponding exposures to non-related counterparties. The existing regulation only requires the banks to disclose the details of related party transactions in their financial statements.</p>
EC3	The supervisor requires that transactions with related parties and the write-off of related-party exposures exceeding specified amounts or otherwise posing special risks are subject to prior approval by the bank's Board. The supervisor requires that Board members with conflicts of interest are excluded from the approval process.
Description and findings re EC3	<p><i>Section 3.4(d) of the Prudential Guideline</i> requires banks to ensure that their credit policies specifically address lending to directors as part of related parties or insider lending policies. However, the guideline should be further strengthened by specifically providing measures that regulate transactions with all related parties (not only confined to directors of banks) and require that such transactions should be at arm's length.</p> <p><i>Section 3.21 of the Prudential Guidelines</i> requires all facilities for write-off to be approved by the boards and if the facilities are to related parties, the prior approvals of the CBN are required. By virtue of the provision of <i>Section 18 of BOFI Act</i>, an interested director is excluded from the approval process</p> <p>The legal and regulatory framework does not prescribe which person/s/ or body/bodies should be empowered to decide on related party exposures.</p>
EC4	The supervisor requires that banks have policies and processes in place to prevent persons benefiting from the exposure and/or persons related to such a person from being part of the process of granting and managing the exposure.
Description and findings re EC4	<p>Managers, officers and directors are required to disclose their interests in loans and advances granted by institutions at board meetings. (BOFI Act – Section 18)</p> <p>During on-site examinations, CBN supervisors determine whether banks have adequate credit administration procedures and controls to prevent persons who process or manage loans from benefiting from the exposure. The assessors were informed by CBN supervisors that the</p>

	<p>first step during an on-site examination is for the CBN supervisors to check for compliance with legal and regulatory prescriptions, including prescriptions contained in the Prudential Guidelines (which imposes this requirement).</p>
EC5	<p>Laws or regulations set, or the supervisor has the power to set on a general or case by case basis, limits for exposures to related parties, to deduct such exposures from capital when assessing capital adequacy, or to require collateralization of such exposures. When limits are set on aggregate exposures to related parties, those are at least as strict as those for single counterparties, or groups of connected counterparties.</p>
Description and findings re EC5	<p>Except with the CBN's prior approval, a bank is not permitted to have an exposure in excess of ₦50 000 to a director (or any firm, partnership or company in which the director has an interest as shareholder with an interest in excess of 5 percent, director, partner, manager or agent of any individual firm, partnership or private company of which any of its directors is a guarantor) A reference to a director includes a reference to a director's wife/husband, father, mother, brother, sister, son and daughter and their spouses (BOFI Act – Section 20)</p> <p>Except with the CBN's prior approval, a bank is not permitted to have an exposure to any of its officers or employees amounting to more than one year's emoluments to such officer or employee. (BOFI Act – Section 20(2))</p> <p><i>Circular BSD/9/2004 on Large Exposures and Related Party Exposures</i> limits banks' exposures to individual directors and shareholders to 10 percent of banks' paid up capital, except with the prior approval of the CBN. The maximum credit exposure to all insiders is set at 60 percent of bank's paid up capital. In addition, under <i>Section 20(2)(a)(i) of BOFI Act</i>, all facilities granted to directors exceeding the sum of ₦50,000 must be collateralised. The 60 percent limit on the maximum credit exposure to all insiders is high given the historical experience with related party exposures and also relative to international norms.</p> <p>Related party exposures do not constitute impairments from capital.</p>
EC6	<p>The supervisor requires banks to have policies and processes to identify individual exposures to related parties as well as the total amount of such exposures, and to monitor and report on them through an independent credit review process. The supervisor confirms that exceptions to policies, processes and limits are reported to the appropriate level of senior management and, if necessary, to the Board, for timely action. The supervisor also confirms that senior management monitors related party transactions on an ongoing basis, and that the Board also provides oversight of these transactions.</p>
Description and findings re EC6	<p>Banks are required to have policies and processes to identify and monitor the exposure to insiders. All banks are directed to disclose full information on all related-party transactions in their financial statements as per the prescribed format (<i>BSD/1/2004</i>). Regulations also require that all exceptions related to insider facilities are reported to the boards. <i>Paragraph 6.1.6 of the Code of Corporate Governance</i> requires all related-party credit applications pertaining to directors and top management staff (i.e., AGM and above) and parties related to them, irrespective of size, should be sent for consideration/approval to the board credit committees. <i>Paragraph 6.1.8</i> further states that directors whose facilities or that of their related interests remains nonperforming for more than one year should cease to be on the boards of the banks and could be blacklisted from sitting on the boards of any other bank.</p> <p>Banks are required to submit detailed quarterly reports to BSD on all insider facilities. These reports are reviewed and insiders who maintain nonperforming facilities are sanctioned as required by the regulations. The assessors scrutinized banks' quarterly insider facilities reports.</p>
EC7	<p>The supervisor obtains and reviews information on aggregate exposures to related parties.</p>
Description and findings re EC7	<p>Banks are required to submit quarterly returns to supervisors on exposures to related parties. <i>QBR 1650 on e-FASS</i> captures detailed information of the banks' credit exposures to directors, employees and principal shareholders. The analysis of the returns filed by banks would then be used to form the basis for the removal of the directors of some banks that maintained nonperforming facilities.</p>

Assessment of Principle 11	Materially non-compliant
Comments	<p>Abuses arising from related party transactions and exposures, and conflicts of interest were identified as major causes of the 2009 banking crisis. Hopefully the CBN's action in removing executive management in eight banks and sanctioning directors has instilled the necessary discipline into the sector and will serve as a future deterrent measure. In general, the law and regulations on related parties are sparse and minimalistic and need to be reviewed and enhanced substantially, to prevent related party abuse again posing a significant threat to financial stability.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Standardize, inter alia through definition, terminology relating to related parties and insiders. • Expand the definition of related party to include: <ul style="list-style-type: none"> - subsidiaries and affiliates of a bank; - parties that are controlled by or have significant influence over the related parties of a bank; - parties to whom the related parties of a bank are exposed in terms of transactions which were not arm's length transactions; and - the notion of economic dependency • Strengthen the definition of related parties by designating, inter alia, also external auditors as related parties. • Prescribe that all matters involving related party exposures should be decided by the bank's board of directors. • Empower the CBN to exercise its discretion, where relevant and on a case by case basis, to deem the existence of related party relationships, for purposes of determining the total amount of a bank' exposure to a particular related party or group of connected related parties, in addition to those already defined in the current law. • Enhance the existing law and regulation by prohibiting the granting of advances to related parties on more favourable terms than corresponding exposures to non-related counterparties and/or to ensure that such transactions are concluded on an arm's length basis. • Prohibit related parties from being involved in the decision-making process in relation to a related credit or credit facility. • Require that the monitoring and reporting of related party transactions should be discharged by way of independent credit review process. • Adjust substantially downwards the current 60 percent aggregate related party limit. • Amend the legal and regulatory framework to impose a 10 percent single related party limit and an aggregate related party limit, which limits may not be exceeded and in relation to which the CBN should be prohibited from granting any exception or condonation. • Constitute the total amount of an exposure to a related party as an impairment of capital, which means that such an exposure should be deducted for purposes of determining a bank's regulatory eligible capital.
Principle 12	Country and transfer risks. Supervisors must be satisfied that banks have adequate policies and processes for identifying, measuring, monitoring and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining adequate provisions and reserves against such risks.
Essential criteria	
EC1	The supervisor determines that a bank's policies and processes give due regard to the

	<p>identification, measurement, monitoring and control of country risk and transfer risk. Exposures are identified and monitored on an individual country basis (in addition to the end-borrower/end-counterparty basis). Banks are required to monitor and evaluate developments in country risk and in transfer risk and apply appropriate countermeasures.</p>
Description and findings re EC1	<p>There is no guideline issued which is specifically focused on the management of country and transfer risk in the banking industry. <i>Paragraph 4.6 of the Guidelines for Developing Risk Management Framework for Individual Risk Elements in Banks</i> issued in 2007, imposes a generic requirement on banks to establish systems and procedures for risk identification, measurement and control and monitoring of loan and investment portfolio quality and early warning signals. The CBN issued the <i>Framework for Cross-border Cross-border Supervision of Banks</i>, which among others, highlights the following guidelines:</p> <ul style="list-style-type: none"> • approvals to operate foreign operations are subject to the existence of MOUs with the host supervisors; • affected banks are required to have higher capital adequacy as a buffer against any potential capital calls from the host regulators; and • foreign subsidiaries of Nigerian banks can only undertake activities that are permitted for the parent banks in Nigeria. <p>During on-site examinations, CBN supervisors determine that banks' risk management framework gives due regard to the identification, measurement, monitoring and control of all risks, including country and transfer risks, by ensuring that exposures are identified and monitored on an individual country basis (as required on general basis by <i>Guidelines for Developing Risk Management Framework for Individual Risk Elements in Banks</i>). Notwithstanding the absence of specific supervisory guidance on assessing country risk, the assessors sighted an assessment of country risk in a sample of section notes for overseas activities of a local bank.</p> <p>There is no specific prudential standard to guide banks with significant country and transfer risk elements, in managing those risks. Also, there is no specific supervisory work programme for assessment of country/transfer risks to guide the CBN supervisors.</p>
EC2	<p>The supervisor confirms that banks have information systems, risk management systems and internal control systems that accurately monitor and report country exposures and ensure adherence to established country exposure limits.</p>
Description and findings re EC2	<p><i>Paragraph 4 and Appendices A and C of the RBS Framework</i> stipulate the various risk elements, the control functions and the type of information that a bank could consider to accurately monitor and report all types of exposures to ensure adherence to established exposure limits.</p> <p>During the course of on-site examination, CBN supervisors are guided by these in assessing the internal control and MIS for risk reporting, including reporting of country exposures. For those banks that establish country limits, CBN supervisors undergo the same process to ensure the limits are adhered to. (See also BCP12 EC1, above. The internal limit set by the particular bank in relation to its overseas operations was mentioned in the country risk assessment.)</p>
EC3	<p>There is supervisory oversight of the setting of appropriate provisions against country risk and transfer risk. There are different international practices which are all acceptable as long as they lead to risk-based results. These include:</p> <ul style="list-style-type: none"> • The supervisor (or some other official authority) decides on appropriate minimum provisioning by setting fixed percentages for exposures to each country. • The supervisor (or some other official authority) sets percentage ranges for each country, and the banks may decide, within these ranges, which provisioning to apply for the individual exposures. • The bank itself (or some other body such as the national bankers' association) sets percentages or guidelines or even decides for each individual loan on the appropriate provisioning. The provisioning will then be judged by the external auditor and/or by the

	supervisor.
Description and findings re EC3	<p><i>Paragraph 12 of the Prudential Guidelines</i> sets the regulatory requirements with regards to the provisioning practiced by the banks. However, while specific risk weights are assigned to bank's exposures to OECD and other countries; it does not specifically impose fixed percentage of provisioning for its exposures to each country.</p> <p>During course of on-site examination, if the CBN supervisors are of the opinion that the level of provisioning for credit exposures is not sufficient due to certain factors (that might include concerns over countries of which the credits are exposed to), CBN supervisors would require banks to raise additional provisions on those exposures. The assessors obtained verbal confirmation hereof from the CBN supervisors in the cross-border division (which is a specialized division focusing on banks' foreign operations). To date, the CBN has not as yet deemed it necessary to impose additional provisioning requirements, say, in relation to a particular jurisdiction in respect of which it may have concerns.</p>
EC4	The supervisor obtains and reviews sufficient information on a timely basis on the country risk and transfer risk of individual banks.
Description and findings re EC4	The adoption of <i>RBS Framework</i> as opposed to the compliance-based supervision guides CBN supervisors in supervision functions and requires CBN supervisors to review all risks inherent in a bank's operations (including country risk and transfer risk). The risk-based assessment includes the regular off-site assessment of relevant information e.g., country exposures submitted via e-FASS and manual submission by banks to the dedicated team within Banking Supervision Department that specifically supervise offshore operations of Nigerian banks.
Assessment of Principle 12	Largely compliant
Comment	<p>The CBN has provided over-arching and generic guidance for banks in managing their risks, including country and transfer risk. Further, the <i>RBS Framework</i> provides CBN supervisors with guidance on how to assess significant activities of banks including cross-border operations. With the increasing internationalization of the banking system, country and transfer risk is an emerging risk requiring increasing attention.</p> <p>Hence the following recommendations are suggested:</p> <ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Manage country and transfer risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, which constitutes it as an emerging and, perhaps, even a significant risk exposure in the case of certain banks. • Require a bank to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant country and transfer risk exposure.
Principle 13	Market risk. Supervisors must be satisfied that banks have in place policies and processes that accurately identify, measure, monitor and control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposures, if warranted.
Essential criteria	
EC1	The supervisor determines that a bank has suitable policies and processes that clearly articulate roles and responsibilities related to the identification, measuring, monitoring and control of market risk. The supervisor is satisfied that policies and processes are adhered to in practice and are subject to appropriate Board and senior management oversight.
Description and findings re EC1	CBN's guideline for <i>Developing Risk Management Framework for Individual Risk Elements in Banks</i> (Section 4.5.1) requires that the boards and managements of banks ensure that adequate policies are in place to manage and mitigate the adverse effects of risks and further stress the importance in Section 5.2.1 on market risk. The guideline enables banks to develop their respective strategy for managing each individual risk elements and provided the minimum supervisory expectations in terms of banks' market risk management framework.

	<p>Banks are also required to submit their completed risk management frameworks for assessment by CBN supervisors to ensure that the minimum prescribed standards are met. Banks are also required to use both quantitative and qualitative measurements to assess individual risk elements, including market risk.</p> <p>In the course of on-site examinations, CBN supervisors assess the effectiveness of banks' market risk management frameworks, while assessing the treasury operations. This is carried out via ensuring adherence to the internal framework that has been reviewed by CBN supervisors earlier. The assessors confirmed that such assessments are encapsulated in the section notes for the treasury operations in the case of a particular bank.</p> <p>To date, Nigeria has not adopted the 1996 Market Risk Amendment and, consequently, has not computed a market risk capital requirement or required banks to hold capital against their market risk exposures. (The CBN intends comprehensively attending to market risk in the envisaged updated regulatory framework for prudential supervision.)</p> <p>The guidance in the <i>Developing Risk Management Framework for Individual Risk Elements in Banks</i> on market risk (<i>Section 5.2</i>) is extremely brief and without sufficient details. The granular guidance in managing market risk is critical in light of emerging risk arising from market movement e.g., the market risk impact of the failure in stock exchange during the 2008 crisis.</p> <p>The CBN supervisors are not equipped with specific supervisory programme on market risk in assessing the significant risk drivers, particularly in treasury operations.</p>
EC2	<p>The supervisor determines that the bank has set market risk limits that are commensurate with the institution's size and complexity and that reflect all material market risks. Limits should be approved by the Board or senior management. The supervisor confirms that any limits (either internal or imposed by the supervisor) are adhered to.</p>
Description and findings re EC2	<p>Banks are required by <i>circular BSD/10/2003 on Guidelines for the Development of Liquidity Management Policies</i> to set tolerable limits for market risks, depending on the size and nature of their business. <i>Section 12.12 (g)</i> of the <i>Prudential Guidelines</i> also requires banks to constantly mark to market the margin financing portfolio and this is reviewed vis-à-vis assessment of profit and loss of banks.</p> <p>Banks are also required to maintain a net open position (NOP) limit on their foreign exchange balances as may be prescribed from time to time by the MPC, as a control on their market risk (currently it is 1 percent of total shareholders' funds). (CBN Act – Section 12)</p> <p>These limits are approved by the bank's board and CBN supervisors assess the adherence to these limits during onsite examinations via reviewing the compliance reports for treasury operations of banks. In discussion with a CBN supervisor, the assessors confirmed that, when assessing treasury activity of a bank, a CBN supervisor would request a listing of the board-approved limits, and thereupon perform a comparison thereof with the relevant bank's treasury reports.</p> <p>The NOP limit is the only regulatory limit that banks are required to observed as far as market risk exposures are concerned. The requirement under <i>Guidelines for the Development of Liquidity Management Policies</i> in principle only covers liquidity risk management activities and not the entire treasury/market risks operations. As explained in BCP13 EC1, CBN should consider issuing more granular and detailed regulatory guidelines on market risks and market risk management to the banks, which among others to include requirements to set and adhere to specific internal market risk limits.</p>
EC3	<p>The supervisor is satisfied that there are systems and controls in place to ensure that all transactions are captured on a timely basis, and that the banks' marked to market positions are revalued frequently, using reliable and prudent market data (or, in the absence of market prices, internal or industry-accepted models). The supervisor requires banks to establish and maintain policies and processes for considering valuation adjustments/reserves for positions that otherwise cannot be prudently valued, including concentrated, less liquid, and stale positions.</p>

Description and findings re EC3	<p>See BCP13 EC2.</p> <p>Banks are required to constantly mark-to-market their exposure to capital market and also place policies and processes for considering valuation adjustments for positions that otherwise cannot be prudently valued. (Prudential Guidelines – Section 12.12(g))</p> <p>Adherences to these guidelines are assessed via the compliance and internal audit reports on banks' treasury operations, and any shortcoming is communicated during onsite examinations. As previously mentioned, checking for compliance with the legal and regulatory framework constitutes an initial step in an on-site examination.</p> <p>As previously mentioned CBN should consider issuing more granular and detailed regulatory guidelines on market risks and market risk management to the banks.</p>
EC4	<p>The supervisor determines that banks perform scenario analysis, stress testing and contingency planning, as appropriate and periodic validation or testing of the systems used to measure market risk. The supervisor confirms that the approaches are integrated into risk management policies and processes, and results are taken into account in the bank's risk-taking strategy.</p>
Description and findings re EC4	<p><i>Guidelines for the Development of Liquidity Management Policies</i> require banks to periodically stress test the assumptions and accuracy of measurement methodologies for market risk exposures (<i>Section 5.2.3.5</i>).</p> <p>However, the guidelines do not further explain the minimum expectations on how such test should be carried out. Similarly, a supervisory programme to assess the appropriateness of scenario analysis, stress testing and the relevant testing of the system used to measure market risk is also not as yet available to guide CBN supervisors in determining appropriate scenario analysis, stress testing and contingency planning are carried out by banks.</p> <p>As mentioned in BCP7 (Risk Management Process), the current supervisory resources are also not fully comfortable in confronting technical and complex risk and risk management issues (including market risks), especially as regards stress testing and scenario analysis.</p>
Additional criteria	
AC1	<p>The supervisor requires that market data used to value trading book positions are verified by a function independent of the lines of business. To the extent that the bank relies on modeling for the purposes of valuation, the bank is required to ensure that the model is independently tested.</p>
Description and findings re AC1	<p>Under the RBS Framework, supervisory guidance on treasury activities require CBN supervisors to ensure independent assessment of the trading book, systems and control function are carried out by control functions separated from business lines, and this requirement is verified during on-site examinations, particularly when assessing the treasury activities. Any shortcoming is raised in the examination reports. For example, issue on having treasury operation solely responsible for monitoring settlement failures was raised in the examination report of a bank in 2009.</p>
Assessment of Principle 13	<p>Materially non-compliant</p>
Comments	<p>The regulatory and supervisory framework for and supervisory approach to market risk should be improved, inter alia, by adoption of the 1996 Market Risk Amendment, further strengthening regulatory policies and developing a supervisory work program for market risk.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Adopt the 1996 Market Risk Amendment • Manage market risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, as it constitutes an emerging and, perhaps,

	<p>even a significant risk exposure in the case of certain banks. Pay particular attention to a bank's treasury and ALCO activities.</p> <ul style="list-style-type: none"> • Require a bank to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant market risk exposure. • Improve the competencies of supervisors in relation to market risk and market risk management.
Principle 14	Liquidity risk. Supervisors must be satisfied that banks have a liquidity management strategy that takes into account the risk profile of the institution, with prudent policies and processes to identify, measure, monitor and control liquidity risk, and to manage liquidity on a day-to-day basis. Supervisors require banks to have contingency plans for handling liquidity problems.
Essential criteria	
EC1	The supervisor sets liquidity guidelines for banks. These guidelines take into consideration undrawn commitments and other off-balance sheet liabilities, as well as existing on-balance sheet liabilities.
Description and findings re EC1	<p>The <i>RBS Framework</i> considers liquidity risk as one of banks' prime risks. This reinforces CBN's <i>Guidelines for the Development of Liquidity Management Policies (BSD/10/2003)</i>. This Guideline stipulates that banks should maintain adequate liquidity cushion on an on-going basis to cover all maturing obligations (both on and off-balance sheet).</p> <p>At minimum, the guideline requires banks to clearly outline their:</p> <ul style="list-style-type: none"> • composition of assets and liabilities to maintain liquidity; • diversification and stability of liabilities; and • access to inter-bank market. <p>The <i>Guideline for Developing Risk Management Framework for Individual Risk Elements in Banks</i> also specifies that banks are recommended to calculate daily net position (GAP) for the next one or two weeks, monthly GAP for next six months or a year and quarterly thereafter.</p> <p>CBN requires banks to maintain liquidity ratio (percentage of liquefiable assets to cover for potential drawdown of banks liabilities) of 30 percent. A cash reserve requirement of 8 percent also applies. In addition, banks' boards and senior managements are also expected to establish liquidity limits vis-à-vis the banks' liquidity risk appetite. In addition, banks are required to maintain a maximum Loan-to-Deposit ratio of 80 percent.</p> <p>While having the above policies and guidelines on liquidity risk management in place, CBN should ensure that regulatory guidelines on liquidity risk management are in-line with the principles outlined in the <i>2008 Basel Committee on Banking Supervision's Principles for Sound Liquidity Risk Management and Supervision</i>.</p> <p>The CBN has commenced a Quantitative Impact Study (QIS) on the implementation of Basel II and Basel III—banks were required to return their duly completed responses to the CBN by October 20, 2012.</p> <p>The current liquidity ratio requirement is not adequate as the calculation does not incorporate the potential crystallization of the OBS obligations.</p>
EC2	The supervisor confirms that banks have a liquidity management strategy, as well as policies and processes for managing liquidity risk, which have been approved by the Board. The supervisor also confirms that the Board has an oversight role in ensuring that policies and processes for risk-taking are developed to monitor, control and limit liquidity risk, and that management effectively implements such policies and processes.
Description and findings re EC2	<i>The Guidelines for the Development of Liquidity Management Policies</i> prescribed the strategies to be adopted by banks in managing liquidity risks. For instance, banks are required to have well defined asset and liability mix, diversified funding base, adequate stock of liquid assets and limits on maturity mismatches. Among others, the guidelines highlight the following

