

**Progress since the Washington Summit in the
Implementation of the G20 Recommendations
for Strengthening Financial Stability**

Report of the Financial Stability Board to G20 Leaders

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I. Introduction

Since the onset of this crisis, national authorities and international bodies, with the FSB as a central locus of coordination, have advanced a major program of financial reforms, based on clear principles and timetables for implementation that seek to ensure that a crisis on this scale never happens again. This report details the global policy development and implementation that have taken place since the G20 Washington Summit in November 2008.¹

A key piece of the global reform agenda has been addressed with agreement on strengthened bank capital and liquidity standards by the Basel Committee on Banking Supervision (BCBS) and its governing body, the Group of Governors and Heads of Supervision (GHOS). The new standards will significantly improve the quality and quantity of bank capital and enhance the resilience of the banking system. A comprehensive macroeconomic impact assessment has been conducted and has informed transition arrangements that will leave the economic recovery unaffected.

Good progress has been made in defining a policy framework to address the moral hazard risks posed by systemically important financial institutions (SIFIs). The FSB is submitting to the G20 Seoul Summit a set of recommendations and timelines for implementation of this framework.

Legislative and regulatory reforms have progressed in major jurisdictions. These have also provided for the development of system-wide oversight arrangements, such as the US Financial Stability Oversight Council (FSOC), and the EU European Systemic Risk Board (ESRB). As frameworks for macroprudential policy are coming into place in various jurisdictions, the FSB will remain engaged with the development and application of macroprudential tools.

With regulatory requirements on the banking system tightening, the need intensifies for more systematic attention to activities in the shadow banking sector. This sector continues to play an important role in credit intermediation and liquidity transformation outside the rigorous capital and liquidity regulatory framework that applies to banks. Addressing the issues that this raises, and putting in place the needed safeguards, are one of the priorities of the FSB's forward agenda.

¹ And since the April 2008 *Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience*, which can be found at http://www.financialstabilityboard.org/publications/r_0804.pdf.

Improving the over-the-counter (OTC) derivatives markets is another critical component of the reform agenda and includes mandatory reporting of OTC derivatives transactions to trade repositories, which will enable the authorities to assess the build-up of potential vulnerabilities in the financial system. The FSB submitted to the G20 Finance Ministers and Central Bank Governors in October 2010 recommendations on the consistent implementation of the G20's overall policy objectives across jurisdictions. Much work and considerable coordination lie ahead in this area.

Despite significant progress to date on global policy developments, there is much to be done before a more resilient financial system has been secured. The policies that have been agreed need to be implemented consistently across jurisdictions. Recognising that regulations must be nationally appropriate, they also will need to be internationally consistent. As experience shows, in a financially globalised world, uneven regulations across borders will inevitably lead to regulatory arbitrage and defeat of our common regulatory objectives.

Peer reviews are a key element of ensuring internationally agreed standards and policies are being effectively applied to promote a level playing field, enhance efficiency in the financial system and monitor potential new vulnerabilities. This is an area where concrete progress has been made. The FSB published a thematic review on compensation practices in March 2010 and thematic reviews of risk disclosures and of mortgage underwriting and origination practices are underway. We will conduct thematic reviews in the areas of deposit insurance, supervisory intensity and effectiveness, and resolution regimes in the period ahead, and will reassess national progress in addressing compensation practices.

The FSB country peer review of Mexico was published in September 2010 and country reviews of Italy and Spain are scheduled to be completed in early 2011. In addition, several FSB members recently published reports by the International Monetary Fund (IMF) and World Bank which were completed as part of the Financial Sector Assessment Program (FSAP), and other members are scheduled to have updated assessments completed in 2011. This is in keeping with the commitment of FSB members to undergo an FSAP every five years and publish the results. At the same time, the IMF recently decided to make the financial stability assessment component of the FSAP a regular and mandatory part of surveillance for 25 jurisdictions with systemically important financial sectors, most of which are members of the FSB.

The following sections describe in greater detail the measures that have been taken by the FSB and its members to promote financial stability based on the surveys conducted by the FSB Implementation Monitoring Network.

