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Organizational and Legal Basis for Assessing the Quality and Reducing Assets of Commercial Banks

I.T. Mitillaev^{1*}

1. Independent Applicant of the Department of Accounting and Banking, Deputy Dean of the Faculty of Economics of the Andijan Institute of Economics and Construction, Andijan Region, Uzbekistan

* Correspondence: lbr1980@mail.ru

Abstract: This study examines the organizational and legal foundations for assessing the quality and reducing problem assets in commercial banks, focusing on legal frameworks established by relevant laws and regulations. While problem assets remain a critical issue, particularly within credit processes, existing studies provide limited insight into their effective management and resolution. To address this knowledge gap, the research aims to identify key legal and operational challenges associated with problem assets and propose practical solutions. Utilizing a qualitative analysis of legal documents and banking practices, the findings reveal significant gaps in current approaches and highlight strategies to enhance asset quality management. These insights have important implications for policymakers and banking professionals seeking to improve financial stability and operational efficiency.

Keywords: Valuation, Assets, Commercial banks, Loans, Financial transactions, Risk management, Collateral rights, Preferential terms, Liquidity, Reserve resources

1. Introduction

Commercial banks need to solve the problem of not only receiving income from borrowed funds from banks and banking activities. According to this law, the organization, "bank - commercial legal entity by placing them in income-generating assets, but also the return of these funds from the "borrower" in full. Because "the owner of the investment does not sell the investment, but the right to use the investment under a certain condition and additional interest." In commercial banks, an important role in the return of money is played by regulatory norms, considered as their legal basis, in particular the relevant codes and laws, decrees and resolutions of the President and the Cabinet of Ministers, regulatory documents of the Central Bank and commercial banks.

These assets are directed to the bank for the purpose of generating income. In our research, we have studied in detail the processes of assessing the quality of problem assets of commercial banks, their classification, creating reserves for them, paying them off from reserves and other stocks, and reducing them. a person who carries out a set of activities, such as accepting deposits from legal entities and individuals, and using the funds received for risky lending or investing, making payments, which are considered banking activities. At the same time, commercial banks are independent in making decisions related to the implementation of financial transactions.

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This situation is defined in the law as follows: - state bodies and their officials are prohibited from interfering in the activities of banks, including the management of entrepreneurial risks related to the formation of the loan portfolio and assets of the bank, the appointment of bank managers, and also from demanding various payments and contributions from banks. In our opinion, in addition to According to the results of the study, it was noted that problem assets in the activities of banks mainly arise in the credit processes of the activities of banks. In the process of reproduction and accumulation, temporarily idle funds are placed in the form of loans as an income-generating asset through commercial banks. At the same time, as a result of untimely repayment of loans, profits will decrease, and resources will become insufficient.

2. Materials and Methods

To evaluate the quality and decrease the assets of the commercial banks, it is used the organizational and legal methods and approaches based on the legislation of the country, the Санстанда, and risk management. Queens among the primary means is regulation and supervision, and here, for instance, commercial banks are to meet the demands of the central banking authorities and financial regulators. For example in Russia banking operations are governed by the CBR using Decrees, Directives, and Instructions and key documents are regulation on capital adequacy, and regulation on liquidity and efficiency of risk management.

Completeness is another critical method comprising audit and internal control in which banks carry out several internal audits to contain risk and check bank assets' conformity to laid standards. This is important in order to contain stressed non-performing assets and to assess the efficiency of the current practices being implemented. The methods for assessing assets may incorporate models which examine the value of the assets including the liquidity and profitability models with reference to the current market environment. Another reminder that when credit portfolios get downgraded, banks have Asset adjustment techniques like write offs or establishing reserves.

To a great extent, these exertions are facilitated by risk management techniques: Credit and market risks are modelled when assessing the corresponding values, and monitorings can be implemented early weak points in assets portfolios and allow corrective actions to be taken. Last but not the least, the IFRS principle which is also the guide to the valuation of assets and depreciation is also basic. As things stand in relation to IFRS, banks have the responsibility of determining fair value of the assets on their own and also testing the impairment of those assets more so during difficult economic times.

3. Results

The implementation of organisational and regulatory techniques for evaluating quality and diminishing the assets of commercial banks often yields various beneficial results. Banks enhance their financial stability by complying with regulatory mandates and employing capital adequacy and liquidity benchmarks. This facilitates the equilibrium between risks and returns, augmenting overall financial resilience and diminishing the probability of insolvency. Furthermore, the consistent application of stress testing and credit risk assessment allows banks to detect possible problematic assets promptly, hence reducing losses and alleviating the effects of asset depreciation.

