Banking Supervisory Regulation; Comparative Study of the Bankruptcy of Chinese and Congolese Commercial Banks Due to Non-Compliance with Prudential Rules: Causes, Consequences and Suggestions

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ABSTRACT

Recent developments in banking systems pose challenges for both banks and supervisory authorities. Bank control is carried out in a traditional way in the form of legal condition and management ratio. Most rules limit risk in a simple and direct way. Any credit institution is required to have an internal risk control system in place. The purpose of this system is to verify compliance with procedures within the rules in force, to verify compliance with the limits of risks, to ensure the quality of accounting and financial information. Prudential rules are intended to ensure minimum security while harmonizing competition rules. This is the set of rules gradually introduced by the bale agreement and retraced by the national supervisory authorities. In the context of this article we examined the management of prudential rules by the supervisory and regulatory authorities of the Chinese and Congolese banking sector; we highlighted these prudential rules by doing a comparative study compared to Chinese and Congolese commercial banks that went bankrupt due to non-compliance with prudential rules. We have demonstrated the causes of bankruptcy; the consequences of bankruptcy and we have proposed solutions to make bank risk management more efficient by scrupulously observing international and national legislation in China and Congo.

Keywords: BANKING RISK, BANKRUPTCY, PRUDENTIAL RULES OF BANKING SUPERVISION

Introduction

Banks are the leading players in contemporary economies, and their stability is a prerequisite for financial stability and economic growth.

In recent years, banking sectors have faced numerous crises and failutures. The nature and extent of these crises justify the evolution and reform of prudential rules.1

The main objective of regulating the banking industry is to protect depositors or clients against banking

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bankruptcy risk. In other words, the banking supervisory authorities' primary goal is to improve the banking system and avoid a financial crisis. That is why any supervisory and regulatory authority must enhance financial security by adopting prudential regulations governing banks. He/she must improve the quality of banking practices and develop a cooperative framework for banking control. In this context, banking regulation is an indispensable mechanism for monitoring credit institutions, preventing systemic risk, and avoiding a generalized economic crisis. As such, banks' statute represents a safety basket that guarantees a monetary policy and a prudential control of credit institutions to limit taking excessive risks. Besides, the banking regulation also aims at promoting the modernization of banking sectors to adapt the operating rules of banking actors and keep their operations in constant evolution.\(^2\) This aim has made banks' role in economic and financial stability evolve in recent years. This paper compares the Chinese and Congolese banking supervisory regulations under the bankruptcy of the International Bank of Africa in Congo (BIAC) and the Baoshang Bank in China. These two commercial banks went bankrupt due to their managers' mismanagement and non-compliance with prudential rules, whose primary purpose is to limit the excessive risk. This situation resulted in negative fallouts to both customers and all society. This paper attempts to demonstrate the responsibilities of the relevant authorities of both states and commercial banks and the customers' situation of this bankruptcy.

In China, the banking supervisory and control fall within the State Council's competence, while in Congo, this role falls within the Central Bank of Congo's competence. The responsibilities of both states are: to regulate the banking sector, to standardize the regulation, to prevent and dissipate banking risks, to protect the rights and legitimate interests of depositors and clients, and finally, to encourage the sound development of the banking sector. Managers of commercial banks have the mission of supervising rules' implementation, conducting proper management that averts any crisis, and facilitating an internal audit committee to detect any mismanagement. Regarding depositors, their situation is under control in China since the Central Bank of China has noticed the Baoshang Bank's mismanagement beforehand, thus allowing the state to protect the customers' rights. The situation is chaotic in the Congo because customers do not know how to take back their savings funds. In this perspective, the first part of this paper highlights some essential notions about banking regulation, supervision, and control; The second part makes a brief overview of the bankruptcy of both commercial banks in DR. Congo (Democratic Republic of Congo) and China; The third part explores prudential management rules of these banks. The fourth part analyzes the banking risks, their prevention, and their supervisors; the fifth part concerns the consequences of mismanagement; legal responsibility constitute part six of this paper. Constructive suggestions represent the last parts, highlighting similarities and divergences between Chinese and Congolese banking laws.

\(^2\) Ibid, p.27
I. Essential Notions

A. Governmental Regulation

According to Chinese and Congolese laws, the governmental regulation in banking monitoring and supervision falls under the jurisdiction of the state council's banking regulatory authority and the Central Bank of Congo. Article 1 of the Chinese Banking Regulation of 2006 states that: "this law is formulated to strengthen regulation of the banking industry, to standardize regulation, to prevent and dispel banking risks, to protect the lawful rights and interests of depositors and other clients, and to encourage the sound development of the banking industry." The state council's banking regulatory authority is responsible for regulating all financial institutions established in the Chinese banking sector and their business activities.3

As can be seen, these rules originate from the parliament and are related to banking supervision and security. As such, and in China, for example, the state council's banking regulatory authority must implement regulation of financial institutions. It illustrates that one of the objectives of regulating the banking industry is to guarantee the public's confidentiality in the banking industry.

In Congo, article 176 of the Constitution stipulates that the Central Bank of Congo is the institution of the Congo's banking issuance. It is independent and has management autonomy. As such, its goal is to: 1) conserve public funds; 2) ensure a safeguarding and monetary stability; 3) define and implement the monetary policy; 4) control all banking activities, and 5) provide economic and financial advice to the government. Article 37 of the Banking Law of 2002 also specifies that: “The Central Bank shall regularly proceed to documentary and on-site control of any credit institution to establish whether it has a sound management or it complies with regulatory provisions governing the banking activity and control.” Article 38, paragraph 2 of the same Law adds that: “The Central Bank’s Inspectors verify if:

- The Credit Institution’s operations are conducted in a manner that violates laws and regulations in force;
- The Credit Institution’s management structures, administrative and accounting organization, or its internal control have serious shortcomings;
- The Credit Institution refuses or hinders its control. In this case, inspectors can: 1) notify a warning; 2) issue an injunction for all appropriate corrective measures; 3) take any safeguard measure deemed necessary, in particular, the appointment of a Provisional Central Representative; 4) appoint a Director or Provisional Manager of the Bank; 5) withdraw an approval.”