II. Building high quality capital and liquidity standards and mitigating procyclicality

Bank capital and liquidity standards (Basel III)

Strengthening of bank capital and liquidity standards remains a lynchpin of the G20 financial sector reform objectives, and the BCBS and its governing body, the GHOS, have made significant progress in moving the work forward. The design of the new global regulatory framework, often referred to as “Basel III”, was approved at the GHOS meeting on 26 July 2010² and the calibration of the new minimum requirements and capital buffers were approved at the GHOS meeting on 12 September 2010.³ The implementation phase and transitional arrangements were also agreed at the September GHOS meeting.

The new framework fundamentally strengthens the resilience of the banking system through several prudential measures:

- *Considerable enhancement in the quality of capital* – There is much greater focus on common equity, the highest-quality component of bank capital in absorbing losses. The definition of common equity and other regulatory capital components are also strengthened by applying stricter criteria for eligibility and by deducting certain types of assets of questionable quality, such as goodwill, from common equity;
- *Significant increase in the level of capital* – The minimum level of common equity will be increased from 2% to 4.5%. Similarly, the minimum level of Tier 1 capital will be increased from 4% to 6%. On top of this, banks will be required to hold a capital conservation buffer of 2.5% in the form of common equity to withstand future periods of stress;
- *Promotion of the build-up of capital buffers to mitigate procyclicality* – Banks will be required to build-up capital buffers in good times that can be drawn down in periods of stress through two types of capital buffers. The capital conservation buffer of 2.5% (as noted above) will be comprised of common equity; it will impose a constraint on banks’ discretionary distributions such as dividend payments and bonuses, as a bank’s capital level moves closer to the minimum requirements. In addition, the BCBS issued a proposal in July 2010⁴ for a countercyclical buffer of 0 to 2.5% which would be imposed when, in the view of national authorities, excess aggregate credit growth is judged to be associated with an excessive build-up of system-wide risk. The countercyclical buffer will have to be covered with common equity or other fully loss-absorbing capital.
- *Improvement in the risk coverage of the capital framework* – The capital requirements for trading book exposures, complex securitisations, and exposures

² The BCBS 26 July 2010 press release *The Group of Governors and Heads of Supervision Reach Broad Agreement on Basel Committee Capital and Liquidity Reform Package* can be found at <http://www.bis.org/press/p100726.htm>.

³ The BCBS 12 September 2010 press release *Group of Governors and Heads of Supervision Announces Higher Global Minimum Capital Standards* can be found at <http://www.bis.org/press/p100912.htm>.

⁴ <http://www.bis.org/publ/bcbis172.pdf>.

to off-balance sheet vehicles were substantially strengthened.⁵ The BCBS is now finalising rules that will strengthen the capital requirements and risk management standards for counterparty credit risk;

- *Introduction of a leverage ratio as a supplementary measure to the risk-based capital requirements* – In order to help contain the build-up of excessive leverage in the financial system, serve as the backstop to the risk-based capital requirements and help address model risk, a leverage ratio will be introduced with a view to migrating to a Pillar 1 treatment, subject to appropriate review and calibration;
- *Introduction of global minimum liquidity standards* – New global minimum liquidity standards based on the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) will be introduced. The LCR will make banks more resilient to potential short-term disruptions in their access to funding. In addition, the NSFR addresses longer-term structural liquidity mismatches in banks' balance sheets.

In accordance with the G20 Leaders statements, the new bank capital and liquidity standards will be phased in over a timeframe consistent with sustained economic recovery and limited market disruptions, with a transition horizon informed by assessments of the macroeconomic impact of the reforms. Jointly, the FSB and BCBS assessed the macroeconomic implications of the transition to the full implementation of the Basel III reforms and published an interim report⁶ in August 2010. The report provided key inputs to the decision on the implementation phase and transitional arrangements made at the GHOS meeting in September 2010.

