Proceedings of the Faculty of Economics in East Sarajevo
Year 2020, Issue 21, pp. 21-35
Received: 5th November 2020

UDC 336.763.2/.3:[336.71:005.334
DOI: 10.7251/ZREFIS2021069D
Review Paper

Damjan Danilović

Faculty of Economics Pale,
University of East Sarajevo,
Bosnia and Herzegovina

✉ damjan.daničovic@ekofis.ues.rs.ba

Strahinja Miljković

Faculty of Law (temporary in Kosovska Mitrovica),
University of Priština,
Serbia

✉ strahinja.miljkovic@pr.ac.rs

FEATURES OF THE REGULATORY REGIME OF BANKS AND CORPORATE GOVERNANCE

ОСОБЕНОСТИ РЕГУЛАТОРНОГ РЕЖИМА БАНАКА И СИСТЕМА КОРПОРАТИВНОГ УПРАВЉАЊА

Summary: *Social relations, economic development and capital concentration have conditioned the development of legal science in the field of companies. Few legal areas have been so susceptible to legal evolution, especially in the last few decades, where the tendency for permanent changes remains to be seen. Through its development, the company law has expressed its own legal institutes, and the legislature has a number of different legal relationships and facts. In particular, banks with their many personalities are singled out within companies. The credit deposit business conditions specific legal relations, which again affects the creation of a special legal framework. Corporate governance systems are characteristic of the steak-holder approach, which stems from the fact that banks have other people's money, and potential losses are made up of state funds, or budget funds. Banking operations, i.e. the management system thus becomes the public interest. This is especially manifested in the creation of a control framework, in order to preempt the development of systemic risks, which are very emphasized by the banks. These risks may be at both the international and national level, subject to both international and national regulatory control. All this affects a range of personalities in the internal organization of banks, and overall the creation of a special legal framework.*

Keywords: *banks, business, regulators, corporate governance*

JEL classification*:* *G21,G34*

Резиме: *Усложњавање друштвених односа, привредни развој и концентрација капитала су условили развој правне науке у области компанија. Мало која правна област је у толикој мјери била подложна правној еволуцији, што се посебно односи на задњих неколико деценија, при чему је и даље примјетна тенденција перманентих промјена. Компанијско право је кроз свој развој изњдрило својствене правне институте, а легислатива регулишe бројне и различите правне односе и чињенице. Нарочито се у оквиру компанија издвајају банке са својим бројним особеностима. Кредитно депозитно пословање условљава специфичне правне односе, што опет повратно утиче на креацију специјалног правног оквира. Системи корпоративног управљања банкама су карактеристични по стејкхолдерском приступу, који проистиче из чињенице да банке располажу са туђим новцем, а евентуални губици се надомјештају из државних фондова, или буџетских средства. Банкарско пословање, тј. систем управљања тиме постаје јавни интерес. То се посебно манифестује на креирање оквира контроле, ради предупређења наступања системских ризика, који су код банака веома наглашени. Ти ризици могу бити и на интернационалном и на националном нивоу, сходно чему подлијежу како интернационалној тако и националној регулаторној контроли. Све то утиче на низ особености у интерној организацији банака, а све укупно на креирање специјалног правног оквира.*

Кључне ријечи: *банке, пословање, регулатори, корпоративно управљање*

JEL класификација: *G21,G34*

1. THE NOTION, SIGNIFICANCE AND FEATURES OF THE FINANCIAL SECTOR

Since banks are typical representatives of financial sector companies, it is necessary to look briefly at the importance of the financial sector, which results from the characteristics of its function. The financial sector includes those companies that deal with market placement and fundraising. It includes banks, insurance and resurging companies, investment funds, microcredit organizations and leasing companies. Viewed from a global level, the importance of good banking legislative arises from several facts. On the one hand, almost all cash flows, including international business transactions, are conducted through banks, where legal order and security are necessary. On the other

hand, there is a risk of a negative systemic effect both nationally and internationally, which is why the formation of global and national regulatory bodies that serve the control of financial sector companies is visible.

Banks in this sense fall into high-risk categories of entities, because negative economic developments or high-risk operations can very easily lead to insolvency of the bank and a whole range of creditors. The third fact is a high degree of correlation between the state of the banking sector and economic development. Financial sector companies have a big impact on national economic systems. A good financial sector creates the necessary preconditions for a good or better real sector, which is in the function of social and economic well-being. Therefore, an efficient financial market, which implies effective financial institutions, is the key to the economic development of each state (Mishkin 2006). The financial sector is the most important source of economic financing in a number of countries. The impact of the financial sector on real terms is realized through the connection of supply and demand in the market, in a way that the entity that has excess funds through financial institutions markets funds to an economic entity that needs to perform business activities, but also a very important role of the financial sector in the very editing and standardization of financing in financial markets (Šoškić and Zivkovic 2006)