The above provisions demonstrate the Congolese State’s firm commitment to ensure permanent and effective control of commercial banks by the Central Bank of Congo. This control's legislative objective is to meet international banking requirements, protect commercial banks against bankruptcy, and secure depositors’ funds.

3 Article 2(1) of the Law of the People’s Republic of China on Banking Regulation, 2006
B. Regulatory Association

A regulatory association is a set of rules that guarantee the control of banks by their associations. These are the inter-banking associations that, while respecting their members' legal status, operate specific controls to ensure credibility, transparency and avoid their members' bankruptcy. At the same time, they also safeguard the interest of the customers.

Article 31 of the Law of the People's Republic of China on Banking Regulation provides that the state council's banking regulatory authority shall guide and supervise the activities of self-regulated associations of the banking industry. These associations have to submit their self-regulatory charter of the banking industry to the state council's banking regulatory authority for record filing.\(^4\)

In DR. Congo, the Central Bank of Congo must approve banking associations and control their charter and activities.

C. Public Supervision

As mentioned above, China's banking regulatory authority and the Central Bank of Congo provide public supervision to ensure credibility and security against bankruptcy. A permanent control of commercial banks and financial institutions must be carried out rigorously to ensure the banking system's integrity and soundness. Particular attention must be given to the procedure of evaluation, monitoring, management and control of risks. Banking supervision is a constant activity aiming to protect depositors and economic operators and avoid risks arising from poor management or excessive commitments. In Algerian Banking Law, for instance, the legislator has set up a rigorous control mechanism. This Central Bank’s control mechanism benefits from the International Monetary Fund's assistance and cooperation with other Central Banks. It relates primarily to the establishment of the operational organization, procedures and methods of control and supervision.\(^5\) The permanent effort of the Money and Credit Council of the Bank of Algeria and the Banking Commission in matters of regulation, management and supervision, is in line with this strategic objective to develop financial institutions.\(^6\)

1) Scope of Supervision

The supervision and control of commercial banks in both countries - China and Congo – are governed by comprehensive regulatory frameworks. The Central Banks of Congo and China are entitled to carry out such supervision and control through documents or on-site. For the documentary control, compliance with relevant banking regulations is based on commercial banks and financial institutions’ declarations or reports. The reporting system of commercial banks and financial institutions is regulated by laws that determine the content and periodicity, deadlines of such statements.

\(^4\) Article 31 of the Law of the People’s Republic of China on Banking Regulation, 2006
\(^5\) Marie-Helene Mongeau, the control & supervision of bank, p. 114, docplayer.fr, Algeria, 2016
\(^6\) Marie-Helene Mongeau, the control & supervision of bank, p. 114, docplayer.fr, Algeria, 2016
2) Control & Supervisory Activities

The four primary functions of banking supervision are: 1) The micro-prudential supervision upon documentary basis; 2) The general supervision upon the inspection on-site; 3) The control of foreign trade operations and transfers; 4) The control of the banking system and measures to combat money laundering and the financing of terrorism.

II. The bankruptcy of the Commercial Banks in China & DR. Congo

A. The bankruptcy of the Baoshang Bank

For the first time in 20 years, the People's Bank of China has announced in its quarterly monetary policy statement that Baoshang Bank will be declared bankrupt. The relevant authority will liquidate the original capital and rights of unprotected creditors according to law. This decision is a first of its kind since the banking authority often refuses to let any commercial banks go bankrupt to do not undermine the country's banking system's image. The decision came out after finding serious insolvency during the regulator's review of Baoshang's business. Baoshang bank is a rural bank that was established in the province of Inner Mongolia. It was placed under the Chinese banking regulator's control in June 2019 because of its serious credit risks. The objective of this one-year takeover was to protect the rights and interests of depositors and other clients. The Chinese central bank's takeover of Baoshang Bank is the first since the Hainan Development Bank seizure in 1998. It has resulted in a tightening of liquidity for banks in China, leading large institutions to become reluctant to lend to commercial banks. In August 2020, the China Finance newspaper revealed that Tomorrow Group had used more than 200 shell companies to borrow 156 billion Renminbi (RMB) (22.5 billion dollars) to Baoshang Bank. In the past twelve months, China has seen at least six banking operations in five provinces as slowing economic growth and disruptions caused by the Covid-19 outbreak have constrained local lenders' balance sheets. Many local banks have also faced corporate governance failures, forcing the Chinese government to help four regional banks since the crackdown on off-balance sheet funding began in 2018. But Baoshang's closure is the first case in China since the Shantou Commercial Bank's bankruptcy in 2001. Despite these banks' closure, the regulators should not allow bankruptcy to become the norm for suffered lenders. From this analysis, the exact bankruptcy’s root causes of Baoshang commercial bank are the mismanagement of depositors’ funds. The managers of this commercial bank loaned the depositors’ money to one of the bank’s shareholders, who could not repay it on time.
The International Bank for Africa in Congo “BIAC” suffers a credit crisis, which places it under the control and administration of the Central bank of Congo (BCC) for a possible new investor to take it over. The BIAC was declared bankrupt after the following circumstances: The term of its Michel Losembe finishes after three years of management. The BCC itself proposed to appoint Mister Michel Losembe with a core objective of strengthening the management system of the BIAC and facilitating a new substantial shareholder to take part in the bank's capital. After that, Mrs Anne Mbuguje was appointed as an acting general director of the BIAC, yet on the BCC proposal and led the entity for a few weeks. The new managerial team led by Israel Tsasa Bilo Ngabul, whose mission was to make a stimulus plan within 180 days, placed BIAC under its supervision and control. Finally, the governor of the Central Bank of Congo filed a complaint against the administrators and the former management team of the BIAC, which was followed by a strict request to freeze the bank accounts of these administrators and the bank assets of their related companies.  