- The new definition of capital will be phased in over a period of five years. The standards will be introduced in 2013 and fully implemented on 1 January 2018. Existing public sector injection of capital will be grandfathered until the end of 2017 and capital instruments that no longer qualify for non-common equity Tier 1 capital or Tier 2 capital will be phased out over 10 years beginning 1 January 2013.
- The minimum required level for common equity and Tier 1 capital will be phased in beginning in 2013 and will become effective at the beginning of 2015. This implies that the minimum common equity and Tier 1 capital will increase from the current 2% and 4% levels to 3.5% and 4.5%, respectively, at the beginning of 2013 and to 4.5% and 6%, respectively, at the beginning of 2015.
- The capital conservation buffer of 2.5%, comprised of common equity, will be phased in progressively from 1 January 2016 and will become fully effective on 1 January 2019.
- For the leverage ratio, a parallel run period will begin in 2013 and run until 2017, with a view to migrating to a Pillar 1 treatment on 1 January 2018 based on appropriate review and calibration. Bank level disclosure of the leverage ratio and its components will begin from 1 January 2015.

⁵ The BCBS July 2009 document *Enhancements to the Basel II Framework* can be found at <http://www.bis.org/publ/bcbs157.pdf>.

⁶ The FSB and BCBS interim report *Assessing the Macroeconomic Impact of the Transition to Stronger Capital and Liquidity Requirements* can be found at http://www.financialstabilityboard.org/publications/r_100818b.pdf.

- The LCR will be introduced on 1 January 2015, and the NSFR will be introduced as a minimum standard by 1 January 2018 based on appropriate review and calibration.

The FSB-BCBS macroeconomic impact assessment will continue its analysis using the agreed Basel III framework and prepare a final report by the end of 2010.

Basel II implementation

At the Pittsburgh Summit, G20 Leaders reaffirmed their commitment to adopt the Basel II framework, with all major G20 financial centres to adopt Basel II by 2011 and the other G20 countries progressing toward adoption. Most countries have already fully adopted Basel II, and the remaining countries are still in the process. The effects of the financial crisis became manifest in 2007 and built-up prior to the implementation of Basel II.

Risk management

Standards for risk management have also been raised. The BCBS has strengthened guidance for use in the Pillar 2 *Supervisory Review Process* of Basel II to address key lessons of the crisis covering firm-wide governance, the management of risk concentrations, securitisation exposures, stress testing, valuation practices and exposures to off-balance sheet activities. The BCBS has also published supervisory guidance on sound compensation practices, corporate governance and supervisory colleges as outlined below. National authorities too have strengthened their guidelines for risk management practices including requirements for stress tests. In addition to its standard-setting activities, the BCBS' near-term focus is on the timely and effective implementation of agreed regulatory standards.

The Senior Supervisors Group (SSG), composed of senior financial supervisors of ten countries, has provided an example of the way supervisors can flexibly organise themselves to address in a timely way issues of common interest. The SSG meets several times a year and has provided key contributions in identifying leading practices in areas such as risk management and disclosure.

In October 2009 the SSG issued a report *Risk Management Lessons from the Global Banking Crisis of 2008*⁷ that sets out the results of a self-assessment exercise conducted by twenty global financial institutions to benchmark their own risk management practices against official and industry recommendations that had been issued since the outbreak of the crisis in 2008. The report also incorporated supervisory assessments of risk management practices of a number of the firms. Despite the significant improvement in firms' risk management practices, what emerged from the exercise were ten critical areas of needed improvement that encompassed governance, incentives, internal controls, and infrastructure. While the list was not exhaustive, supervisors believe that without meaningful progress in these areas, any improvements firms made in risk management practices would be undermined. The SSG members are following up, through their individual ongoing supervision, on firms' remediation efforts to improve their risk management practices. The SSG has specific follow-up work underway on IT infrastructure and risk appetite.

⁷ http://www.financialstabilityboard.org/publications/r_0910a.pdf

Leveraging on the guidance and reports from the BCBS, SSG and other international bodies, the national authorities have taken measures to strengthen risk management practices of banks in their jurisdiction. Regulations and supervisory guidance on banks' risk management practices have been tightened and were reviewed to cover new issues that became apparent during the crisis, such as liquidity risk, reputation risk, securitisation, valuation, remuneration and stress testing. In some jurisdictions such as in the US and EU, horizontal stress testing exercises were conducted to assess the resilience of the banking system and take relevant actions if necessary.