	<p>area:</p> <ul style="list-style-type: none"> • issues to consider in formulating a liquidity management policy; • suggested strategies; • setting limits on maturity mismatches; • restricting dependence on intra group liquidity; • ability to access wholesale markets; • use of assets; • control and systems; and • contingency planning. <p>Supervisory expectations on managements' roles and responsibilities in relation to ALCO are not clearly specified in the guidelines.</p> <p>In the course of onsite examination (particularly in assessing treasury operations as significant activities), CBN supervisor determine that banks have developed and are implementing the strategy, at minimum meet the criteria in the guidelines. Terms and reference of boards, boards risk committees and ALCOs are reviewed to ensure the necessary functions expected of these oversight functions are discharged accordingly. CBN supervisors also review the liquidity management strategy to determine that liquidity risk positions are in line with the approved risk appetite by boards. The assessors scrutinized such an assessment, the supporting working papers and documentation (including the terms of reference of the board and its committees) and the related section notes for the treasury activity of a local bank.</p>
EC3	<p>The supervisor determines that a bank's senior management has defined (or established) appropriate policies and processes to monitor, control and limit liquidity risk; implements effectively such policies and processes; and understands the nature and level of liquidity risk being taken by the bank.</p>
Description and findings re EC3	<p>CBN supervisors, during on-site examinations, assess the policies and processes put in place by senior managements of banks to ensure compliance with the provisions of the <i>Guidelines for the Development of Liquidity Management Policies</i>. The assessors were informed by CBN supervisors that the first step during an on-site examination is for the CBN supervisors to check for compliance with legal and regulatory prescriptions, including prescriptions contained in the Prudential Guidelines (which imposes this requirement). The assessors were given access to a particular bank's policies and procedures which constituted a source for the preparation of assessment/section notes on treasury operations.</p> <p>In addition, the CBN's circular <i>No. 44 of 2009</i> provides the basis for the computation of liquidity ratios i.e., computed on an ongoing basis to determine compliance with prudential requirements. When there are shortfalls, banks are required to take remedial actions in line with the <i>Supervisory Intervention Framework</i>. CBN supervisors also, via review of the liquidity risk policies of banks, determine whether banks have their own internal limits. The adherence to the limits are checked via the regular reporting of banks' liquidity positions to the ALCO (ALCO papers) and board risk committees.</p> <p>As mentioned in BCP14 EC1, the calculation of liquidity ratio for regulatory purpose is not adequate as it does not include the impact of crystallization of OBS commitments.</p>
EC4	<p>The supervisor requires banks to establish policies and processes for the ongoing measurement and monitoring of net funding requirements. The policies and processes include considering how other risks (e.g., credit, market, and operational risk) may impact the bank's overall liquidity strategy, and require an analysis of funding requirements under alternative scenarios, diversification of funding sources, a review of concentration limits, stress testing, and a frequent review of underlying assumptions to determine that they continue to be valid.</p>
Description and findings re EC4	<p>The <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i> provide minimum expectations to banks in developing overall risk management policies and procedures. Generally, banks are required to have in place comprehensive risk management processes to identify, measure, monitor and control all</p>

	<p>material risks. The Guidelines also require banks to conduct periodic stress testing of the assumptions underlying the liquidity strategy, the results of which should be reviewed and analyzed to evaluate the impact on the business.</p> <p>It is not stipulated whether the determination of net funding requirements should take into account also how other risks could impact the need for funding. Furthermore, no limits are specified to prevent concentration of funding by depositor, by maturity, or from volatile sources.</p> <p>It is recommended that the CBN included the following elements in liquidity risk management prudential guideline:</p> <ul style="list-style-type: none"> • net funding requirements are to be assessed in the context of a broader review of how other risks could impact the need for funding; and • limits or ratios to prevent concentration of funding to top depositors, by maturity, and from volatile sources, such as reliance on the swap market or inter-bank market to fund the assets.
EC5	<p>The supervisor obtains sufficient information to identify those institutions carrying out significant foreign currency liquidity transformation. Where a bank or banking group's foreign currency business, either directly, or indirectly through lending in foreign exchange to domestic borrowers, is significant, or where a particular currency in which the bank has material exposure is experiencing problems, the supervisor requires the bank to undertake separate analysis of its strategy for each currency individually and, where appropriate, set and regularly review limits on the size of its cash flow mismatches for foreign currencies in aggregate and for each significant individual currency.</p>
Description and findings re EC5	<p>During on-site examinations, the foreign exchange transactions of banks are assessed and the risks to which they are exposed are identified and analyzed. CBN supervisors also make use of the data submitted via e-FASS, specifically on the liquidity position, broken down into Naira and non-Naira position, to carry out offsite analyses on banks' liquidity risk exposures by different currencies. To mitigate the impact of mismatch between inflows and outflows of foreign exchange, limits are placed on the NOP. Where it is considered that the level of risk is significant in relation to the size and complexity of banks, in-depth foreign exchange examinations are conducted by the CBN supervisors. The assessors scrutinized samples of several banks' e-FASS liquidity position reports, which, inter alia, are used to perform the aforementioned assessment.</p> <p>The CBN does not explicitly require banks to have proper liquidity risk management policies governing the foreign currency operations (apart from merely having a NOP limit in place).</p>
EC6	<p>The supervisor determines that banks have contingency plans in place for handling liquidity problems, including informing the supervisor.</p>
Description and findings re EC6	<p>The <i>Guidelines for the Development of Liquidity Management Policies</i> require banks to have in place contingency funding plans (CFP) approved by their boards for dealing with major liquidity problems. These plans must be regularly tested, updated on the basis of the outcome of liquidity stress tests, and be reported to and approved by the banks' boards in order for the internal policies and processes to be adjusted accordingly.</p> <p>During the course of onsite examinations, CBN supervisors request and review banks' CFP to determine whether the plans, at minimum, are in-line with the requirements under the regulatory guidelines. The assessors scrutinized the CBN supervisors' treasury section notes in relation to a local bank's liquidity plan/CFP.</p> <p>However, the following elements are not available in the guidelines:</p> <ul style="list-style-type: none"> • to impose on banks to have separate CFPs for the overseas branches or subsidiaries; and • to include requirement for clear escalation procedures detailing when and how each of the plans can and should be activated and determination of expected lead time needed to tap additional funds from each of the contingency sources under stressed scenario.

Additional criteria	
AC1	The supervisor determines that, where a bank conducts its business in multiple currencies, foreign currency liquidity strategy is separately stress-tested, and the results of such tests are a factor in determining the appropriateness of mismatches.
Description and findings re AC1	<p>The <i>Guidelines for the Development of Risk Management Frameworks</i> requires banks to conduct appropriate stress tests on a regular basis to identify sources of potential liquidity strain, which may include any potential liquidity strain arising from its takings in foreign currencies. The guideline further elaborates that the frequency and scope of the stress testing should be proportionate to the nature, scale, and complexity of the bank's activities, as well as to the size of their liquidity exposures, but the expectation is that stress testing should be carried out no less frequently than annually.</p> <p>In the course of examination, at minimum the CBN supervisors review the liquidity policy to determine whether banks adhere to the minimum regulatory standards in relation to carrying out liquidity stress test. The assessors scrutinized a particular local bank's liquidity policies which were attached to the CBN supervisors' section notes on the bank's treasury activity.</p>
AC2	The supervisor confirms that banks periodically review their efforts to establish and maintain relationships with liability holders, maintain the diversification of liabilities, and aim to ensure their capacity to sell assets.
Description and findings re AC2	<p>The <i>Guidelines for the Development of Risk Management Frameworks</i> requires banks' boards to provide the broad policy objective and strategic focus, and for managements to stipulate the proportion of each asset and liability component (i.e., asset/liability mix) to ensure that the bank's liquidity is not impaired. They are also required to ensure the diversification and stability of liabilities (in order for banks to have diversified sources for funding day to day liquidity requirements) and determine the stability of the liabilities/funding sources.</p> <p>During the on-site examination CBN supervisors assess the effectiveness of these funding plans by reviewing the liquidity management policies and ALCO reports. The assessors noted that the CBN supervisors' assessment of ALCO was incorporated in the section notes on the treasury operations of a local bank, and that the bank's liquidity policy was attached.</p> <p>The CBN does not specify and clarify the following expectations in managing funding concentrations:</p> <ul style="list-style-type: none"> • banks to address diversification and concentration risks by establishing internal limits or ratios and identifying party responsible for monitoring and reviewing of these limits and ratios; and • banks to establish internal policies to govern the classification of liquid assets to ensure no over-reliance on illiquid assets.
Assessment of Principle 14	Largely compliant
Comments	<p>CBN supervisors on an ongoing basis monitor a bank's (day-to-day) liquidity risk management by assessing a bank's compliance with the <i>Guidelines for the Development of Liquidity Management Policies</i> while being cognizant of a bank's risk profile. In summary, the guidelines require banks to have a proper strategy for managing liquidity risk, with appropriate internal policies and procedures as well as adequate liquidity contingency plans.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Update the Guidelines for the Development of Liquidity Management Policies, 2003, in the light of important subsequent reforms relating to liquidity risk management, including the BCBS's <i>Principles for Sound Liquidity Risk Management and Supervision (2008)</i> and Basel III. For example, the guidelines should be enhanced by considering the following elements in detail:

	<ul style="list-style-type: none"> - provide clear expectation on the roles and functions of the management vis-à-vis ALCO responsibilities; - assess net funding requirements in the context of a broader review of how other risks could impact the need for funding; - require limits or ratios to prevent concentration of funding to top depositors, by maturity and from volatile sources, such as reliance on the swap market or inter-bank market to fund the assets; - prescribe that banks are required to have separate CFPs for their overseas branches or subsidiaries; - require clear escalation procedures detailing when and how each of the CFT plans can and should be activated and determination of expected lead time needed to tap additional funds from each of the contingency sources under stress scenario; - require the establishment of internal limits or ratios to address diversification and concentration, and identify the party responsible for monitoring and reviewing such limits and ratios; and - require that banks establish internal policies to govern the classification of liquid assets to ensure no over-reliance on illiquid assets. <ul style="list-style-type: none"> • Incorporate into the liquidity ratio requirements the probability of crystallization and impact of OBS obligations. • Require banks with significant multiple currency exposures to have proportionate risk management strategies, policies and processes governing their foreign currency operations. Consideration should be given to imposing separate liquidity ratio requirements in relation to each currency. • Conclude on and respond to the quantitative impact assessment of the liquidity prescription (Liquidity Coverage Ratio and Net Stable Funding Ratio) contained in Basel III.
Principle 15	Operational risk. Supervisors must be satisfied that banks have in place risk management policies and processes to identify, assess, monitor and control/mitigate operational risk. These policies and processes should be commensurate with the size and complexity of the bank.
Essential criteria	
EC1	The supervisor requires individual banks to have in place risk management policies and processes to identify, assess, monitor and mitigate operational risk. These policies and processes are adequate for the size and complexity of the bank's operations, and the supervisor confirms that they are periodically adjusted in the light of the bank's changing risk profile and external market developments.
Description and findings re EC1	<p><i>Guidelines for Developing Risk Management Framework for Individual Risk Elements in Banks (paragraph 5.3)</i> provide minimum standards for risk management policies, and processes to identify, assess and mitigate operational risk. Among others, the guidelines expect banks' operational risk management framework to have the elements of risk identification, measurement and the development of Key Risk Indicators (KRI). Under <i>RBS Framework</i>, CBN supervisors also maintain Knowledge of Business (KoB) files for banks with a view to ensure that the risk management frameworks that banks develop are adequate for banks' sizes and complexities of operations. The banks' risk management frameworks (including operational risk management framework) are thus assessed based on the KoB of banks and the resultant risk profiles of those banks.</p> <p>During onsite examinations, CBN supervisors review banks' internal operational risk management (ORM) policies and walk-through the ORM process to determine banks' adherence to the above guidelines. Critical lapses are noted and communicated to banks for further actions. For example, during a 2009 onsite review of a bank's international operations, CBN supervisors raised several critical ORM lapses that caused a hike in operational risk profile of the activity. The assessors noted the highlights of this assessment in the section notes on the particular bank's international operations.</p>

	<p>However, there is no detailed requirement issued to the industry to ensure banks have in place risk management policies and processes to identify, assess, monitor and control/mitigate specifically operational risk.</p>
EC2	<p>The supervisor requires that banks' strategies, policies and processes for the management of operational risk have been approved and are periodically reviewed by the Board. The supervisor also requires that the Board oversees management in ensuring that these policies and processes are implemented effectively.</p>
Description and findings re EC2	<p>In line with the <i>Guidelines for Developing Risk Management Framework for Individual Risk Elements in Banks</i>, CBN requires banks' overall risk strategies and significant risk management policies (which, should include ORM) to be reviewed by the banks' boards (<i>paragraph 4.2</i>). Banks' board risk management committees are also expected to be responsible for ensuring adherence to banks' risk management policies and procedures (which should include ORM) as required under <i>paragraph 4.3.1</i>. In addition, <i>RBS Framework</i> expects CBN supervisors to ensure that risk managements, risk control plans and functions of banks are approved by the boards and implemented by the banks' managements. Thereafter, the risk frameworks and processes are expected to be regularly reviewed by the boards. In short, CBN supervisors hold the banks' boards responsible for risk management frameworks and functions of banks.</p> <p>To assess the effectiveness of the boards oversight over risk management functions (including ORM function), CBN supervisors review the qualifications of board members to ensure that they meet the requisite technical knowledge and understanding of the business and the operations of the bank. A CBN supervisor explained to the assessors that this was a common supervisory process undertaken by CBN supervisors-in-charge of assessing board oversight functions (or undertaken by other senior CBN supervisors, e.g., relationship managers and/or team leaders.)</p>
EC3	<p>The supervisor is satisfied that the approved strategy and significant policies and processes for operational risk are implemented effectively by management.</p>
Description and findings re EC3	<p>Via on-site examination of banks, CBN supervisors review and determine whether banks' staff have a full understanding of the operational risk controls and that these controls are implemented accordingly. CBN supervisors also engage with banks' managements to ensure that they provide adequate oversight.</p> <p>There is no specific supervisory programme to guide CBN supervisors in assessing overall operational risk and operational risk management of banks, other than limited patches of guidance in several separate supervisory programmes for specific significant activities.</p>
EC4	<p>The supervisor review the quality and comprehensiveness of the bank's business resumption and contingency plans to satisfy itself that the bank is able to operate as a going concern and minimise losses, including those that may arise from disturbances to payment and settlement systems, in the event of severe business disruption.</p>
Description and findings re EC4	<p>The <i>RBS Framework</i> require CBN supervisors to determine the presence and to assess banks' contingency plans as part of banks' business continuity strategies to ensure that banks are able to operate as going concern in times of crises. <i>The Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks (Section 5.3.3.1 (a) and (b))</i> also require banks to:</p> <ul style="list-style-type: none"> • have the ability to estimate the probability of the occurrence of an operational loss event and its potential impact. This entails an evaluation of group wide operational risk through a business impact analysis; and • put in place effective internal reporting practices and systems that are consistent with the scope of operational risk defined by supervisors and the banking industry. <p>Banks are also expected to develop mechanisms for assessing and reviewing their internal risk management policies, processes and procedures for individual risk elements (including ORM), at least quarterly. The results of such review are expected to be properly documented and reported to the banks' boards for consideration and approval.</p>

	<p>The CBN supervisors would then consider and assess the adequacy of each bank's risk management policies and strategies (including ORM), at minimum the internal policies and procedures are determined to meet the above regulatory requirements. In assessing the adequacy of banks' risk management systems, CBN supervisor focus, among others on:</p> <ul style="list-style-type: none"> • the banks' sizes and nature of operations; • adherence to the code of corporate governance; and • the quality of the bank's policies and systems for managing specific risks. <p>The assessors sighted a bank's ORM policies and strategies, which were attached to a section note on a bank's treasury operation.</p>
EC5	<p>The supervisor determines that banks have established appropriate information technology policies and processes that address areas such as information security and system development, and have made investments in information technology commensurate with the size and complexity of operations.</p>
Description and findings re EC5	<p><i>The RBS Framework (Section Notes on IT/Business Continuity)</i> requires CBN supervisors to ensure banks establish and maintain IT systems commensurate with the size and complexity of the operations. Banks are also expected to ensure that there are adequate controls in place to protect their systems from failure and must ensure that their systems are sufficiently sound to support the effective management and, where applicable, the quantification of the risks. The CBN has also issued an <i>e-banking Guideline</i> as a framework for IT related product offerings.</p> <p>As part of the supervisory risk assessment of banks, CBN supervisors assess whether banks have established appropriate information technology policies and processes that address areas such as information security and system development. During the course of onsite examination, CBN supervisors assess the MIS structure of the significant activities under review and determine its appropriateness. For example, in reviewing the treasury operations of a bank, CBN supervisors carried out walk through test on the communication flow between the bank's system and CBN RTGS and commented on the instance of communication failure. The assessors noted references to the foregoing in both the section notes and supervisory letter issued to a particular bank.</p>
EC6	<p>The supervisor requires that appropriate reporting mechanisms are in place to keep the supervisor apprised of developments affecting operational risk at banks in their jurisdictions.</p>
Description and findings re EC6	<p>The CBN requires banks to submit a range of data, including return on fraud and forgeries. Currently, CBN is at the initial (discussion) stage in an attempt to put in place a shared service arrangement to, among others, develop a database on operational risk loss data. This initiative is part of the collaboration between CBN and banks.</p>
EC7	<p>The supervisor confirms that legal risk is incorporated into the operational risk management processes of the bank.</p>
Description and findings re EC7	<p>The RBS framework for banks and other financial institutions identifies legal and regulatory risk as one of the seven inherent risk categories, other than and separate from the operational risk category. Similarly, all the generic requirements for overall risk management as per the <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements</i> and general supervisory expectations on risk management, as per <i>RBS Framework</i>, are applicable for banks in managing legal and regulatory risks.</p> <p>During the course of examination, inherent legal and operational risk level is generally measured via the non-compliance cases and consequently, CBN supervisors' walk-through the compliance process to identify the gaps that cause the non-compliance issues. The assessors noted the assessment of legal/regulatory risk management in section notes sighted, in line with the RBS Framework requirement in relation to "Legal and Regulatory Risks."</p>
EC8	<p>The supervisor determines that banks have established appropriate policies and processes to assess, manage and monitor outsourced activities. The outsourcing risk management programme should cover:</p> <ul style="list-style-type: none"> • conducting appropriate due diligence for selecting potential service providers;

	<ul style="list-style-type: none"> • structuring the outsourcing arrangement; • managing and monitoring the risks associated with the outsourcing arrangement; • ensuring an effective control environment; and • establishing viable contingency planning. <p>Outsourcing policies and processes should require the institution to have comprehensive contracts and/or service level agreements with a clear allocation of responsibilities between the outsourcing provider and the bank.</p>
Description and findings re EC8	<p>Via on-site examination, CBN supervisors determine that banks have established appropriate policies and processes to assess, manage and monitor all operational controls (also in relation to outsourcing activities), in line with the RBS Framework requirement that CBN supervisors verify that banks have strong outsourcing controls. The assessors confirmed the foregoing in discussion with CBN supervisors.</p> <p>However, CBN does not have prudential guidelines on outsourcing activities, which among others, should include the following elements:</p> <ul style="list-style-type: none"> • perform due diligence review on the capabilities and expertise of the outsourcing vendors prior to the selection; • obtain approval from banks boards to outsource any function; • obtain written undertaking by the outsourcing vendors to comply with the secrecy provision; • ensure service agreements with the outsourcing vendors include a clause on professional ethics and conduct in performing their duties. The service agreement should also clearly define the roles and responsibilities of the outsourcing vendor; • ensure the service agreement clearly stipulates the right to terminate the service if the outsourcing vendors fail to comply with the conditions imposed; • ensure proper reporting and monitoring mechanisms to ensure that the integrity and quality of work conducted by the outsourcing vendors; • perform regular test and review the work done by the outsourcing vendors; • ensure the right to inspect the books and internal control environment of the outsourcing vendors; and • have contingency plan in the event that the arrangements with the outsourcing vendors are suddenly terminated.
Additional criteria	
AC1	<p>The supervisor determines that the risk management policies and processes address the major aspects of operational risk, including an appropriate operational risk framework that is applied on a group-wide basis. The policies and processes should include additional risks prevalent in certain operationally intensive businesses, such as custody and correspondent banking, and should cover periods when operational risk could increase.</p>
Description and findings re AC1	<p><i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements</i> requires banks to develop strategies for managing each risk element as part of the overall strategy for evolving efficient risk management systems. This guideline is organized by risk categories (including operational risk) and should be adopted based on banks' sizes and complexities, which may include the various group operations within the banks.</p> <p>During the on-site examinations, CBN supervisors determine whether these various units/investment (e.g., subsidiaries) within banks are significant activities and ensure that the requirements under the guideline is adhered to for these activities as well (in addition to the banks operations on solo basis). The assessors noted that all section notes dealt separately with operational risk and addressed the level of inherent operational risk in the relevant bank, as is required by the RBS Framework, which identifies operational risk separately and distinctly.</p>
Assessment of Principle 15	Largely compliant
Comments	The supervisor is satisfied that a bank has in place risk management policies and processes

