

C. REGULATORY FRAMEWORK AND THE LICENSING PROCESS

1. REGULATORY FRAMEWORK

The ongoing implementation of medium- and long-term objectives of the Bank of Albania, consolidated, even during 2010, the work for drafting new regulations and making several amendments to existing regulations on banking supervision, which took into consideration the compliance with the provisions required under the Law on Banks, the implementation of Basel Committee's principles and standards for effective supervision, European Council directives and the best practices in the field of regulation and supervision of financial institutions.

1.1. NEW REGULATORY ACTS OF SIGNIFICANCE TO BANKING SUPERVISION

- Regulation "On risk management in the activity of non-bank financial institutions" (approved by Bank of Albania Supervisory Council Decision No. 25 of 24/03/2010) as a thorough review of the existing regulation, was drafted in accordance with and pursuant to provisions of the Law "On Banks in the Republic of Albania", taking also into consideration the World Bank's expertise on risk management rules for microcredit financial institutions in Albania.

The regulation provides the risk management rules on non-bank financial institutions and completes the regulatory and supervisory framework on non-bank financial institutions, the licensing criteria of which are actually stipulated in the Regulation "On licensing of non-bank financial institutions".

The new regulation, unlike the regulation in force, makes several new definitions: about risk exposure indicator and limits; about the maximum exposure limit of an entity to a connected person or group of persons; stipulates the specific limits of total large (aggregate) exposure for entities that conduct financial leasing; defines the liquidity risk and determines risk management requirements for the entity; defines the open foreign currency position and sets forth limits for open foreign currency positions that the entity may hold at the end of each business day; defines more simplified requirements on credit risk management by non-bank financial institutions based on days in

arrears on loan repayment; stipulates credit risk management requirements for microcredit financial institutions, etc.

- In view of meeting the new requirements, indicators, etc., of the new regulation on risk management in the activity of non-bank financial institutions, the “Reporting system of non-bank financial institutions” (approved by Decision No. 26 of 24/03/2010 of the Bank of Albania’s Supervisory Council) was drafted in collaboration with the Statistics Department.

- Regulation “On defining the decision-making level on supervision of banking and financial activities” (approved by Bank of Albania’s Supervisory Council Decision, No. 36 of 26/05/2010), as a thorough review of the existing regulation, emerged as a necessity for implementing the provisions stipulated under the new Law on Banks. It sets out the division of powers even at the lowest decision-making levels, in accordance with the existing practices of the licensing and supervision process. The revised regulation sets out the level of power exercised by managing bodies at the Bank of Albania in the decision-making process as regards its supervisory function, by applying the principle of delegating powers closer to persons exercising specific relevant functions. The Regulation aims, through this delegation process, to facilitate the decision-making process in the field of banking and financial supervision.

- The Regulation “On management of risk from open foreign currency positions” (approved by Bank of Albania’s Supervisory Council Decision, No. 48 of 14/07/2010), as a thorough review of the existing regulation, drafted in accordance with and pursuant to the provisions of the Law “On Banks in the Republic of Albania”, taking also into consideration the Basel Committee document on Capital Accord (or Basel II) and EU Directive 2006/48/EC on calculating open foreign currency positions and foreign exchange risk management.

The regulation sets out the rules and criteria for calculating and reporting open foreign exchange positions of banks, aiming at managing the exchange rate risk.

This regulatory act incorporates into a single document the rules and the method of calculating open foreign currency positions; it provides new definitions on some items/transactions that will be part of the structural foreign currency position by setting out the approval criterion by the Bank Albania as well; it adjusts the net open foreign currency position calculation approach to the stipulations made in the Basel document and the European Directive; it establishes a more prudent monitoring of open foreign currency position and sets out more detailed requirements for drafting policies and procedures necessary to identify, measure, monitor and control the exchange rate risk; and it adapts the existing reporting form to the new requirements set forth in this regulatory act.

- Manual “On conservatorship and liquidation of banks” (approved by Decision of the First Deputy Governor of the Bank of Albania, No. 11207 of 31/12/2010), was drafted in accordance with and pursuant to the provisions

of the Law "On Banks in the Republic of Albania" and took into consideration the Central Bank of the Republic of Kosovo manual, drafted with the assistance of the Federal Deposit Insurance Corporation (FDIC).

The manual sets out procedures and actions for realizing the process of conservatorship and liquidation, which complete the supervisory authority's operational framework in the event a bank or a foreign bank branch is put into conservatorship/liquidation - an integral part of the Albanian banking system, which so far has not undergone any such experiences.