Credit-deposit business due to the positive and negative effects it may cause condition the creation direction of the banks' legal framework. As much as 90% of the money the bank has is other people's money, which the bank receives from its clients in the form of long-term deposits, and the same money is placed in loans by the banks, resulting in the bank's production function becoming liquidity security, since the bank could not suddenly respond to clients' requests for deposit returns (Macey and O'Hara 2003). The main characteristic of banking operations is the existence of disparities in the bank's asset structure and its liabilities (Hassanein and Wahsh 2012). Each depositor has the right to request a refund at any time, and laws prohibit the conduct of banks that restrict deposit returns. Banks could not make a refund to a significant number of clients because the money was placed in long-term loans. Therefore, regulatory control and deposit insurance are necessary in order to maintain the necessary level of trust of depositors and reduce moral hazard under these conditions. The position of the banks is specific. They are also the biggest debtors and the biggest creditors, because they collect money in the form of deposits from a large number of persons (diffusion on the trusted side), on the other hand they have a wider economic role because the biggest creditors are the economies of the most developed countries such as Germany and Japan (Laeven 2013).

The money raised is used to lend to the economy, so any mismanagement of the banking sector leads to less financial success, or even losses, which is very negatively reflected in economic growth due to direct increases in capital prices. Unlike the U.S. and Western Europe, where the highest percentages of capital needed for companies are provided on stock exchanges, southeast Europe's banking system is specific because of stock market illiquidity, so banks are the main economic financiers. Consequently, the role of the regulator must be even more prominent. The high leverage ratio of borrowing relative to its own capital makes banks more volatile than other forms of industrial companies, justifying increased social care for the good functioning of banks (Tung 2012).

In bank management, a very personal phenomenon emerges. Moral hazard represents the lender's unwanted (immoral) behavior from the lender's point of view, which reduces the ethos of debt repayment (Mishkin 2006). In the case of financial institutions it is manifested by the investment of money by management in riskier businesses, or securities, in order to make greater profits, but according to higher profits, as a rule, the risk of failure of the business venture increases, directly endangering their investors and depositors, and by systemic effect more other persons. Management is aware that states must save important banks, and in some cases they have no fear of taking high risks.

The current situation is such that the banking system has no alternative, but the potential negative effects must be pre-taxed by regulatory control and good legitimacy. If the collapse of the entire banking system were to be faked, it is clear that it would stop the financing of economies and the circulation of money. Therefore, there is a need for regulated functioning of the banking system, but the necessity of its functional sustainability hides the danger of the various negative effects that the system can cause. The work will briefly present the specifics of the banking framework manifested through the national and supranational regulatory system, and then certain specifics in the internal organization of banks.

2. SUPRANATIONAL BANKING REGULATORS

The economic development of numerous countries in the second half of the 20th century led to an expansion of international business. There has been integration of the world financial system, in which there is a high degree of mutual influence (both good and bad) subjects within the system. The 2007 world financial crisis unequivocally confirmed this. The mortgage crisis in the U.S. was caused by a drop in property prices that was significantly given as a security for mortgage lenders. A lack of credit worthiness combined with poor loan security led to huge financial losses and the loss was still being made worldwide. It has been noted that risky behavior by bank management is becoming a global problem, as limited liability on the one hand and a tendency to make as much profit as possible "pushes" bank management into increasingly risky business ventures (Kern 2004). Particularly problematic is the fact that systemic banks must be saved from public finance funds, regardless of possible misconduct by management. The moral hazard at the international level "works for" the fact that the G-20 countries' authorities have publicly committed to systematically rescuing financial institutions in the event of a financial crisis, although the complete absence of resilience of interbank markets has been confirmed (Rochet 2010).

These facts and a number of others have accelerated the formation of certain bodies that are trying to establish a separate regulatory system globally, which in addition to control should have special normative activity. Establishing this system is a process of continuous development.

There are different bodies participating in the international regulatory process. In common, they do not have the recognized status of regulators as such on the basis of international acts, but the fact that there is a strong international regulatory process. At the top of the hierarchical ladder is the G20 Forum, made up of presidents of the most developed countries in the world. The forum essentially creates political processes at global levels, which employ the policies of member states, as well as their legal frameworks. The main direction that is taken in terms of banks is the irreplaceable role of banks in the world economy with increased global control to pre-order moral hazards and problems "too big to fail". The forum affects the co-ordination of transnational regulatory networks. Transnational regulatory networks are special forums made up of central bank governors, international regulators and leading industrialists, who, based on collective decision-making and consensus, adopt soft-rights acts (Lee 2014).

In that essence, the legal standards and procedures of supranational banking regulators have the character of soft law, which means they are not binding. The most important acts on promoting bank capital adequacy and risk reduction were adopted by the Financial Stability Board. The board was initially constituted as a Forum, but after the 2008 global financial crisis, the board was able to provide a new one. In 2013 became a body that conducts general monitoring of systemic risks. The board has tasks of maintaining financial stability, transparency and openness of the financial system, compliance with international financial standards, which it achieves through a range of functionalities: noticing the deficiencies of the financial system and supervision of actions needed to overcome deficiencies, promote coordination and exchange of information between the bodies responsible for financial stability, to monitor market development and the implications of development on regulatory policy, and to cooperate with the IMF to implement early warning measures (Ferran and Kern 2011). The board influenced the harmonization of standards through several phases. The implementation of Basel 3 standards is currently recommended. Although the legal nature of these acts is non-binding, in practice they have not been left to the free will. The factual strength of the organizations that adopt them and those who promote them make up for their casualty. Strong support for accepting them into national legal systems is given by the World Bank (SB) and the International Monetary Fund (IMF), who openly call for their use. Indirectly, the SB and the IMF influenced their acceptance in a way that they evaluate the relationship between states and regulators, and publish special reports on compliance with recommended principles and codes by states (Brummer 2011). The immediate method may condition the acceptance of different standards as a condition of credit arrangements.