	<p>to identify, assess, monitor and control/mitigate operational risk, which policies are commensurate with the size and complexity of the bank. Detailed guidance on operational risk management is lacking.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Manage operational risk as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, as operational risk constitutes a significant risk exposure in the case of banks. • Require banks to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant operational risk exposure. • Improve the competencies of supervisory staff in relation to operational risk and operational risk management. • Develop guidance in relation to banks' outsourcing activities.
Principle 16	Interest rate risk in the banking book. Supervisors must be satisfied that banks have effective systems in place to identify, measure, monitor and control interest rate risk in the banking book, including a well defined strategy that has been approved by the Board and implemented by senior management; these should be appropriate to the size and complexity of such risk.
Essential criteria	
EC1	The supervisor determines that a bank's Board approves, and periodically reviews, the interest rate risk strategy and policies and processes for the identification, measuring, monitoring and control of interest rate risk. The supervisor also determines that management ensures that the interest rate risk strategy, policies and processes are developed and implemented.
Description and findings re EC1	<p>The <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks (Section 5.2)</i> does not contain any specific provisions dealing with IRRBB or IRRBB risk management, though there are generic provisions which are tangentially relevant, such as the following:</p> <ul style="list-style-type: none"> • set of systems and procedures, appropriate to the size and complexity of its operations for identifying, measuring, monitoring and controlling market risk; • detailed analyses of assets and liabilities on the overall balance sheet structure of banks to identify the overall market risk; and • accurate and timely measurement of market risk for proper risk management and control. <p>The <i>RBS Framework</i> also does not provide specific and detailed supervisory programme to guide CBN supervisors in assessing IRRBB.</p>
EC2	The supervisor determines that banks have in place comprehensive and appropriate interest rate risk measurement systems and that any models and assumptions are validated on a regular basis. It confirms that banks' limits reflect the risk strategy of the institution and are understood by and regularly communicated to relevant staff. The supervisor also confirms that exceptions to established policies, processes and limits should receive the prompt attention of senior management, and the Board where necessary.
Description and findings re EC2	<p>See BCP16 EC1</p> <p>In view of the inherent pricing structure of banking system balance sheet, which are almost 100 percent on floating rate pricing (for both assets and liabilities), there was minimal emphasis by CBN supervisors for banks to have appropriate risk measurement capabilities to manage IRRBB. Based on samples of section notes on treasury operations, CBN supervisors focus on trading operations and overall market risk but minimal priority on IRRBB.</p>

	Nevertheless, the situation may change and hence, in order to preemptively manage exposures to interest rate risk in the banking book moving forward, CBN should consider having internal limit structure to monitor the interest rate exposures at the bank level.
EC3	The supervisor requires that banks periodically perform appropriate stress tests to measure their vulnerability to loss under adverse interest rate movements.
Description and findings re EC3	<p>The <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks (Section 5.2.3.5)</i> expects banks to stress-test the assumptions and accuracy of the basic methodologies used to model risk exposures in order to quantify the potential impact on the business. In addition, CBN, via the Macro-surveillance Division of Financial Policy & Regulation Department, initiated top-down stress approach in June 2012, whereby banks are required to conduct stress test based on standard templates provided by CBN. Among the shocks applied is the move in yield curve, which reflect the impact of IRRBB. Moving forward, CBN plans to conduct the exercise on six-monthly intervals.</p> <p>The results of the FPRD's top-down stress test exercises have always been shared with the BSD. The two departments, BSD and FPRD, make joint presentations to the MPC regarding the state of the banking industry, using inputs from the stress test results.</p>
Additional criteria	
AC1	The supervisor has the power to obtain from banks the results of their internal interest rate risk measurement systems, expressed in terms of the threat to economic value, including using a standardised interest rate shock on the banking book.
Description and findings re AC1	Under the <i>BOFI Act (Section 25(2))</i> , CBN supervisors have the power to obtain any information to assist in the supervisory process. However, as far as IRRBB is concern, there was no standard regulatory requirement for banks to submit such information.
AC2	The supervisor assesses whether the internal capital measurement systems of banks adequately capture the interest rate risk in the banking book.
Description and findings re AC2	Although CBN supervisors assess the capital management of banks via on-site examination and ensure banks consider all elements of significant risk types in their capital management, IRRBB was not a top of the priority in view of the pricing structure of the balance sheet in the banking system, which suggest that the CBN may consider this a low risk. As explained by a CBN supervisor to the assessors, both the bulk of a bank's assets and liabilities are floating rate in nature, resulting in low IRRBB exposures.
AC3	The supervisor requires stress tests to be based on reasonable worst case scenarios and to capture all material sources of risk, including a breakdown of critical assumptions. Senior management is required to consider these results when establishing and reviewing a bank's policies, processes and limits for interest rate risk.
Description and findings re AC3	See BCP16 EC3
AC4	The supervisor requires banks to assign responsibility for interest rate risk management to individuals' independent of and with reporting lines separate from those responsible for trading and/or other risk-taking activities. In the absence of an independent risk management function that covers interest rate risk, the supervisor requires the bank to ensure that there is a mechanism in place to mitigate a possible conflict of interest for managers with both risk management and risk-taking responsibilities.
Description and findings re AC4	The <i>Guidelines for the Development of Risk Management Frameworks for Individual Risk Elements in Nigerian Banks</i> in general, requires the risk management functions to be independent of the risk taking functions. In addition, <i>RBS Framework</i> also expects CBN supervisors to ensure the risk management functions are independently separated from the business units. This principle in the guideline and <i>RBS Framework</i> should also be applicable to IRRBB.
Assessment of Principle 16	Materially non-compliant

Comments	<p>IRRBB is not separately and specifically identified in the legal, regulatory or supervisory frameworks as a separate risk. The IRRBB exposures of banks appear modest, in view of variable interest rates (mostly) applying to both assets and liabilities. Nonetheless, the interest rate profile of the system may change in the future, and it is imperative that the CBN be suitably prepared.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Apply also, mutatis mutandis, relevant BCP7 recommendations. • Manage IRRBB as a separate risk, in the light of the nature and extent of the activities of the banking sector and of individual banks, as it constitutes an emerging and, perhaps, even a significant risk exposure in the case of certain banks. • Require banks to hold an appropriate (in other words, in relation to the threat which a bank's risk exposure poses to economic value) amount of regulatory eligible capital against significant IRRBB exposure. • Improve the competencies of supervisors in relation to IRRBB and IRRBB management. • FPRD's (top-down) stress test exercise (which includes shocks to IRRBB) results should be shared with BSD, to give supervisors greater insight into source and impact of potential vulnerabilities from IRRBB. <p>See BCP6 and BCP7 for related generic recommendation/s.</p>
Principle 17	<p>Internal control and audit. Supervisors must be satisfied that banks have in place internal controls that are adequate for the size and complexity of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations.</p>
Essential criteria	
EC1	<p>Laws, regulations or the supervisor establish the responsibilities of the Board and senior management with respect to corporate governance to ensure that there is effective control over a bank's entire business.</p>
Description and findings re EC1	<p>In the first instance, banks are companies, and as such, subject to the CAM Act. In the second instance, banks are subject to the BOFI Act and the subsidiary legislation there-under, such as the Code of Corporate Governance.</p> <p>Sections 244 and 279 of CAM Act and Section 4 of the Code of Corporate Governance for Banks in Nigeria prescribe the duties and responsibilities of directors of banks in Nigeria. The CBN Code of Corporate Governance Section 6.1.15 requires DMBs to report on Corporate Governance compliance in their annual reports. Sections 5.4.5 to 5.4.7 of the Code stipulate that banks are to conduct an independent review of the board performance, by external consultants, and the reports thereof be submitted to CBN. Also CBN will henceforth conduct an annual appraisal of banks' directors and the database for that assessment is being built. Similarly, Section 4 of the Code of Corporate Governance issued in 2006 specified the size, composition, and qualifications of the board of directors of banks, to make them have effective control over the bank's entire business.</p>
EC2	<p>The supervisor determines that banks have in place internal controls that are adequate for the nature and scale of their business. These controls are the responsibility of the Board and/or senior management and deal with organizational structure, accounting policies and processes, checks and balances, and the safeguarding of assets and investments. More specifically, these controls address:</p> <ul style="list-style-type: none"> • Organizational structure: definitions of duties and responsibilities, including clear delegation of authority (for example, clear loan approval limits), decision-making policies and

	<p>processes, separation of critical functions (for example, business origination, payments, reconciliation, risk management, accounting, audit and compliance).</p> <ul style="list-style-type: none"> • Accounting policies and processes: reconciliation of accounts, control lists, information for management. • Checks and balances (or “four eyes principle”): segregation of duties, cross-checking, dual control of assets, double signatures. • Safeguarding assets and investments: including physical control.
Description and findings re EC2	<p>The Risk Management Framework requires banks to establish and maintain an effective system of internal control, including the enforcement of official lines of authority and appropriate segregation of duties. The bank’s internal control structure should therefore, ensure the effectiveness of the process relating to the management of individual risk elements. The extant laws and regulations include the BOFI Act; CAMA; Code of Corporate Governance (Sections 7.1.3, 7.1.4 & 8.1.4) and various Circulars issued to banks from time to time.</p> <p>The CBN, in line with the RBS Framework, appraises the internal controls of banks and determines their adequacy, taking into consideration the size and complexity of their business, to ensure the safeguard of assets and investments and prompt reconciliation of accounts. The rules on segregation of duties as well as the reporting line of the internal auditor to the board and the dotted line reporting relationship to the MD/CEO are clearly stipulated—its existence and application is appraised as part of the analysis of the organogram of a bank. (Assessors verified these assertions by way of discussion with relevant parties and scrutiny of relevant documentation.)</p> <p>Major failures in corporate governance at banks have been identified as one of the main factors which contributed to the 2009 banking crisis. Undoubtedly, there were major gaps and breakdowns of internal controls. Though important regulatory reforms have been undertaken and the supervisory approach and processes have been significantly enhanced, at this stage, it is too early to come to a conclusive conclusion on whether supervisory effectiveness is at an acceptable and satisfactory level, though the signs are positive. However, fundamental concerns include whether the stakeholders (including the internal auditor, the external auditor and the supervisor) are effectively challenging one another, and whether the supervisors are willing to act, not only in respect of compliance issues, such as relating to breaches of prudential requirements, but also in respect of corporate governance, risk management and internal control weaknesses, breaches and excesses.</p> <p>It is of grave concern that the very weaknesses (Section 2) and very challenges (Section 3) which the Corporate Governance Code, dated July 1 2006, identified, were at the root of and contributed materially to the onset of the banking crisis of 2009. These weaknesses and challenges included:</p> <ul style="list-style-type: none"> • Ineffective board oversight functions. • Fraudulent and self-serving practices among members of the board, management and staff. • Overbearing influence of chairman or MD/CEO, especially in family-controlled banks. • Weak internal controls. • Non-compliance with laid-down internal controls and operation procedures. • Ignorance of and non-compliance with rules, law and regulations guiding banking business. • Passive shareholders. • Poor risk management practices. • Abuses in lending, including lending in excess of single obligor limit. • Sit-tights directors. • Succumbing to pressure of other stakeholders. • Technical incompetence, poor leadership and administrative ability • Ineffective management information system.

	<ul style="list-style-type: none"> • Insider lending. • Rendition of incorrect or false returns. • Lack of transparency and disclosure. <p>The 2008 Bank Supervision Annual Report noted that the average regulatory capital adequacy of 21.9 percent of the banking sector at the end of December 2008 was satisfactory, when compared with the regulatory minimum of 10 percent. A few months later, it was determined that the regulatory capital adequacy was of the order of only 5 percent. Uneven supervision and enforcement was also identified as one of the main factors which contributed to the 2009 banking crisis. Similar comments apply as were made above in relation to corporate governance.</p>
EC3	Laws, regulations or the supervisor place the responsibility for the control environment on the Board and senior management of the bank. The supervisor requires that the Board and senior management understand the underlying risks in their business and are committed to a strong control environment.
Description and findings re EC3	The Code of Corporate Governance for Banks in Nigeria places the responsibility for the control of banks on board and senior management. The Code requires that appointments to the board and top management should be based on merit and such appointees should have a good understanding of the bank's underlying risks. Section 7.0–7.1.4 stipulates the role of the board and senior management in ensuring that a risk management framework is put in place for the bank. In addition, Section 2.1 of the Risk Management Framework provides that it is the overall responsibility of the board and management of each bank to ensure that adequate policies are put in place to manage and mitigate the adverse effects of all risk elements in its environment.
EC4	The supervisor has the power to require changes in the composition of the Board and senior management to address any prudential concerns related to the satisfaction of these criteria.
Description and findings re EC4	<p>The CBN is empowered to require or make changes in the composition of the board and senior management of banks to address prudential concerns.</p> <p>This power was exercised in 2009 when the CBN removed the board and management of eight banks in Nigeria, following the findings of the CBN/NDIC Joint Examination. (BOFI Act – Section 35(2)(c) & (d))</p>
EC5	The supervisor determines that there is an appropriate balance in the skills and resources of the back office and control functions relative to the front office/business origination.
Description and findings re EC5	<p>Banks must have control functions in place to regularly monitor and evaluate the adequacy of the internal control system and procedures in the institutions.</p> <p>The CBN onsite examination reviews the staff complement of banks and ensures that they are adequately qualified and suitable for the positions and are not assigned multiple conflicting tasks that could compromise their ability to act properly. Any observed weaknesses or shortcomings are reported and appropriate recommendations made. Follow-up actions are carried out to ensure compliance. The introduction of the risk based supervision has enhanced this, as proactive assessment of the systems and personnel are carried out. (Assessors verified these assertions by way of discussion with relevant parties and scrutiny of relevant documentation.)</p>
EC6	The supervisor determines that banks have a permanent compliance function that assists senior management in managing effectively the compliance risks faced by the bank. The compliance function must be independent of the business activities of the bank. The supervisor determines that the Board exercises oversight of the management of the compliance function.
Description and findings re EC6	The CBN requires each bank to have a chief compliance officer who should not be below the rank of a general manager, in addition to having an independent internal control and audit function. Section 8.1.3 of the CBN Code of Corporate Governance for Banks in Nigeria

	<p>requires banks' internal control function to report to the board, but forward a copy to the MD/CEO. Quarterly internal audit reports must be made to the Audit Committee, and made available to supervisors on field visits.</p> <p>The initial assessment is done through the appraisal and approval of the organogram, the RBS review of the internal audit control functions and ensuring that the reporting line is correct. (Assessors verified these assertions by way of discussion and scrutiny of relevant documentation.)</p>
EC7	The supervisor determines that banks have an independent, permanent and effective internal audit function charged with (i) ensuring that policies and processes are complied with and (ii) reviewing whether the existing policies, processes and controls remain sufficient and appropriate for the bank's business.
Description and findings re EC7	<p>Each bank is required to have in place an independent internal audit function. (Code of Corporate Governance for Banks – Section 8.1.1 to 8.1.4.)</p> <p>In line with RBS Framework, during on-site examinations, supervisors assess the organogram as it relates to the internal audit function, the adequacy of the internal audit function to ensure that policies and processes are complied with, and that they remain sufficient for the size and complexity of the bank's business. (Assessors verified these assertions by way of discussion with relevant parties and scrutiny of relevant documentation.)</p>
EC8	<p>The supervisor determines that the internal audit function:</p> <ul style="list-style-type: none"> • has sufficient resources, and staff that are suitably trained and have relevant experience to understand and evaluate the business they are auditing; • has appropriate independence, including reporting lines to the Board and status within the bank to ensure that senior management reacts to and acts upon its recommendations; • has full access to and communication with any member of staff as well as full access to records, files or data of the bank and its affiliates, whenever relevant to the performance of its duties; • employs a methodology that identifies the material risks run by the bank; • prepares an audit plan based on its own risk assessment and allocates its resources accordingly; and • has the authority to assess any outsourced functions.
Description and findings re EC8	<p>The internal audit function of banks should be adequately equipped, have experienced staff that are continuously trained and are independent. Also, the internal audit function should have unfettered access to the records, data, files and any staff. (Code of Corporate Governance for Banks – Section 8.1.7.)</p> <p>The onsite examination reviews the scope/quality of audit plan and its implementation to ascertain the congruence with banks' risk profile as reflected in the identified significant activities, including outsourced functions. (Assessors verified these assertions by way of discussion with relevant parties and scrutiny of relevant documentation.)</p>
Additional criteria	
AC1	In those countries with a unicameral Board structure (as opposed to a bicameral structure with a Supervisory Board and a Management Board), the supervisor requires the Board to include a number of experienced non-executive directors.
Description and findings re AC1	The number of non-executive directors should be more than that of executive directors, and that they should be people of diverse experience with knowledge of business and financial matters. At least two independent non-executive directors should be appointed to the Board. The independent directors must be individuals with vast experience and high degree of success and professionalism that would contribute positively to the decision-making and strategic thinking of the banks. (Code of Corporate Governance for Banks – Sections 5.3.2, 5.3.5, and 5.3.6) The Approved Persons Regime Circular further elaborates on the quality of all types of directors of banks.

AC2	The supervisor requires the internal audit function to report to an audit committee, or an equivalent structure.
Description and findings re AC2	The internal audit function is required to report to the board through its board audit committee. (CAMA) Internal audit should report to the board audit committee and forward a copy of its report to the MD/CEO of the bank. (Code of Corporate Governance – Section 8.1.3)
AC3	In those countries with a unicameral Board structure, the supervisor requires the audit committee to include experienced non-executive directors.
Description and findings re AC3	Members of the bank's board audit committee should be non-executive directors and ordinary shareholders appointed at Annual General Meeting (AGM) and some of them should be knowledgeable in internal control processes. (Code of Corporate Governance for Banks – Section 8.1.4.)
AC4	Laws or regulations provide, or the supervisor ensures, that banks must notify the supervisor as soon as they become aware of any material information which may negatively affect the fitness and propriety of a Board member or a member of the senior management.
Description and findings re AC4	Information that will negatively affect the fit and proper person of a board member should be disclosed. (CAMA) Banks should establish 'whistle blowing' procedures that encourage (including by assurance of confidentiality) all stakeholders (board members, management, staff, customers, suppliers, applicants etc) to report any unethical Activity/breach of the corporate governance code can be reported using, among others, a special email or hotline to both the bank and the CBN. (Code of Corporate Governance for Banks – Section 6.1.12)
Assessment of Principle 17	Largely compliant
Comments	<p>Supervisors are satisfied that banks have in place internal controls that are adequate for the size and complexity of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding the bank's assets; and appropriate independent internal audit and compliance functions to test adherence to these controls as well as applicable laws and regulations. Major failures in corporate governance at banks have been identified as one of the main factors which contributed to the 2009 banking crisis. Undoubtedly, there were major gaps and breakdowns of internal controls. Though important regulatory reforms have been undertaken and the supervisory approach and processes have been significantly enhanced, at this stage, it is too early to come to a conclusive conclusion on whether supervisory effectiveness is at an acceptable and satisfactory level, though the signs are positive. However, fundamental concerns include whether the stakeholders (including the internal auditor, the external auditor and the supervisor) are effectively challenging one another, and whether the supervisors are willing to act proactively, not only in respect of compliance issues, such as relating to breaches of prudential requirements but also in respect of corporate governance, risk management and internal control weaknesses, breaches and excesses. Training of all stakeholders on their duties and responsibilities in relation to all key aspects of banking, and the consequences of breaches and failures of such duties and responsibilities, is necessary.</p> <p>The following recommendation is proposed: Training in all aspects of banking, including, especially, corporate governance (including the roles and responsibilities of the various stakeholders, such as directors, senior management, CEO, COO, CFO, CRO, CIA, CCO, external auditors and the supervisors), risk management (including key risks, such as credit risk, market risk, operational risk, IRRBB, country and transfer risk, and issues such as concentration and large exposures, and related parties) and internal controls) of all stakeholders, including (boards of) directors, executive management, bank personnel, external auditors and supervisors, including on the consequences of breaches and failures of such duties and responsibilities, should be undertaken on an ongoing basis.</p>

Principle 18	Abuse of financial services. Supervisors must be satisfied that banks have adequate policies and processes in place, including strict “know-your-customer” rules, that promote high ethical and professional standards in the financial sector and prevent the bank from being used, intentionally or unintentionally, for criminal activities.
Essential criteria	
EC1	Laws or regulations clarify the duties, responsibilities and powers of the banking supervisor and other competent authorities, if any, related to the supervision of banks’ internal controls and enforcement of the relevant laws and regulations regarding criminal activities.
Description and findings re EC1	<p>The <i>Economic and Financial Crimes Commission Act (Part II and Part III)</i> and the <i>Money Laundering Prohibition Act - MLPA (Section I Article 13)</i>, provide the duties, responsibilities and powers of the CBN supervisors and other competent authorities to control criminal activities. Pursuant to the regulation-making power under <i>BOFI Act</i>, CBN instructed all banks to put in place adequate policies, practices and procedures that will ensure a rigorous customer due diligence through a circular (November 28, 2001) on ‘<i>Know Your Customer</i>’ (KYC) Directive.</p> <p>The existing laws and regulations are not adequate in relation to the criminalization of AML/CFT. (While the CBN is the authority in supervising anti-money laundering (AML) activities (within banking industry), National Financial Intelligence Unit (NFIU) is the over-arching authority for the whole country.)</p> <p>Nigeria’s AML/CTF progress in 2011 relative to its action plan was not considered sufficient by FATF and Nigeria was implored to work towards full implementation of a regime capable of thwarting money laundering and terrorism financing.</p> <p>The CBN commenced full implementation of its AML/CFT Risk-based supervision framework in 2012, and it issued its AML/CFT risk assessment template and questionnaire in August 2012. Accordingly, it is too early to conclude on the effectiveness hereof. Of concern is that the returns are not in electronic format, which would imply significant human and manual intervention, and there does not appear provision for fixing the accountability for the quality of the information in the returns to a (sufficiently) senior person. It is not clear how robust and secure the database of information will be.</p> <p>The Money Laundering (Prohibition) Act (MPLA), 2011, criminalized all the money laundering predicate offences, except fraud and child exploitation. The two omitted predicate offences have now been included in the recent amendment transmitted to the National Assembly (NASS) under signature of the president. The NASS held a public hearing in September 2012. The gazette CBN AML/CFT regulation 2009 (as amended) criminalizes all money laundering predicate offence, as required by FATF.</p>
EC2	The supervisor must be satisfied that banks have in place adequate policies and processes that promote high ethical and professional standards and prevent the bank from being used, intentionally or unintentionally, for criminal activities. This includes the prevention and detection of criminal activity, and reporting of such suspected activities to the appropriate authorities.
Description and findings re EC2	<p>Under <i>Circular to all Banks and Other Financial Institutions: KYC Directive</i>, CBN requires banks to put in place policies and procedures for countering the risks that they might be used to further financial crime. Banks are also required to submit information to CBN and NFIU on unusually huge and suspicious transactions. The directive further strengthens the countering of financial crimes via the daily limit of cash transaction by customers, being a cash withdrawal limit of ₦150,000 and ₦1 million by individuals and corporate customers, respectively.</p> <p>CBN, via the AML Division of Financial Policy & Regulation Department developed supervisory programme vis-à-vis RBS Framework to cater specifically for supervision of AML. Currently, AML Division leverage off banking supervisors to satisfy itself that all AML regulations are adhered to by banks via the regular on-site inspections (AML Division is in the</p>

midst of setting-up its own supervisory unit). A thematic review was once carried out, in 2010, to ascertain the level of banks' compliance with the *KYC Directive*. During the thematic examinations, CBN supervisors reviewed samples of customers' information forms to determine whether the information was updated as per requirement under the *KYC Directives*. The major finding from that thematic review was that banks did not update the KYC information and hence, banks had been instructed to address the issues. CBN planned to carry out such thematic review on annual basis starting from the one scheduled towards the end of 2012.