The drafting of the manual emerged as a necessity for enforcing the provisions required under the Law "On Banks in the Republic of Albania", which makes room for and obliges the authority to fulfil and put in place more detailed procedures for these processes, particularly taking into consideration the situation of the global financial crisis. The latter proved that although the countries had in place the legal and regulatory framework necessary for these processes, the occurrence of such phenomena highlighted shortcomings in this framework.

1.2. ADDITIONS AND AMENDMENTS TO THE REGULATORY FRAMEWORK

- Additions and amendments were made to the Regulation "On supervision of savings and loan associations and their unions" (approved by Bank of Albania's Supervisory Council Decision, No. 65 of 29/09/2010). Amendments to this Regulation, in response to concerns raised by savings and loan unions, waive the limit on loans with a maturity term of over three years and limit the loans with a maturity term of over 5 years in terms of certain amounts of capital, deposits or liabilities. Also, the maximum loan maturity term was extended from 5 to 10 years and several requirements were put in place for loans with a maturity term of over 7 years, in order to limit the exposure to this type of credit risk, determining at the same time the need for specific policies on over 5-year loans.

The amendments make room for long-term lending in order to boost lending for investment purposes for the development of projects in the agriculture sector, and they will not provide a negative impact on the financial sustainability of savings and loan associations and their unions.

- Some additions and amendments were made to the Regulation "On the management of risk arising from large exposures of banks" (approved by Bank of Albania's Supervisory Council Decision No. 88 of 22/12/2010). These amendments aimed at mitigating and facilitating the measures taken by the authority during the global financial crisis on the management of concentration risk, primarily alleviating the maximum permissible limit for investments (exposures) of banks in their affiliates, or in one or more subsidiaries of the parent bank (from 10% to 20%), and reinstating the treatment by reduction of 20% of exposures to banks and financial institutions operating in OECD countries.

Also, the amendments make a clarification about the treatment of government securities, which shall be considered deductible collateral only when issued in the national currency, creating consistency in regulation, as long as the latter allows for exception of exposure in the national currency to the same counterparty - Albanian Government. In the meantime, a provision has been added that entitles the Bank of Albania to impose more restrictive temporary requirements to a bank or banks in the system than those provided in this regulation, if necessary.

The amendments were based on stress testing of the financial stability and of banks' abilities to absorb possible losses from the materialization of shock events, conducted recently by the highest regulatory authorities in the EU area, in coordination and cooperation with the European Commission, which was assessed as successful and was commended by financial markets.

- Some additions and amendments were made respectively to the Regulations "On capital adequacy ratio" and "On risk management in the activity of non-bank financial institutions" (approved by Bank of Albania's Supervisory Council Decisions No. 89 and No. 90 of 22/12/2010). The amendments relate to the list of OECD countries applicable to counterparties banks are exposed to, which are considered in calculating the risk weighted assets for purposes of calculating the capital adequacy.

The amendments aimed at providing a reference list of the OECD countries for purposes of applicability of these regulative acts by banks and non-bank financial institutions, driven by the addition of some countries to OECD membership (such as Slovenia, Israel and Chile) during 2010. Thus, banks and financial institutions already possess a reference to the list of OECD countries, whose changing does not always lead to the need for regulatory changes, whereas the supervisory authority, whenever it deems it reasonable, may make exceptions from this list, depending on these country's financial situation and developments.

2. LICENCING

2.1 GRANTING A LICENCE, PRELIMINARY APPROVAL

Pursuant to the Law "On the Bank of Albania", the Bank of Albania is the sole competent authority in charge of granting licences and supervising all banks in the Republic of Albania.

Law No. 9662 of 18/12/2006 "On Banks in the Republic of Albania" (hereafter referred to as the "Law on Banks", for simplicity) and by-laws issued by the Bank of Albania provide the criteria and conditions to grant a licence for conducting banking and financial activity to banks and other non-bank financial institutions in the Republic of Albania.

As in the previous two years, during 2010 no bank licence applications were submitted.

Year 2010 highlighted several changes related to:

- Shareholders' structure and shareholders' equity of banks,
- Increase in banking business and products,
- Expansion of bank networks within the territory of the Republic of Albania,
- Appointment of bank administrators,
- Licensing of non-bank financial institutions,
- Licensing of foreign exchange bureaus,
- Licensing of savings and loan associations.

