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Model of Banking Activity Government Regulation System

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Модель системи державного регулювання банківської діяльності

Abstract. In the article, the basic elements of banking activity government regulation system have been analyzed, namely, the aim, the functions, the object, the subject, the instruments and the principles. The main focus was given to elaboration of the interaction system of the subjects of the banking activity government regulation system. Application of system elements structuring methodology will enable to determine the nature of interrelations between the elements of banking activity government regulation system through building its information structure.

Анотація. В статті проаналізовано основні елементи системи державного регулювання банківської діяльності, а саме: мета, функції, об'єкт, суб'єкт, інструменти, принципи. Особливу увагу приділено побудові схеми взаємодії суб'єктів системи державного регулювання банківської діяльності. Застосування методики структурування елементів системи дозволить визначати характер взаємозв'язків між елементами системи державного регулювання банківської діяльності, завдяки побудові їх інформаційної структури.

Key words: banking activity, government regulation, system, the National Bank of Ukraine (NBU).

Ключові слова: банківська діяльність, державне регулювання, система, Національний банк України (НБУ).

Articulation of issue. The necessity to study and form a system of banking activity government regulation system is determined by the trends that are formed in the modern economic systems and crisis phenomena of the recent years. The given issue gains extreme topicality in the countries with bank-centric model of financial market development in the times of intensification of international economic integration and globalization processes for the reason that the banking sector is the main center of the country's financial resources accumulation. With regard to the importance of banking institutions, formation of the government regulation system adequate to the today's realities is a factor of effective banking system functioning and an important prerequisite of the country's socio-economic growth.

Analysis of research and publications. Research of theoretical and practical issues of banking activity government regulation have been studied by I. Dudka, M. Kovalenko, S. Lobozyńska, Ye. Mordan', S. Khodakevych, O. Chechel'. However, despite the fundamental scientific works in this field, scholars focus on the research of separate components of the banking activity government regulation system. At the same time, the issue of building up a comprehensive model of banking activity government regulation system is understudied.

Research objective. The aim of the research is the analysis of the key components of the banking activity government regulation system and definition of their interrelationship nature.

Main research findings. The basic elements of any system are the aim, functions, objects, subjects, principles and instruments. Thereat, agreeing with the viewpoint of N. Shul'ha [1], it is reasonable to study the system as a complex of separate elements being closely logically interdependent, being one entity and preserving this integrity over extended periods. In order to define the contents and the nature of interrelations among the banking activity government regulation system components it is worth to study them in more detail.

In accordance with art. 55 of the Law of Ukraine “On the National Bank of Ukraine”, the main aim of banking regulation is defined as the banking system security and financial solvency, depositors and creditors protection [2].

To the researcher’s [3] point of view, the aims to be achieved as the result of the regulation process can be classified into fundamental and instrumental. Fundamental aims are the aims that do not need additional grounding. Instrumental aims are the aims that are the instruments of achieving fundamental aims [4].

Fundamental aims of banking activity government regulation encompass provision of banking system functioning stability and depositors and creditors protection.

Instrumental aims cover: development of powerful and efficient legislative base, risk and system crises prevention etc. S. Khodakevych [5], partially shares this opinion and admits that the aim of banking sphere government regulation is support of national banking system sustainability, separate banks bankruptcy prevention, support of competition in the banking sphere, compliance with the needs of the society and clients of banks in obtaining qualitative banking services.

The author [6] admits that the efficiency of government regulation primarily depends on the government policy aims in the banking sphere. These aims are as follows: provision of laws and rules observation, which presupposes a high level of banking activity control and strengthening officials’ responsibility; fostering the development of innovative and investment model of social reproduction, economic protection of strategically important operations; monopoly restriction and competition support in banking activity, support of ample banks concentration policy with the aim of their competitiveness enhancement; foreign bank equity qualitative and relevant quantitative components control; meeting the needs of the society in various banking services; elimination of potential crises in the banking sphere; building up transparency of the banking sector functioning; provision of efficient banking activity, maintenance of the proper standardization and professionalism level in the banking activity.