Major failures in corporate governance at banks, including internal controls, were a main contributing factor to the 2009 banking crisis. It is still too early to conclusively conclude whether or not the corporate governance, including internal controls, at banks are now of an acceptable standard.

The legal and/or regulatory framework does not explicitly and specifically prescribe that the CBN, when considering a new bank license application, should identify and determine the suitability of major shareholders, including the ultimate beneficial owners, and others that may exert significant influence.

A bank is prohibited from employing a person who is or at any time was adjudged bankrupt or has suspended payment to or has compounded with his creditors or who is or has been convicted by a court for an offence involving fraud or dishonesty or professional conduct. Prior to the appointment of a director or CEO, a bank is required to seek and obtain the CBN's written approval for the proposed appointment. No person shall be appointed or remain a director, secretary or an officer of a bank who is of unsound mind or as a result of ill health is incapable of carrying out his duties, is declared bankrupt or suspends payments or compounds with his creditors, or is convicted of any offence involving dishonesty or fraud, or is guilty of serious misconduct in relation to his duties, or in the case of a person possessed of professional qualification, is disqualified or suspended from practicing his profession by the order of any competent authority. Any person whose appointment with a bank has been terminated or who has been dismissed for reasons of fraud, dishonesty or conviction of an offence involving dishonesty or fraud shall not be employed by any bank. (BOFI Act – Section 19 and 48).

The *CBN Guidelines for Obtaining a Commercial Banking License in Nigeria*, dated September 2010, specifies that, as part of the documentation accompanying an application for a commercial banking license, signed fitness and propriety questionnaire and declaration should be submitted in respect of each proposed shareholder, director and manager.

The CBN representatives indicated that implicitly and informally the abovementioned considerations do constitute key issues when coming to a decision whether or not to issue a banking license. A key requirement for a new banking license is a feasibility report on the proposed deposit-taking financial institution, which provides information on the ownership structure detailing names of proposed investor(s), profession/business and percentage shareholding. As part of the license application evaluation process, the CBN conducts background checks (fit and proper tests) on major shareholders and others that could exert significant influence to determine their suitability, and the CBN rejects the shareholding of anyone that is considered not suitable. The CBN conducts capital verification exercise to ascertain the sources of the initial and additional capital injection into banks. In the process of the 2004/2005 banking sector consolidation exercise, ₦406.4 billion was raised by banks from the capital market but only ₦360 billion was accepted by the CBN after verification. The recapitalization exercise and capital verification process also led to the inflow of Foreign Direct Investment (FDI) of US\$652 million and GBP162,000. (The above assertion was made during a discussion between responsible CBN staff and the assessors—written records confirming the fact that CBN conducts background checks were found in the license application file scrutinized by the assessors.)

Other relevant components of the legal and regulatory framework include the "Approved Persons Guidelines," "Requirements for a New Banking License" Ref BSD/BLR/05, "CBN Guidelines for Obtaining a Commercial Banking License" and "Code of Corporate Governance."

	<p>By way of the prescriptions contained in the “Approved Persons’ Regime,” the CBN strives to ensure that only fit and proper persons are considered for appointment to top management positions in banks, as well as hold significant shareholdings (a shareholding in excess of 5 percent).</p> <p>A range of initiatives taken since 2009, including the enforcement of the corporate governance code and updating of the corporate governance code, the authorities have attempted at inculcating into the system the importance and benefits of corporate governance, risk management and internal controls.</p>
EC3	In addition to reporting to the financial intelligence unit or other designated authorities, banks report to the banking supervisor suspicious activities and incidents of fraud when they are material to the safety, soundness or reputation of the bank.
Description and findings re EC3	<p>Banks are required to submit monthly returns to the CBN on fraud and forgery. Further, in collaboration with NFIU, banks are required to report to both institutions cases that relate to financial crimes. <i>Section 2 of the CBN Framework for AML/CFT</i> requires banks to inform NFIU and CBN whenever they detect a known or suspected criminal violation of MLPA or a suspicious transaction related to money laundering activity or a violation of other laws & regulations.</p> <p>There is reporting by banks to the CBN and NFIU on suspicious activities and incidents of fraud when they are material to the safety, soundness or reputation of the bank. Suspicious Transactions Reports (STRs) are only submitted to NFIU, in line with the revised FATF recommendation 29 and internationally generally accepted best practice.</p>
EC4	<p>The supervisor is satisfied that banks establish “know-your-customer” (KYC) policies and processes which are well documented and communicated to all relevant staff. Such KYC policies and processes must also be integrated into the bank’s overall risk management. The KYC management programme, on a group-wide basis, has as its essential elements:</p> <ul style="list-style-type: none"> • a customer acceptance policy that identifies business relationships that the bank will not accept; • a customer identification, verification and due diligence programme; this encompasses verification of beneficial ownership and includes risk-based reviews to ensure that records are updated and relevant; • policies and processes to monitor and recognize unusual or potentially suspicious transactions, particularly of high-risk accounts; • escalation to the senior management level of decisions on entering into business relationships with high-risk accounts, such as those for politically exposed persons, or maintaining such relationships when an existing relationship becomes high-risk; and • clear rules on what records must be kept on consumer identification and individual transactions and their retention period. Such records should have at least a five year retention period.
Description and findings re EC4	<p>Circulars on <i>KYC Directive (November 28, 2001)</i> and <i>CBN AML/CFT Regulation 2009</i> require banks to maintain well documented policies and procedures to prevent and detect money-laundering and terrorist financing. Among others, the directive expects banks to clear record keeping on customers’ transactions. The directive is further reinforced by <i>AML/CFT Regulation 2009 Section 1.3</i>, which requires financial institutions to conduct Customer Due Diligence (CDD). Adherences to these policies are assessed via regular and thematic (as explained in EC2) examinations.</p> <p>As part of the regular examinations, CBN supervisors also review banks’ internal AML/CFT policies and procedures to determine any explicit internal guideline in place that limits banks from transacting with certain group of customers. The last thematic examination on KYC, conducted in 2010, revealed that the CBN supervisors review papers presented to the banks’ boards and senior managements on AML/CFT to determine whether business relationships with high risk customers are subjected to higher approving authorities. By means of the specific supervisory programme (which the assessors scrutinized), developed by the AML Unit, CBN supervisor should be in a position to review the KYC policies and processes to ensure that it is well documented as well as communicated to all relevant staff and integrated</p>

	<p>into the bank's risk management.</p> <p>See also CBN Circular 28 on "Additional Know Your Customer (KYC) requirement in respect to designated non-financial business and professionals (DNFBPs)"</p>
EC5	<p>The supervisor is satisfied that banks have enhanced due diligence policies and processes regarding correspondent banking. Such policies and processes encompass:</p> <ul style="list-style-type: none"> • gathering sufficient information about their respondent banks to understand fully the nature of their business and customer base, and how they are supervised; and • not establishing or continuing correspondent relationships with foreign banks that do not have adequate controls against criminal activities or that are not effectively supervised by the relevant authorities, or with those banks that are considered to be shell banks.
Description and findings re EC5	<p>The assessors determined that CBN supervisors review banks' policies and procedures regarding their corresponding banking relationships and determine whether appropriate customers due diligence are carried out on these banks to fully understand the extent of AML/CFT risks that these banks are exposed to. Where lapses are found, CBN supervisors recommend corrective actions to address them. In addition, CBN has in place formal and informal arrangements for information sharing and cooperation with other supervisory authorities, which can be used to request a status report on the banks with which correspondent relationship is intended by local banks.</p> <p>CBN has also issued specific circular, prohibiting Nigerian banks from providing financial services to certain activities and/or countries. For example, circular <i>(BSD/DIR/CIR/GEN/03/020)</i> dated August 10, 2009 restricted banks from rendering financial services to government agencies and front companies of the Democratic People's Republic of Korea (North Korea) for their involvement in nuclear, ballistic missile and other weapons of mass destruction.</p> <p>Apart from North Korea, no special measures are required in relation to correspondent banks from countries which do not apply or insufficiently apply the FATF recommendations, for example, high-risk countries or countries with strategic AML/CFT deficiencies already identified that had still not made sufficient progress in addressing the deficiencies identified in their action plan.</p> <p>Though there is no specific legislative prescription in this regard, the CBN's (unwritten) policy is not to license shell banks.</p> <p>It appears that correspondent relationships in Nigeria may not involve the maintenance of "payable-through accounts" (PTA) agreements. Nor does there appear to be a prohibition against the establishment or maintenance of correspondent relationships with foreign banks that do not have adequate controls against criminal activities or that are not effectively supervised by relevant authorities.</p>
EC6	<p>The supervisor periodically confirms that banks have sufficient controls and systems in place for preventing, identifying and reporting potential abuses of financial services, including money laundering.</p>
Description and findings re EC6	<p>CBN supervisors, via regular on-site examination and thematic AML review assess the AML controls in place in banks. However, more periodic on-site review on AML/CFT should be conducted, depending on the materiality and issues of concerns of the banks. Moving forward (as explained in EC2), the AML Division has planned to have regular KYC thematic (at least on annual basis) for all banks, subject to its effort to set-up supervisory unit within the division. Currently, all AML reviews (both part of regular on-site examination and AML thematic review) are conducted by the bank supervisors from Banking Supervision Department. AML Division should also consider expanding the proposed annual review on KYC to also include overall control on AML/CFT of banks. Such comprehensive scope would provide an overall view on AML/CFT control at banks on regular and periodic basis.</p>
EC7	<p>The supervisor has adequate enforcement powers (regulatory and/or criminal prosecution) to take action against a bank that does not comply with its obligations related to criminal activities.</p>

Description and findings re EC7	<p>The <i>BOFI Act</i> and <i>AML/CFT Regulation 2009 Article 1.18.1</i> empower CBN to investigate and enforce sanctions. These relevant laws and regulations enables CBN to exercise intervention powers, which includes the power to issue directions and removal of directors from office in certain circumstances, including where CBN is satisfied, that the bank has contravened a provision of the law.</p> <p>Outright criminal activities are referred to the appropriate government agencies e.g., the police and the EFCC. CBN is currently in the midst of reviewing the law to criminalise the AML offenses.</p>
EC8	<p>The supervisor must be satisfied that banks have:</p> <ul style="list-style-type: none"> • requirements for internal audit and/or external experts to independently evaluate the relevant risk management policies, processes and controls. The supervisor must have access to their reports; • established policies and processes to designate compliance officers at the management level, and appointed a relevant dedicated officer to whom potential abuses of the bank's financial services (including suspicious transactions) shall be reported; • adequate screening policies and processes to ensure high ethical and professional standards when hiring staff; and • ongoing training programmes for their staff on KYC and methods to detect criminal and suspicious activities.
Description and findings re EC8	<p><i>Section 360 of CAMA</i> sets out the duties and powers of auditors. In addition, <i>Section 29 of BOFI Act</i> empowers CBN to demand information from the auditors.</p> <p>In ensuring that the internal auditors carry out their duties with respect to auditing the AML/CFT control functions, CBN supervisors review the internal audit reports on AML/CFT control and determine the appropriateness of the internal audit assessments on these functions.</p> <p>In addition, CBN circular (<i>BSD/8/2002</i> dated August 23, 2002) requires banks to appoint Chief Compliance Officers (CCO) responsible for enforcing the provisions of the AML/CFT. Via onsite examinations, CBN supervisors ensure that the positions are in place.</p> <p>Further, <i>Section 19 of the BOFI Act</i> prohibits banks from employing persons who had been adjudged bankrupt, convicted for fraud or dishonesty or professional misconduct. In addition, banks must conduct fit and proper test when hiring their employees and must at all times obtain the prior approval of the CBN when hiring new employees to ensure that those that had been blacklisted for fraud or abuse of the financial system would not be engaged in the banking system.</p> <p>Similarly, CBN also expect continuous training of employees on KYC and methods of detecting criminal and suspicious activities. The training programme and which banks' staff undergo, particularly staff that are responsible for AML/CFT control, should be reviewed, to ensure the right people obtain the necessary training.</p>
EC9	<p>The supervisor determines that banks have clear policies and processes for staff to report any problems related to the abuse of the banks' financial services to either local management or the relevant dedicated officer or to both. The supervisor also confirms that banks have adequate management information systems to provide managers and the dedicated officers with timely information on such activities.</p>
Description and findings re EC9	<p>Via <i>RBS Framework</i>, banks are expected to have adequate management information systems in place to provide managements with timely information, including on abuse of financial services. CBN also requires banks to put in place whistle-blowing mechanisms, which allow information to be passed in confidence as per CBN Circular (<i>BSD/GA/ICB/VOL.4/16</i>) and the provisions of <i>Sections 6.1.1 –6.1.14 of the Code of Corporate Governance</i>.</p> <p>Via the on-site examinations, CBN supervisors request and assess banks' internal whistle-blowing frameworks to determine that at minimum, they meet the expectations of CBN circular. As part of the assessment on <i>Financial Analysis</i> (as required under <i>RBS Framework</i>), CBN supervisors access and assess the banks' internal reporting system to</p>

	determine that banks' senior managements and boards have access to critical frauds and AML/CFT information on timely basis. CBN supervisors also request and review the reports submitted to banks' boards and senior managements to ensure appropriate information on AML/CFT and frauds are escalated to banks' boards and senior managements. The assessors noted that the section notes on a local bank's foreign activities included an assessment of the appropriateness of the system of reporting fraud and related controls, under the heading "Financial Analysis."
EC10	Laws and regulations ensure that a member of a bank's staff who reports suspicious activity in good faith either internally or directly to the relevant authority cannot be held liable.
Description and findings re EC10	<p>CBN has in place the whistle blowing mechanism as per <i>Section 6.1.12 of the Code of Corporate Governance</i>. Furthermore, <i>Section 6 (10) of Money Laundering (Prohibition) Act, 2011</i> which provides that the directors, officers and employees of Financial Institutions and Designated Non-Financial Institutions who carry out their duties under this Act in good faith shall not be liable to any civil or criminal liability or have any criminal or civil proceedings brought against them by their customers. The <i>FOI Act</i> also encourages whistle blowing by providing protection from civil or criminal liability to whistle blowers.</p> <p>The current law and regulations with regards to whistle blowing systems appear appropriate to ensure robust reporting and protection for whistle blowers.</p>
EC11	The supervisor is able to inform the financial intelligence unit and, if applicable, other designated authority of any suspicious transactions. In addition, it is able, directly or indirectly, to share with relevant judicial authorities information related to suspected or actual criminal activities.
Description and findings re EC11	<p>The <i>AML/CFT Act</i> allows CBN to inform NFIU and other relevant agencies of any suspicious transaction. In addition, CBN is able to share directly/indirectly information with judicial authorities. The staff of CBN had also under various oaths delivered to the court, documents and information as requested by them on suspected or actual criminal activities. Under the <i>Freedom of Information Act 2011</i>, the CBN, similar to any public institution, may be compelled to make information available to the public.</p> <p>Generally, CBN supervisors are able to inform the FIU of any suspicious transactions and share with the relevant judicial authorities information related to suspected or actual criminal activities.</p>
EC12	The supervisor is able, directly or indirectly, to cooperate with the relevant domestic and foreign financial sector supervisory authorities or share with them information related to suspected or actual criminal activities where this information is for supervisory purposes.
Description and findings re EC12	<p>The CBN had executed several <i>Memoranda of Understanding (MOU) with foreign supervisors e.g., CBRC (China), SA Reserve Bank (South Africa) and FSA (UK)</i>. On the domestic front, the FSRCC provides an avenue for information sharing among domestic regulators via a master MOU signed by all regulators on FSRCC. These MOUs provide avenues for CBN to share supervisory information with various internal and external regulators, including information on abuse of financial services.</p> <p>For those jurisdictions without formal information sharing arrangement, the informal channel has, so far, been effective in ensuring CBN supervisors obtain the relevant information (including on abuse of financial services) for supervisory purpose. For example, in July 2012 OCC had shared with CBN its concern on AML control of UBA (NY), a branch of UBA Nigeria. It is of serious concern that the UBA head office and/or the CBN did not pick up these issues before the OCC.</p>
Additional criteria	
AC1	If not done by another authority, the supervisor has in-house resources with specialist expertise for addressing criminal activities.
Description and findings re AC1	Although general abuse of financial services and overall AML regulation is handled elsewhere (if outside banking sector e.g., NFIU), CBN has develop its own resources in the area of

	AML/CFT via setting up of AML Division of Financial Policy and Regulation Department. CBN via this unit has a working relationship with the EFCC, NFIU and the Police. The <i>CBN Act</i> , <i>BOFI Act</i> , <i>AML/CFT Act</i> , and other regulatory circulars appear to provide adequate authority for tackling financial crimes.
Assessment of Principle 18	Materially non-complaint
Comments	<p>Though relevant legislation (<i>The Money Laundering Prohibition Act</i> and <i>the Anti-Terrorism Act</i>), KYC guidelines and other regulations are in place to control and check the abuse of financial services, there are fundamental gaps and weaknesses. CBN supervisor is equipped with an appropriate supervisory program and has used this program to assess banks' compliance with the relevant law and regulations as well as to determine whether a bank has adequate policies and processes in place which would prevent the bank from being used intentionally and unintentionally for criminal activities. In the light of the 2011 FATF conclusion on Nigeria, the governance breakdowns which contributed to the 2009 banking crisis and the 2011 report by the OCC on a bank's CML/CFT failings, there remain grave concerns about the quality of implementation and adherence in relation to AML/CFT. As some of the changes to the legal and regulatory framework were implemented only very recently, it is not as yet appropriate to comment on the quality of implementation thereof.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Amend the relevant laws and regulations to bring them in compliance with the international standards, inter alia by criminalizing AML/CFT. • Require that AML/CFT statutory returns, to be completed by a bank, are in electronic format, to facilitate effectiveness and efficiency, and to minimize human manual intervention. Also, the returns should be signed off by senior personnel who are held responsible and accountable for the quality of the information submitted. Sound validation, inter alia by way of onsite verification, and editing controls should be in place to ensure optimal quality information is uploaded into the relevant database/s. • Launch initiatives to improve the effectiveness of AML/CFT in Nigerian banks, including focused thematic examinations of various aspects of a bank's AML/CFT functions, and perform quality control checks to control and monitor such effectiveness. • Maintain a no tolerance policy in respect of criminality and corporate governance abuses and breakdowns, react promptly, firmly and forcefully, and impose strong and effective sanctions.
Principle 19	Supervisory approach. An effective banking supervisory system requires that supervisors develop and maintain a thorough understanding of the operations of individual banks and banking groups, and also of the banking system as a whole, focusing on safety and soundness, and the stability of the banking system.
Essential criteria	
EC1	The supervisor has policies and processes in place to develop and maintain a thorough understanding of the risk profile of individual banks and banking groups.
Description and findings re EC1	CBN implements the <i>Risk-based Supervision (RBS) Framework</i> based on the <i>Supervisory Framework for Banks and Other Financial Institutions in Nigeria</i> . The framework provides a process to assess the safety and soundness of banks, specifically methodology that is used to evaluate risk profiles, financial conditions, risk management practices, and compliance with applicable laws and regulations. The framework assists in the evaluation of risks through an early identification of emerging risks. This is assessed through the Knowledge of Business (KOB) and the Risk Assessment Summary (RAS). The <i>RBS Framework</i> promotes a supervisory process based on the risk profile of banks. It also enables evaluation of risk through the separate assessment of inherent risks and risk management processes. In addition, the Framework is applicable on a consolidated basis (although CBN has yet to apply consolidated supervision fully). It includes assessments of all material entities (subsidiaries,