In his complaint about the BIAC's mismanagement, the governor of the Central Bank of Congo, Deogratias Mutombo, affirms that "the mismanagement of the BIAC by its former administrators deserves criminal penalties under articles 27, 79, 80 & 85 of the Banking Law of DR. Congo." However, this statement is surprising because the Central Bank of the Congo governor has previously stated that BIAC was doing better that there was nothing serious about this mismanagement. He continued by affirming that the crisis was just a slight passing wind caused by the ion of the bank's refinancing, and no depositor was thereby at risk. How to explain this change while knowing that the Central Bank of Congo carried out the audit and control of the BIAC? If there was mismanagement, the governor of the Central Bank, who has a close look at the situation of all the commercial banks in Congo, knew such a crisis but did not intervene on time to stop it; therefore, he needs to be held responsible for it. In this case, even the findings of the Central Bank's audit, affirming that BIAC was doing better, are questionable. Not only former BIAC's managers but also inspectors, and governor of the BCC, who participated in such an audit, should be prosecuted as an accomplice to the mismanagement of the BIAC. Similarly, one lawyer stated that: “if there was a mismanagement which the audit report did not mention, all of the above persons (governor of the BCC, inspectors & former administrators of BIAC) were guilty of the criminal association offence according to the Congolese Criminal Code.”  

While being a very complex issue, the BIAC bankruptcy is almost similar to the Baoshang commercial bank. The BIAC’s managers used the depositors' funds to lend to Mr Blattner, a majority shareholder of this bank, to finance his own company SOFIA. Unfortunately, on the due payment date, Mr Blattner could not repay his debt to the BIAC. Consequently, when some depositors wanted to withdraw their funds, BIAC was unable to serve them. Eventually, it was even difficult for BIAC to pay its workers' wages and the charges of its service

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Faced with this issue, usually, BIAC’s managers should force Mr Blattner, by any legal means necessary, to pay back his debt and resulting interests. But they were powerless and could not do so because they dealt with the majority shareholder who could threaten to sack them from their jobs. The commercial banking regulator, the Central bank of Congo, could not discover this problem earlier because Mr Blattner had strong relationship ties with the various political authorities who protected him. Instead of anticipating the BIAC’s bankruptcy, the Central Bank of Congo and the Congolese government attempted to redress BIAC agony or default situation. The laxity and complicity of the Central Bank of Congo exacerbated BIAC’s depositors, workers, and service providers' distressful situation.

III. Prudential Rules of the Management

According to provisions of the 2002 Law related to the Activity and Control of Credit Institutions in Congo, the Central Bank of Congo has issued the following rules:

- The minimum capital;
- Prudential own funds;
- The division of risks;
- The monitoring of the currency exchange;
- The Liquidity;
- The risk of transformation in the medium and long term;
- The limitation of participations;
- Final provisions.

Article 21 of the Chinese Banking Regulation stipulates that relevant authorities should specify prudential operation rules for the banking industry's financial institutions. The banking regulatory authority of the state council may also formulate these rules following laws and administrative regulations. For this paragraph, prudent operation rules must include risk management, internal control, capital adequacy, quality of assets, reserves for losses, risk concentration, affiliated transactions, liquidity of assets, etc.

Besides, financial institutions in the banking sector must strictly respect the prudential operation rules. However, the Chinese Banking Regulation provides that if a financial institution in the banking industry violates the prudential operation rules, the state council's banking regulatory authority or its highest agency at the provincial level must order rectification within the stipulated time limit. Suppose this regulatory authority does not carry out the rectification within the prescribed time limit. Its act will seriously endanger the financial institution's stable operation in the banking industry or harms the lawful rights and interests of depositors or other clients. In that case, the following measures may be adopted upon approval of the banking regulatory authority of the state council or the person-in-charge of its highest agency at the provincial level, depending on

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13 Alain BOLODZWA, DRC’s Economic Situation, in Bosolo na Politik Officiel, TV Shows, 24, October 2020
14 Alain BOLODZWA, DRC’s Economic Situation in Bosolo na Politik Officiel, TV Shows, 24, October 2020
the circumstances: (1) to order a suspension of part of its businesses or to halt approval of its engagement in new companies; (2) to restrict the distribution of dividends and other revenue; (3) to restrict the transfer of assets; (4) to order the transfer of equity of controlling shareholders or curtail the rights of the relevant shareholders; (5) to order the adjustment of directors or senior management personnel or to restrict their rights; and (6) to halt approval of the establishment of additional branches.\textsuperscript{15}

**A. Minimum Capital**

In DRC, commercial banks need to have a minimum capital of USD 5 million, set by the Central Bank of Congo, at their registration onto the approved banks' list. This amount constitutes a minimum capital, but the issuing authority reserves, at the time of the bank approval, the right to ask for more capital according to the prevision of activities submitted to it.