Unlike the previously stated international regulatory bodies, the EU system has a special regulatory organization of the banking system. It currently rests on two systems, which are a Snique Monitoring System and a Single Resolution System. The European Central Bank (ECB) is at the top of the hierarchical ladder of the Single Monitoring System. In the early stages, this system included members of the European Monetary Union, but legislating extended the authority to other EU members, if it was systemically important banks. The ECB has established exclusive jurisdiction over banks, which it conducts in co-operation with competent national bodies, by national regulators

implementing ECB-controlled banking supervision policies to maintain the stability of the financial system, the single market and the equal position of banks. The ECB has the authority to control the compliance of banks operations with the banking legislation, but does not have the authority to enforce regulations concerning systemic risks that exceed the level of a particular bank, i.e. it does not have jurisdiction over systemic risk control at the macro level (Petit 2019). Therefore, control is exercised over each individual bank within the range of capital adequacy, liquidity and exposure to risks. In addition to performing individual controls, managing a single monitoring system implies the establishment of a system of rules, procedures and practices.

In addition to the ECB, there are other bodies at the Union level such as the Systemic Risk Committee and the European Banking Agency (EBA). Unlike the ECB, these other two important bodies do not have the status of a regulator whose decisions, attitudes and recommendations must be respected. The task of the Systemic Risk Board is to evaluate systemic risks at the macro level, exchange information about risks with supervisory bodies, co-ordinate international bodies in charge of oversight, and make corrective recommendations (Ferran and Kern 2011). The EBA is a body that, through various activities generally speaking, contributes to the development of control of the banking system, but more in the form of consultants, intermediaries and bodies that study and recommends the improvement of bank control, without prerogative to instruct banks to take concrete measures, or to sanction (European Court of Auditors 2014). Initially, the role of bank supervision was performed by the EBA, until 2014, when it became the responsibility of the ECB.

The stability of the banking and commercial system in general can be significantly damaged by the insolvency of major banks. To prevent adverse effects at the EU level, a Single Resolution Mechanism has been established. Analogous to the Single Monitoring System, it implies special bankruptcy procedure rules for banks of European Monetary Union member states, but also for banks outside the monetary union if they are of public interest. Bankruptcy of banks in international frameworks should reflect the principle of universality, for their macroeconomic position, where the goal of bankruptcy is not only to distribute assets among trustees, but to preserve the financial stability of the system and prevent negative effects on other entities in the financial system (Lehmann 2017). In order for the bank's bankruptcy fate to be uniquely resolved in all member states, and to put all creditors in an equal position, as well as to prevent the collapse of systemically important banks, a single bankruptcy procedure is envisioned. The single mechanism of the EU resolution reflects the universal concept of bankruptcy. If there is a public interest then the jurisdiction of the Resolution Committee (EU) (No 806/2014, 5) is activated. This implies that under the control of the Board, the reorganization of the bank will be carried out by competent bodies in all member states in a unique manner, in accordance with the right of the parent state (the place of registration of the bank).

If the reorganization requires the use of additional funds, it is provided in the Joint Resolution Fund (European Commmision 2014, 70-79). It is evident that the specified mechanism provides a systemic approach in case bankruptcy causes market volatility. The lack of public interest (the systemic importance of the bank) omits the board's jurisdiction, so that bankruptcy is conducted in accordance with national regulations. The principle of equality of creditors (investors) is especially important in bankruptcy law with a foreign element in the European Union. Bankruptcy of banks and insurance companies with branches in different Member States applies the rules of the country where the work permit was obtained, while in other companies there is a main procedure and ancillary proceedings, in which local procedures are applied, and thus different treatment of creditors in the collection of claims (European Commmision 2001, 3).

3. NATIONAL REGULATORY SYSTEM

The business of each entity that may endanger a large number of other entities with its business should be specially controlled, because it enters the sphere of public interest. Complex financial institutions have a large number of transactions with a large number of persons, so national regulators have a key role to play in controlling their risk (Seniors Supervisors Group 2014). If the regulatory system is viewed globally, then national regulators are at the bottom of the hierarchical ladder. Thus, a regulatory system has been created in the EU in which the ECB is the supreme body, and the national Central Banks represent its "operational hands", with absolute supremacy of the ECB's competences, so that provisions of national laws are invalid if contrary to ECB prerogatives (Siekman 2005). It is impossible for international regulators to control all national banks, but this only

applies to the most important ones. They remained under the control of national regulators, which in addition operationally enforced international standards aimed at combating negative systemic effects. The entire activity of the regulator can be divided into control and normative. This prevents possible shareholder inactivity, failures in the work of internal bodies and poor internal organization, which can have negative consequences for the work of the bank. Control activity is manifested through giving consent to banks in various segments in which the legislation requires it, then through regular controls of legality in the work of banks and taking various measures to eliminate irregularities. Historical and comparative views point to the fact that the competences of regulators are constantly expanding.