The structural changes to bank ownership consisted in changes to the non-qualifying holding in the banks' stock ownership. Related to these changes, banks do not request approval; however, pursuant to the Law on Banks, they are obliged to notify the Bank of Albania of them. These reports are also accompanied by appropriate documentation, as stipulated under Bank of Albania's by-laws, chiefly under the Regulation "On licensing banks and branches of foreign banks to conduct their activity in the Republic of Albania" (hereafter referred to, for simplicity, as "On Bank Licensing"), approved by Bank of Albania's Supervisory Council Decision, No. 14 of 11/03/2009. The banks that have informed the Bank of Albania of changes to their shareholder structures are: Credins Bank, Intesa Sanpaolo Bank Albania and National Commercial Bank. Also, during 2010, some banks have managed to increase their shareholders' equity, mainly through capital injection from shareholders in the form of cash and through capitalization of profits earned and accumulated during the past years. In concrete terms, the National Commercial Bank, Tirana Bank, Veneto Banka, ProCredit Bank, Emporiki Bank (Albania), Credins Bank, Societe Generale Albania Bank, First Investment Bank Albania have reported growth of shareholders' equity.

In implementing their strategies, banks are seeking for additional banking and financial activities, new products and services. Applications for approval of additional activities and other banking products are based on Bank of Albania's legal provisions and regulations. Specifically, during 2010, the banks submitted 7 applications for obtaining Bank of Albania's approval to conduct financial activities not included in their licence annex. They consist mainly in the following activities:

- a) Factoring and financing of commercial transactions;
- b) Trading of transferable securities, other negotiable instruments and financial assets, including transactions in gold;
- c) Participation in issues of all kinds of securities including underwriting and placement as agent (whether publicly or privately) and provision of services related to such issues;
- d) Intermediation in monetary transactions for asset management such as cash or portfolio management, fund management, custodial, depository and trust services;

- e) Settlement and clearing services for financial assets, including securities, derivative products and other negotiable instruments, etc.

These activities affect the development of the Albanian financial market, mainly the trading of those financial instruments that are less known by the public. The vitalization of Tirana Stock Exchange will be an important driver to the trading of financial instruments. This tendency shows that banks tend to expand their business in terms of diversification of banking products and services by offering more investment options to their customers. This phenomenon is also observed in 2011. The effects of additional activities carried out by banks remain to be tested in the forthcoming periods.

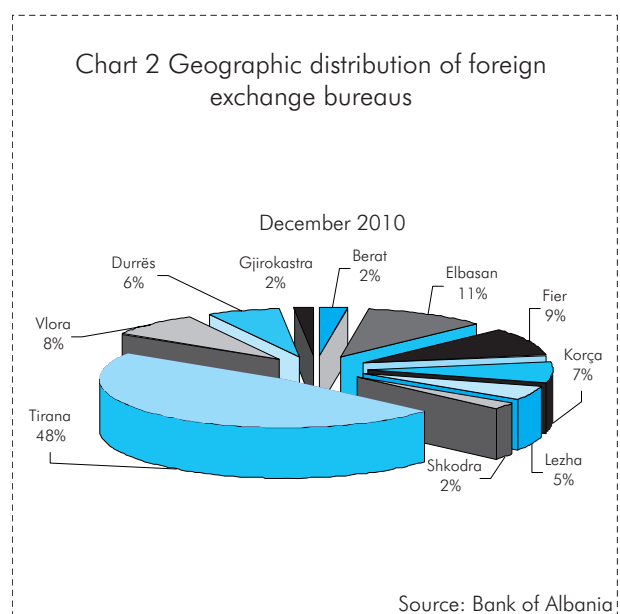
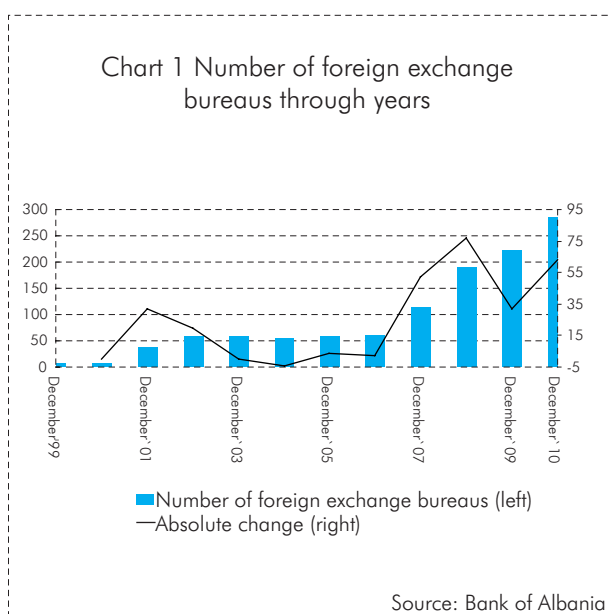
Electronic banking products and services are a facility that banks offer to their customers. They consist in debit and credit cards, ATMs and POSs, internet banking, mobile and SMS banking, etc. These electronic banking products/services are provided by 14 banks. In 2010, the number of electronic cash cards issued by banks was 694.848 or 128.914 cards more than in 2009. The number of debit cards was 667.548 and that of credit cards was 27.300. In the meantime, the total number of ATMs installed by banks was 771 and that of POSs was 4.903. During 2010, 3 new cases of e-banking products were approved, consisting in implementing internet banking, mobile banking and electronic banking cards.