In his turn, O. Prysyzhnyuk [7] states that the main high-priority tasks of

government regulation and monitoring in order to provide for banking system stability and reliability are: monopolization limitation and competitive environment formation in the banking sector; investors and depositors protection for inefficient bank management; provision of transparency in the overall banking system and for every bank in particular; regulation of the quantitative component and estimation of the optimal foreign capital share in the banking sector.

Agreeing with the scholars [3, 4, 5, 6, 7, 8], it is worth specify that the aim of banking government regulation is provision of the banking system stable functioning and sustainable development as well as depositors and creditors protection.

The essence of banking system government regulation is revealed through fulfillment of functions imposed by the society and the financial sector state of the country. The degree of adequacy to which the government regulation system will perform its coordination functions in the banking sector will affect banking business development and further economic growth in the home economy.

To the author's [9] point of view, banking system government regulation functions: are based on control problems; have objective nature; are the components of banking industry management content; are relatively independent; are realized through the banking system regulation mechanism; are aimed at the object of regulation.

Domestic science also covers authorial approaches to understanding banking system government regulation functions. For instance, M. Surzhyn'skyy [10] considers banking regulation as a government regulation function aimed at the provision of:

- banking institutions performance constancy and financial status reinforcement;
- aiming and fostering banking activity in the crediting sphere performance of high-priority economy development tasks and social welfare gain;
- cashflow scientific management in the national economy;
- formation depositor protection assurance system, individuals protection in particular.

Provided the maximum taking into account legislative provisions and the economic essence of banking activity government regulation, it is worth defining the following functions [9]:

- institutional – aimed at competitive environment provision in the banking activity, equality of the banking market participants of all ownership forms, free entrance and exit from the given market segment, which is realized via legislative and statutory instruments development, acceptance and implementation;

- regulatory – presupposes banking business organization process regulation, banking activity regulation on the credit, currency and stock markets;

- social (protective) – provision of social care and banking market participants protection;

- supervisory – detection of the current legislative and regulatory base violations and provision of adequate response of the supervisory bodies to the implementation of sanctions against violators. The supervisory function is fulfilled through banking supervision, tax audit, government economic control, law enforcement agencies control and financial monitoring;

- stabilization – provision of the country's banking sector security, which refers to detection forecast of internal and external threats to the banking system; execution of a set of prompt and long-term measures aimed at their prevention and neutralization;

- coordination – establishing cooperation between regulatory government bodies. Proper fulfillment of the cooperation function fosters avoiding duplicated regulatory and supervisory functions, the specialists' time economy, and reduction of financial expenses on the appropriate personnel;

- integration – facilitation of the Ukrainian banking system integration in the world banking market.

The researchers [3, 11] complement the abovementioned list of functions with the following:

- analytical – presupposes data mining, analysis and evaluation of banking institutions functioning results and macroeconomic indices of the country, which

have direct influence on the banking sector. This enables timely response to destabilizing factors of banking system development and implementation of the appropriate precautions;

- methodological – refers to the development of the system of notions, methods, principles, norms, techniques, ways and means of activity organization needed to perform banking regulation;

- information – presupposes obtaining and provision of official information about the banking system status for the purpose of internal and external use.

Integration of the scholars' points of view [3, 9, 10, 11] enabled to form the following set of banking activity government regulation functions, namely: regulatory; social (protective), supervisory, stabilization, coordination, integration, analytical, methodological and information.

Agreeing with the scholar's [6] point of view, the object of government regulation is the banking system of Ukraine, i.e. the aggregate of banks, institutions in their interrelation, which are joined and function as a result of the activity of the government and the society.

Among the scientists there is no unity of thought as to the subject of banking activity government regulation. To the author's [3] point of view, the subjects of regulation are the NBU, government bodies, self-regulatory and organizations.