The position of the regulator will unequivocally lead to the conclusion that the system of corporate governance of banks is and should be stakeholder. In this way, regulators maintain a certain degree of depositor's confidence that the business of financial intermediaries is conducted in accordance with the law, which is a guarantee that the deposited money is safer. Business goals are not only profitable, but also satisfying the interests of other stakeholders (Ljubojević and Ljubojević 2010). The position of banks as basic economic financiers raises their social and legal responsibility to a higher level compared to other companies. The reason is that bank losses directly affect all other interested parties financially. This can very easily cause distrust of depositors, which calls into question the functioning of the entire financial system. Regulators make up for lack of transparency and provide a degree of trust for depositors. By the fact that the corporate governance system is stakeholder, it directly determines the margins of legal responsibility of members of banking bodies, i.e. the actions of persons with duties, which should be not only in the interest of the company, but also other stakeholders, primarily depositors. Corporate governance standards for the financial sector are at a higher level than the real sector, and their focus is on protecting stakeholders outside shareholders (Davis 2011). In Bosnia and Herzegovina, the Entity Banking Agencies have a regulatory role, in other countries they are Central Banks (Službeni glasnik R.Srbije, 2015, 15) and other bodies in complex systems such as the United States.

It is characteristic for all subjects (institutions) of the financial sector to be established according to the license system. The state allows only those persons who meet all legal requirements, who are more numerous and stricter with banks (Službeni glasnik R Srpske 2017d, 1-3), to engage in banking activity. The establishment procedure is much more complex and time-consuming compared to other companies thus it is carried out under the supervision of regulators who approve its phases. The legislation defines the conditions for acquiring the status of the founder of the bank or the acquirer of qualified participation, so that in the initial phase, the Agencies give their consent for the fulfillment of the stated conditions. Therefore, the ownership structure is selected as the most important stakeholders in companies. The appointment of members of key office holders is subject to mandatory regulatory consent that controls the fulfillment of the conditions of that domain. All important internal acts such as the founding agreement, statute, internal organization regulations, organization of risk management system, risk assessment policy, appointment policy, etc., must also be approved by the Agency. Fulfillment of conditions related to the capital of the bank is imperative and their non-fulfillment prevents the establishment of a bank. In each of the above segments, in case of subsequent changes, the obligatory consent of the Agency is required. Thus e.g. the decision on the holders of key functions becomes final only with the approval of the Agency, until then it is in the form of a proposal. Status changes also fall within the scope of decisions for which consent must be obtained.

At least once a year, but if needed more often the Agency controls the bank, analyzing all important business segments and various internal organizational systems of the bank in order to preserve confidence in the banking system and ensure stability, security and protection of depositors (Službeni glasnik R Srpske 2017g, 1-8). Depending on the compliance of the bank's operations with the legislation, risk, systemic significance, etc., the agency estimates the frequency of controls. Observed shortcomings, depending on the severity of violations of regulations, entail ordering banks to take various measures. Due to a violation of the law, one or more persons may be deprived of consent to be appointed to the board, banned from performing all functions in the bank, suspended voting rights in the bank or request termination of shareholder status (Službeni glasnik R. Srpske 2017c, 204; Službeni glasnik R.Srbije 2015, 114). Therefore, according to the right to appoint holders of key functions, the Agency has the right to dismiss them. It is a novelty of our legislation, which has its roots in Anglo-American law. Reasons for dismissal may be the termination of the legal conditions for appointment, acting contrary to legal provisions, preventing the regulator from controlling the solvency and legality of the bank's operations (Službeni glasnik R Srpske 2017c, 62-74). In the case of minor violations of regulations, a warning is issued, but the continuation of actions contrary to the

prohibition withdraws the dismissal from office in the bank. Significant violations of regulations can cause the introduction of compulsory administration. The compulsory administrator is appointed by the Agency, all powers of the bank's management are transferred to him and he supervises, secures and manages the bank under the control of the Agency (Službeni glasnik R Srpske 2017g, 1-16; Službeni glasnik R. Srbije 2015, 115).

The rules of bankruptcy procedure are also special. Bankruptcy is carried out by special bodies, usually financial sector regulators, and not by the competent courts. In addition to control, the Agency is also responsible for bank restructuring and termination procedures (Službeni glasnik R Srpske 2017c, 1). An important goal of bankruptcy in general is to achieve a successful reorganization. Liquidation is a consequence of the inability of financial measures to succeed with adequate measures. With banks, this is not left to chance. The Agency is exclusively competent to make decisions on this, appreciating the public interest. So if it is a systemically important bank, then a decision on reorganization is made. The agency conducts and controls the entire bankruptcy procedure. Characteristic of bank bankruptcy is the restriction of creditor autonomy when deciding on the course of bankruptcy, while in the case of non-financial entities the most important decisions are within the competence of bankruptcy creditors.