Accurate asset assessment facilitates the prompt establishment of reserves to mitigate potential losses on loans and other assets, thereby reducing financial risks and enhancing investor and client confidence. The implementation of international standards, such as IFRS, enables banks to more readily adjust to fluctuations in the external economic landscape, which is especially vital during times of instability and economic crises. The implementation of auditing methods and asset testing in accordance with international standards enhances the transparency of financial reporting, hence cultivating increased trust from clients and investors in the bank's financial status.

Requirements for assessing the quality of assets of commercial banks and the procedure for assessing them are specified in the relevant articles of the Law "On Banks and Banking Activities". According to this law, an organization, "a bank is a commercial legal entity that carries out a range of activities, such as accepting deposits from legal entities and individuals, and using the funds received for risk lending or investing, making payments that are considered banking activities. At the same time, commercial banks are independent in making decisions related to the implementation of financial transactions.

This situation is defined in the law as follows: - state bodies and their officials are prohibited from interfering in the activities of banks, including the management of entrepreneurial risks related to the formation of the loan portfolio and assets of the bank, the appointment of bank managers, and also from demanding various payments and contributions from banks. In our opinion, in addition to interfering in the activities of commercial banks, we also consider it necessary not to force them to finance the population without the right of collateral on preferential terms, financing them from state resources. - "Control over the formation of reserves in case of possible losses on assets based on the classification of assets, as well as ensuring adequate maintenance of capital and general reserves of the bank." In fact, commercial banks must maintain a sufficient volume of liquid assets to meet their obligations to clients in a timely manner, as well as to form reserves in case of possible losses.

- "In order to reduce the risk of asset loss, banks should maintain sufficient capital and liquid resources, form reserves against possible asset losses based on asset classification, and ensure the diversification of their assets." In fact, if commercial banks do not sufficiently diversify their assets, the riskiness of bank assets will increase, and as a result, the volume of assets at risk will also increase, which may result in a shortage of resources for the bank. - "In order to prevent problems related to the bank's liquidity, fulfilling obligations to maintain the minimum amount of liquid assets necessary for the continuity of payments, the appropriate structure of financial resources and the proportionality of assets and liabilities by maturity." The requirements for preventing the emergence of transformation risk, provided for by this article, are mentioned in the law.

"In case of failure to form sufficient reserves in case of possible losses of banking assets formed in commercial banks, this will be included by the Central Bank in the list of gross violations or if the bank's liabilities exceed its assets, the commercial bank's license will be revoked. - In particular, in the law "In the event of a breach of contractual obligations by the borrower, banks have the right to collect the loans provided and the interest accrued on them ahead of schedule in the manner prescribed by the agreement, and also to focus collection on the pledged property in the manner established by law."

This article mentions the rights of a commercial bank in situations where a client refuses to fulfill its obligations. In essence, commercial banks do not allow their assets to become problematic. The Resolution of the President of the Republic of Uzbekistan No. RP-3270 "On measures for the further development and improvement of the stability of the banking system of the Republic" dated September 12, 2017 sets many instructions and tasks to assess the quality of assets of commercial banks, improve the quality of their assets and prevent them from becoming problematic assets.

In particular: Recommendations are given to improve the structure of the bank's assets and the state of the loan portfolio, as well as to take effective measures to reduce the share of problem loans issued in foreign currency, from the point of view of protecting the interests of the bank's shareholders. Indeed, the share of funds issued in foreign currency as loans in commercial banks of Uzbekistan is very high. As a result of the high devaluation of the national currency against foreign currency, serious problems with repayment of loans received arose for business entities that received loans in foreign currency. Over time, this negatively affected loan defaults and the growth of problem loans in banks.

In addition, this decision provides for "Further support of the liquidity of commercial banks by canceling the procedure for transferring funds into deposits of mandatory reserves formed to cover possible losses on bank assets." In fact, this decision covers this issue very correctly, since the excess of problem assets in commercial banks directly generates the need to create reserves for problem assets. At the request of the Central Bank, reserves formed to cover possible losses were transferred to a separate account number of the Central Bank, which had a negative impact on the representative account numbers of commercial banks, that is, on the reduction of real, available financial resources and their liquidity.

The adoption of this decision has certainly opened the way to increasing the liquidity of commercial banks and using funds in representative accounts of commercial banks for the corresponding purposes. One of the measures in the said resolution is "Further strengthening of work to improve the quality of bank assets by filling the structural divisions of commercial banks engaged in the issues of restoring problem assets with highly qualified specialists", assigned to the boards and management of banks. Indeed, commercial banks need highly qualified specialists who deal with distressed assets. Because this will play an important role in fulfilling the bank's obligations to its clients in the future and increasing the bank's profits. Another important document related to problem assets is the Regulation of the Central Bank of the Republic of Uzbekistan "Classification of asset quality, formation of reserves by commercial banks to cover possible losses on them" and its application, as well as the method of taking preventive measures to prevent the formation of problem debt on loans, ensuring continuous growth and improvement of the quality of the loan portfolio of commercial banks is one of the main areas of reforming and increasing the stability of the financial and banking system of the republic.