Existing authorized commercial banks must continuously ensure that their prudential funds provide them with the required solvency level. As defined by the Central Bank of Congo, credit institutions' funds cannot at any time fall below the amount of the minimum capital.

Every bank must justify that its assets effectively exceed the liabilities it owes to third parties at least equal to the minimum capital.

In China, the minimum of registered capital for establishing national commercial banks is RMB 1 billion. The minimum amount of registered capital for setting urban commercial banks is RMB 100 million. The minimum amount of registered capital for the establishment of rural commercial banks is RMB 50 million. The registered capital needs to be paid up in full. The state council's banking supervision and administrative authority may adjust the minimum amount of registered capital following reasonable management requirements, provided that the minimum amounts stipulated in the preceding paragraph are satisfied.\textsuperscript{16}

**B. Prudential Own Funds**

Constitute own prudential funds of banks, the amount or sum of:

- Own funds;
- Complementary own funds;
- Possibly any provision required by the central bank, but which are not yet constituted by the concerned bank;
- Subordinated loans (quasi-capital).

A subordinated loan is a financial institution's commitment from a donor or funder to strengthen the economic structure.

**C. Solvency**

Banks have to respect a minimum ratio of 10\% between the own prudential funds and banks' real risk in DRC in managing their resources. It is 8\% in China.

\textsuperscript{15} Article 37 of the Law of People's Republic of China on Banking Regulation of 2006
\textsuperscript{16} Article 13 of the Commercial Banking Law of the People’s Republic of China of 2003
D. Internal Control

The control of the banking sector reflects the setting of adequate requirements, the verification of their applications, and the supervision of credit institutions’ behavior. Under internal control, the administration of the bank itself monitors the implementation of supervisory rules. It allows the bank to comply with the regulations and requires the bank manager to make good management to avoid any crisis.

In most cases, an audit committee accompanies the administration of the bank. The audit or accounts committee actively monitors issues related to the preparation and control of comparable and financial information (management control, internal control, the credibility of communicated financial information, etc.)

Failure to respect banking prudential rules is the leading cause of the bankruptcy of these both commercial banks. Violated Prudential rules are related to the internal and public control rules: All internal control managers of the Chinese and Congolese commercial banks should protect depositors’ funds. Lending these funds to one of the bank’s shareholders constitutes a severe risk. The reason is that in the event of insolvency, there will be no possibility to oblige the shareholder to repay the funds. The Central Banks must verify the non-observance of public control. In the Congo case, the Central Bank of Congo should detect the BIAC’s problem, stop it from happening, and anticipate the liquidation to preserve depositors’ interests. Unfortunately, at some point, the Central Bank of Congo alleged that the BIAC’s financial situation was under control and depositors should not worry about it.

IV. Risk & Its Management

Under Article 21, paragraph 2 of the Chinese Banking Regulation, prudential rules must include risk management, internal control, etc. The banking governance requires strictly limit the action of the bank's executives or board of directors to guarantee the interests of all stakeholders such as clients, depositors, shareholders, etc. The bank's executives must work to ensure stability and growth in banking activities. Thus, to avoid any risk in banking management, each law imposes the solvency ratio. In banking management, the bank manager must not consider this solvency ratio as insolvent.

There is a strong relationship between law and risk. Regulations constantly evolve to permit the legislator to discern and establish the best relationships between individuals. To these relationships will be attached specific legal rights and obligations, whose violations produce proper sanctions. As such, the law must satisfy individuals’ security and justice need by considering all the risks associated with legal relationships.\(^\text{17}\) It is one-way norms need to use to find responses to potential risks to contain harmful consequences. In any jurisdiction, the legislator, judge and prosecutor attempt to determine the most appropriate rules to apply to cases related to property, inheritance, debts, economy, etc. Towards the uncertainty of the economic relations concluded between individuals through contracts, the law must lay down rules applicable to any risk that will occur. It
should also determine in advance the party who will bear the consequences of such risk. In the case of the obligation’s non-performance, the law provides several options: existence or absence of a party’s fault, damage, causal link, force majeure, etc. The legal responses can be imperative or supplementary according to parties’ will. If the legislator’s solutions cannot cover all practical issues, the law refers to legal principles and precedents to guide judges in their works. It gives them the freedom to adapt and rebalance their services judicially. According to Lévy-Bruhl, the law is “a set of mandatory rules determining the social relations imposed on a society at all times”.

Yet, the contemporary society is haunted by a risk’s fear that calls for security. This has led the author to conclude that: “risk is now imposed as a new legal rationality or a new way of reasoning in law”. This new phenomenon of risk exists in any legal disciplines. Insurance law is the first discipline that emphasized the notion of risk and gave it a modern view inspired by mathematical thought and economic theory. The insurance field locates itself between law, economics and risks. It carries a natural symbiosis between three visions of risk: legal, mathematical and economical. In insurance law, risk represents an uncertain event that is quantified or quantifiable. It applies to a known circumstance but whose occurrence is uncertain. For its quantification and qualification, mathematical and economic instruments are used. For instance, statistics are used to highlight probabilities of its occurrence.

In contract law, the risk is defined as “any deviation from the line drawn or from the initial social, economic or financial project upon which contracting parties initially agreed”. The Congolese Civil Code Book III takes risks into account by differentiating two big categories of contracts: aleatory contracts and commutative contracts. Under the aleatory contract, “at the contract formation’s time, at least one of the two parties do not know the exact service’s scope that he (she) will be required to perform, because it depends on an uncertain event”.

