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Troaca, Victor

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Proper funds of banking romanian companies

Ph. D. reader Victor Troacă,
"Titu Maiorescu " University , Tg-Jiu

ABSTRACT.

The development of the activity by the banking companies, in normal conditions, imposes on that these ones should dispose on a certain volume of proper funds, determined in accordance with their size, the profile of operations and the assumed risks. The specific of banking activity imposes on the necessity that these ones should permanently ensure a certain level of proper funds, which should not lower under the level of statutory capital requests established by the regular authority, namely the National Bank of Romania. The importance of proper funds for a banking company is rendered evident also by the lawgiver, by means of fact that , in order to be made, a banking company needs a minimum level of distinct proper funds or an initial capital, which nowadays is situated at the equivalent level of 5 milion Euro. The level of proper funds of the societies are always pursued by the statutory authority, for which reason the banking companies have the obligation to determine and report regularly these funds to the National Bank of Romania. There is presented in the paper the componence of proper funds of a banking company, the way of their determination and regular minimum requests of proper funds in which the banking societies should frame.

Key words: bank, banking funds, minimal fund request.

JEL classification: G21, G32

1. The proper funds structure of a banking company

In order to ensure the development in normal conditions with the ensurance of respecting the minimum statutory requests, the banking companies are ceaselessly preoccupied to ensure the necessary volume of proper funds.

Proper funds of a bank are made up of those resources which are being of its disposal with a permanent lasting character.

The importance of proper funds determination for the activity of a bank, as well as the necessity to assure a permanent efficient surveillane of the activity of every bank have determined the Romanian authority having responsibilities in the surveillane of banking field respectively the National Bank of Romania to regulate the structure of proper funds, the calculus methodology of proper funds and to establish the minimum requests the banking companies

should accomplish at an individual level, as well as the acceptance of the notion of proper fund at a consolidated level.¹

Proper funds of a banking company are made up of those patrimonial elements that are responsive to the following requests: are utilizable at any time and with priority in order to absorb the eventual losses, do not imply fixed costs for the involved banking company they are also effectively put at its disposal and wholly paid for.

At the individual level proper funds of banking societies are made up of *Level 1 proper funds* and *Level 2 proper funds*. The formalization of determination relation for banking proper funds is as follows:

$$(1) \quad \mathbf{Fp = Fp1 + Fp2}$$

in which:

Fp = total of proper funds of a bank;

Fp1 = Level 1 proper funds;

Fp2 = Level 2 proper funds.

2. Level 1 proper funds

Level 1 proper funds represent that component of proper funds made up of:

- Registered capital subscribed and paid in, except for the cumulative preferential actions or, in case, the endowment capital put at the disposal of the branch in Romania by the mother society with the headquarters in a third state, outside the European Union (Cs);
- The capital premii, fully cashed, afferent to registered capital (Pc);
- Legal reserves, statutory and other reserves, as well as the profit (Rz);
- Net profit of the last financial exercise, reported until its repartition according to destinations established by the general assembly of the shareholders, in the limit of the amount meant to be allocated to any of the destinations mentioned above (Pn);

In order to determine the Level 1 proper funds, of the value total of the mentioned elements, the following elements are to be inferred:

- The registering value in accountancy of the proper actions detained by the bank involved (Vac);
- The reported result, representing loss (Prr);
- Loss of current period registered until the date of proper funds determination (Prc);
- Value of registering in accountancy of intangible assets (In).

Making a synthesis, the calculus relation of Level 1 proper funds can be made as follows:

$$(2) \quad \mathbf{Fp1 = (Cs + Pc + Rz + Pn) - (Vac + Prr + Prc + In)}$$

¹ Regulation no.18/23/14.12.2006 regarding the proper funds of credit and investments institutions, issued by the National Bank of Romania and the National Committee of Movable Values.

3. Level 2 proper funds

Level 2 proper funds, taken into the calculus of total proper funds of a banking society are made up, at their turn, out of two assembled components, namely:

- ✓ *Level 2 proper funds of basis (Fp2b)*, and
- ✓ *Additional Level 2 proper funds (Fp2s)*.

The determination relation of Level 2 proper funds is:

(3) $Fp2 = Fp2b + Fp2s$.

Level 2 proper funds (Fp2b) are determined by totalizing the following elements:

- Reserves from the reevaluation of tangible assets adjusted by the afferent fiscal obligations (Rzi);
- Other elements that accomplish a series of statutory conditions, with the previous agreement of the National Bank of Romania (Aer);
- Titles for an endless period and other instruments of the same kind which accomplish the general conditions of respecting their subordinate character (Vts)

The calculus relation can be made this way:

(4) $Fp2b = Rzi + Aer + Vts$

The following specifications must be made with reference to the criteria the last two component elements of Level 2 proper funds of basis must accomplish:

- Elements that can be taken into calculus of the indicator "Level 2 proper funds of basis", having the previous agreement of the National Bank of Romania, must accomplish a series of statutory conditions, that is to say: they have to be at the disposal of the respective banking company without restrictions to cover the risks specific to the banking activity, when the losses and value deficits have not been identified yet; to be refound in the book keeping and their level to be established by the leadership of the banking society, verified by independent auditors, communicated to the National Bank of Romania and subject to its surveillance. There can be included also the public and private non repayable subventions.
- Titles for an endless period and other instruments of the same kind could be included in the calculus of Level 2 proper funds of basis providing that they should include the general conditions of respecting the subordinate character, as well as the following specific requests:
 - The repayment cannot be done at the holder's initiative or without the previous approval of the National Bank of Romania; the repayment cannot be requested during the first 5 (five) years from the issue of titles, and subsequently the repayment can be accepted by the national Bank unless it is sure that the proper funds of the involved banking society remain adequate, for at least a future period of two years;
 - The issue agreement must ensure that the involved bank has the option to postpone the payment of afferent interest;
 - The creditor's debt for the banking society must be entirely subordinated to the debts of all the other un subordinate debtors;
 - The titles' prospectus of emission must specify the fact that the afferent unpaid main and interest are being at the disposal of the bank in order to cover the losses, in conditions of assurance of the activity continuity;

- The amounts taken into account to have been entirely paid.

Additional Level 2 proper funds (Fp2s) are made up of cumulative preferential shares for a determined period (Vap) and the capital under a shape of subordinate loan (Vis). The calculus relation can be made as follows:

(5) $Fp2s = Vap + Vis$

The two elements which make up Additional Level 2 proper funds can be taken into the calculus of the proper funds of banking societies unless they do have the agreement of the National Bank of Romania and in the conditions when the firm and stipulated by contract obligations assure that, in case of bankruptcy or liquidation of the respective banking company, these ones have an inferior rank in comparison with all the other creditors' debts and they shall be repayable only after all the other unrepayable debts have been already paid at that time. Therefore, the agreement stipulations must accomplish the general conditions referring to the subordinate debt, namely:

- i. The subordination has to be effective, in the sense that: the subordinate creditor's debts have an inferior rank as compared to all the unsubordinate creditors, and in case of liquidation, the subordinate creditors must not be able to receive or retain any amount or assets until all the unsubordinate creditors shall have been paid or entirely indemnified; the creditors give up their right to compensate the amounts they owe to the banking company for the subordinate amounts the bank owes to them in its turn; and,
- ii. The agreement must not contain stipulations that can lead to the anticipate repayment or to the increasement of the initial costs of the debt, as: clause of simultaneous declaration of bonds exigibility following a guilty non-fulfilment of one of them; clause of negative lien, according to which the constitution of guarantees by the bank involved on any of its assets for obligations, titles and other debts constitutes itself as guilt case.

These conditions, referring to the subordinate debt are valid for all the specific elements that can be taken into the calculus of Level 2 proper funds.

In the determination of proper funds, the component elements of Level 2 proper funds are taken into a calculus, in certain statutory limits, as follows:

- total of Level 2 proper funds cannot exceed 100% of Level 1 proper funds;
- total of cumulative preferential shares value for a determined period and of capital shaped as subordinate loan that can be taken into account in the calculus of proper funds, cannot exceed 50% of value of Level 1 proper funds.

It has to be underlined at the same time the fact that, in order to attain its targets of prudence, to determine the level of total proper funds which are taken into account, the statutory authority can also establish a series of *deductions* from the elements of proper funds mentioned above. This type of elements are designedly stipulated and regulated by the surveillance authority.

4. Minimal fund request

The assurance by the banking societies of a proper funds level, which to respond to the statutory requests, represents an extremely important preoccupation of their management. The assurance of accomplishment of minimum requests of proper funds level is compulsory, and their

level is determined by the volume of activity and risks which the developed activity is exposed to. In accordance with the present² regulations, the banks have to dispose on a proper funds level situated permanently at a level at least equal to the sum of the following *capital requests*:

- for the credit risk and the decreasing risk of debt value afferent to the whole activity except for the operations out of transactional portfolio, 8% of the total of values level-headed at risk of calculated exposures, determined in accordance with the special regulations issued by the surveillance authority in this sense;
- for the position risk, the discount risk and credit risk of the counter match afferent to the operations out of transactions portfolio, the capital requests also determined in accordance with punctual regulatings issued by the surveillance and regulating authority;
- for the currency risk, wares risk and operational risk afferent to the entire activity the capital requests are determined separately in accordance with special regulations.

A special attention is imposed to be given by the banking groups which, in order to determine *the proper funds at a funded level*, namely afferent both to proper activity and its branches which, in accordance with special regulations, find themselves in their consolidation area, must take into account the funded values of the elements that enter into the calculus of the proper funds at an individual level.

5. Conclusion

The assurance by the Romanian banking of the minimum level of own funds required is a regulatory requirement of banks each bank. For the management of each banking company has the responsibility of adoption of appropriate measures to enable the calculation of a minimum requirement of own funds in accordance with the authority and National Bank of Romania, on the other hand, sizing of the so manner so as to generate profitability and employment in the minimum regulatory capital. This requires the implementation of mechanisms and systems that allow first regulatory compliance requirements, on the other hand, adequate monitoring and steering of business so as to generate expected financial flows, and where necessary ,to provide external sources of funds for allocation to the minimum regulatory requirements.

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3. * * * The Regulation no.13/18/14.12.2006 regarding the determination of minimum requests of capital for the credit institution and investments companies, issued by the National Bank of Romania and the National Committee of Movable Values

² The Regulation no.13/18/14.12.2006 regarding the determination of minimum requests of capital for the credit institution and investments companies, issued by the National Bank of Romania and the National Committee of Movable Values.