The scholar [6] distinguishes the subjects of banking activity government regulation according to the directions of their application, namely: banking regulation (the President of Ukraine, the Verkhovna Rada of Ukraine, The Cabinet of Ministers of Ukraine, the National Security and Defense Council of Ukraine, the Association of Ukrainian Banks); banking supervision (National Bank of Ukraine (NBU), Deposit Guarantee Fund); banking control (Ministry of Finance of Ukraine, Ministry of Interior of Ukraine, Security Service of Ukraine, the State Audit service of Ukraine, courts of general jurisdiction, the Prosecution Service of Ukraine).

S. Khodakevych [5] classifies the subjects of government regulation into two groups according to the given institutions areas of responsibility: 1) institutions of direct banking activity government regulation (the President of Ukraine, the

Verkhovna Rada of Ukraine, the NBU, Deposit Guarantee Fund); 2) institutions of significant influence on the banking activity (the Government of the country via Government Commission of Financial Services Market Regulation of Ukraine and the National Securities and Stock Market Commission, the State Financial Monitoring Service of Ukraine, the Competition Authority of Ukraine).

The work [8] states that the subject of government regulation is the individual (citizen), who is instantiated in the government bodies and posts – the President of Ukraine, Members of the Verkhovna Rada of Ukraine, Cabinet of Ministers of Ukraine, and regional state administrations.

The abovementioned discrepancies in the list of subjects generate the problem of building up the optimal system of banking activity government regulation in Ukraine from the institutional point of view. It is worth noting that the efficiency of banking sector regulation and supervision depends mainly on its institutional structure, the degree of clarity of the regulation and supervision bodies task definition, the degree to which the bodies, which develop the financial and economic policy of the state and are responsible for their implementation, understand them.

To the author's point of view, the following list of the subjects of banking activity government control is the most complete: the President of Ukraine, the Verkhovna Rada of Ukraine, the Cabinet of Ministers of Ukraine (the Ministry of Finance), the Antitrust Committee of Ukraine, the NBU, the National Securities and Stock Market Commission, Deposit Guarantee Fund and the State Financial Monitoring Service of Ukraine.

Under article 106 of the Constitution of Ukraine [13], the powers of the President of Ukraine include: appointment to the posts and dismissal from the posts of half of the members of the Council of the National Bank of Ukraine; nomination of candidates for the post of Chairman of the National Bank of Ukraine to the Verkhovna Rada of Ukraine and presentation of the subject of the Chairman's dismissal from the post. In addition, the President of Ukraine approves the NBU income and expenditure budget, which takes account of planned profits that must be remitted to the State Budget of Ukraine; The President appoints the auditing firm that

carries out the NBU activity audit and approves the auditor's report.

Another body that participates in banking activity government regulation in the Verkhovna Rada of Ukraine. In accordance with the Constitution of Ukraine (art. 75) [13], the Verkhovna Rada of Ukraine is the single legislative body in Ukraine, thus, it enacts laws on banking activity.

Moreover, under article 85 of the Constitution of Ukraine [13], the powers of the Verkhovna Rada of Ukraine include: appointment and dismissal from the post of the Chairman of the National Bank of Ukraine at the instance of the President of Ukraine; appointment and dismissal of half of the members of the Council of the National Bank of Ukraine.

The legislative initiative in the Verkhovna Rada of Ukraine belongs to the President of Ukraine, the Cabinet of Ministers of Ukraine and the National Bank of Ukraine.

Under article 113 of the Constitution of Ukraine [13], the supreme body in the executive bodies system is the Cabinet of Ministers of Ukraine. Powers of the Cabinet of Ministers in the field of financial policy and banking activity in particular, are exercised through the Ministry of Finance of Ukraine. Under the Regulations on the Ministry of Finance of Ukraine [19], The Ministry of Finance of Ukraine is the main body in the central executive bodies system responsible for formation and provision of implementation of state financial, fiscal, tax and customs policy (except for management of taxes, duties and customs payments as well as tax and customs policy implementation), policy in the sphere of government financial control, fiscal management of budget funds, accounting, emission and conducting lotteries, organization and control of the generation of securities, strict accounting documents, mining, production, use and storage of precious metals, precious gems, precious organogenic gems and semiprecious stones, their circulation and accounting, in the sphere of prevention and anti-money laundering procedures or financing of terrorism.