The insurance contract is the perfect illustration of risk: While the insured knows the exact extent of his insurance, the insurer does not know the precise extent of services he is required to perform. It depends on the risks’ occurrence covered by the limited time of the agreement. The Congolese Civil Code Book III also considers other risk elements, such as force majeure or the fortuitous event that could disrupt the contract’s enforcement.

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18 Mihaela Varnav, the management of banking risk : Study applied to warning advice & information, Thesis, Paris I University, 2007, p.42
19 DESGORGES R., good faith in contracts law, current role & perspective, these, Paris II, p.50, 1992
20 Mihaela varnav, op cit, p.42
21 DESGORGES R., op cit.
22 Ibid.
After the United States' financial crisis, which led to a growing need for risk management and a strategy for establishing clear structures in financial organizations, the emphasis is now on improving measures and managing specific risks such as liquidity risk, credit risk, and market risk.

According to Tazari, the risk can stand for the probability that an event or set of circumstances could occur. In economic theory, a risk is a price to pay. This price expresses revenue and its level of importance related to the execution of an important project. In the banking system, the risk can come from a lack of liquidity, high volatility of financial markets, and banks' willingness to expose themselves to risks.

Article 27 of the Law of the People's Republic of China on Banking Regulation stipulates that the state council's banking regulatory authority must establish a rating system and a risk alert mechanism for regulation of financial institutions. It should also determine the frequency and scope of on-site inspection and other measures that need to be adapted based on the financial institution's rating and risk profile. Article 28 of the same Law provides that the state council's banking regulatory authority must set up personal responsibility systems to discover and report sudden incidents in the banking industry. Suppose the banking regulatory authority finds a sudden incident that may trigger systematic risk in the banking industry or seriously affect social stability. It must immediately report to the person in charge of the state council's banking regulatory authority. It means that the administration must notify the People's Bank of China and the state council's finance department immediately.

A. The Market Risk

Generally, the market risk is the risk of losses in positions due to the market variables such as volatility and price fluctuations. The market risk is composed of risks related to interest rates, currency, commodity price, real estate, etc. Like credit risk, commercial banks can either use the standard approach or their internal model to assess this market risk.24

1) Market risk: the standard approach

The extent of market risk varies depending on the type of market risk. Interest rate risk is associated with holding debt securities and other instruments or taking a position on these securities and instruments. The interest rate risk is also linked to all securities with identical behavior to those mentioned above, such as non-convertible priority shares. Convertible bonds are also treated as debt securities or property titles.25

The interest rate risk's capital requirement depends on the specific risk associated with each securities debt and the general market risk associated with the interest rate risk of real estate. General market risk is related to

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24 Boubacar Naby Camara, prudential rules and banking risk: impact of the structure and level of regulatory capital, thesis, Limoges University, p.27, 2010
25 Boubacar Naby Camara, prudential rules and banking risk: impact of the structure and level of regulatory capital, thesis, Limoges University, p.28, 2010
unfavorable variations in market interest rates that result in a loss of securities’ value held by a commercial bank. Thus, regulators require commercial banks to have proper capital to cover this risk.26

The risk of a position in real estate titles arises from holding these titles or taking a position on such titles in the trading book. Minimum requirements are needed to cover this risk and relate to long or short positions in all instruments with a market behavior similar to that of shares other than non-convertible priority shares.27 Concretely, these are ordinary shares with or without voting rights, convertible debt securities with behavior identical to that of shares and commitments to acquire or transfer shares. The internal capital requirement on real estate titles for specific risk is 8% or 4%. The requirement for general market risk is set at 8%.28

Regarding derivative instruments on real estate titles, they are converted into a position on respective underlying. Balanced positions on each share or an identical stock index can fully offset each other. A single net position can be obtained to which the requirements for specific and general risk apply.

Exchange risk is the risk associated with an unfavorable change in exchange rates. Banks should cover the risk of taking a position in foreign currencies and gold and can exploit two options to measure exchange risk on all positions in foreign currencies and gold. The first is a simplified method that treats all currencies on the same plan. The second uses internal methods that consider the adequate degree of risk according to their portfolio’s composition. The internal capital requirement represents 8% of the overall net opened position. Also, positions taken to cover against unfavorable effects of an exchange fluctuation may be excluded from calculating the opened net position in foreign currencies. But these positions must meet certain conditions specified by the supervisory authority.29

The commodity risk is related to holding or taking a position in physical products that can be traded on a secondary market. These are agricultural commodities, minerals (including oil) or precious metals, except gold. This risk is more difficult to hedge than that linked to foreign currencies and interest rates. It is because commodities are traded in less liquid markets. A change in supply and demand can have more significant effects on prices and volatility.30

B. Credit Risk

Credit risk is the risk of a loss inherent to a creditor about the repayment of his debts. There are two types of risk: the default risk that occurs in the event of default of a creditor to pay back the principal debt or its interest,
and the risk of the credit quality deterioration. The main point in explaining the credit risk is the failure to pay, and a loss of a bank expresses a state of insolvency noted at a given time.