III. Addressing systemically important financial institutions (SIFIs) and resolution regimes

The FSB is submitting policy recommendations to the G20 Seoul Summit in November 2010 to address the moral hazard risks posed by systemically important financial institutions (SIFIs). The recommendations suggest that the policy framework for SIFIs should combine:

- a resolution framework and other measures to ensure that all financial institutions can be resolved safely, quickly and without destabilising the financial system and exposing the taxpayer to the risk of loss;
- a requirement that SIFIs and initially in particular global SIFIs (G-SIFIs) have higher loss absorbency capacity to reflect the greater risks that these institutions pose to the global financial system;
- more intensive supervisory oversight for financial institutions which may pose systemic risk;
- robust core financial market infrastructures to reduce contagion risk from the failure of individual institutions; and
- other supplementary prudential and other requirements as determined by the national authorities.

The work is very complex as SIFIs vary in their structures and activities, and hence, in the nature and degree of the risks posed to the global financial system. Furthermore, for some measures, the work will involve legal reforms that may take a number of years to implement. It will also require the national authorities to pursue in a collaborative manner the work programme and processes set out by the FSB. As experience is gained, the FSB will review how to extend the framework to cover a wider group of SIFIs, including financial market infrastructures, insurance companies and other non-bank financial institutions that are not part of a banking group structure.

Increasing the loss absorption capacity of SIFIs

The new bank capital and liquidity framework will have a positive impact on reducing risks at SIFIs. However, these measures are primarily aimed at ensuring that all banks have sufficient loss absorption capacity to meet the risks arising from their own exposures, and not at protecting the system from the negative externalities created by SIFIs. For this reason,

the FSB, in collaboration with the BCBS, is developing a well-integrated approach that is more specifically focused on SIFIs.

The IMF, FSB, and Bank for International Settlements (BIS) submitted a paper⁸ to the G20 Finance Ministers and Central Bank Governors in November 2009 discussing the formulation of guidelines on how the national authorities can assess the systemic importance of financial institutions, markets, or instruments. The paper outlines conceptual and analytical approaches to the assessment of systemic importance. Leveraging on this, work is underway at the BCBS on a methodology to assist the FSB and the national authorities in assessing the systemic importance of financial institutions at a global level, focusing on their size, interconnectedness and substitutability. The International Association of Insurance Supervisors (IAIS) will also conduct similar exercises for the insurance sector.

Drawing on relevant qualitative and quantitative indicators, the FSB and national authorities, in consultation with the BCBS, Committee on the Global Financial System (CGFS), Committee on Payment and Settlement Systems (CPSS), International Organisation of Securities Commissions (IOSCO) and IAIS, will determine by mid-2011 those institutions to which the FSB recommendations for financial institutions that are clearly systemic in the global financial system (G-SIFIs) will initially apply. For these institutions, based on the nature and degree of risks they pose to the global financial system, an additional degree of G-SIFI loss absorbency and the instruments through which this additional loss absorbency can be met will be recommended by December 2011. Depending on national circumstances, this higher loss absorbency could be drawn from a menu of viable alternatives and could be achieved by a combination of capital surcharges, contingent capital and bail-in debt. In some circumstances, the FSB may recognise that further measures, including liquidity surcharges, tighter large exposure restrictions, levies, and structural measures could reduce the risks or externalities that a G-SIFI pose. A Peer Review Council (PRC) will also be established, comprising senior members of the relevant national authorities having G-SIFIs operating as home and host in their jurisdictions, with the aim of assessing whether the measures are being applied consistently on a country-by-country basis and commensurate with the risk posed on a G-SIFI by G-SIFI basis. The PRC will report annually to the FSB.

Improving the intensity and effectiveness of SIFI supervision

Measures are also being considered to enhance the intensity and effectiveness of supervision especially for SIFIs. The FSB, in consultation with the IMF, has developed and submitted to the G20 Finance Ministers and Central Bank Governors in October 2010 recommendations for enhanced supervision based on lessons learned from the supervisory experiences during the crisis.⁹ At present, not all supervisors have adequate mandates, independence and appropriate resources to carry out their supervisory duties to oversee

⁸ The FSB, IMF and BIS November 2009 paper *Guidance to Assess the Systemic Importance of Financial Institutions, Markets and Instruments: Initial Considerations — Background Paper* can be found at http://www.financialstabilityboard.org/publications/r_091107d.pdf.