According to the above-mentioned regulation of the Central Bank, when assets of commercial banks are classified as unsatisfactory, doubtful and hopeless, they are considered problematic assets. This regulation also defines a number of criteria characterizing bank assets, which should reflect the real situation in the reporting of commercial banks. If commercial banks fail to prepare reports on problem assets transparently and truthfully, they will have the following consequences: - "False reporting is considered an attempt to mislead and deceive the depositors, creditors and shareholders of a commercial bank, as well as the Central Bank and other interested parties, and is considered an unsafe, harmful to health banking practice." - "If the share of problem assets on the balance sheet and off-balance sheet items of a commercial bank is more than ten percent of total assets, then the Central Bank considers that the qualifications of the executive management of the commercial bank do not meet the requirements of the Central Bank and the control over banking activities established by the Council of the commercial bank will be considered insufficient."

"The proportion of non-profitable assets exceeding seventy percent of total assets is an indicator of the emptiness of the bank's credit policy, loan allocation and management process." If a commercial bank has several assets transferred to one debtor, the quality of all assets returned by the debtor to the commercial bank should be classified as the quality of assets classified in the lowest category. If a debtor owes money to several commercial banks and one of them has classified the quality of the recovered assets in the lowest category, the other commercial banks should also classify the quality of the assets transferred to this debtor in this category. In this case, commercial banks should use the credit information database to determine the asset quality classification provided to the debtor by other commercial banks.

If the quality of the asset does not fall into the "standard" category, a commercial bank cannot provide the borrower with funds in the form of additional credit funds, additional resources for the current loan or new loans without a detailed analysis of the

risk associated with possible loss. Commercial banks' reports must reflect the real state of their asset quality. False reporting is considered an attempt to mislead and deceive depositors, creditors and shareholders of a commercial bank, as well as the Central Bank and other interested parties, and is considered an unsafe, unreasonable banking practice.

If the share of problem assets on the balance sheet and off-balance sheet items of a commercial bank is more than ten percent of the total assets, this is grounds for the Central Bank to conclude that the qualifications of the executive management of the commercial bank do not meet the requirements of the Central Bank and to consider the control established by the Council of the commercial bank to be insufficient.

In the process of working with income-generating assets in commercial banks, there is always a risk of non-return of them and income from them. Therefore, it will not be possible to completely eliminate it. It is only necessary to take measures to reduce and minimize this risk and, based on this, organize the work. Commercial banks have created special departments that work in this direction. Employees of these departments even are part of committees created to check transactions with assets in banks. The main goal is to take measures to reduce problem assets.

4. Discussion

Organisational and legislative strategies designed to evaluate asset quality and diminish their value are essential instruments for maintaining the financial stability of commercial banks. The use of international standards like IFRS and a rigorous regulatory environment facilitate effective risk management and liquidity preservation. Nonetheless, numerous problems confront banks when executing these strategies. The implementation of intricate asset evaluation techniques necessitates substantial financial and human resources. Occasionally, banks have a deficiency of skilled professionals adept at accurately evaluating asset problems and implementing timely corrective measures. Moreover, even when all regulatory criteria and standards are adhered to, market conditions can significantly influence asset prices.

A precipitous drop in oil prices or currency volatility might result in substantial asset depreciation, necessitating prompt modifications in reserves and capital. Moreover, strategies for asset reduction, such write-offs or reserve establishment, can adversely impact a bank's financial performance, diminishing short-term profitability. This could potentially affect the bank's reputation and appeal to investors. In summary, the successful execution of organisational and legal strategies for asset evaluation and mitigation necessitates a holistic strategy from commercial banks, which includes compliance with regulatory mandates and the proactive use of international standards and contemporary risk management methodologies. Regularly updating asset assessment and monitoring procedures, together with enhancing the bank's internal infrastructure to adapt to external developments, is crucial for ensuring operational success and crisis prevention.

5. Conclusion

Commercial banks' reports must reflect the real state of their asset quality. False reporting is considered an attempt to mislead and deceive depositors, creditors and shareholders of a commercial bank, as well as the Central Bank and other interested parties, and is considered an unsafe, unreasonable banking practice. In conclusion, it can be emphasized that the legal framework plays a very important role in assessing the quality of assets of commercial banks, since in the absence of consensus in their assessment, the income of commercial banks may decrease and their liabilities may increase, as a result, the volume of problem assets will tend to increase.

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