Credit risk includes risk on debts of governments, banks, investment firms, other businesses and retail customers. One of Basel Committee II capital regulation's new features is that it lets banks choose between the standardized and the internal rating approach for taking credit risk into account. The risk associated with securitization is subject to special measures by the regulator.\(^{31}\)

Credit risk: In the standardized approach, the risk is assessed using external credit ratings performed by rating agencies (e.g., Standard and Poor's, Moody's, Fitch IBCA). Regulators then transform these assessments into weights. They consider factors such as the issuers’ size and scope assessed by the external body, assigned reviews and the definition of the used payment default. This approach allows considering credit risk in the calculation of the risk-weighted capital ratio.\(^{32}\)

Credit risk is considered depending on the debtors' nature (State, banks, companies, debts from the retail portfolio, and loans guaranteed by commercial and residential real estate and loans). Debts on governments and their Central Banks are weighted according to their rating. Credit risk is also linked to retail customers' loans, debts and loans guaranteed by residential real estate and off-balance sheet items (transfer of loans, financial commitments, etc.)\(^{33}\)

In addition to rules established to take credit risk into account, the regulator allows banks to use specific techniques to mitigate the credit risk they face. Credit risk mitigation techniques involve taking first-rank real securities in the form of liquidities or titles covering the exposures, third-party guarantees for loans, the purchase of protection, and deposit and loans netting agreement with the same counterparty.

The alternative to the standardized approach for calculating credit risk is the internal rating approach. Credit risk linked to the securitization activity was considered a factor that aggravates the recent subprime crisis. However, provisions existed previously to take this risk into account in calculating capital requirements, even if they turned out to be insufficient. The aim was to achieve correct hedging of exposures resulting from conventional or synthetic securitization structuring transactions. Banks' exposures resulting from securitization operations relate to loans backed by mortgages, credit enhancements, lines of credit, interest rate, credit derivatives, and reserve accounts. When an institution transfers the assets under traditional securitization, exposures to these assets may be excluded from its risk-weighted assets. But for this to happen, a considerable part of the credit risk must be transferred to third parties. The bank should also not retain effective or indirect control over indirect exposures.\(^{34}\) Like other credit risks, the bank can choose between the standardized and internal ratings to determine its capital requirement for securitization.

\(^{31}\) BOUBAR Naby Camara, op cit., 31
\(^{32}\) BOUBAR Naby Camara, op cit., 30
\(^{33}\) COLLARD Ch. et Roquilly Ch; Legal Performance : For a strategic vision of Company Law, LGDT, special edition, pp. 105-130, 2012

\(^{34}\) BOUBAR Naby Camara, op cit., p.41
As mentioned above, the management of this risk occurs in the circumstance where the financial crisis of 2008 has challenged practices of taking measures and managing credit risks. As a result, the banking regulator has to promote the financial system's security rules by setting prudential regulations for banks and carrying out supervisory actions that are preventive or designed to avoid crises. Traditionally, banking rules pursued three types of objectives: protecting depositors, predicting the systemic risk, and the payment systems' security. International regulatory institutions seek to promote security rules that apply globally to prevent the global financial system's systemic risk and harmonize competition among banks.

C. Operational Risk

Operational risk stands for the risk of losses resulting from maladjustment or failure attributable to personal procedures, internal systems, or external events. A bank is exposed to operational risk due to deficiencies related to operations, personnel, internal systems or external events. Banks have the option of using three methods to calculate capital requirements for operational risk: The basic indicator approach, the standardized approach and the advanced measurement approach.

In the basic indicator approach, banks must hold an internal operational risk capital corresponding to the weighted average of a fixed coefficient \( \alpha \) of their positive average gross annual product over the last three years. But a yearly gross product less than or equal to zero must be excluded from the calculation. The Basel Committee sets the coefficient \( \alpha \) at 15%.

In the standard approach, the banks’ activities are divided into eight business lines: corporate finance, market activities, retail banking, commercial banking, payments and settlements, agent function, assets management and retail brokerage. The gross product is used as an approximate global indicator of the activity’s volume for each business line and the exposure’s degree to operational risk. The capital requirement is calculated by multiplying the gross product by a specific beta factor. In the entire banking sector, beta is an approximate proportion’s measure between the history of operational risk losses for a given business line and the aggregate amount of gross product. The total requirement is equal to the three-year average of all business lines' capital requirements for each year.

In the advanced measurement approach, banks use their internal system to determine operational risk's capital requirement. But for a bank to be allowed to use its internal system, it must meet several qualitative and quantitative criteria. It must, among other things, have an independent operational risk management’s department responsible for the design and implementation of the institution's functional risk management system. The regulator must also prove that its approach to measuring operational risk has reliability comparable to the internal rating approach for credit risk concerning the holding period of one year and the confidence interval at the threshold of 99.9 percentiles. The capital requirement should be calculated, taking into account expected (PA) and unexpected losses (IP), unless the bank can demonstrate that the internal operating method
adequately covers expected losses. Operational risk can be mitigated by factors such as insurance policies. But this mitigation is limited to 20% of the total capital requirement for operational risk. Also, the insurer’s compensation capacity must be rated at least A.\(^\text{35}\)

The capital regulation put in place under Basel II agreements gives priority to the banks’ internal models in assessing and hedging their risks. It is based on three pillars: minimum capital requirements, banking supervision and market discipline. Although a significant advance in capital regulation, this instrument showed its limits during the recent subprime crisis, even if the illiquidity phenomena amplified this crisis. There was a confidence crisis in banking institutions' actual solvency, although most of them had relatively high regulatory capital ratios. These difficulties encountered by the banking system have shown that capital regulation has not been a sufficient incentive to mitigate the excessive risk-taking behavior of banks.\(^\text{36}\)

An examination of the direct losses resulting from the operational risk indicates that most of them come from improper practices or inadequate control within the banks' commercial activities. In most cases, these losses harm the reputation of the concerned bank and sometimes lead to bankruptcy. Besides, money laundering and the financing of criminal or terrorist activities are the priorities for all governments. Therefore, governments are likely to pressure commercial banks to reinforce the detection of funding for illegal activities. It makes financial resources to be devoted to surveillance, monitoring, and intelligence.