The peculiarity of banks is the existence of special state funds on the basis of which the state insures deposits. In order to achieve the trust of depositors, it is necessary that these be public law bodies, and that all banks enter the deposit insurance system. In the constellation of relations where on the one hand there is a need to establish a good management system of the banking sector, creating a framework in which there must be depositors' confidence in the banking system, and on the other hand the impossibility of returning deposited amounts to depositors in the short term. States establish special deposit insurance funds as a guarantee to depositors, i.e. special public law agencies that manage deposit insurance funds (Službeni glasnik BiH 2013, 1-34). Quite simply, banking cannot be imagined without the trust of depositors. Deposit insurance funds are generally accepted solutions in comparative rights as well. It is the obligation of all banks to be members of the deposit insurance fund. Membership for banks creates an obligation to allocate certain monetary percentages to the Fund for all received deposits. The funds raised represent a guarantee to depositors that they will be paid certain amounts of money if the bank receiving the deposit would not be able to refund the deposited funds. The outbreak of the last financial crisis threatened the withdrawal of deposits and the financial collapse of banks within national economies, so that a number of countries increased the amounts of insured deposits. These measures have certainly had a significant impact on maintaining confidence in the banking sector. True, this method of securing confidence in the banking sector is not absolute, as it is a limited secured fund, since no country guarantees full deposit insurance. No country is ready to fully assume all the risks of deposit insurance. Even if states were willing to fully insure deposits, we believe this would not be a good legal solution. On the contrary, it would be bad for the corporate governance system, as it could be interpreted as a signal of permission to freely take risks at any cost.

Unlike international regulatory bodies, which have seized normative competence for themselves (adoption of legal acts), national regulators have legally established normative competence. Such legal solutions are thought to have been most influenced by the need for international regulators to rapidly transpose the standards they adopt or the reforms they implement into national legal systems. This can be a good thing, but also a disadvantage from the point of view of state sovereignty. Another disadvantage is the merging of functions. Namely, the same person (regulator) adopts binding acts and controls their application. International standards in this case require organizational separation. In any case, every regulatory important aspect of banks' control and operation is accompanied by regulatory regulations, starting with the system of external and internal controls, criteria for key function holders, risk systems, restructuring measures, remuneration systems, reporting and other important aspects of banking operations. Legislation has gone in the direction of "over-regulation", so there are scientific understandings that legal regulations are a substitute for the system of corporate governance of banks. This development of legislation is necessary, because many segments can negatively affect the orderly business. Based on the experiences of the last five decades, it can be concluded that in addition to good legislation, the organization of regulators is as well a key factor for a good and orderly banking system.

4. INTERNAL SPECIFICS OF BANKS

Banks are in regards of their organization typical companies, i.e. the most complex forms of economic Society. The basic form of society by the logic of things must be a form with limited liability, because it is the only way to facilitate the aggregation of capital and concentration of management power, as a condition of the necessity of corporate governance (Chrakham 2003). Historically, and especially in the last financial crisis, banks can cause abnormally high financial losses, which can be further compensated exclusively from state budgets. Only the form of limited liability can, in addition to the previously mentioned advantages, represent a safe haven for members of the company (shareholders) and for members of management boards from liability for potentially high amounts of financial losses. Credit deposit operations require the possession of high amounts of financial assets, so that the legal minimum amounts of share capital are raised to higher levels compared to other types of companies.

Based on the previously presented part of the article, the significant presence of the regulator is noticeable. The freedom of decision-making of the company's management and shareholders must be within a defined framework. Monitoring bodies prescribe certain lending standards, where the freedom of decision-making of management is partially limited due to the narrowed circle of negotiations (Kern 2004). This is not the case only with the rules of crediting, but also with other segments of business and internal organization that the Agency regulates through normative activity. The conduct of the bank's business requires each body to move within the set limits, and otherwise it would face legal liability.

General regulations regulate the corporate governance system exclusively according to the unicameral model. In contrast, the system of corporate governance of domestic banks is "bicameral", which implies the constitution of the supervisory board as a special supervisory body. In "unicameral" systems, a number of board members are members of the executive board. The advantage of a unicameral system is the achievement of a combination of specialized knowledge and skills of executive directors and general knowledge and breadth of experience of non-executive directors, in which non-executive members perform supervisory functions over executive directors, while executive members enable informed boards and closeness to real problems. 2008). On the other hand, unicameral systems lead to a concentration of management power and potentially more difficult management control, especially if the functions of the chairman of the board and the general manager are merged at the same time. Due to the importance of a good system of internal and external control for the corporate governance system in the banking sector, it is considered that the bicameral system is a more adequate solution, because at the same time membership of a certain number of members in the control and management structure is a potential danger. Information asymmetry does not have to be reduced in a unicameral system, because the executive board can withhold information from the boards of directors as well as the shareholder structure. On the other hand, good practices can compensate for the "inability" of supervisory boards to monitor real business opportunities.