⁹ http://www.financialstabilityboard.org/publications/r_101101.pdf.

banks' activities. In some cases, supervisory authorities lack powers to carry out early interventions. The FSB recommendations set forth actions needed to resolve these issues.

Improving coordination and cooperation amongst supervisory agencies in the oversight of the most important global financial firms is crucial. Progress has been made with supervisory colleges now in operation for all the large, complex financial groups that the FSB has identified as needing colleges. The BCBS issued a paper in October 2010, *Good Practice Principles on Supervisory Colleges*¹⁰, setting out eight principles which aim to promote and strengthen the operation of supervisory colleges.

Meanwhile, in May 2010, IOSCO published a report *Principles Regarding Cross-Border Supervisory Cooperation*¹¹ which sets forth mechanisms to improve cross-border supervisory cooperation amongst securities regulators.

Improving the capacity to resolve firms in crisis

Any effective approach to addressing the moral hazard risk posed by SIFIs needs to have effective resolution regimes at its base. Such resolution regimes should make it feasible for any financial institution – including globally operating SIFIs (G-SIFIs) – to be allowed to fail without systemic disruptions and without taxpayer losses.

Three complementary sets of actions, each of them necessary, should be adopted to address the issues posed by SIFIs. We need (i) effective resolution regimes and tools; (ii) a framework for cross-border coordination; and (iii) sustained recovery and resolution planning to ensure that SIFIs are at all times resolvable.

The FSB will set out by mid-2011 criteria for assessing the resolvability of SIFIs which should be taken into account in determining the systemic risk of a G-SIFI and the key attributes of effective resolution regimes, including the minimum level of legal harmonisation and legal preconditions required to make cross-border resolutions effective. The work will draw on available principles and recommendations and be undertaken in close cooperation with the BCBS Cross-border Bank Resolution Group (CBRG), IMF, IOSCO, and IAIS. In March 2010, the BCBS issued its final *Report and Recommendations of the Cross-border Bank Resolution Group*¹² which set out recommendations falling into three categories: strengthening national resolution powers and their cross-border implementation; firm-specific contingency planning; and reducing contagion. A number of G20 jurisdictions have adopted legislation or are considering legislation that responds to the CBRG recommendations, including by adopting effective national resolution powers and a framework for coordinated resolution of financial groups within their jurisdictions. In June 2010, the IMF published its proposals¹³ for improving coordination in the resolution of cross-border banks. The IAIS has also initiated work to develop a supervisory paper on crisis management and cross-border resolution of insurance companies.

¹⁰ <http://www.bis.org/publ/bcbs177.pdf>.

¹¹ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD322.pdf>.

¹² <http://www.bis.org/publ/bcbs169.pdf>.

¹³ The 11 June 2010 IMF report *Resolution of Cross-Border Banks—A Proposed Framework for Enhanced Coordination* can be found at <http://www.imf.org/external/np/pp/eng/2010/061110.pdf>.

The FSB will also review restructuring mechanisms, including a statutory or contractual basis for “bail-ins”, debt-to-equity conversions and other innovative tools that can potentially provide for loss absorption by equity holders and creditors to determine their practical, financial, and legal feasibility and market capacity. The FSB will also examine the viability of such mechanisms in national and cross-border contexts. Such mechanisms require that a robust insolvency resolution regime be in place.

Impediments to the effective resolution of a G-SIFI derive from major differences in national resolution regimes and an absence of agreements for joining up home and host regimes in cross-border resolution. Therefore, the FSB recommends that jurisdictions should provide resolution authorities with the legal capacity to cooperate and to share information across borders. For each G-SIFI, there should be institution-specific cooperation arrangements between relevant home and host authorities. The FSB will monitor progress in the establishment of these arrangements.