Another significant source of operational risk is associated with execution errors and inefficient processes. Basic control processes' inadequacies provoke the majority of risk management issues and have a considerable impact on financial institutions' functioning. This source of risk includes, among other things, the procedures of approval and monitoring of the conformity of operations.

Operational risk management is at the center of most of the losses recorded during the crisis. The wrong valuations of assets are the root cause of the most severe malfunctions. Several weaknesses can explain these operational dysfunctions based on the banking practices of risk management. Commercial banks have no choice. The only solution they need to have recourse on is to restore shareholders, regulators, and customers' confidence to improve their operational risk management capabilities.

**D. Liquidity Risk**

The risk is related to the possibility of withdrawals of funds from the bank by the depositors. The judgment conditions these withdrawals that depositors have about the market value of the bank and its solvency. When debt holders judge that the bank's assets' discounted value is lower than that of their engagements, they rush to withdraw their funds, knowing that the first arrivals will be the first to be served. This move, called a bank run, can push the bank into bankruptcy.

\(^{35}\) BOUBAR Naby Camara, op cit., p.42  
\(^{36}\) BOUBAR Naby Camara, op cit., p.42
In other words, this liquidity occurs when massive withdrawals of depositors lead to insolvency of the bank at issue. Indeed, to respond to this movement of enormous leaves, the bank is obliged to raise funds, even at costs higher than average. But, if these costs are very high, they can lead to an undervaluation of the bank’s assets, thus rendering it insolvent. However, the bank can borrow from other banks to avoid the risk of insolvency. Finally, the liquidity risk relates to the types of threats, such as the interest rate risks. Some of the bank's liquid assets are sensitive to changes in interest rates. Hence, the effective management of interest rate risk allows banks to avoid some liquidity problems.

The enforcement of prudential rules also involves risk management. Governance requires strictly limiting the commercial banks’ managers' actions or boards of directors to guarantee all parties' interests, such as depositors, shareholders, service providers, and workers.

The liquidity risk can arise from a lack of liquidity, high volatility in financial markets, and commercial banks' desire to expose to risks. In the case of two commercial banks, their managers desired to expose themselves to liquidity risk by lending funds to one of the shareholders to finance his company’s activities. Managers should have considered the shareholders’ insolvency before taking such a decision because they were incapable of forcing them to pay back their debt. For the BIAC’s bankruptcy, the Central Bank of Congo should be condemned for its complacency and complicity because its governor, during the external control, alleged that the BIAC’s financial situation was satisfactory; therefore, customers should not worry about it. It demonstrates that the Central Bank of Congo’s governor covered the BIAC’s mismanagement before public opinion. However, the Central Bank of China fought against the Baoshang Bank’s mismanagement by detecting it earlier and anticipating its bankruptcy. This strategy helped to safeguard the depositors’ interests.

V. Mismanagement’s Consequences

The mismanagement of these two commercial banks resulted in their bankruptcy with serious negative consequences in society. It means that these commercial banks were no longer able to satisfy or pay depositors’ funds due to financial difficulties. They were in a state of payment’s suspension. Bankruptcy leads to commercial banks’ liquidation that involves the assets’ sale and the liquidity’s seizure to pay creditors such as depositors, service providers, and workers. If it remains some assets, they will be distributed to banks’ shareholders.

The social consequences stemming from commercial banks’ bankruptcy concern a broad category of people since depositors, service providers, employees, and shareholders cannot enjoy their rights and access their funds anymore.

VI. Legal Responsibility of Supervisors & Commercial Banks

The legal responsibility of the supervisor is to veto and control compliance with the law and regulations. The supervisor must exercise this responsibility in strict accordance with the law and regulations.
when the supervisory personnel do not comply with the law, they are liable and must answer for their actions and responsibility.

Article 43 of the Law of the People's Republic of China on Banking Regulation provides that: "where personnel of banking regulatory authority that engage in regulatory work commit any of the following acts, he shall be subjected to an administrative penalty under the law. Where a criminal offence is constituted, criminal liability shall be pursued under the law:

(1) Examine and approve the establishment of, changes in or termination of financial institutions in the banking industry, or the scope of business or the types of services within the scope of business of such financial institutions in violation of provisions;
(2) Conduct on-site inspection of financial institutions in the banking industry in violation of provisions;
(3) Fail to report sudden incidents in accordance with article 28 hereof;
(4) Inspect bank accounts or apply to freeze funds in violation of provisions;
(5) Adopt measures against or penalize financial institutions in the banking industry in violation of provisions;
(6) Conduct an investigation on the relevant entity or individual in violation of the provisions of article 42 hereof;
(7) Other acts constitute an abuse of power or dereliction of duty.

Personnel of the banking regulatory authority of the state council engaging in supervision and administration duties who are guilty of fund embezzlement or corrupt practices, disclosure of state or commercial secrets, and personal privacy shall be liable for criminal prosecution according to laws if the case constitutes a criminal offence; where the case does not constitute a criminal offence, administrative sanctions shall be imposed in accordance with rules."

Under Congolese law, the legislator invests the Central Bank of Congo with a general mission and power of supervision and control of all the commercial banks. In this context, the Central Bank monitors the regulations' implementation according to the periodic documents prepared by commercial banks, the inspection’s investigation reports, and the auditors' reports.

Suppose the Central Bank of Congo finds out that a commercial bank does not operate according to its laws and administrative rules or its internal control has serious shortcomings. In that case, it may issue a warning to the bank's managers to take any appropriate corrective measures. Commercial banks must guarantee their customers' interest and the regulative authority's confidence to avoid bankruptcy. Consequently, in non-compliance with the legal and regulatory requirements, the bank may be subject to disciplinary and judicial sanctions.