Supervisory boards elect both the management structure and the membership of other control bodies. Therefore, all these bodies, i.e. their membership, are accountable to the supervisory board for their work, and the supervisory board to the shareholders. The supervisory function over the work of the management and operations of the bank is the basic function of supervisory boards, where the supervisory board is the key body for establishing risk management system, implementing strategic and short-term planning, which has the duty to establish internal control in accordance with regulatory regulations (Službeni glasnik R Srpske 2017c, 3). In "bicameral" systems, the control function of the supervisory board is clearly indicated, and the strict separation of the control position from the management position reduces the "blurring" of responsibilities.

Solving the first agency problem in companies has spawned various legal institutes. In order for the management to work in the interest of the company, i.e. in order for the work in the interest of the company to be best realized in practice, professional qualifications of the membership of the management are necessary. Legislation for non-financial companies does not emphasize these facts, although persons with duties in the company are required to act in accordance with the care of a good businessman. These are generally accepted standards of care that apply to persons with duties in a company. Banking legislation has gone a step further. Positive assumptions of independence, i.e. the qualification of key function holders in the bank has been regulated in more detail, which has increased the level of attention that key function holders should show in their work. In the domestic

legislation, in the case of banks, the assumptions of independence are standardized at the most demanding level.

Decisions on the assessment of members of banking bodies more precisely set minimum standards in the assessment of qualifications, procedures and the role of the Banking Agency in assessing the fulfillment of mandatory conditions for holders of key bank functions. The assessment in terms of good reputation and sufficient experience is performed before the election of members, during the term and in other cases deemed relevant by the bank, where the assessment results must be adequately documented (Službeni glasnik R Srpske 2014, Službene novine FBiH 2013a, 3-6). It is the obligation of banks to have constituted appointment committees that have a number of duties related to the evaluation and implementation of appointment policies, evaluation and proposal of membership, evaluation of competencies of existing membership, etc. (Službeni glasnik R Srpske 2017c, 81). No person may be appointed independently to a key position in the bank until the Agency gives its consent and issues a decision on appointment. By synthetic interpretation of the provisions of the Decision on conscientious conduct of members of banking bodies, conscientious conduct implies cumulative application of professional and ethical standards of conduct harmonized with legal powers and business goals, business strategy and policy of the bank, in order to achieve balance of interests of interested parties (Službeni glasnik R Srpske 2013a, 4-5). The performance of duties and responsibilities of members of the bank's bodies must be clearly defined by the bank's statute, internal regulations on the work of the management and supervisory board, where membership is mandatory for mutual cooperation in achieving the best interests of the bank, ensuring critical, objective and comprehensive discussion and adequate and timely information (Službeni glasnik R Srpske 2013a, 6). It is evident that positive regulations regulate a whole range of facts and circumstances, which are applied cumulatively when assessing the responsibility of membership, and to strive to establish responsibility in accordance with the attention of "experts", which is a higher rank of responsibility than it is in non-financial companies.

Considering the organization of internal control bodies, it can be seen that banks, regardless of size, must have different control bodies constituted, while for systemically important banks they must have additional bodies. For example, the Law on Companies for Open Joint Stock Companies provides for the constitution of an audit committee and / or an internal auditor. Banks must have both bodies. The Audit Committee performs control of financial statements, legality of work of banking bodies, etc., but the legislation also emphasizes the function of analysis and reporting on the implementation of risk management strategies and policies (Službeni glasnik R Srpske 2017c, 78; Službene novine FBIH 2003, 32). The internal auditor is responsible for identifying, monitoring and assessing risks, as well as verifying that the bank has an internal control system in place, which ensures that risks are managed in a way that mitigates those risks to an acceptable level, and cooperates with the audit committee in the field of determining the completeness and credibility of financial information (Službeni glasnik R Srpske 2017c, 323; Službene novine FBIH 2003, 32). Interpretation of legal norms shows that the Audit Committee and the internal auditor do not have the exclusive function of controlling legal and financial acts and legal procedures, but also establishing adequate policy and the overall risk management system.

Considering the internal risk management systems of companies, one can state the most diverse variety of forms. It all depends on the size of the company, the scope of business, the overall organization of the company, regulatory requirements and the like. The outbreak of the last financial crisis highlighted one direction of establishing a systemic and permanent function in risk control. Company regulations for non-financial companies do not require the establishment of special bodies that would deal exclusively and in a systematic way with risk control. Banking regulations, on the contrary, require the establishment of a special risk management body, elected by the supervisory boards of banks (Službeni glasnik R Srpske 2017c, 89).