Under the guidance of the FSB Cross-border Crisis Management Group (CBCM), the major cross-border financial institutions and their national authorities have, over the past year, undertaken to produce recovery and resolution plans (RRPs). While work on RRP is not complete – and indeed needs to be an ongoing undertaking – the work on RRP and related discussion amongst home and host authorities have been a productive beginning. The FSB recommends that RRP that assess an institution’s resolvability be mandatory for all G-SIFIs. The CBCM has identified practices in four technical areas that pose significant impediments to effective resolution. These relate to: booking practices; the use of intra-group guarantees; global payments operations; and information systems. All involve complexity in the structure of cross-border financial institutions, particularly the use of multiple legal entities in the execution of transactions and in the conduct of overall business. The CBCM has begun to explore options to address these problems and will report by end-2011 on practical measures taken to improve resolvability, addressing obstacles associated with booking practices, global payments, intra-group guarantees and information systems.

Strengthening deposit insurance

The BCBS and the International Association of Deposit Insurers (IADI) jointly developed the *Core Principles for Effective Deposit Insurance Systems*¹⁴, which was published in June 2009. The *Core Principles* are designed to be adaptable to a broad range of country circumstances, settings and structures. They are a framework for effective deposit insurance practices and will be included in the revised *FSB Compendium of Standards*. A methodology for the assessment of national deposit insurance systems will be developed by the end of 2010, and the FSB is planning a thematic peer review of the implementation of the *Core Principles* by member jurisdictions in 2011 (see Section VI).

IADI, jointly with the IMF, has reviewed plans to unwind the exceptional level of deposit guarantees provided by some jurisdictions during the crisis, and provided feedback to the FSB. In some countries, deposit insurance schemes have been modified or are under review, and changes are expected to be in line with the *Core Principles*. For instance, the

¹⁴ <http://www.bis.org/publ/bcbs156.pdf>.

European Commission has proposed¹⁵ changes to existing European rules to further improve protection for depositors and retail investors. Furthermore, the European Commission has launched a public consultation on options to improve protection for insurance policy holders, including the possibility of setting up insurance guarantee schemes in all member states. In Switzerland, a significant enhancement of the overall capacity and the establishment of an *ex ante* funding component is under review.

Strengthening core financial infrastructures

The interconnectedness of SIFIs with other market participants, especially other SIFIs, has been a significant factor driving public intervention to prevent failure of SIFIs. The CPSS and IOSCO, together with regional and national authorities, are working to reduce contagion risk through improvements to the robustness of core financial market infrastructures that tie SIFIs together, both as this relates to payment and securities settlement and to central counterparties in the OTC derivatives markets (see Section IV).

Developments at the national and regional level

Efforts to address the moral hazard risk posed by SIFIs are also undertaken by national and regional authorities.

- In the US, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010¹⁶ (Dodd-Frank Act) was enacted in July 2010. Under the Dodd-Frank Act, the FSOC was established with the remit to identify emerging systemic risks and to improve regulatory coordination among the relevant agencies. The Dodd-Frank Act introduces a new framework for the resolution of nonbank financial companies that are determined to be systemically important. While the Dodd-Frank Act provides for firms to be designated as systemically important by the FSOC, the determination that a firm is systemic and should be resolved under Title II of the Dodd-Frank Act would occur near the time of failure through a recommendation by two-thirds of the Board of Governors of the Federal Reserve and two-thirds of the Board of the Federal Deposit Insurance Corporation (FDIC) to the Secretary of the Treasury, who in consultation with the President would make a determination to appoint the FDIC as receiver for the failing firm. The regime provides the FDIC with powers that are similar to the powers the FDIC has as receiver of a failed bank. Specifically, the FDIC has the power to provide loans or guarantees to help stabilise the company. The FDIC also has the power to sell the assets or operations of the company; to transfer the company's assets, liabilities and operations to a "bridge" financial institution established by the FDIC; and to impose losses on shareholders and creditors.
- In the EU, the European Commission is currently preparing proposals for the establishment of an EU-wide crisis management framework. The second

¹⁵ The European Commission *Report from the Commission to the European Parliament and to the Council* can be found at http://ec.europa.eu/internal_market/bank/docs/guarantee/20100712_report_en.pdf.

¹⁶ *A Brief Summary of the Dodd-Frank Wall Street Reform and Consumer Protection Act* can be found at http://banking.senate.gov/public/files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf.