It is necessary to prosecute commercial banks’ managers under bankruptcy offences and abuse properties for mismanaged commercial banks. The Central Bank of Congo’s governor must also be prosecuted for complicity in the bankruptcy offence for having recognized the BIAC’s financial situation lately, which aggravated the issue. A civil action against these banks’ managers must also be considered.
VII. Convergence & Difference

-The resemblances between the Chinese and Congolese legislations are as follow: In both countries, the regulatory and supervisory authorities are the governmental banks. For instance, in Congo, it is the Central Bank of Congo, while in China, it is the state council's banking regulatory authority. In both countries' jurisdiction, these governmental banks ensure the public control of all the commercial banks. Every commercial bank must carry out internal controls that respect the relevant legal requirements. Also, the regulatory charter of banking associations is controlled and approved by each government's central banks. Chinese and Congolese laws hold responsible for any commercial bank which does not comply with the relevant legal requirements. The sanctions can either be judicial or administrative, depending upon the gravity of the facts.

Moreover, concerning divergences, the Chinese legislator notes that prudential operative rules involve risk management, internal control, capital adequacy ratio, quality of assets, reserves for losses, risk concentration, affiliated transactions, liquidity of assets, etc. For the Congolese legislator, prudential operations involve minimum capital, prudential capital, risk division, foreign exchange supervision, liquidity, etc.

Concerning the risk, the Chinese legislator has introduced the rating system and a risk alert mechanism for regulating financial institutions in the banking industry and should determine the frequency and scope of on-site inspection. However, the Congolese law empowers the Central Bank of Congo with the mission of control to secure customers and solve risks. The role of the Central Bank or Colleges of Auditors' control is to detect these risks. Furthermore, Congolese law requires a minimum capital of USD (united states dollar) 5 million to get state approval for a commercial bank, while in China, the minimum amount is RMB 1 billion.

Finally, it is essential to emphasize that the Chinese banking surveillance system adapts well to modern realities and better guarantees customers' trust and protection.

-Regarding the similarities, the mismanagement, violation of prudential rules, and the non-compliance with the bank reserves have caused both commercial banks' bankruptcy. The mismanagement identified in both banks is due to the lack of stringent internal controls. The managers of these two banks should have exercised rigorous and routine internal control to avoid any crisis. The result of this control could have allowed them to detect all of the management’s discrepancies to be rectified where it is necessary. Prudential rules of banks are binding provisions adopted by the monetary authorities that aim at preventing banks from going bankrupt to ensure the proper functioning of financial markets. As monetary authorities, the People's Bank of China and the Central Bank of Congo elaborate these rules so as managers of commercial banks comply with them to avoid bankruptcy. Similarly, managers of commercial banks have to respect the banking reserves to avoid going bankrupt.

Two elements need to emphasize the differences: the monetary authority's role in commercial banks' external control and depositors' safety. The external control or audit of commercial banks is carried out by the Central

38 Article 21 of Chinese law of Banking Regulation, 2006
Bank of Congo, inspectors, and the People's Bank of China. In China, the People's Bank of China protected depositors and other customers' rights and interests by taking over the control and supervision of the Baoshang Bank in June 2019. However, in Congo, the Central Bank and inspectors seem to be accomplices with managers of the BIAC when exercising their audit mission. As mentioned above, the reason is that the last audit report affirmed that the management of the BIAC was sound, and there was no risk for depositors and other clients. But, sometimes later, the governor of the Central Bank of Congo brought a complaint revealing the mismanagement of the former directors of BIAC, which resulted in the bank's bankruptcy. For depositors' safety, the People's Bank of China was proactive in securing depositors' interests toward the Baoshang Bank's mismanagement by taking control of the bank for one year. However, the Central Bank of Congo took over the BIAC to protect the managers' mismanagement. Unfortunately, this situation put the interests of depositors at risk because they do not know how to recover their funds during the bankruptcy—currently, the moment they brought a lawsuit in court against BIAC to claim their funds.

VIII. Constructive Suggestions

Due to the non-observance of prudential rules, our suggestions are towards strengthening the control over these commercial banks by relevant authorities, including financial prosecutors. To reach this goal, the Congo must adopt new legislation that will create a specialized group of financial magistrates to ensure the control and transparency of management's effectiveness in various commercial banks. The relevant authority should also increase penalties related to the offence of abuse of goods or credit to severely punish commercial banks' managers and their accomplices for their mismanagement. It is an efficient way for relevant authorities to protect commercial banks, depositors, and other clients against maladministration.

Materials and methods

We used normative comparative and documentary methods in this work.

Conclusion

Countries worldwide must strengthen the mechanisms of control and supervision of financial institutions. It is in this view that Chinese and Congolese legislators have adopted the law about banking regulation. In analyzing these different laws, the Chinese and Congolese legislators entrusted supervision and control to the state council's banking regulatory authority (China) and the Congo's central bank (DRC). In the exercise of their missions, these banking regulatory authorities have the main objective of ensuring financial institutions' control and supervision to safeguard the bank's customers and shareholders' interest. By doing so, they prevent commercial banks from going bankrupt. Each country's banking regulation sets out some prudential rules that commercial banks need to implement. In violation of these rules, a defaulted commercial bank or its personal

39 China Magazine (2020), a Chinese commercial bank goes bankrupt, 12 August

will be held liable and therefore sanctioned accordingly. Besides, the banking regulatory authorities of both states try to prevent risks and assure their strict management.

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