Research on the impact of the remuneration system of board members within banks on the provocation of the global financial crisis has conflicting indicators. One side takes the view that a poor compensation system is one of the most important factors influencing the provocation of the crisis. On the other hand, there are perceptions, which are considered more correct, that the remuneration system is only one of the bad segments of the previous management, in addition to which the bad work of rating agencies and the bad role of internal auditors proved (Weight 2011). The essence of the issue is that the compensation system that can expose banks to excessive risks is bad. Simply put, if the fees do not reflect the real results achieved, and then it is a bad compensation system, because high fees for "bad" results only further financially burden the banks. Also, investing in riskier business activities or

securities can bring currently high profits, but there is an immanent high level of risk, so the compensation system should be adjusted in such a way that it does not stimulate management to riskier business ventures, but long-term stability. Within the compensation system, the legislation regulated a number of issues such as fee structures, limitation of variable fees, obligation to retain certain amounts of fees whose effects are realized in a relatively longer period of time, payment of a certain part of fees in financial instruments, severance pay restrictions, etc. Banks must have a fee committee established, which is a very important body from the point of view of implementing an adequate remuneration system in accordance with legislation and internal regulations (Službeni glasnik R Srpske 2013a, 12; Službene novine FBiH 2013a, 12). Internal regulations in the fee system for each bank must be approved by the Banking Agency, which controls compliance with the rules of the specified domain.

There are a number of different regulations and rules that strive to achieve capital adequacy of banks, i.e. ensuring the liquidity of banks. It would be inexpedient to cite all bylaws in the argumentation of this statement, especially since some of them go beyond the legal aspects, because they prescribe quantitative ways of measuring capital, reserves, risks, etc. Capital standards are in every sense stricter than non-financial companies. First, the minimum basic capital is set very high. The rules on large exposures and participation in the capital of other financial and non-financial companies have been set very restrictively. First, the conditions for acquiring the position of a bank founder and a qualified shareholder have been tightened. The legislation has gone so far as to allow the Agencies to assess the ability of the founders to manage the bank as a condition for acquiring the status of a bank shareholder. Given the too strict criteria, it can be inferred that they will be interpreted very flexibly.

The regulators approves the purchase of shares worth over 5% of the bank's share capital as well as the acquisition of the position of the bank's founder, regardless of the estimated share capital (Službeni glasnik R.Srbije 2018, 3–5). The total amount of the bank's membership shares may not exceed 50% of the bank's share capital in the case of financial organizations, and the total amount of shares in non-financial organizations may not exceed 25% of the share capital (Službeni glasnik R Srpske. 2017c, 111; Službene novine FBIH 2003, 22: Službeni glasnik R.Srbije 2015, 34). A high exposure of a bank exists if the bank grants a loan of 10% or more to one person in relation to its own capital. The large exposure of the bank requires the consent of the supervisory board, and the maximum exposure to one person or group of related parties must not exceed 25% of the capital (Službeni glasnik R Srpske 2017c, 106-108). These restrictions make it more difficult to limit the risks to which the bank may be exposed. Determining the existence of high risk indicators in accordance with bylaws also leads to various restrictions on the freedom of decision-making of the management and the implementation of appropriate standards, but all this is necessary in order to keep the risks under control.

5. CONSLUSION

Credit-deposit business, as the core of banking activity, raises banking business to the level of public interest. Considering the global picture, the role of banks ranges from significant to the most important economic financiers, which in itself speaks in favor of the previous statement, because the state of economic systems largely depends on the state of the banking system. The internationalization of business has conditioned a high level of mutual influence, so that the failure of systemically important banks can cause systemic negative effects at the international level.

Banks generally have more foreign or deposited money at their disposal, compared to their own. At the same time, there is a maturity disparity between deposited and placed money, so that banks would not be able to respond to significant requests for deposit returns. In such circumstances, regulatory control and the deposit insurance system play a key role in maintaining depositors' confidence in the banking system. The legal framework envisages a number of special solutions so that banking operations can take place. The international regulatory system is constantly evolving, often being supremacist in relation to national legal systems that are aligned with adopted international standards. The highest degree of integration of the international regulatory process has been achieved at the EU level, where a Unique Supervisory Mechanism and a Single Resolution Mechanism have been established. With the new reform of banking legislation, national regulators gain an extension of their powers. Their competence is control and normative.

The need to control banking operations has predominantly influenced the corporate governance system. The organization of the bank is complex, so there are different control bodies that are all together under the control of the supervisory board. The accountability system of key function holders in the bank has been set at a higher level, all in order to prevent risks. The by-laws of the regulator determine in more detail the various elements of the internal control system, as well as the principles and rules according to which banks, i.e. banking bodies should act.

REFERENCES

Alexander, Kern. 2016. "The European Central Bank and Banking Supervision: The Regulatory Limits of the Single Supervisory Mechanism." *European Company and Financial Law Review* 24 (13). doi:10.1515/ecfr-2016-5001.

Brummer, Chris. 2011. ''How International Financial Law Works (and How it Doesn't)''.*Georgetown Law Journal* 99(2): 257-328.

Chrakham, Jonatan. 2003. *Guidans for the Directors of Banks.* Washington: The World Bank

Davis, Kevin. 2011. *Regulatory Reform Post the Global Financial Crisis:An Overview.* Melbourne: ACFS.

European Commision 2014. Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010. Bruxeles.

European Commision. 1995. Convention of Insolvency Procedings Eu of the Council. Bruxeles.

European Commision. 2001. *Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings.* Bruxeles

European Court of Auditors. 2014. European banking supervision taking shape-EBA and its changing context. Luxemburg.