Communication on a new EU framework for crisis management in the financial sector was published in October¹⁷ and will be followed by a legislative proposal in June next year.

- In the UK the special resolution regime (SRR), a statutory toolkit for resolving failing banks and building societies, was established by the Banking Act of 2009. The SRR contains three tools to resolve a failing bank or building society: i) transfer all or part of a failing bank's business (including the deposits) to a private sector purchaser; ii) transfer of some or all of a failing bank's business to a bridge bank – a company owned and controlled by the Bank of England – with a view to a future private-sector sale; and iii) a power for the Treasury to take the failing bank into temporary public ownership. The UK Government is currently considering what improvements may be required to enhance safeguards and overall effectiveness of the regime in the context of proposed changes to the UK's regulatory architecture.
- In Germany, a recent draft Act for the Restructuring and Orderly Resolution of Credit Institutions provides Germany's Federal Financial Supervisory Authority (BaFin) with a range of resolution powers, including the powers to transfer all, or part, of its business to an existing entity or a temporary bridge bank.
- In Switzerland, the special resolution regime is currently being reviewed in order to close gaps identified during the financial crisis. Key amendments will be the introduction of a bridge bank authority and a strengthened legal basis for the conversion of debt into equity (debt-equity swap). In addition, the recognition of foreign insolvency procedures will be facilitated. Finally, the special resolution regime, which so far has applied to banks and securities dealers, will also apply, with certain amendments, to insurance undertakings.
- Japan has necessary resolution regimes based on the Deposit Insurance Law, etc. In principle, as a resolution without making deposit insurance payments, resolution is carried out through selected financial administrators or Bridge Bank System (transfer of insured deposits to the assuming financial institutions and implementation of financial assistance to those institutions). And in the case where there is a risk that the failure of a financial institution will cause a significant adverse effect on the maintenance of stability of the financial system, special resolution is carried out through measures to deal with crisis, including capital injection, protection of total amount of certain liabilities, such as deposits, and temporary nationalisation according to the financial condition of the financial institution.
- The Central Bank of Brazil is currently analysing responses to the 2009 public hearing of a legislative proposal, including a law of preventive measures to be taken by the central bank in order to reduce the probability of failure of financial institutions and facilitate their orderly resolution. It reorganises the deposit insurance agency and allows the central bank to grant loans to them as well as to institutions which work as central counterparts.

¹⁷ http://ec.europa.eu/internal_market/bank/docs/crisis-management/framework/com2010_579_en.pdf.

- In China, the Peoples Bank of China (PBC) is now working on establishing a clearly-layered risk resolution and payment arrangement for SIFIs; strengthening responsibilities of institutions, shareholders and creditors; quickening the establishment of deposit insurance mechanisms; and giving full play of its supportive role as the central bank.

IV. Improving the OTC derivatives markets

To address weaknesses in the infrastructure of the OTC derivatives markets, at the Pittsburgh Summit, G20 Leaders agreed that all standardised OTC derivatives contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties (CCPs) by the end of 2012. They also agreed that OTC derivatives contracts should be reported to trade repositories.

The G20 reaffirmed this commitment at the Toronto Summit and agreed to accelerate the implementation of strong measures to improve transparency and regulatory oversight of OTC derivatives in an internationally consistent and non-discriminatory way. Work is proceeding through initiatives in international bodies, and legislative actions have already been taken in some major jurisdictions that facilitate meeting the deadline agreed by G20 Leaders.

To support implementation of the G20 clearing and trading objectives, in April 2010 the FSB formed the OTC Derivatives Working Group led by representatives of CPSS, IOSCO and the European Commission, to identify factors that make derivatives suitable for clearing and set out policy options to support the consistency of implementation of clearing, trading and reporting requirements across jurisdictions.

The FSB submitted to the G20 Finance Ministers and Central Bank Governors in October 2010 a report on *Implementing OTC Derivatives Market Reforms* that sets out 21 recommendations addressing implementation of the G20 commitments.¹⁸ The report aims to set ambitious targets for fully implementing the G20 commitments, while minimising the potential for regulatory arbitrage. It sets deadlines to meet the end-2012 objectives and specifies bodies to take the recommendations forward. The report is only a step toward consistent implementation of the G20 commitments, and highlights work to be done. The OTC Derivatives Working Group will monitor implementation of these recommendations and provide an initial progress report by 31 March 2011.