In the executive bodies structure, the State Financial Monitoring Service of Ukraine plays an important role, the activity of which is aimed at and coordinated by the Cabinet of Ministers of Ukraine through the Minister of Finance of Ukraine [14].

The main tasks of the State Financial Monitoring Service of Ukraine are: 1) implementation of the government policy in the sphere of anti-money laundering and terrorism financing as well as submission of proposals as to its formation; 2) mining, processing and analysis of information on the financial transactions subject to financial monitoring; 3) formation and provision of single government information system functioning in the anti-money laundering and terrorism financing sphere.

Carrying out supervisory activity, the State Financial Monitoring Service of Ukraine cooperates with the NBU in the anti-money laundering and terrorism financing sphere. In particular, information on the transactions subject to the compulsory control and doubtful transactions is sent to the State Financial Monitoring Service of Ukraine by the banks via the NBU [14].

With account taken of the fact that banks pursue professional activity at the securities market, National Securities and Stock Market Commission is the direct participant in the banking activity government regulation system. Under the Regulations on the National Securities and Stock Market Commission [15], the National Securities and Stock Market Commission is a government collegial body subordinate to the President of Ukraine and accountable to the Verkhovna Rada of Ukraine.

With the aim of efficient government regulation and banking risks prevention in Ukraine, the Government formed the Deposit Guarantee Fund. It began its activity with signing the Decree “On Measures of Commercial Bank Depositors Rights Protection”, which sanctioned the Regulations on the Deposit Guarantee Fund formation procedure, its funds formation and use.

In its activity, the Deposit Guarantee Fund refers to the Law of Ukraine “On the Deposit Guarantee System” [16]. Under article 3 of this Law, the Fund is the institution, which performs special functions in the sphere of individual deposit guarantee and insolvent banks withdrawal from the market and liquidation to the extent permitted by law. Therefore, the Deposit Guarantee Fund fosters achievement of the main aim of banking activity government regulation, namely protection of depositors’ rights and lawful interests and enforcement of trust to the banking system

of Ukraine.

Another institution, which participates in banking activity regulation and supervision, is the Antitrust Committee of Ukraine. Under article 1 of the Law of Ukraine “On the Antitrust Committee of Ukraine” [17], it is a special status government body, the aim of which is the provision of government protection of competition in the entrepreneurial activity and in the state procurement sphere. The Antitrust Committee of Ukraine cooperates with the NBU as to supervision and antitrust law compliance by the banks.

The National Bank of Ukraine is the major lever of influence on the banking activity because it is responsible for national monetary unit stability and banking system functioning support. The National Bank of Ukraine as the supreme bank of the state coordinates functioning of credit institutions and performs monetary and financial processes management functions in the economy of the state, supports the economic policy of the Cabinet of Ministers of Ukraine if it not at variance with national monetary unit stability provision. Its powers as to banking regulation at the level of the central administrative office are imposed on various departments with the account taken of their functional area [5].

Characteristics of the legal nature of the NBU, namely its economic independence, is instrumental for banking activity government regulation implementation. The current legislation states that any interference of legislative and executive bodies or their officers into execution of functions and powers of the Council of the National Bank or the Board of the NBU is unacceptable in any way other than within the framework provided by the Law of Ukraine “On the National Bank of Ukraine” [2].

This legal status of the National Bank of Ukraine provides for its independence in exercising the single government monetary policy, facilitates prevention of unregulated money emission, budget deficit financing limitation. It is necessary to ascertain that the legal status of the NBU is characterized by the dual legal nature: on the one hand, it is the government body authorized to exercise government management in the sphere of banking activity, on the other, it is a banking institution

that conducts banking transactions, acts as the tender of last resort for other banks [18]. The peculiarity of the legal status, the tasks and functions of the NBU define the nature of its relationship with the President, the Verkhovna Rada of Ukraine and the Cabinet of Ministers of Ukraine. Acting in the single social system as a specific central government body in the state bodies system, The NBU has autonomy, its activity is characterized by optimum independence as to monetary system management in Ukraine.

Fig. 1 represents the banking activity government regulation system in Ukraine.