	<p>branches, or joint ventures) both in Nigeria and internationally.</p> <p>However, detailed supervisory programmes on inherent risks assessment are not available. These programmes are critical to ensure CBN supervisors are properly guided in assessing the inherent risks.</p>
EC2	The supervisor monitors and assesses trends, developments and risks for the banking system as a whole. The supervisor also takes into account developments in non-bank financial institutions through frequent contact with their regulators.
Description and findings re EC2	<p>The CBN supervisors monitor and assess the development in the banking system via regular offsite reviews. The <i>RBS Framework</i> places greater emphasis on the early identification of emerging risks and impacts from external environment. CBN, via Macro-surveillance Division (MSD) of Financial Policy and Regulation Department, initiated a top-down stress testing exercise that involves all banks. The first exercise was conducted in June 2012 and CBN plans for the exercise to be conducted on 6-monthly basis to determine the level of inherent risks of banks (and the whole system) in their activities and their subsidiaries. Moving forward, there will be greater coordination between MSD and Banking Supervision Department (BSD) whereby the MSD will provide regular macro surveillance assessment to BSD as input to the environmental scanning for purpose of identifying emerging risks emanating from external environment.</p> <p>The non-bank institutions are supervised by their respective regulatory institutions (e.g., insurance companies by NICOM) and <i>Section 43 of CBN Act</i> established the Financial Services Regulation Coordinating Committee (FSRCC) for the purpose of coordinating the supervision of financial institutions (both bank and non-bank) and preventing regulatory arbitrage. According to this section, the FSRCC consists of the governor of CBN who is the Chairman, the managing director of NDIC, the director General of SEC, the Commissioner NICOM, the Registrar-General, Corporate Affairs commission and a representative of the Federal Ministry of Finance. Via FSRCC, an MOU between the parties has been signed for effective information sharing. This assists in providing CBN supervisors the information on the development of other sectors. The CBN also carries out joint examination with NDIC, SEC.</p> <p>Overall the <i>RBS Framework</i> is adequate and the relevant regulations are in place to monitor and assess the trends, developments and risks for the banking system including the developments in non-bank financial institutions through frequent contact with their regulators.</p>
EC3	The supervisor uses a methodology for determining and assessing on an ongoing basis the nature, importance and scope of the risks to which individual banks or banking groups are exposed. The methodology should cover, inter alia, the business focus, the risk profile and the internal control environment, and should permit relevant comparisons between banks. Supervisory work is prioritized based on the results of these assessments.
Description and findings re EC3	<p>The supervisor uses the <i>RBS Framework</i> in determining and assessing the scope of risks to which banks are exposed as per the <i>Supervisory Framework for Banks and Other Financial Institutions in Nigeria, July 2008</i>. The supervisory process covers the analysis, planning, action taken, documentation, reporting and follow up, which requires frequent reassessment at various stages of the supervisory process. Analysis and monitoring include reviews of information submitted by banks as well as meetings with key individuals at the banks (during onsite examinations) to discuss trends and emerging issues. The scope of this work depends on the sizes, complexities and the risk profiles of banks. The results of the analysis are used to update the Risk Matrix and the Risk Assessment Summary (RAS). It provides a prospective risk profile and a focus on significant activities that pose critical threats to banks, the basis of which regulatory/supervisory actions to be initiated are established.</p> <p>The RBS process does not cater for the peer comparison (qualitative and quantitative), although the supervisor conducts monthly balance sheet analysis, which includes peer reviews of banks.</p>
EC4	The supervisor confirms banks' and banking groups' compliance with prudential regulations and other legal requirements.
Description and findings re EC4	CBN Supervisors conduct regular onsite and offsite examination of banks to ensure compliance with prudential regulations and requirements. Further, banks are required and

	<p>their external auditors are expected to timely inform CBN supervisors of any breach of laws/regulations as provided by the laws, prudential requirements and explicit supervisory expectations. External auditors of banking institutions are required by law to inform CBN of any non-compliance with laws and regulations by the institutions. (<i>BOFI Act – Section 29 (6)</i>) Also, as part of the regular offsite monitoring, CBN supervisors monitor the regulatory limits e.g., capital adequacy ratio, single obligor limit and liquidity limit via the data submission through e-FASS. Any instance of breach of regulatory limits, Banks are required to explain any instances of breach of regulatory prudential limits, and if the explanations are not satisfactory, the banks are sanctioned with monetary penalties. The assessors sighted examples of e-FASS reports on regulatory limits (including capital adequacy ratios, single obligor limits and liquidity limits) and banks' compliance therewith.</p> <p>In ensuring compliance with regulatory requirements, <i>RBS Framework</i> also promotes reliance on compliance functions of banks. CBN Supervisors assess the compliance functions for all significant activities of banks to determine the level of reliance they can place upon these functions. In assessing the functions, the CBN supervisors review the roles and responsibilities of the functions (including those of the chief compliance officers), the internal policies and procedures governing the compliance functions, the compliance reports as well as the monitoring and follow-up actions on compliance issues.</p> <p>The current supervisory framework which includes onsite and offsite examination is adequate to ensure that banks and banking groups comply with prudential requirements.</p>
EC5	The supervisor requires banks to notify it of any substantive changes in their activities, structure and overall condition, or as soon as they become aware of any material adverse developments, including breach of legal or prudential requirements.
Description and findings re EC5	<p>Banks are expected to notify the supervisor of any substantive changes in their activities, structure and overall condition.</p> <p>In addition, banks must, as per circular dated 1 November 2007 (<i>BSD/DIR/GEN/CIR/V01/014</i>) submit statutory returns on a daily, weekly, mid-monthly, monthly, quarterly and semi-annually basis through e-FASS. These submissions are analysed offsite and such analyses are also used to identify substantive changes in banks' activities and overall conditions.</p> <p>Banks are required, based on the provision of <i>Section 27 (2)</i> of <i>BOFI Act</i>, to publish details of penalties paid as a result of contraventions of the act and any policy guideline.</p> <p>External auditors of banks on the other hand, are required by law to inform CBN of any non-compliance with laws and regulations by the institutions (<i>BOFI Act – Section 29 (6)</i>).</p>
EC6	The supervisor has an adequate information system which facilitates the processing, monitoring and analysis of prudential information. The system aids the identification of areas requiring follow-up action.
Description and findings re EC6	CBN has in place an online information system (e-FASS), which facilitates the processing, monitoring and analysis of prudential information submitted by banks on a daily, weekly, mid-monthly, monthly, quarterly and semi-annually basis. The system has the capacity to compute key financial and regulatory/prudential ratios. The statutory returns are appraised by offsite analysts and where necessary an onsite visit is made for follow-up and monitoring. Currently, the e-FASS is undergoing a review to enhance its features including the incorporation of on-site module.
Additional criteria	
AC1	The supervisor employs a well defined methodology designed to establish a forward-looking view on the risk profile of banks, positioning the supervisor better to address proactively any serious threat to the stability of the banking system from any current or emerging risks.
Description and findings re AC1	<p>The RBS Methodology provides forward-looking assessment of banks' risk profiles and directions of the risks. The directions of risks are assessed based on a certain time horizons for the respective banks. The time horizons considered are indicated in each case.</p> <p>The criteria used by CBN supervisors when assessing the direction of risk is not granularly stated in the <i>RBS Framework</i> e.g., determination of the risk directions should take into</p>

	accounts the assessment of the potential changes in business and economic climates, and the business focuses and risk management strategies.
Assessment of Principle 19	Largely compliant
Comments	<p>The <i>RBS Framework</i> provides an adequate supervisory process, essentially based on the risk profiling of banks, enabling CBN supervisors to have appropriate understanding of the safety and soundness of banks in the system, and has a forward-looking focus. The framework enables a better evaluation of risks through the separate assessment of inherent risks and risk management processes, which also requires CBN supervisors to understand the effect of the external environment, firstly at the level of the banking system and, secondly at the level of the whole economy.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • include peer comparison among banks with similar risk profiles to ensure appropriateness and reasonableness of the RBS assessment; and • develop specific and granular criteria for assessing the direction of risk. Among others, CBN may consider the utilisation of scenario-based stress testing on credit, market and liquidity risks for both the macro and micro level as a tool to provide a forward-looking assessment of a bank's capacities to withstand potential significant adverse macro-financial shocks, as well as the resulting implications to the earnings and capital. In this regard, CBN supervisors should leverage off the top-down stress test exercises conducted by the Macro Surveillance Division of Financial Regulation & Policy Department. <p>See also the recommendations to BCP7</p>
Principle 20	Supervisory techniques. An effective banking supervisory system should consist of on-site and off-site supervision and regular contacts with bank management.
Essential criteria	
EC1	The supervisor employs an appropriate mix of on-site and off-site supervision to evaluate the condition of banks, their inherent risks, and the corrective measures necessary to address supervisory concerns. The specific mix may be determined by the particular conditions and circumstances of the country. The supervisor has policies and processes in place to assess the quality, effectiveness and integration of on-site and off-site functions, and to address any weaknesses that are identified.
Description and findings re EC1	<p>The CBN implements the <i>RBS Framework</i>, which covers the whole supervisory cycle from supervisory planning to issuance of supervisory reports and ratings. This process includes on-going off-site monitoring and on-site examination. Offsite monitoring provides an early warning of the potential areas of concern or risk exposure as well as macro information about the banking industry. The analyses form part of the Knowledge of Business (KOB) documents for all banks. The on-site examinations enhance the process by providing further confirmation of the off-site micro surveillance. Onsite examination also provides the best means of determining the institution's adherence to laws and regulations and helps to prevent problem situations from remaining uncorrected and deteriorating to the point that resolution is required. The <i>BOFI Act (Sections 32 to 34)</i> empowers CBN Supervisors to carry out onsite examination of banks. Similarly, for offsite supervision, <i>BOFI Act (Section 25)</i> requires banks to submit such information, documents, statistics or returns, as the CBN may deem necessary. Circular dated November 1, 2007 (<i>BSD/DIR/GEN/CIR/V01/014</i>) requires all banks to submit statutory returns on a daily, weekly, fortnightly, monthly, quarterly and semi-annually basis. Since the <i>RBS Framework</i> requires a continuous assessment of banks, the understanding, developed through this assessment, enables CBN supervisors to tailor the on-site examinations of banks to their risk profiles.</p> <p>The internal guidelines and procedures on the quality assurance process in the <i>RBS Framework</i> are not adequate to ensure adequate control over the quality of assessment. The rating assigned by the CBN supervisors that reflects the condition of banks should be subjected to quality assurance processes where the supervisory concerns raised and supervisory actions required by the CBN supervisors are challenged by their peers (either</p>

	<p>internally and/or across different departments).</p> <p>The assessors are concerned about the coordination, information sharing and communication between the off-site and on-site functions of both the CBN and NDIC, respectively, as well as between CBN and NDIC, in view of examples of suboptimal coordination, information sharing and communication. With effect from 2013, the CBN's offsite and on-site functions will be housed in the new CBN building in Lagos—hopefully this will assist in largely resolving the above-mentioned issues.</p>
EC2	<p>The supervisor has in place a coherent process for planning and executing on-site and off-site activities. There are policies and processes in place to ensure that such activities are conducted on a thorough and consistent basis with clear responsibilities, objectives and outputs, and that there is effective coordination and information sharing between the on-site and off-site functions.</p>
Description and findings re EC2	<p><i>Section 12</i> of the <i>RBS Framework</i> details the supervisory process, which includes analysis, planning, documentation, reporting and follow-up. Risks assessments therefore, are updated on a continuous basis through a process of information sharing between onsite and offsite functions. The level of regulatory interventions and resources required for each bank depend on its composite risk rating. On-site and off-site supervisory strategies are prepared at the beginning of each fiscal year and outlines work planned and resources required. The scope of the work planned is based on the Risk Assessment Summary (RAS). The focus is on the activities and risk management processes identified in the RAS as significant risk areas. The RAS is used to prioritise the supervisory plan for upcoming year and supervisory resources allocations are influenced by a bank's size, complexity, risk profile and systemic impact.</p>
EC3	<p>On-site work, conducted either by the supervisor's own staff or through the work of external experts, is used as a tool to:</p> <ul style="list-style-type: none"> • provide independent verification that adequate corporate governance (including risk management and internal control systems) exists at individual banks; • determine that information provided by banks is reliable; • obtain additional information on the bank and its related companies needed for the assessment of the condition of the bank, the evaluation of material risks, and the identification of necessary remedial actions and supervisory actions, including enhanced off-site monitoring; and • monitor the bank's follow-up on supervisory concerns.
Description and findings re EC3	<p>CBN requires banks annually to engage independent consultants to appraise the quality of the boards' oversight functions, in order to confirm adherence to good corporate governance, which reports are then submitted to the CBN for its scrutiny.</p> <p>To determine the quality of information (whether the structured/statutory information submissions on a daily, weekly, mid-monthly, monthly, quarterly and semi-annually basis or ad-hoc information requests) provided by banks, CBN supervisors use a multiple authentication process during on-site examination e.g., via walk-through process and reviewing the published financial statements, and comparing the results with the submitted information. For example, in examining the treasury activities of banks, CBN supervisors trace samples of information generated by back office functions (e.g., blotter reports on FGN bonds and T-bills) to the sub ledger and finally the financial statements. This information is then compared with the data submitted via e-FASS to determine the completeness and accuracy of the figures.</p> <p>The <i>RBS Framework</i> requires that policies and procedures be put in place for assessing the quality, effectiveness and integration of onsite and offsite examinations, and for steps to be taken in addressing identified weaknesses. Monitoring and follow-up should be an integral part of this process. In addition, the RBS framework requires continuous monitoring and follow-up of banks.</p> <p>In general, the onsite work carried out by the supervisors and/or external experts appears adequate to address the corporate governance, risk management and internal controls of the banks as well as proper monitoring and follow up on supervisory concerns.</p>

EC4	<p>Off-site work is used as a tool to:</p> <ul style="list-style-type: none"> • regularly review and analyse the financial condition of individual banks using prudential reports, statistical returns and other appropriate information, including publicly available information; • follow up on matters requiring further attention, evaluate developing risks and help identify the priorities and scope of further work; and • help determine the priorities and scope of on-site work.
Description and findings re EC4	<p>The off-site surveillance function involves monitoring of the financial performance and condition of banks via regular reviews of banks' financial data and information submitted to CBN under regulatory requirements or as specifically requested, and banks' returns are monitored on a continuous basis. These returns from banks are analysed and regulatory concerns on the health of each bank are documented. This process is complemented by ad-hoc information that CBN supervisors obtained from other formal and informal sources e.g., the media. Supervisory letters are sent to banks on any issues identified that require immediate attention while areas that need follow up are referred to the onsite function for further actions. The issues and recommendations communicated to the banks are followed-up on a timely basis and the results included in the RAS updates. As timely follow up is a critical component of continuous supervision, banks are given reasonable, but firm, deadlines for corrective action and are expected to provide regular reports on progress achieved. The KOBs prepared by off-site team on banks assist to determine the priorities and scope of onsite work to be carried out.</p> <p>Offsite surveillance appears to be adequate to enable regularly review and analysis of the financial condition of the banks with proper follow up actions taken on supervisory concerns. The offsite surveillance work also compliments the onsite supervision in helping determine the priorities and scope of the onsite work.</p>
EC5	<p>Based on the risk profile of individual banks, the supervisor maintains sufficiently frequent contacts as appropriate with the bank's Board, non-executive directors, Audit Committee and senior and middle management (including heads of individual business units and control functions) to develop an understanding of and assess such matters as strategy, group structure, corporate governance, performance, capital adequacy, liquidity, asset quality and risk management systems.</p>
Description and findings re EC5	<p><i>Section 31 (2) (c) of BOFI Act</i> empowers the CBN to maintain contact with banks' board members, non-executive directors, audit committee members, senior managements and any staff, in order to monitor developments in banks and assess their understanding of the risks inherent in their operations.</p> <p>The relationship managers (RM) are the focal points of contact with banks, maintaining regular on-going communications throughout the supervisory process (namely analysis, planning, execution, reporting and follow-up). For larger banks with greater systemic impacts, the engagements involve at least quarterly visits. Information requested from banks is based on specific requirements arising from the risk assessment process (in addition to the statutory returns). During onsite examinations, CBN supervisors engage with banks' managements and external auditors. These engagements are followed up by reporting to the CEOs and the board members.</p> <p>In general, CBN supervisors appear to maintain sufficient contact with banks' key managements to provide effective process to assess the safety and soundness of those banks.</p> <p>However, engagements with board members (particularly with the members of board risk management committees and/or board audit committees) are not common outside the onsite examination process.</p>
EC6	<p>On an ongoing basis during on-site and off-site supervisory activities, the supervisor considers the quality of the Board and management.</p>
Description and findings re EC6	<p>In considering the quality of the boards (including board committees) and managements of banks, CBN supervisors are guided by the <i>RBS Framework</i>, which provides the assessment framework in determining the overall rating board and senior management oversights.</p>

	<p>The assessors determined that during the onsite examinations, CBN supervisors review boards' terms and references, and minutes of boards meetings as well as various board-related and management-related committees to conclude the above supervisory assessments. CBN supervisors also interview the member of the banks' boards and senior management. Board members and senior management are also appraised using 'fit and proper' test as per circular (FPR/DIR/GEN/01/016) dated June 21, 2011 on <i>Approved Persons Regime</i>. The appraisals are carried out upon new appointments and reappointments of directors. For example, a proposal for appointment of an independent director of a particular bank was rejected in December 2011 after offsite analysis discovered that the candidate did not fulfill the "independence" requirement. In addition, Annual appraisal of boards and individual members are carried out and report submitted to the CBN as per <i>Section 5.4.7 of the Code of Corporate Governance</i>.</p>
EC7	<p>The supervisor evaluates the work of the bank's internal audit function, and determines whether, and to what extent, it may rely on the internal auditors' work to identify areas of potential risk.</p>
Description and findings re EC7	<p>Under the <i>RBS Framework</i> and methodology, the assessments of internal audit functions are carried out as part of the assessments on the risk management control functions of banks. The assessments are carried out on a horizontal basis for each significant activity as well on vertical (track 2) basis for overall internal audit functions. Detailed supervisory programme is in place to guide CBN supervisors in assessing the effectiveness of the functions.</p> <p>The assessors determined that in assessing banks' internal audit functions, CBN supervisors review the internal audit departments' structures, reporting lines, internal audit programmes, internal audit plans and internal audit reports.</p>
EC8	<p>The supervisor communicates to the bank the findings of its on- and off-site supervisory analyses by means of written reports or through discussions or meetings with management.</p>
Description and findings re EC8	<p>The assessors determined that after an examination, CBN supervisors hold exit discussions with the management of affected banks to discuss their findings. Supervisory letters are then sent to those banks (addressed to the chairmen of boards), highlighting areas of concern and requiring the banks to provide concrete action plans and time frames to address lapses (as per discussion during the exit meetings). The offsite function also sends supervisory letters to banks informing of lapses observed during off-site monitoring and requesting banks to carry out remedial actions where necessary.</p>
Additional criteria	
AC1	<p>The supervisor meets periodically with senior management and the Board to discuss the results of supervisory examinations and the external audit. The supervisor should also meet separately with the independent Board members, as necessary.</p>
Description and findings re AC1	<p>The results of onsite examinations and off-site surveillance are discussed with management and the Board (refer to BCP20 EC 8). The external auditors of the bank are also required to be present at such meetings. When necessary, CBN supervisors have separate meetings with independent directors to seek insights into the roles played by the boards and their committees. Results of supervisory examinations are communicated to banks' senior managements, boards and external auditor and when necessary engagements with independent director are also conducted.</p> <p>Nevertheless, CBN supervisors should also regularly engage the board members of banks outside the onsite examination process (please see similar comment in EC5), particularly with non executive and independent directors.</p>
Assessment of Principle 20	<p>Largely compliant</p>
Comments	<p>There is a proper mix of on-site and off-site supervisors to evaluate the condition of banks and their inherent risks. However, efforts should be in place to increase the quality of the assessment by having independent proper quality assurance process to determine the ratings of banks and more engagement is recommended with the banks' board members, particularly the independent and non-executive members, outside the onsite examination period.</p>

