

Abstract

This thesis aims to provide eclectic legal and economic insight into the history, current principles and possible future development of bank capital adequacy regulation. We have worked with a variety of legal and economic literature and official Basel Committee publications. Our goal was to explore the economic background behind the Basel standards and find its legal ramifications and the incentives they create.

In the first chapter, we analyze the economic rationale for banking regulation, explain possible methods of bank capital regulation and juxtapose them with other means of regulatory measures in the field of banking. The first chapter also gives overview of the Basel I framework, its implementation process, describes its utilization of new regulatory techniques, as well as its weaknesses.

Second chapter provides overview of Basel II approval process and discusses its transparency and institutional framework. Problematic issues of CRD directive in the Czech Republic are discussed in contrast with norms of due legislation process.

In the next chapter, we describe the mechanics of the Basel II framework. In greater detail, we focus on the issues of securitization, off-balance sheet exposures and methods of “promise-shifting” in the financial system. Examples are used to illustrate the regulatory shortcomings of Basel II regime in light of the recent financial crisis.

In the fifth chapter we explore the workings of proposed Basel III rules and assess its capability to address the weaknesses of Basel II and effectively increase the soundness of the global banking system. We also discuss some more general issues of financial innovation and risk perception, that, as we conclude, are the weak spots of every regulatory framework. Finally, we propose some “broad stroke” fundamental principles of new banking regulatory regime, based on the findings of this thesis (and hindsight).

Keywords

capital adequacy, Basel I, Basel II, Basel III, banking regulation