Fig. 1. The banking activity government regulation system in Ukraine.

Despite the significant number of government bodies, the National Bank of Ukraine is one and almost the single regulator in this sphere, and its links to other

elements of this structure are considered “insignificant”. This approach to banking activity government regulation system formation is one of the most debatable in the modern theory and practice.

However, the most effective institutional organization of the banking activity government regulation is able to minimize the effects of the financial economic crisis, provide for the stable functioning of the banking institutions system in general and certain banks in particular as well as enhance trust in the state banking system.

Banking system is one of the most important subsystems of the country’s national economy, thus, its effective functioning must comply with the basic principles of the economy government regulation.

It is worth to include the following principles [12]: scientificity, conformity of interests, purposefulness, priority and feasibility, consistency, complexity, flexibility and adaptability, sufficiency, organizational and legal as well as economic and organizational provision principles, the principle of graduality and phasing of the economy government regulation, the priority of law over the economy, integrity of economics and politics, efficiency, transparency and responsibility.

At the same time, eminent scholars in the sphere of banking regulation and supervision [3] admit that the efficient banking regulation must be grounded on the application of the banking system regulation principles, which will enable to enhance banking system security and financial stability, depositors and creditors’ protection, that the regulatory government policy in the sphere of banking relations must be based on such principles as elasticity, consistency, justice and sufficiency.

It is worth adding the following principles, which may facilitate more efficient banking activity regulation: legitimacy (the subjects of regulation act in accordance with the current legislative base); purposefulness (the selected banking regulation policy must provide for the efficiency of its activity, i.e., it must be aimed at the achievement of the main aim – banking system stability and depositors and creditors’ protection); coherence (decision-making as to banking system regulation performed by the subjects of regulation undoubtedly depends on the current state of the country’s socio-economic development); balance of interests; transparency;

operational independence (banking activity regulation is performed without any infringements to the economic independence of the banking activity subjects); responsibility.

Generalization of the existing points of view enables to distinguish the set of basic banking activity government regulation principles and complement them with the economy government regulation principles, namely: scientificity, consistency, complexity, efficiency, elasticity, sufficiency, legitimacy, purposefulness, coherence, conformity of interests, operational independence and responsibility.

In order to build up an effective government regulation system, government bodies must have a certain set of available instruments of influence on the banking system.

On the basis of government regulation methods classification, the author [3] figuratively classify all the government regulation instruments into structural (that influence banking system structure formation) and behavioural (that influence its behaviour).

However, the best grounded list of instruments was given in the work [6]. Hence, regulatory influence exercise instruments can be classified according to the type of regulation lever, namely: monetary relations, banking prudential regulations, banking services market entry and exit.

Hence, the monetary relations regulation instruments encompass: reserve requirements, interest rates on the operations of the central bank, open market operations, banks refinancing; foreign exchange regulation, setting monetary expansion targets and direct quantitative control.

The instruments of banking services market entry and exit encompass: banking system access regulation, regular banking reports and banks audit; means of compulsory influence on troubled banks; getting insolvent banks under special control, appointment of the provisional administration, activity suspension, banks organization, reorganization and liquidation.

With reference to the notion of “system”, there are interconnections between the basic elements of banking activity government regulation. It is possible to define

their nature having built up the pattern of interdependence of the aim, the subjects, the objects, the functions, the principles and tools of controlling.

With the aim of forming the information structure of the set of elements in the banking activity government regulation system with the division of elements into levels with greater and minor prepotency, the system elements structuring technique was applied [20]. Building up the information model enables to structure the elements of banking activity government regulation system, reveal their interrelation and distinguish primary and secondary elements.