Ferran, Eilis, and Kern K. Alexander. 2010. "Can Soft Law Bodies Be Effective? Soft Systemic Risk Oversight Bodies and the Special Case of the European Systemic Risk Board." *SSRN Electronic Journal.* doi:10.2139/ssrn.1676140.

Hassanein, Medhat & Wahsh, Rehab. 2012. ''CEO duality and bank performance: The consistent null.'' *Banks and Bank Systems* 7: 14-23.

Kern, Alexander. 2004. ''UK Corporate Governance and Banking Regulation: The Regulators Role as Stakeholder'' *Stetson Law Review* 33: 991-1034.

Lehmann, Matthias. 2016. "Bail-In And Private International Law: How To Make Bank Resolution Measures Effective Across Borders." *International and Comparative Law Quarterly* 66 (1): 107–42. doi:10.1017/s0020589316000555.

Ljubojević, Čedomir and Gordana Ljubojević. 2010. ''Konkurentska prednost i socijalna odgovornost kompanija.'' Škola Biznisa 1: 63-72

Macey, Jonathan and O'Hara, Maureen. 2003. ''The Corporate Governance of Banks.'' *Economic Policy Review* 9: 91-107.

Mishkin S. Frederi. 2006. Monetarna ekonomija, bankarstvo i finansijska tržišta.. Beograd: Data status.

Petit, Christy Ann. 2019. "The SSM and the ECB Decision-Making Governance." *The European Banking Union and the Role of Law*, 108–29. doi:10.4337/9781788972024.00013.

Radović Vuk. 2008. "The road to an independent board of directors." *Legal life* 12.

Rochet, Jean Charles. 2010. ''Systemic Risk: Changing the Regulatory Perspective'' *International Journal of Central Banking* 6: 259-276.

Seniors Supervisors Group. 2014. *Progres Report on Counterparty Data.* Basel,

Siekman Helmut. 2005. ''Die Unabhangigkeit von EZB und Bundesbank nach geltendem recht und dem Vertrag uber eine Verfassung fur Europa.'' *Goethe Universitat-Institut for Law and Finance Working Paper* 35.

Službene novine FBIH. 2003. Zakon o bankama Federacije BiH. Brojevi 39/98, 32/00, 48/01, 27/02, 41/02, 58/02, 13/03, 19/03, 28/03. Sarajevo

Službene novine FBiH. 2013a. Odluka o politici i praksi naknade zaposlenima u banci. Broj 60/13.Sarajevo

Službene novine FBiH. 2013b. Odluka o procjeni članova organa banke FBiH. Broj.60/13. Sarajevo

Službeni glasnik BiH. 2013. Zakon o osiguranju depozita u bankama Bosne i Hercegovine. Brojevi 20/02, 18/05, 100/08, 75/09, 58/13. Sarajevo

Službeni glasnik R Srpske. 2003. Odluka o minimalnim standardima sistema interne kontrole u bankama Broj 12/03. Banja Luka

Službeni glasnik R Srpske. 2013a. Odluka o politici i praksi naknade zaposlenima u banci. Broj 80/13

Službeni glasnik R Srpske. 2013b. Odluka o savjesnom postupanju članova organa banke. Broj, 80/13. Banja Luka

Službeni glasnik R Srpske. 2014. Odluka o procjeni članova organa banke RS. Brojevi 80/13, 15/14. Banja Luka

Službeni glasnik R Srpske. 2017a. Odluka o načinu provođenja nadzora banaka i preduzimanju mjera nadzora. Broj 116/17. Banja Luka

Službeni glasnik R Srpske. 2017b. Zakon o Agenciji za bankarstvo Republike Srpske. Brojevi 59/13, 4/17. Banja Luka.

Službeni glasnik R Srpske. 2017c. Zakon o bankama Republike Srpske. Broja 4/17. Banja Luka

Službeni glasnik R Srpske. 2017d. Odluka o uslovima i postupku izdavanja dozvola, odobrenja i saglasnosti bankama koje obavljaju djelatnost u Republici Srpskoj. Broj 63/17. Banja Luka.

Službeni glasnik R Srpske. 2017g. Odluka o uslovima uvođenja i obavljanja privremene uprave u banci. Broj 117/17. Banja Luka

Službeni glasnik R.Srbije. 2015. Zakon o bankama Republike Srbije. Brojevi 107/2005, 91/2010, 14/2015. Beograd.

Službeni glasnik R.Srbije. 2018. Odluka o sprovođenju Zakona o bankama koja se odnosi na davanje preliminarnnog odobrenja, dozvole za rad banke i pojedinih saglasnosti i odobrenja Narodne banke Srbije. Brojevi 82/2015, 29/2018. Beograd.

Šoškić Dejan, Živković Boško. Finansijske institucije i tržišta. Beoograd: Ekonomski fakultet.

Tung, Frederic and Wang Xue. 2012. Bank CEOs Inside Debt Compensation, and the Global Financial Crisis, Accessed 13.02.2019. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1570161,

Weight, Cliff. 2011. *Remuneration Corporate Governance and the Banking Crisis*. Hertfordshire:Chase Cambria Company.