	<p>It is recommended that the CBN:</p> <ul style="list-style-type: none"> • develop an independent formal governance process on quality assurance of overall ratings determined for banks and supervision in general, which may include the involvement of the CBN's risk management and internal audit functions; and • ensure regular and timely communications of any supervisory issues with banks' boards members, even outside the onsite examination process.
Principle 21	Supervisory reporting. Supervisors must have a means of collecting, reviewing and analyzing prudential reports and statistical returns from banks on both a solo and a consolidated basis, and a means of independent verification of these reports, through either on-site examinations or use of external experts.
Essential criteria	
EC1	The supervisor has the power to require banks to submit information, on a solo and a consolidated basis, on their financial condition, performance, and risks, at regular intervals. These reports provide information on such matters as on- and off-balance sheet assets and liabilities, profit and loss, capital adequacy, liquidity, large exposures, asset concentrations (including by economic sector, geography and currency), asset quality, loan loss provisioning, related party transactions, interest rate risk and market risk.
Description and findings re EC1	The CBN has the power to require banks to submit to it information on solo basis. (BOFI Act – Section 25) (Upon implementation of the updated draft Consolidated Supervision Framework, the CBN should be empowered to request consolidated financial reports and prudential returns. (Circular reference BSD/DIR/CIR/07/V.1/11 dated August 27, 2007 on Consolidated Supervision – Section 3.4.2.1.1.2.1.) The CBN has in place a robust RBS Framework and a prudential guideline for the risk profiling of banks.
EC2	The supervisor provides report instructions that clearly describe the accounting standards to be used in preparing supervisory reports. Such standards are based on accounting principles and rules that are widely accepted internationally.
Description and findings re EC2	With effect from the 2012 financial year, all banks are required to apply IFRS. The CBN prescribes minimum and additional disclosure requirements. (CBN Circular BSD/DIR/CIR/04/004 dated January 18, 2010 on the minimum disclosure requirements in the published accounts.)
EC3	The supervisor requires banks to utilize valuation rules that are consistent, realistic and prudent, taking account of current values where relevant.
Description and findings re EC3	The CBN issued a Prudential Guidance (PG) which stipulates, inter alia, valuation rules. Section 3.11 of the PG specifies that banks must obtain prior approval of the CBN before any revaluation surplus on fixed assets is recognized in their books. (The CBN is in the process of developing guidelines on valuation of bonds and other fixed income financial instruments.)
EC4	The supervisor collects and analyses information from banks at a frequency (e.g., monthly, quarterly and annually) commensurate with the nature of the information requested, and the size, activities and risk profile of the individual bank.
Description and findings re EC4	<p>Banks are required to submit their returns (daily, weekly, monthly, quarterly, and semi-annually) in order to provide timely information to the regulatory authorities. (CBN circular BSD/DIR/GEN/CIR/VI/014 dated November 1, 2007)</p> <p>The assessors confirmed that these returns are received from the banks electronically, through the e-FASS, and are analyzed to ascertain compliance with prudential and other requirements</p>
EC5	In order to make meaningful comparisons between banks and banking groups, the supervisor collects data from all banks and all relevant entities covered by consolidated supervision on a comparable basis and related to the same dates (stock data) and periods (flow data).
Description and	Banks are required to apply a uniform accounting year-end of December 31, which enables

findings re EC5	direct comparison between banks, reduces the possibility of obfuscating transactions at year end and enhance transparency in the banking industry. (CBN Circular BSD/DIR/GEN/VOL.2/004 dated June 18, 2009)
EC6	The supervisor has the power to request and receive any relevant information from banks, as well as any of their related companies, irrespective of their activities, where the supervisor believes that it is material to the financial situation of the bank or banking group, or to the assessment of the risks of the bank or banking group. This includes internal management information.
Description and findings re EC6	<p>The CBN is empowered to request and receive relevant information from banks. Also, banks are required to submit to the CBN a statement of their assets and liabilities and analysis of loans and advances and other assets at all its locations, including those outside Nigeria. (BOFI Act – Section 25 and 33)</p> <p>The updated draft Framework for Consolidated Supervision of Financial Institutions in Nigeria dated May 2011 requires that all risks incurred by a banking group, no matter where they are booked, are evaluated and controlled on a global basis. (To date, the CBN has not implemented consolidated supervision.)</p> <p>The CBN is not empowered to request and receive relevant information from the related entities of banks.</p>
EC7	The supervisor has the power of full access to all bank records for the furtherance of supervisory work. The supervisor also has similar access to the bank's Board, management and staff, when required.
Description and findings re EC7	The CBN is empowered to have full access to all bank's records in furtherance of its supervisory work—for instance, the Director of Banking Supervision shall have a right of access at all times to the books, accounts and vouchers of banks; have power to require from directors, managers and officers of banks such information and explanation as he deems necessary for the performance of his duties. (CBN Act and BOFI Act – Section 31)
EC8	The supervisor has a means of enforcing compliance with the requirement that the information be submitted on a timely and accurate basis. The supervisor determines that the appropriate level of senior management is responsible for the accuracy of supervisory returns, can impose penalties for misreporting and persistent errors, and can require that inaccurate information be amended.
Description and findings re EC8	The CBN has power to enforce compliance with the requirement that information be submitted on a timely and accurate basis. Also, a bank can be sanctioned for misreporting. (BOFI Act – Section 31 and 60) In addition, banks are subject to very stiff sanctions, including the removal of the CEO, for false rendition of returns. The CEO and Chief Compliance Officers are required to certify that each statutory return submitted to the CBN does not contain any untrue statement of material fact and that the financial statements contain fair view of the financial condition of the reporting entity. (Code of Corporate Governance – Section 6.1.3 and 6.1.4)
EC9	The supervisor utilizes policies and processes to confirm the validity and integrity of supervisory information. This includes a program for the periodic verification of supervisory returns by means either of the supervisor's own staff or of external experts.
Description and findings re EC9	The assessors confirmed that banks submit both hard and soft copies of statutory returns, which are analyzed by the supervisors and that the CBN undertakes onsite reviews to confirm the validity and integrity of information reported by banks. In addition, routine examinations and spot checks are carried out to validate/verify that risk management and internal controls exist in banks and that information analyzed off-site on banks is reliable. For instance, the Monthly Bank Return 300 obtained off-site from the returns submitted by banks is reconciled and compared on-site. In other instances, consultants are engaged to assist the supervisors. This was the case during the banking consolidation program of 2004/2005. In addition, the CBN engaged consultants for its Project Alpha reform program to facilitate the recapitalization processes of the intervened banks.

	There is no legal duty on a bank to notify the CBN of all material information regarding the a bank's activities, structure or overall condition or material adverse developments as soon as possible.
EC10	The supervisor clearly defines and documents the roles and responsibilities of external experts, including the scope of the work, when they are appointed to conduct supervisory tasks and monitors the quality of the work. External experts may be utilized for routine validation or to examine specific aspects of banks' operations.
Description and findings re EC10	The CBN is empowered to appoint and commission external experts to carry out supervisory responsibilities. (BOFI Act – Section 1) Whenever consultants are engaged, their duties and responsibilities, including the scope of the work, are clearly defined and documented in their engagement letter. Key examples include the engagement of consultants to guide the implementation of RBS and banking sector reforms.
EC11	The supervisor requires that external experts bring to its attention promptly any material shortcomings identified during the course of any work undertaken by them for supervisory purposes.
Description and findings re EC11	See BCP21 EC10.
Assessment of Principle 21	Largely compliant
Comments	Supervisors are empowered to obtain information from banks, but not from entities related to banks, and have a means of collecting, reviewing and analyzing prudential reports and statistical returns from banks on a solo, but not (as yet) on a consolidated basis, and a means of independent verification of these reports, through either on-site examinations or use of external experts. (To date, the authorities have not as yet implemented consolidated supervision.) The following recommendations are proposed: <ul style="list-style-type: none"> • Give consideration to incorporating into the e-FASS system a workflow module (for handling also correspondence and other routine supervisory tasks) and an on-site supervision module (including work programs and work papers), to leverage e-FASS and optimize the efficiency of supervision. • Require a bank to notify the CBN of all material information regarding the bank's activities, structure or overall condition or material adverse developments as soon as possible.
Principle 22	Accounting and disclosure. Supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with accounting policies and practices that are widely accepted internationally, and publishes, on a regular basis, information that fairly reflects its financial condition and profitability.
Essential criteria	
EC1	The supervisor has the power to hold bank management and the bank's Board responsible for ensuring that financial record-keeping systems and the data they produce are reliable.
Description and findings re EC1	In the first instance, a bank is a company and, as such, is also subject to the relevant corporate legislation. A company is required to cause accounting records to be kept, which records should be sufficient to show and explain the transactions of the company and shall be such as to disclose with reasonable accuracy the financial position and performance of the company. Annually, the company is required to prepare financial statements (which reflect a true and fair view of the state of affairs and performance of the company) which are required to be accompanied by an auditor's report. The financial statements are required to comply with prescribed accounting standards. A company is required to appoint an (independent

	<p>external) auditor to audit the financial statements. Failure to comply with the requirements constitutes an offence and, upon conviction, could result in a fine. A company acts through its members in general meeting or its board of directors or through officers or agents appointed by or under authority derived from the members in general meeting or the board of directors. (CAM Act – Section 63, 65, 331-341 and 358)</p> <p>A bank is required to keep proper books of account with respect to all the transactions of the bank to enable a true and fair view of the state of affairs of the bank to be reflected in financial statements, in compliance with the prescribed accounting standard. A bank is required to submit to the CBN various statutorily prescribed returns, duly completed and populated, as well as such other information, documents, statistics or returns as the CBN may deem necessary for the proper understanding of the returns. The banks' financial statements are required to give a true and fair view of the state and performance of a bank. A bank is required to appoint a CBN approved auditor who is required to express an opinion on whether the financial statements reflect a true and fair view of the state and performance of the bank. Prior to the publication of the bank's annual audited financial statements, a bank is required to submit the bank's draft annual audited financial statements to the CBN for approval. Failure to comply with the abovementioned requirements would render the bank guilty of an offence and liable to a fine upon conviction. (BOFI Act – Section 24, 25, 27 and 28).</p> <p>It has been recognized at the highest levels that major failure in corporate governance at banks and inadequate disclosure and transparency about the financial position of banks contributed to the 2009 banking crisis. (The Nigerian Banking Industry: What went wrong and the way forward" by Governor Sanusi, dated February 26, 2010.) The role of the external audit procession in this context, seemingly, has not as yet (sufficiently) come under the spotlight. The external auditors issued unqualified audit reports in respect of all the existing banks for the 2008 financial year.</p>
EC2	The supervisor has the power to hold bank management and the bank's Board responsible for ensuring that the financial statements issued annually to the public receive proper external verification and bear an external auditor's opinion.
Description and findings re EC2	<p>See BCP22 EC1.</p> <p>Every bank is required to appoint an external auditor, being a person previously approved by the CBN and who is required to issue an audit report on the annual financial statements. An external auditor is required to be a member of a recognized professional body and carrying on a professional practice as accountant and auditor. Persons who may have conflicts of interest, such as a shareholder of the bank, a director of the bank, an officer of the bank, etcetera, shall not be eligible for appointment as the external auditor of the bank. (BOFI Act – Section 29) An external auditor is required to maintain an arms'-length relationship with a bank which it audits—accordingly, the external auditor is restricted from rendering certain services, which could cause a conflict of interest, to the bank which it audits. An external auditor's tenure as an external auditor of a bank is limited to 10 years. (Code of Corporate Governance – Section 8.2.0)</p>
EC3	The supervisor requires banks to utilize valuation rules that are consistent, realistic and prudent, taking account of current values where relevant, and to show profits net of appropriate provisions.
Description and findings re EC3	A bank's audited annual financial statements are required to be prepared in accordance with IFRS and audited in accordance with Nigerian Auditing Standards (which are based on International Standards of Auditing) For regulatory purposes, a bank is required to comply with more stringent requirements in certain areas, such as provisioning. (Prudential Guidelines for Deposit Money Banks)
EC4	Laws or regulations set, or the supervisor has the power, in appropriate circumstances, to establish, the scope of external audits of individual banks and the standards to be followed in performing such audits.

Description and findings re EC4	<p>The CBN is empowered to order a special examination or investigation of the books and affairs of a bank where it considers this to be in the public interest to do so, where the bank has been carrying on its business in a manner detrimental to the interest of its depositors and creditors, or the bank has insufficient assets to cover its liabilities to the public or the bank has been contravening the provisions of the law. The CBN is empowered to appoint qualified persons other than officers of the CBN to conduct such examination or investigation of the books and affairs of the bank. (BOFI Act – Section 33)</p> <p>(Note: In terms of ISAs, an audit is per definition an unlimited scope engagement. Any limitations placed on the scope of the external auditor's audit would impair the audit. An external auditor is permitted to perform limited scope, focused, engagements—which would not be audits and where the level of assurance to be drawn there from would be limited.)</p>
EC5	Supervisory guidelines or local auditing standards determine that audits cover such areas as the loan portfolio, loan loss reserves, nonperforming assets, asset valuations, trading and other securities activities, derivatives, asset securitizations, and the adequacy of internal controls over financial reporting.
Description and findings re EC5	<p>With effect from 2012, a bank's audited annual financial statements are required to be compiled in accordance with IFRS and the independent external audit is required to be performed in accordance with Nigerian Auditing Standards, which are based on International Standards of Auditing (ISAs).</p> <p>ISAs prescribe a full scope audit, in other words, an audit where the auditor is not constrained and has access to all necessary and relevant information. IFRS prescribes that the totality of the entity's financial position and performance should be accounted for and disclosed on a basis which renders a true and fair view thereof.</p>
EC6	The supervisor has the power to reject and rescind the appointment of an external auditor that is deemed to have inadequate expertise or independence, or not to be subject to or not to follow established professional standards.
Description and findings re EC6	<p>Only an auditor who is a member of one of the professional bodies recognized in Nigeria, and is carrying on in Nigeria a professional practice as accountant and auditor, and is approved by the CBN may be appointed as the auditor of a bank. (BOFI Act – Section 29)</p> <p>The BOFI Act does not specifically and explicitly empower the CBN to remove a bank's auditor who does not discharge his responsibilities satisfactorily</p>
EC7	The supervisor requires banks to produce annual audited financial statements based on accounting principles and rules that are widely accepted internationally and have been audited in accordance with internationally accepted auditing practices and standards.
Description and findings re EC7	See BCP22 EC1 and EC5.
EC8	Laws, regulations or the supervisor require periodic public disclosures of information by banks that adequately reflect the bank's true financial condition. The requirements imposed should promote the comparability, relevance, reliability and timeliness of the information disclosed.
Description and findings re EC8	<p>BCP22 EC1 and EC5.</p> <p>Subject to the prior written approval by the CBN of the draft audited annual financial statements, a bank is required to publish its audited annual financial statements, which gives a true and fair view of the state of affairs and performance of the bank, within four months of the bank's financial year end. The audited annual financial statements are required to be placed in the public domain and furnished to the CBN. (BOFI Act – Section 27 and 28) CBN has prescribed a common year end of December 31 for all banks.</p> <p>A CBN circular sets out the minimum information to be disclosed in banks' financial statements. (CBN circular BSD/DIR/GEN/CIR/04/004 of January 19, 2010)</p>

EC9	The required disclosures include both qualitative and quantitative information on a bank's financial performance, financial position, risk management strategies and practices, risk exposures, transactions with related parties, accounting policies, and basic business, management and governance. The scope and content of information provided and the level of disaggregation and detail should be commensurate with the size and complexity of a bank's operations.
Description and findings re EC9	See BCP22 EC8. Financial statements should include both qualitative and quantitative information on the bank's financial performance, corporate governance and risk management, in line with the size and complexity of its operations. (CBN circular BSD/DIR/GEN/CIR/04/004 of January 19, 2010 on Minimum Information to be Disclosed in the Financial Statements)
EC10	Laws, regulations or the supervisor provide effective review and enforcement mechanisms designed to confirm compliance with disclosure standards.
Description and findings re EC10	Off-site and on-site examinations assess, inter alia, whether a bank is in compliance with disclosure requirements. (Assessors verified this assertion by way of discussion and scrutiny of relevant documentation.)
EC11	The supervisor or other relevant bodies publish aggregate information on the banking system to facilitate public understanding of the banking system and the exercise of market discipline. Such information includes aggregate data on balance sheet indicators and statistical parameters that reflect the principal aspects of banks' operations (balance sheet structure, capital ratios, income earning capacity, and risk profiles). (Assessors verified this assertion by way of discussion and scrutiny of relevant documentation.)
Description and findings re EC11	CBN is empowered to publish aggregated information on the banking sector, based on the returns which banks are required to submit to the CBN, inter alia as part of the CBN's Statistical Bulletin and the semi-annual Financial Stability Report. (BOFI Act – Section 25 and 26) Since 2009, the CBN has not published an annual bank supervision report. With effect from 2011, a semi-annual Financial Stability Report (FSR), which strives to cover also what previously was covered by the annual bank supervision report, has been issued.
Additional criteria	
AC1	The supervisor meets periodically with external audit firms to discuss issues of common interest relating to bank operations.
Description and findings re AC1	Supervisors, accounting standards setting bodies, external audit firms and the FRCoN meet periodically to discuss issues of common interest relating to banks' operations and financial reporting. Such meetings have been few and far between, which appears to point to capacity and capability constraints on the part of the CBN. External auditors are also present at the opening and exit discussions held with banks during on-site examination. As a matter of practice, the BSD furnishes external auditors of banks with copies of its onsite findings reports issued to the banks at the conclusion of an on-site examination. (Assessors verified this assertion by way of discussion and scrutiny of relevant documentation.)
AC2	External auditors, whether or not utilized by the supervisor for supervisory purposes, have the duty to report to the supervisor matters of material significance, for example failure to comply with the licensing criteria or breaches of banking or other laws, or other matters which they believe are likely to be of material significance to the functions of the supervisor. Laws or regulations ensure that auditors who make any such reports in good faith cannot be held liable for breach of a duty of confidentiality.
Description and	The audited annual financial statements are required to disclose in detail penalties paid as a

findings re AC2	<p>result of contravention of the provisions of the BOFI Act and provisions of any policy guidelines, and the auditor's report shall reflect such contravention. If the auditor is satisfied that there has been a contravention of the BOFI Act or an offence under any other law has been committed by the bank or any other person; or losses have been incurred by the bank which substantially reduce the bank's capital' or any irregularity has occurred; or he is unable to confirm that the claims of depositors or creditors are covered by the assets of the bank, he is required immediately to report the matter to the CBN. (BOFI Act – Section 27 and 29) The BOFI Act does not contain any provision to protect an auditor who made such a report in good faith.</p> <p>External auditors of banks are required to render reports to the CBN on bank's risk management practices, internal control and level of compliance with regulatory directives. The implementation of this requirement still poses a challenge to supervisors as they have not been able to finalize the scope and wording of such reports. (Code of Corporate Governance for Banks – Section 7.1.4)</p>
AC3	Laws, regulations or the supervisor require banks to rotate their external auditors (either the firm or individuals within the firm) from time to time.
Description and findings re AC3	The audit tenure of a bank's external audit firm is limited to 10 years, after which the external audit firm is not permitted to be reappointed as the bank's external audit firm for 10 years. (Code of Corporate Governance – Section 8.2.3; Prudential Guidelines for Deposit Money Banks – Section 4.2)
AC4	The supervisor requires banks to have a formal disclosure policy.
Description and findings re AC4	<p>See BCP22 EC5 and EC7.</p> <p>Various disclosure requirements are imposed on banks. However there is no formal requirement for a bank to have a formal disclosure policy.</p> <p>Inadequate disclosure and transparency about the financial position of banks has been identified as having contributed to an extremely fragile financial system. (Prudential Guidelines for Deposit Money Banks, dated July 2010)</p>
AC5	The supervisor has the power to access external auditors' working papers, where necessary.
Description and findings re AC5	The legal and/or regulatory framework does not specifically and explicitly empower the CBN to obtain access to external auditor's working papers, where necessary.
Assessment of Principle 22	Largely compliant
Comments	<p>Generally, the CBN seemingly ensures that each bank maintains adequate records drawn up in accordance with accounting policies and practices that are widely accepted internationally, and publishes, on a regular basis, information that fairly reflects its financial condition and profitability. However, the 2009 banking crisis came about partly as a result of material failures in this area, and there is a lingering concern that not enough has been done as yet, perhaps, to improve the quality of corporate governance insofar as it relates to and involves the internal audit/auditor or the external audit/auditor, or the quality of the application of accounting, auditing and disclosure.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Reconsider the wisdom of CBN's approval of a bank's draft annual audited financial statements prior to their publication, as provided for by Section 27 of the BOFI Act, as it holds the potential for the CBN to be held (co-) responsible (whether explicitly or implicitly) for the content of the annual audited financial statements upon publication thereof (it is conceivable that such an approval could constitute the basis of a future lawsuit against the CBN.)