The elements in the system are interrelated, as a result it is possible to present the following structure of banking activity government regulation model (Fig. 2)

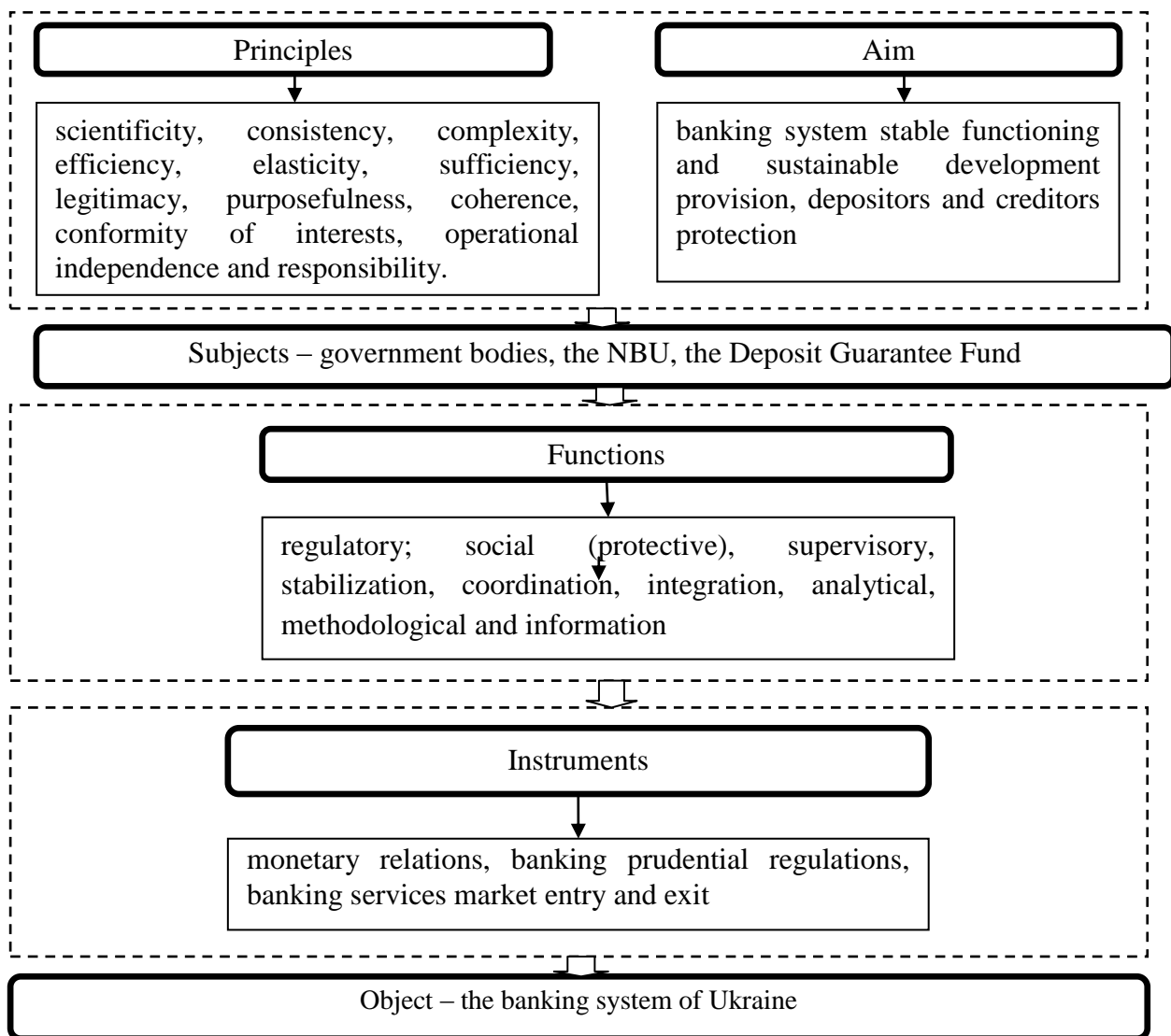


Fig. 2. Banking Activity Government Regulation System Model

Research Findings. Therefore, the analysis of institutional provision of banking activity government regulation system justifies that a significant number of government bodies participate in government regulation of this sphere. However, the levers of influence on its effective functioning are not formed and distributed enough efficiently. Thus, building up a comprehensive model of banking activity government regulation system will facilitate banking system financial stability, banking market equilibrium state, competitive environment formation and provide for the sustainable development of the overall banking system.

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