Banks and non-bank financial institutions submitted 53 requests for the approval of administrators they had appointed, pursuant to the Law "On Banks in the Republic of Albania", on which respective preliminary approvals were granted. Of the approved bank administrators, 12 cases were for members of the bank steering council, 5 cases for members of the Audit Committee, 6 cases for general/executive director, 2 cases for deputy director-general, and 28 cases for head of department/division/directorate.

The upward tendency for licence applications at the Bank of Albania by non-bank financial institutions continued in 2010. 4 new licences were granted by the Bank of Albania to non-bank financial institutions in response to their application for conducting financial activity (such as lending, financial lease, microcredit and factoring). In the meantime, there is noticed a tendency to establish financial institutions that provide payment and money transfer services via mobile phones. Specifically, in 2010, Sogelease sh.a., Capital Invest sh.a., Tranzit Ltd., and Albanian Factoring Services (AFS) sh.a., applied to and were granted a licence by the Bank of Albania for operating as non-bank financial institutions. It is worth noting that year 2010 marked the entry into the market of a non-bank financial institution that conducts factoring, which so-far has been part of activities carried out only by some banks operating in the Albanian market.

Also, pursuant to regulatory requirements, during 2010, Bank of Albania's consent was given for the transfer of capital ownership of two non-bank financial institutions. At end-2010, the number of non-bank financial institutions reached 17.

The further development of the Albanian financial market, along with the rules taken and applied by the Bank of Albania for curtailing the informal economy, were accompanied by a doubling of the applications, compared to a year earlier, for conducting foreign exchange operations by different entities extended across the whole territory of the country. As a result, the number of foreign exchange bureaus licensed in 2010 increased swiftly (66 new foreign exchange bureaus were licensed, from 32 in 2009). During 1999² -2010, a period over which the conduct of foreign exchange activity by entities licensed by the Bank of Albania is extended, 2008 marked the highest increase of new actors entering the foreign exchange market, which was materialized with 77 new licences, while 2010 comes immediately after it with regard to the pace of the increase in the number of licensed foreign exchange bureaus.



All applications submitted by entities during 2010 were finalized with a licence granted by the Bank of Albania. Foreign exchange bureaus licensed pursuant to Bank of Albania's criteria, are located and perform their activity in 24 main cities of Albania. If we refer to their geographic distribution by districts, there is noted a concentration of about 48% of them in Tirana. This concentration has decreased year in year out due to the distribution of the licensed foreign exchange bureaus to other districts of the country.

Three licences for foreign exchange bureaus were revoked upon their own request.

Number in 2009	New licences	Revocation	Number in 2010
221	66	3	284

Table 1 Number of foreign exchange bureaus licensed until 2010

² Year 1999 marked the commencement of foreign exchange activity by entities licensed by the Bank of Albania.

An important part of activity for many foreign exchange bureaus is also the acting as a money transfer agent for the account of financial institutions AK-INVEST and Financial Union Tirana licensed by the Bank of Albania. During 2010, 52 foreign exchange bureaus were licensed for conducting this additional activity.

The process having started in 2009 for implementing the regulatory requirements, in order to formalize the money transfer market by approving non-bank financial institutions' agents that carry out money transfer operations for their account, continued even during 2010 at a higher pace of increase to its full completion. It is worth stressing that many new entities that had newly started their activity were involved in this process. Money transfer agents approved by the Bank of Albania carry out this activity for the account of non-bank financial institutions AK-Invest and Financial Union Tirana. The total number of money transfer agents approved for both institutions reached 108 at end-2010.

Table 2 Number of money transfer agents for the account of non-bank institutions (as at end 2010)

	Ak-Invest	Financial Union Tirana
Money transfer agents	14	94
Foreign exchange bureaus that are also money transfer agents	64	67
Total	78	161

Source: Bank of Albania

During 2010, 4 new savings and loan associations were licensed and 13 such associations were revoked the licence as a result of their merging with an existing company, taking the number of savings and loan associations to 126 and the number of their unions to 2.