	<ul style="list-style-type: none"> • Establish and maintain specialist capacity and capabilities on bank accounting, bank auditing, bank financial and risk disclosure, and the corporate governance roles of an internal auditor and an external auditor. (The CBN/BSD/FRPD specialist should be tasked with ensuring that the legal, regulatory and supervisory framework and the supervisory approach and practice are in line with sound internationally generally accepted standards and practices. The (senior) specialist should be responsible for driving the agenda relating to accounting, auditing, disclosure and corporate governance issues relating to bank internal audit/auditor and bank external audit/auditor, both internally (in CBN/BSD/FRPD) and externally, in relation, firstly, to the banks but, also, in relation to other key stakeholders, such as the accounting and auditing profession's representative bodies, the individual accounting and auditing firms and the FRCoN. So, for example, the periodic meetings between bank supervisors, the external auditors' professional representative body, bank external auditors and FRCoN to discuss issues of common interest relating to bank audits and bank accounting should be reinstated and the agenda be driven by the CBN's/BSD's/FRPD's relevant (senior) specialist. Furthermore, the CBN's/BSD's/FRPD's relevant specialist/s should develop a reporting template, and indicate the frequency, for external auditors of banks to render reports to the CBN on bank's risk management practices, internal controls and level of compliance, in order to give effect to the provisions of Section 7.1.4 of the Code of Corporate Governance for Banks.) • Require a bank to develop and implement formal policies in relation to internal audit, external audit and (financial, corporate governance, risk and controls) disclosure. • Empower the CBN to obtain access to an external auditor's external audit working papers in respect of a bank in the event that a bank becomes a problem bank. • Provide protection for an external auditor against claims of breach of contract, duty or confidentiality arising from that fact that an auditor in good faith furnished a report, inter alia in relation to legislative breaches or irregularities, as provided for in Section 29(7) of the BOFI Act, to the CBN. • Amend the BOFI Act so that it specifically and explicitly empowers the CBN to remove a bank's auditor who does not discharge his responsibilities satisfactorily
Principle 23	Corrective and remedial powers of supervisors. Supervisors must have at their disposal an adequate range of supervisory tools to bring about timely corrective actions. This includes the ability, where appropriate, to revoke the banking license or to recommend its revocation.
Essential criteria	
EC1	The supervisor raises supervisory concerns with management or, where appropriate, the Board, at an early stage, and requires that these concerns are addressed in a timely manner. Where the supervisor requires the bank to take significant remedial actions, these are addressed in a written document to the Board. The supervisor requires the bank to submit regular written progress reports and checks that remedial actions are completed satisfactorily.
Description and findings re EC1	<p>General Uneven supervision and enforcement was identified as one of the main factors which contributed to the 2009 banking crisis.</p> <p>The useful <i>Supervisory Intervention Framework of February 2011</i>, provides for a graduated framework with general and specific thresholds for regulatory engagement in banks in respect of specified prudential indicators. Supervision should involve assessing the safety and soundness of a regulated and supervised financial institution, providing feedback to the institution and encouraging it to improve, applying corrective, enforcement and sanctioning actions where necessary, intervening on a timely basis in the management of the institution if necessary, and, finally resolving a problem institution, even to the extent of liquidating it, if all else fails, in order to achieve the overarching supervisory objective of financial stability. The process includes on-going supervision, involving both off-site monitoring and on-site examination of an institution. Supervisory measures, whether informal or formal, are designed to address practices, conditions or infractions which could result in risk or loss of damage. Informal supervisory measures include a supervisory letter, board resolution and MoU. Formal supervisory measures include termination of NDIC insurance, consent order, temporary cease</p>

and desist order, removal and prohibition, suspension of dividends (in the case of banks which become undercapitalized), monetary penalties and prompt-corrective-action. Other supervisory measures include investigations, suspicious activity reports, referral to other agencies and actions against professionals. The nature and severity of the problem will determine the tools to be used and the graduation of the extent of intervention by the authorities. Circumstances which are fraught with systemic risk will engender the most extreme responses from the authorities, such as the CBN injecting funds into an ailing bank, NDIC providing partial/full liquidity support and blanket guarantees being issued.

(The power to implement the measures mentioned in the CBN's Supervisory Intervention Framework derives from Section 35 (2) of BOFI Act and Section 32(1) of NDIC Act.)

Legal and Regulatory Framework

The legal and regulatory framework contains a multitude of prescriptions which a bank is required to comply with. In the event of non-compliance by the bank, in some instances specific corrective, enforcement and/or sanctioning actions are prescribed, including disclosure. The ultimate sanction is the withdrawal of the bank license and liquidation of the bank. (BOFI Act – Section 5, 7, 8, 11, 12, 13, 14, 15, 16, 17, 18, etc)

Where a NDIC examination of an insured institution reveals that an insured institution or directors or staff have engaged or are engaging or are about to engage in unsafe and unsound practices in conducting the business of the institution, or have violated or are violating any provisions of any law or regulation to which the insured institution is subject, or where such violation may lead to insolvency or dissipation of the assets of the insured institution, the NDIC shall submit the report of the examination to the management of the bank with the specific directive to address the situation by taking corrective measures. If such corrective action is not fully implemented within the stipulated time-frame, the NDIC is required, in consultation with the CBN, to initiate such further corrective actions which it may deem necessary to redress the situation. (NDIC Act – Section 32)

The CBN is empowered to conduct special examination/investigation of the books and affairs of a bank where it is satisfied that it is in the public interest to do so; or the bank has been carrying on its business in a manner detrimental to the interest of its depositors and creditors; or the bank has “insufficient” assets to cover its liabilities to the public; or the bank has been contravening the provisions of the law. Where a bank informs the CBN that it is likely to become unable to meet its obligations or is about to suspend payment or is insolvent or the CBN is satisfied that the bank is in a grave situation, the CBN governor may exercise powers aimed at containing, remedying and/or resolving the situation. Where the CBN concludes that the state of affairs of the bank does not improve, the CBN may turn over control and management of the bank to the NDIC, whereupon the NDIC may require the bank to submit an acceptable recapitalization plan, prohibit the bank from extending any further credit or incurring additional capital expenditure without the NDIC's approval, require the bank to take such steps or to do or not to do any act or thing whatsoever in relation to the business of the bank or its directors or officers as the NDIC may stipulate; or with the approval of the CBN remove any director, manager or employee of the bank; or with the approval of the CBN appoint any person as director or manager of the bank. In the event that the bank cannot be rehabilitated, the NDIC may recommend to the CBN other resolution measures, including the revocation of the bank's license. (BOFI Act – Section 35, 36, 37 and 39)

Supervisory framework – Off-Site and Site Examination

The communication of findings of examinations is addressed in Supervisory Guide 6 of the CBN/NDIC RBS Framework. The CBN/NDIC communicates the results of supervisory work on a timely basis, through its interim letters and supervisory letters. In line with the Risk Based Supervisory Framework, interim letters and supervisory letters are issued within the stipulated timeframe of within 35 and 45 days respectively after the conclusion of onsite examination. Interim letters are addressed to the individuals at the institution responsible for the significant activities or control function reviewed while the supervisory letters are issued to the chief executive officers of banks and copied to the chairman of the audit committee. Generally, supervisory letters highlight key issues affecting an institution's risk profile that are of concern to the supervisors. The letters also detail remedial actions required of the institutions, the required timing of the corrective action and when the supervisors would return for necessary

	<p>follow-up. The banks also submit progress reports on the implementation of supervisors' recommendations.</p> <p>Conclusion Notwithstanding the important and substantial progress since 2009, the concern remains that, though the legal and regulatory framework relating to corrective, enforcement and sanctioning actions has improved substantially, the willingness to act may still be weak. For example, it is generally recognized that the smallest bank is insolvent, with no reasonable prospect of a return to solvency or of sustainable viability, and not being systemically relevant—yet it has remained in limbo for an inordinate period of time. Accordingly, there is a concern that the authorities lack the willingness to fully apply the Intervention Framework and finally resolve a bank which is hopelessly insolvent. (During the mission close-out meeting, the Governor gave the assurance that this bank would be resolved in due course. Subsequently, the mission chief was informed that the bank had been recapitalized.)</p>
EC2	The supervisor participates in deciding when and how to effect the orderly resolution of a problem bank situation (which could include closure, or assisting in restructuring, or merger with a stronger institution).
Description and findings re EC2	<p>The CBN and NDIC are empowered to effect orderly resolution of a “failing” bank. (BOFI Act – Section 35 to 38) (NCIC Act – Section 37 to 39)</p> <p>Broadly, the CBN and NDIC were guided by these provisions during the period 2009 to date, in addressing the banking crisis.</p>
EC3	The supervisor has available an appropriate range of supervisory tools for use when, in the supervisor's judgment, a bank is not complying with laws, regulations or supervisory decisions, or is engaged in unsafe or unsound practices, or when the interests of depositors are otherwise threatened. These tools include the ability to require a bank to take prompt remedial action and to impose penalties. In practice, the range of tools is applied in accordance with the gravity of a situation.
Description and findings re EC3	<p>See also BCP23 EC1.</p> <p>The CBN/NDIC has at its disposal supervisory measures to deal with situations where a bank is not complying with laws, regulations or supervisory decisions or is engaged in unsafe or unsound practices that threaten the interest of depositors. The supervisory tools are categorized into informal and formal measures in the CBN Supervisory Intervention Framework. The choice of the Actions would be guided by the following key considerations: (i) nature of the situation; (ii) cause and/or motivation; (iii) history of compliance; (iv) systemic impact; (v) risk exposure or profile; (vi) parties involved (e.g., insiders); (vii) management attitude; and (viii) prospects. Informal Actions are usually applied to banks with a composite risk rating of low or moderate and may not be publicly disclosed by the institutions and are generally not enforceable in law. On the other hand, formal actions are legally enforceable agreements requiring a bank to take remedial measures towards its enforcement. They are applied when: (i) composite risk rating is above average or high; (ii) informal Actions have been unsuccessful; (iii) unsafe and unsound practices are evident; and (iv) there are violations of laws, rules, regulations and written agreements.</p>
EC4	The supervisor has available a broad range of possible measures to address such scenarios as described in EC 3 above and provides clear prudential objectives or sets out the actions to be taken, which may include restricting the current activities of the bank, withholding approval of new activities or acquisitions, restricting or suspending payments to shareholders or share repurchases, restricting asset transfers, barring individuals from banking, replacing or restricting the powers of managers, Board directors or controlling owners, facilitating a takeover by or merger with a healthier institution, providing for the interim management of the bank, and revoking or recommending the revocation of the banking license.
Description and findings re EC4	<p>See also BCP23 EC1 and 3.</p> <p>The supervisors have in place an intervention framework which prescribes measures to be taken in ensuring banks' compliance with prudential thresholds in seven critical areas (capital adequacy, asset quality, liquidity, earnings, risk management, internal control and system</p>

	<p>failures). Detailed corrective measures are stipulated when banks fail to meet prudential requirements in any of the specified areas.</p> <p>A review of the examination reports of some of the CBN intervened banks showed that a variety of these measures were deployed in the resolution of the problems of the institutions.</p> <p>It appears that the <i>Supervisory Intervention Framework</i> may not be fully aligned with and grounded in the BOFI Act. For example, Section 37 of the BOFI Act only relates to significantly undercapitalized banks with a CAR ratio in the range between 2 percent and 5 percent—accordingly, all other scenarios provided for in the PCA regime are not provided for under the BOFI Act.</p>
EC5	The supervisor has the power to take measures should a bank fall below the minimum capital ratio, and seeks to intervene at an early stage to prevent capital from falling below the minimum. The supervisor has a range of options to address such scenarios.
Description and findings re EC5	<p>The <i>Supervisory Intervention Framework</i> clearly specifies the options available to CBN when a bank falls below the minimum capital adequacy ratio.</p> <ul style="list-style-type: none"> • For undercapitalized banks (i.e., banks with capital adequacy ratio of 5-10 percent for a period of at least three months), the options available to the CBN are: (i) restriction of investment in other subsidiaries/related companies, investment in fixed assets and dividend payment; (ii) conduct of special examination; and (iii) placing the bank in CBN/NDIC Watch List and inform the bank that it has been so placed. • For significantly undercapitalized banks (CAR of between 2-5 percent) supervisory actions to consider in addition to the ones above include, among others: (i) restriction on new lending to recoveries made; (ii) requesting a business plan on how fresh funds are to be injected into the bank and (iii) CBN to review business plan within two weeks and communicate to the bank its acceptability or otherwise. • For insolvent banks with CAR less than zero, the bank's license would be revoked by the CBN if the actions above do not stabilize the bank. <p>In August 2011, the licenses of the three banks that showed lack of capacity and/or capability to recapitalize were revoked and their assets and certain liabilities were bridged by the NDIC. This was after efforts made to turnaround the business of the banks failed to yield positive results. (Assessors validated these assertions by way of discussion with market participants.)</p> <p>Some of the other enforcement actions which were taken by the CBN during the past three years include the following:</p> <ul style="list-style-type: none"> • Imposed holding action on a bank in 2012. • Imposed holding action on another bank in 2009. • CBN intervention and removal of top management of eight banks in 2008.
EC6	The supervisor applies penalties and sanctions not only to the bank but, when and if necessary, also to management and/or the Board, or individuals therein.
Description and findings re EC6	The supervisor is empowered to apply penalties and sanctions also to the management and/or the board of directors, or individuals therein, under specified circumstances, for example, where a director, manager or officer facilitates the payment of a dividend under prescribed circumstances. (BOFI Act – Section 17, 18, 28, 49, 50, etc.)
Additional criteria	
AC1	Laws or regulations guard against the supervisor unduly delaying appropriate corrective actions.
Description and findings re AC1	The Service Compact with all Nigerians (SERVICOM), a program of the Federal Government for ensuring efficient service delivery in Nigeria, mandates all service providers in Nigeria to provide timely and efficient services to customers. Supervisors also subscribe to a Code of

	<p>Conduct for Bank Supervisors and during annual performance appraisals; timeliness in service delivery is appraised.</p> <p>However, see the conclusion to BCP23 EC1.</p> <p>The Supervisory Intervention Framework contains a Prompt Corrective Action regime, which has triggers relating to capital adequacy, liquidity, asset quality, earnings, internal controls, risk management and persistent complaints of system failure.</p>
AC2	The supervisor has the power to take remedial actions, including ring-fencing of the bank from the actions of parent companies, subsidiaries, parallel-owned banking structures and other related companies in matters that could impair the safety and soundness of the bank.
Description and findings re AC2	Banks are permitted to establish non-operating financial holding companies to hold interest in the banks as well as other related non-bank subsidiaries. The banks within the group are ring-fenced from their related companies to protect them from actions within the group that could impact their safety and soundness. (<i>Regulation on the Scope of Banking Activities & Ancillary Matters, No. 3, 2010</i>)
AC3	When taking formal remedial action in relation to a bank, the supervisor ensures that the regulators of non-bank related financial entities are aware of its actions and, where appropriate, coordinates its actions with them.
Description and findings re AC3	The FSRCC, which is the organ tasked with the co-ordination of supervisory activities in the Nigerian financial system, has an established mechanism for information sharing. Consequently, regulators of non-bank financial entities, which are members of the FSRCC, like SEC, NAICOM and NSE are informed when remedial action is being taken by banking sector supervisors.
Assessment of Principle 23	Largely compliant
Comments	<p>Supervisors have at their disposal an adequate range of supervisory tools to bring about timely corrective actions. This includes the ability, where appropriate, to revoke the banking license or to recommend its revocation. These powers were promptly deployed during the 2009 banking crisis. However, there is a concern that the authorities may lack the resolve to fully apply the Intervention Framework and finally resolve a bank which is hopelessly insolvent.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Remove Part 4, titled Supervisory Actions in the Event of a Systemic Banking Distress, of the <i>Supervisory Intervention Framework</i> from the public domain, for avoidance of moral hazard. • Update the Supervisory Intervention Framework to ensure it is fully aligned with and grounded in the relevant provisions of the BOFI Act, and is not open to the charge that it is, or some of its provisions are, <i>ultra vires</i>. • Apply zero tolerance in relation to actions or inactions which put financial stability at risk, as well as in relation to corporate governance transgressions, non-compliance with statutory prescriptions and submission/disclosure of substandard quality of data or information. • Act promptly, resolutely and forcefully in applying corrective, enforcement and sanctioning actions, and in resolving problem banks, especially in instances which hold the potential to imperil financial stability.

Principle 24	Consolidated supervision. An essential element of banking supervision is that supervisors supervise the banking group on a consolidated basis, adequately monitoring and, as appropriate, applying prudential norms to all aspects of the business conducted by the group worldwide.
Essential criteria	
EC1	The supervisor is familiar with the overall structure of banking groups and has an understanding of the activities of all material parts of these groups, domestic and cross-border.
Description and findings re EC1	<p>CBN supervisors are expected to be familiar with the overall structure of banks, their subsidiaries and understand their activities. <i>Regulation on the Scope of Banking Activities & Ancillary Matters (No. 3, 2010)</i> streamlines the activities of banks and clearly defines all material parts of the banking groups, domestic and cross-border. The <i>Supervisory Framework for Banks and Other Financial Institutions in Nigeria (July 2008)</i> and the <i>RBS Framework</i>, also expects the CBN supervisors to have full understanding of the overall structure of banks and their group, and this understanding must be reflected in the Knowledge of Business (KOB) documents.</p> <p>A scrutiny by the assessors of a KOB (September 30, 2011) for a particular bank revealed that it contained adequate information on the organizational structure of the bank and its holding company.</p> <p>Notwithstanding the above, consolidated supervision, especially in relation to financial holding companies (FHCs) is new area for CBN supervisors whose capacity and capabilities in this area of consolidated supervision has not as yet been tested. Also note that the updated draft <i>Consolidated Supervision Framework</i> has not yet been implemented.</p>
EC2	The supervisor has the power to review the overall activities of a banking group, both domestic and cross-border. The supervisor has the power to supervise the foreign activities of banks incorporated within its jurisdiction.
Description and findings re EC2	<p>The CBN is empowered to obtain information from a bank and from its branches outside Nigeria. (BOFI Act – Section 25) The <i>RBS Framework</i> also requires a review of risk management of banks on a consolidated basis.</p> <p>The CBN is not empowered to obtain information from or supervise a bank's foreign bank subsidiaries or from a bank holding company's foreign bank subsidiaries. Nor is the CBN (explicitly, directly and unambiguously) empowered to obtain information from or supervise a financial holding company's related entities.</p> <p>The CBN is empowered to supervise financial holding companies (FHCs). (See BOFI Act – Section 66, as amended in December 2011)</p>
EC3	The supervisor has a supervisory framework that evaluates the risks that non-banking activities conducted by a bank or banking group may pose to the bank or banking group.
Description and findings re EC3	<p>CBN supervisors use the information gathered to determine if the non-banking activities/subsidiaries of banks pose any significant risks, which is expected under the <i>RBS Framework</i>. This involves the consideration of all intra-group exposures and risks. The supervisor assesses instances of multiple gearing, leveraging, contagion and risks from shared services. CBN supervisors then assess the linkage between these levels of risks, which emanate from the various investments within group, to the banks' capital levels.</p> <p>In determining the impact of non-bank subsidiaries, CBN obtain information from the respective supervisory authorities via MOUs. Domestically, an MOU was signed with the major domestic financial regulators namely NICOM, NDIC and via FSRCC platform. At the international front, MOUs were also signed with host regulators of Nigerian banks' subsidiaries. As for those countries without MOUs (namely OCC of the U.S. and the U.K. FSA), the information sharing by these authorities are deemed to be effective even without formal MOUs.</p>

	<p>As for non-financial subsidiaries, CBN supervisors have encourage the banks to divest their investments as to ensure emerging risk from these exposures, which the supervisors may not familiar with, are kept at minimum. There are instances where supervisory actions were taken on banks that failed to divest the non-financial subsidiaries even after recommendation by CBN. The assessors saw the foregoing reflected in a follow up supervisory letter issued to a local bank, where the CBN emphasized the need for that bank to divest its non-financial investments.</p>
EC4	<p>The supervisor has the power to impose prudential standards on a consolidated basis for the banking group. The supervisor uses its power to establish prudential standards on a consolidated basis to cover such areas as capital adequacy, large exposures, exposures to related parties and lending limits. The supervisor collects consolidated financial information for each banking group.</p>
Description and findings re EC4	<p>The CBN has the power to impose prudential standards (on capital adequacy) on a consolidated basis for a banking group, being a group where the bank is the holding company of the group. (BOFI Act – Section 13)</p> <p>In addition, <i>The updated draft Framework for Consolidated Supervision</i> and <i>RBS Framework</i> provides that the supervisor should collect consolidated financial information for banking groups and assess their risk on group-wide basis. Furthermore, <i>Section 3 of Prudential Guidelines</i> addresses the risks of exposure to related parties and sets lending limits.</p> <p>The CBN is empowered to supervise financial holding companies (FHCs). (See BOFI Act – Section 66, as amended in December 2011) However, the <i>Framework for Consolidated Supervision</i> is still in draft and yet to be formally implemented.</p> <p>On December 20, 2011, an amendment to section 66 of BOFI act was gazette, in terms of which the business of Financial Holding Company was designated—the business of Financial Holding Company being a company set up for the purpose of making and managing (for its own account) equity investments in companies engaged in the provision of Financial Services as Business of Other Financial Institution.</p>
EC5	<p>The supervisor has arrangements with other relevant supervisors, domestic and cross-border, to receive information on the financial condition and adequacy of risk management and controls of the different entities of the banking group.</p>
Description and findings re EC5	<p>See BCP24 EC4, above.</p> <p>The CBN has signed a number of MOUs with domestic and foreign supervisors to enhance cooperation and collaboration with respect to information sharing on the risk management and financial condition of the members of a banking group.</p>
EC6	<p>The supervisor has the power to limit the range of activities the consolidated group may conduct and the locations in which activities can be conducted; the supervisor uses this power to determine that the activities are properly supervised and that the safety and soundness of the bank are not compromised.</p>
Description and findings re EC6	<p>The CBN is satisfactorily empowered to supervise a banking group and ensure that the safety and soundness of the bank is not compromised. Regulation on the <i>Scope of Banking Activities & Ancillary Matters, No. 3, 2010</i> imposes limitations on the activities of banks and clearly defines all material parts of a banking group, both domestic and cross-border. Furthermore, CBN is empowered to approve the locations at which banking activities may be conducted. (BOFI Act – Section 6) The <i>CBN circular BSD/DIR/CIR/GEN/02/014</i> on Off-Shore Expansion provides clear guidelines on overseas investments to ensure that the safety and soundness of banks are not compromised.</p> <p>CBN does not have explicit power to supervise a FHC.</p>
EC7	<p>The supervisor determines that management is maintaining proper oversight of the bank's foreign operations, including branches, joint ventures and subsidiaries. The supervisor also determines that banks' policies and processes ensure that the local management of any</p>