2.2 ACCOMPANYING TABLES ON LICENCING

Table 3 Electronic banking products approved by the Bank of Albania during the past five years

Electronic products	2006	2007	2008	2009	2010	Total
Debit Cards	6	4	2	2		14
Credit Cards	5	3	1	1	1	11
Maestro (Debit) Cards	1		1	1		3
Master (Credit) Cards	-	-	1	2		3
Visa (Debit) Cards				1		1
Visa (Credit) Cards				1		1
MultiCash	1	-	-			1
ATM	6	4	2	2		14
POS	1	2	2	1		6
Internet banking	2	2	3	2	2	11
Phone banking	-	-	1			1
Mobile banking / SMS banking	-	-	1	1	1	3

Source: Bank of Albania

Table 4 Distribution of e-banking products/services as at end-2010

Banks	ATM	POS	Internet Banking	Phone banking	Mobile/SMS banking	Electronic cards
Raiffeisen Bank Albania sh.a.	√	√	√		√	√
National Commercial Bank sh.a.	√	√	√		√	√
Tirana Bank sh.a.	√		√	√	√	√
National Bank of Greece – Albania Branch	√					√
Alpha Bank – Albania Branch	√	√	√			√
ProCredit Bank sh.a.	√	√	√			√
First Investment Bank, Albania sh.a.	√		√			√
Credins Bank sh.a.	√	√	√			√
Union Bank sh.a.	√		√			√
Banka Popullore sh.a.	√		√			√
Intesa Sanpaolo Albania sh.a.	√	√	√			√
Veneto Banka sh.a.	√		√			√
International Commercial Bank sh.a.	√					√
Emporiki Bank sh.a.	√					√

Source: Bank of Albania

Table 5 List of entities licensed by the Bank of Albania through years

No.	Entities	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
1	Banks and branches of foreign banks	13	14	15	16	17	17	16	16	16	16
2	Non-bank financial institutions	4	5	7	7	7	6	6	7	13	17
3	Foreign exchange bureaus	38	58	58	54	58	60	112	189	221	284
4	Savings and loan associations	-	113	131	130	131	125	130	133	135	126
5	Unions of savings and loan associations	-	2	2	2	2	2	2	2	2	2

Source: Bank of Albania

Table 6 Coverage with banking services

	2004	2005	2006	2007	2008	2009	2010
Number of banks	16	17	17	16	16	16	16
Number of employees	2,816	3,479	4,189	5,155	6,493	6,404	6384
Number of branches/agencies in the country	188	250	294	399	511	524	529
Average number of employees per:							
- Bank	176	205	246	322	405	400	399
- Banking unit	15	14	14	13	13	12	12
Number of population (000)	3,127	3,149	3,152 ¹	3,170	3,193.9	3,195 ²	-
Number of population per:							
- Bank	195,438	185,235	185,424	197,013	199,619	199,688	-
- Banking unit	16,633	12,596	10,722	7,945	6,250	6,097	-
- Bank employee	1,110	905	752	615	492	499	-

Source: Bank of Albania

¹ The data on the average number of population for 2003, 2004, 2005 and 2006 have been extracted from the Bank of Albania's Monthly Statistical Report – December 2008 (table 04 – 03).

² The data on the number of population as at 1 January 2008, 1 January 2009 and 1 January 2010 have been extracted from the website of the Institute of Statistics.

Notwithstanding the increased network of bank branches and agencies, year 2010 marked a decrease in the number of bank employees and of average indicators related to their number.

Table 7 Bank network expansion as at end-2010

No.	Banks	No. of branches in the country	No. of agencies	No. of branches abroad	No. of branches and agencies	Change compared to 2009
1	Raiffeisen Bank	103			103	+1
2	National Commercial Bank	27	31	1*	59	+1
3	United Bank of Albania	4	2		6	0
4	Veneto Banka	8			8	0
5	Tirana Bank	49	3		52	+5
6	National Bank of Greece - Albania Branch	5	25		30	0
7	International Commercial Bank	9			9	+1
8	Alpha Bank - Albania Branch	48			48	0
9	Intesa Sanpaolo Bank Albania	17	14	1	32	-5
10	ProCredit Bank	25	17		42	-3
11	Emporiki Bank	13	11		24	+1
12	Credit Bank of Albania	1	2		3	0
13	Credins Bank	28	6		34	+1
14	Societe Generale Albania Bank	42			42	0
15	Union Bank	15	15		30	-1
16	First Investment Bank	5	4		9	0
	TOTAL	399	130	2	531	+1

*) The number of the National Commercial Bank branches abroad is verified and revised. More specifically, the National Commercial Bank has one branch in the Republic of Kosovo, which operates through 15 units throughout the whole territory of Kosovo.