	cross-border operations has the necessary expertise to manage those operations in a safe and sound manner and in compliance with supervisory and regulatory requirements.
Description and findings re EC7	<p>The CBN supervisors assess management and governance within banks, so as to ensure that proper oversight of the banks' operations, including foreign operations, is maintained. (<i>RBS Framework</i>) The CBN, via the BSD, has established a specific unit, dedicated to supervision of -border operations.</p> <p>(The <i>Draft Framework for Consolidated Supervision of Banks in Nigeria</i> requires supervisors of entities within a banking group or financial conglomerate to assess whether senior management has the necessary expertise to manage the operations in a safe and sound manner. In addition, the fitness and propriety of senior management is assessed, as well as the structure of the group and the risk therein.)</p>
EC8	<p>The supervisor determines that oversight of a bank's foreign operations by management (of the parent bank or head office and, where relevant, the holding company) includes: (i) information reporting on its foreign operations that is adequate in scope and frequency to manage their overall risk profile and is periodically verified; (ii) assessing in an appropriate manner compliance with internal controls; and (iii) ensuring effective local oversight of foreign operations.</p> <p>For the purposes of consolidated risk management and supervision, there should be no hindrance in host countries for the parent bank to have access to all the material information from their foreign branches and subsidiaries. Transmission of such information is on the understanding that the parent bank itself undertakes to maintain the confidentiality of the data submitted and to make them available only to the parent supervisory authority.</p>
Description and findings re EC8	<p>CBN supervisors ascertain that the oversight of banks' foreign operations by management consider all necessary information, including the overall risk profiles of the foreign operations.</p> <p>All banks in Nigeria that apply for investments in foreign subsidiaries are required to sign an undertaking to provide all reports and information requested from it by the CBN. During on-site examinations, supervisors verify that banks' management receive information from their foreign subsidiaries without hindrance, as guided the <i>RBS Framework</i>. This is carried out via reviews of banks' information on their foreign investments and determines whether this information is sufficient to measure the level of risk emanating from these investments.</p> <p>The CBN is empowered to obtain information from entities related to a bank inside and outside Nigeria. (BOFI – Section 25) In practice, CBN will not approve any request for foreign expansion of Nigerian banks if CBN is not satisfied with its ability and that of the banks to obtain information on those operations without fail.</p>
EC9	<p>The home supervisor has the power to require the closing of foreign offices, or to impose limitations on their activities, if:</p> <ul style="list-style-type: none"> • it determines that oversight by the bank and/or supervision by the host supervisor is not adequate relative to the risks the office presents; and/or • it cannot gain access to the information required for the exercise of supervision on a consolidated basis.
Description and findings re EC9	<p>Only with the prior approval of the CBN may a bank may open or close a branch office, whether within or outside Nigeria. (BOFI Act – Section 6).</p> <p>The BOFI Act does not specifically and clearly empower the CBN to require a bank to close a foreign office or impose limitations on their activities.</p>
EC10	<p>The supervisor confirms that oversight of a bank's foreign operations by management (of the parent bank or head office and, where relevant, the holding company) is particularly close when the foreign activities have a higher risk profile or when the operations are conducted in jurisdictions or under supervisory regimes differing fundamentally from those of the bank's home country.</p>
Description and	During on-site examinations, CBN supervisors determine that the parent banks exercise

findings re EC10	adequate oversight over the foreign operations of branches/subsidiaries that have higher risk profile. The process involves the detailed offsite assessments by the designated unit responsible for cross-border supervision. Once this unit determines the level of overall inherent risks of foreign operations of banks, the onsite examiners assess the quality of risk management process over the overseas operations via reviews of the information submission and risk management activities over this information, and determine whether the risk control functions are adequate vis-à-vis the overall risk profile of the cross-border activities. In some instances, banks have been advised to divest or limits the risk taking activities such branches/subsidiaries if CBN supervisors are not satisfied with the banks' risk management capabilities to manage the exposures. The assessors confirmed the foregoing during discussion with CBN supervisors from the dedicated unit responsible for banks' foreign operations.
Additional criteria	
AC1	For those countries that allow corporate ownership of banking companies: <ul style="list-style-type: none"> • the supervisor has the power to review the activities of parent companies and of companies affiliated with the parent companies, and uses the power in practice to determine the safety and soundness of the bank; and • the supervisor has the power to establish and enforce fit and proper standards for owners and senior management of parent companies.
Description and findings re AC1	Supervisors have limited powers over non-regulated parent companies of banks. There are, however, MOUs in place on information sharing that are leveraged upon to obtain required information. Supervisors do not have direct powers to establish and enforce fit and proper standards for owners and senior management of parent companies. However, supervisory review is conducted based on the <i>Framework for Cross-Border Supervision of Banks</i> to ensure that the parent companies are owned and managed by fit and proper persons (but this is applicable only for the cross-border/investment by foreign entities in Nigerian banking system). The CBN has not been in a position to perform consolidated supervision in relation to a banking group which is systemically important in Nigeria, is headquartered outside Nigeria, in the West-African region (where the banking group has a wide network of banks), and the home supervisor is extremely challenged in terms of its legal and regulatory framework and its resources and capabilities and capacities.
AC2	The home supervisor assesses the quality of supervision conducted in the countries in which its banks have material operations.
Description and findings re AC2	CBN supervisors are expected to assess the quality of supervision carried out in countries in which Nigerian banks have material operations, as contained in <i>Section 3.3.1 (e) of the Framework for Cross-Border Supervision of Banks</i> . However, the Framework only came into force in December 2010 and there was no application by Nigerian banks to expand overseas since then. Therefore, the expectation has yet to be implemented.
AC3	The supervisor arranges to visit the foreign locations periodically, the frequency being determined by the size and risk profile of the foreign operation. The supervisor meets the host supervisors during these visits. The supervisor has a policy for assessing whether it needs to conduct on-site examinations of a bank's foreign operations, or require additional reporting, and has the power and resources to take those steps as and when appropriate.
Description and findings re AC3	CBN supervisors visit the foreign locations of Nigerian banks periodically, depending on the size and risk profile of the foreign operations. During such visits, meetings are held with host supervisors and in some instances, joint examinations have been conducted. For example, joint examinations were carried out on GTB and UBA in Ghana in July 2012 and planned examinations on GTB and UBA in Liberia is expected to be carried out in September 2012.

Assessment of Principle 24	Materially non-compliant
Comments	<p>The legal and regulatory framework for consolidated supervision is not yet in place. Notwithstanding, the CBN performs some elements of consolidated supervision in relation to the interests of a bank.</p> <p>(The draft <i>Framework for the Consolidated Supervision of Financial Institutions in Nigeria</i>, which contains a formal process of evaluating the overall structure of the bank and related parties as well as identifying the risks arising from non-banking activities, should provide largely the necessary regulatory platform for effective supervisory function on consolidated basis, though the legal platform is also required. The FSRCC provides a vehicle for coordination among the relevant domestic supervisors and ensures that ongoing supervisory efforts are closely integrated for the local components of a banking group.)</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • Ensure the comprehensive incorporation into the BOFI Act of necessary enabling provisions to facilitate the implementation and performance of consolidated supervision. • Finalize and implement the updated draft <i>Framework for the Consolidated Supervision of Financial Institutions in Nigeria</i>. • Ensure that the supervisory capacity and capability to give effect to consolidated supervision is available. • Amend the BOFI Act to specifically and clearly empower the CBN to require a bank to close a foreign office or impose limitations on their activities under specified circumstances, namely if the CBN determines that the oversight by the bank and/or supervision by the host supervisor is not adequate relative to the risks the office presents and/or it cannot gain access to the information required for the exercise of supervision on a continuous basis.
Principle 25	Home-host relationships. Cross-border consolidated supervision requires cooperation and information exchange between home supervisors and the various other supervisors involved, primarily host banking supervisors. Banking supervisors must require the local operations of foreign banks to be conducted to the same standards as those required of domestic institutions.
Essential criteria	
EC1	Information to be exchanged by home and host supervisors should be adequate for their respective roles and responsibilities.
Description and findings re EC1	<p>Context Nigeria's financial system is dominated by domestic institutions, but international linkages are increasing. The consolidation of the banking sector in 2005–06 generated capacity for several Nigerian banks to expand internationally, establishing subsidiaries particularly in Africa. Meanwhile, a major regional bank headquartered outside Nigeria, and active in 32 African countries, has its largest subsidiary in Nigeria. One of the largest re-insurance companies is a regional entity, with headquarters in Nigeria and offices in much of Africa</p> <p>Assessment The CBN's <i>Framework for Cross-border Supervision, 2010</i>, forms the basis of the CBN policy on information sharing with foreign regulators. The channel of information sharing is described in <i>Section 4.0 on Information Requirements</i> of the framework. Information required is differentiated between preliminary information, regular information for the purpose of supervision and exception information in a crisis situation. This policy is complemented by the overarching CBN <i>Policy on Confidentiality and Relevance of Information</i>. Thus information that is suitable and relevant for supervision is shared with the foreign supervisor. For instance, the College of Supervisors for the West African Monetary Zone (WAMZ), which meets quarterly, is one such forum for such information sharing.</p> <p>The current information sharing framework is adequate for home and host supervisors</p>

	<p>exchanging information for their respective roles and responsibilities. For example in July 2012, information on statutory and prudential requirements was requested and obtained from Bank of Uganda.</p>
EC2	<p>For material cross-border operations of its banks, the supervisor identifies all other relevant supervisors and establishes informal or formal arrangements (such as memoranda of understanding) for appropriate information sharing, on a confidential basis, on the financial condition and performance of such operations in the home or host country. Where formal cooperation arrangements are agreed, their existence should be communicated to the banks and banking groups affected.</p>
Description and findings re EC2	<p>In tandem with the regional expansion of Nigerian banks, the CBN has gradually enhanced cross-border supervision. A dedicated unit for cross-border supervision was created.</p> <p>CBN has entered into MoUs with 12 of the host supervisors and one home supervisor on information sharing and cooperation that are tailored to meet each supervisor's needs. The MOUs contain the details on information sharing, on-site examinations, confidentiality of shared information and consolidated supervision, though they do not cover crisis management nor bank resolution. For examples, MOUs were signed with Banque Centrale Du Congo, National Bank of Rwanda and Bank of Zambia as home supervisor, while with South African Reserve Bank as host supervisor. Further, there is a master MOU with Gambia, Ghana, Guinea and Sierra Leone via the WAMZ platform. Last year, a MoU was entered with Banque Centrale des Etats de l'Afrique (BCEAO) for Ecobank. The affected banks are duly informed.</p> <p>For those supervisory authorities where the CBN does not have formal arrangements, e.g., OCC and U.K. FSA, the information flow currently from these home regulators is effective. For example, the OCC provided a report on UBA (New York) in July 2012, explaining in detail the supervisory concerns that it has.</p> <p>(CBN act is host supervisor for Standard Chartered Bank (U.K.), Citibank (U.S.), Stanbic/IBTC (South Africa) and Ecobank (Togo). For the remaining banks in Nigeria, CBN is the home Supervisor.)</p> <p>A regulatory CAR of 15 percent applies to Nigerian banks with international authorization.</p> <p>CBN supervisors are required to conduct assessments of the supervisory capacities of the proposed host supervisors. CBN also provides training, where necessary, for the host supervisors. Furthermore, CBN supervisors conduct joint examination of foreign subsidiaries with the host supervisors. A College of Supervisors for the WAMZ region was established to harmonise supervisory practices and facilitate exchange of information in the region.</p>
EC3	<p>The home supervisor provides information to host supervisors, on a timely basis, concerning:</p> <ul style="list-style-type: none"> • the overall framework of supervision in which the banking group operates; • the bank or banking group, to allow a proper perspective of the activities conducted within the host country's borders; • the specific operations in the host country; and • where possible and appropriate, significant problems arising in the head office or other parts of the banking group if these are likely to have a material effect on the safety and soundness of subsidiaries or branches in host countries. <p>A minimum level of information on the bank or banking group will be needed in most circumstances, but the overall frequency and scope of this information will vary depending on the materiality of a bank's or banking group's activities to the financial sector of the host country. In this context, the host supervisor will inform the home supervisor when a local operation is material to the financial sector of the host country.</p>
Description and findings re EC3	<p>CBN as home supervisor provides information to host supervisors on a timely basis on the overall framework of supervision under which the banking group operates. Information needs are differentiate between preliminary information, regular information for the purpose of</p>

	<p>supervision and exception information in a crisis situation. Based on MoUs, the host supervisor will inform the CBN when a local operation becomes material in their country.</p> <p>Although in practice, information sharing by CBN as host supervisor or home supervisor has been flowing without major issue, the <i>Framework for Cross-border Supervision</i> does not specify the need for CBN to share information with other supervisory authorities. <i>Paragraph 4 on Information Requirement</i> of the framework only states the need for other supervisory authorities to share information with CBN.</p> <p>Based on the Framework for Cross-border Supervision of Banks, CBN supervisors expect to receive from host supervisors of Nigerian banks, at minimum:</p> <ul style="list-style-type: none"> • examination reports; • details of contraventions and sanctions; • statement of compliance with applicable laws and regulations; and • items of material supervisory concern. <p>For example, CBN Supervisors receive the executive summary of a statutory examination conducted on Skye Bank (S) Limited, a subsidiary of Skye Bank Plc in Sierra Leone, from Bank of Sierra Leone in November 2011.</p> <p>The CBN is scheduled to conduct 18 on-site solo and joint examinations of Nigerian bank's foreign subsidiaries in 2012, of which 13 have been completed.</p> <p>The CBN invites supervisors from the West African sub-region to attend the CBN's structured bank examiner's courses, in order to assist in capacity building.</p>
<p>EC4</p>	<p>The host supervisor provides information to home supervisors, on a timely basis, concerning:</p> <ul style="list-style-type: none"> • material or persistent non-compliance with relevant supervisory requirements, such as capital ratios or operational limits, specifically applied to a bank's operations in the host country; • adverse or potentially adverse developments in the local operations of a bank or banking group regulated by the home supervisor; • adverse assessments of such qualitative aspects of a bank's operations as risk management and controls at the offices in the host country; and • any material remedial action it takes regarding the operations of a bank regulated by the home supervisor. <p>A minimum level of information on the bank or banking group, including the overall supervisory framework in which they operate, will be needed in most circumstances, but the overall frequency and scope of this information will vary depending on the materiality of the cross-border operations to the bank or banking group and financial sector of the home country. In this context, the home supervisor will inform the host supervisor when the cross-border operation is material to the bank or banking group and financial sector of the home country.</p>

Description and findings re EC4	<p>The CBN, as the host supervisor, provides information to home supervisors upon request.</p> <p>CBN is considering proposing the need for the establishment of a college of supervisors for a banking group which operates in 32 countries, mainly in West Africa. Ecobank, a pan-African financial conglomerate, presents particular cross-border supervisory challenges. Headquartered in Lomé, the Banking Commission of the BCEAO zone in Abidjan is responsible for exercising consolidated supervision.⁵ In light of the supervisory weaknesses observed in some of its countries, this is challenging. The CBN supervises the Nigerian operations on a stand-alone basis, but may not observe losses elsewhere in the group, or for instance the build-up of intra-group exposures or double gearing of capital. Discussions with CBN staff suggested that there was little awareness of the bank's overall condition⁶ Since the FSAP mission, the CBN considers proposing to other host supervisors the need for a supervisory college for Ecobank.</p>
EC5	A host supervisor's national laws or regulations require that the cross-border operations of foreign banks are subject to prudential, inspection and regulatory reporting requirements similar to those for domestic banks.
Description and findings re EC5	All foreign banks registered in Nigeria are subject to domestic prudential and other regulatory requirements applicable to Nigerian banks.
EC6	Before issuing a license, the host supervisor establishes that no objection (or a statement of no objection) from the home supervisor has been received. For purposes of the licensing process, as well as ongoing supervision of cross-border banking operations in its country, the host supervisor assesses whether the home supervisor practices global consolidated supervision.
Description and findings re EC6	It is a requirement that the home supervisors are consulted and has issued a letter of "No-Objection" prior to the issuance of approval for foreign banks seeking to establish operations in Nigeria. The expectations on the host supervisors are also taken into account, including for having comprehensive consolidated supervision framework arrangement. (<i>Framework for Cross-border Supervision of Banks</i> – Section 3 and 7) (Since the Framework came into force in December 2010, there was not been any application by a Nigerian bank to expend overseas.)
EC7	Home country supervisors are given on-site access to local offices and subsidiaries of a banking group in order to facilitate their assessment of the group's safety and soundness and compliance with KYC requirements. Home supervisors should inform host supervisors of intended visits to local offices and subsidiaries of banking groups.
Description and findings re EC7	<p>CBN policy is to grant home country supervisors on-site access to local offices and subsidiaries of a banking group in order to assess the safety and soundness of the bank. On the other hand, CBN supervisors have a standard practice of informing in advance the host supervisor of its intended visit to local offices and subsidiaries of Nigerian banking groups. In some instance, joint examinations are conducted with the host supervisor.</p> <p>For example, joint examination on UBA (Liberia) was conducted in July 2012 and joint examination on GTB (Liberia) is expected to be carried out in September 2012</p>
EC8	The host supervisor supervises shell banks, where they still exist, and booking offices in a manner consistent with internationally agreed standards.

⁵ IFC is a major investor in Ecobank and imposes its own liquidity and capital requirements through various financial covenants.

⁶ Note that operations in Togo, which is the home supervisor responsible for exercising group-wide supervision, account only for a small share of the group's asset and deposit base.

Description and findings re EC8	The CBN regulatory framework does not allow 'shell banks' or 'booking offices' to be established in Nigeria.
EC9	A supervisor that takes consequential action on the basis of information received from another supervisor consults with that supervisor, to the extent possible, before taking such action.
Description and findings re EC9	<p>The CBN understands the value of consultation with host supervisors and where necessary consult with them in the adoption of remedial action(s) based on the information provided by the host supervisor.</p> <p>The assessors are aware of supervisory authorities which were not fully satisfied with the nature, extent and timing of information sharing in the aftermath of the 2009 banking crisis.</p>
Additional criteria	
AC1	Where necessary, the home supervisor develops an agreed communication strategy with the relevant host supervisors. The scope and nature of the strategy should reflect the size and complexity of the cross-border operations of the bank or banking group.
Description and findings re AC1	<p>The CBN has adopted several communication strategies with different supervisors, which facilitate the exchange of information in a timely and efficient manner, based on the size and complexity of the bank. For instance, the CBN facilitated the establishment of the College of Supervisors of WAMZ, to enhance exchange of information within the region.</p> <p>Generally, there is adequate communication channels between the Home and Host supervisor which is commensurate with the size and complexity of the cross-border operations of a bank or banking group.</p> <p>However, obstacles include language barriers, differences in quality of supervision, reporting requirements and off-site monitoring systems. Some Nigerian banks have expanded into jurisdictions where supervision and enforcement capacity is weak, data reliability problematic and prudential returns not subject to rigorous quality controls.</p>
Assessment of Principle 25	Largely compliant
Comments	<p>The CBN has in place a <i>Framework for the Supervision of Cross-Border Institutions</i> and this document forms the basis of its cross-border supervisory activities. In addition, CBN has a unit within BSD, dedicated to the supervision of cross-border institutions. There are MoUs in place with other foreign regulatory agencies in jurisdictions where Nigerian banks have presence. In the case of other jurisdictions which have not signed formal information sharing arrangements with the CBN, there are informal arrangements for information sharing, for instance, in the case of the OCC and U.K.FSA. In certain circumstances, the information sharing via informal arrangements is more active than those via the formal arrangements. Foreign banks operating in Nigeria are subjected to the same regulatory and supervisory regimes as applied on domestic banks.</p> <p>The following recommendations are proposed:</p> <ul style="list-style-type: none"> • empower the CBN to share information with other supervisory authority; and • consider carrying out a one-off review exercise of, and thereafter at regular intervals, review all the host supervisory authorities of Nigerian banks, to assess the nature and quality of the regulatory and supervisory frameworks, supervisory approaches and quality of supervision, including enforcement and resolution. <p>PS: The recent CBN circular impeding Nigerian banks' capacity to capitalize their foreign subsidiaries appears to run contrary to the spirit of enhancing cross-border cooperation.</p>

**APPENDIX I. SUMMARY OF ASSESSMENT OF COMPLIANCE WITH THE
CORE PRINCIPLES**

Basel Core Principles	Ratings ⁷				
	C	LC	NMC	NC	N/A
1. Objectives, independence, powers, transparency, and cooperation		X			
1.1. Responsibilities and objectives		X			
1.2. Independence, accountability and transparency		X			
1.3. Legal framework		X			
1.4. Legal powers		X			
1.5. Legal protection		X			
1.6. Cooperation		X			
2. Permissible activities	X				
3. Licensing criteria		X			
4. Transfer of significant ownership			X		
5. Major acquisitions		X			
6. Capital adequacy		X			
7. Risk management process		X			
8. Credit risk		X			
9. Problem assets, provisions, and reserves		X			
10. Large exposure limits			X		
11. Exposure to related parties			X		
12. Country and transfer risk		X			
13. Market risks			X		
14. Liquidity risk		X			
15. Operational risk		X			
16. Interest rate risk in the banking book			X		
17. Internal control and audit		X			
18. Abuse of financial services			X		
19. Supervisory approach		X			
20. Supervisory techniques		X			
21. Supervisory reporting		X			
22. Accounting and disclosure		X			
23. Corrective and remedial powers of supervisor		X			
24. Consolidated supervision			X		
25. Home-host relationships		X			
Totals	1	17	7		
Sub-totals—pertaining only to BCP1		6			

⁷ Ratings: C: Compliant; LC: Largely compliant; MNC: Materially non-compliant; NC: Non-compliant; N/A: Not applicable