Strong standards for and oversight of CCPs are essential if they are to be useful in reducing systemic risk. In May 2010, the CPSS and IOSCO published a consultative report, *Guidance on the Application of the 2004 CPSS-IOSCO Recommendations for Central Counterparties to OTC Derivatives CCPs*¹⁹, to promote consistent application and interpretation of their existing standards for CCPs so as to better address risks associated with clearing OTC derivatives. In parallel, in light of the growing importance of trade repositories, CPSS and IOSCO also published a consultative report, *Considerations for Trade Repositories in OTC Derivatives*

¹⁸ http://www.financialstabilityboard.org/publications/r_101025.pdf.

¹⁹ <http://www.bis.org/publ/cpss89.pdf>.

*Markets*²⁰, which discusses a set of factors that should be considered by trade repositories in designing and operating their services, and by relevant authorities in regulating and overseeing trade repositories. The consultative reports will be reflected in the CPSS and IOSCO comprehensive review of their standards for all financial market infrastructures (FMIs) and a public consultation on the standards for FMIs is expected in early 2011.

Separately, the IOSCO Task Force on Commodity Futures Markets is providing an update to the G20 Seoul Summit on their work on advancing the G20's request to implement the recommendations from this Task Force's March 2009 report²¹ and continue its work consistent with the G20 Pittsburgh Statement on energy and oil markets to:

- Assess the regulatory powers of prudential regulators;
- Collect data to identify and monitor large concentrations of trader positions in national oil markets;
- Collect related over-the-counter (OTC) oil market data;
- Take steps to combat market manipulation; and
- Publish more data to the market by producing a disaggregated data report.

IOSCO also has formed a Task Force on OTC Derivatives Regulation. This Task Force was formed in October 2010, and, with the involvement of other appropriate authorities, will produce a report on exchange and electronic trading of OTC derivatives by 31 January 2011. In consultation with CPSS, the OTC Derivatives Regulators' Forum (ODRF) and other authorities, it also will produce a report by 31 July 2011 on: i) minimum data reporting requirements and standardised formats for reporting to trade repositories and ii) the methodology and mechanism for the aggregation of trade repository data on a global basis.

In addition, prudential and regulatory authorities have been working together since January 2009 through the ODRF, which provides such authorities with a forum to cooperate, exchange views and share information related to OTC derivatives CCPs and trade repositories on a regular basis. The ODRF's objectives are to promote consistent oversight approaches for OTC derivatives CCPs and trade repositories through international cooperative oversight arrangements, and coordinate the sharing of information by CCPs and trade repositories with regulators. Some of the work the ODRF has undertaken is specific to trade repositories, such as defining what authorities consider to be the appropriate functionality for trade repositories and the data that, in turn, should be reported to authorities.

Legislative actions at the national and regional level

Efforts to strengthen the infrastructure of the OTC derivatives markets are taking place at national and regional levels.

- Under the US Dodd-Frank Act, primary regulatory responsibility for OTC derivatives is shared between the Commodity Futures Trading Commission

²⁰ <http://www.bis.org/publ/cpss90.pdf?frames=0>.

²¹ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD340.pdf>.

(CFTC) and the Securities and Exchange Commission (SEC). At a high level, the Dodd-Frank Act requires central clearing for all swaps that the CFTC or SEC, as applicable, determine are required to be cleared. It includes a limited exemption from the mandatory clearing requirement for counterparties that are not financial entities and who also are using swaps to hedge or mitigate commercial risks. Generally, swaps subject to the clearing requirement are required to be traded on an exchange or swap execution facility unless no exchange, or swap execution facility, makes the swap available for trading. Furthermore, the Dodd-Frank Act requires that all swaps, both centrally and non-centrally cleared, be reported to a data repository or, if no data repository will accept the transaction, to the CFTC or the SEC, respectively.

- In the EU, the European Commission's proposal²² on market infrastructures (CCPs and trade repositories) was published in September 2010. This proposal is still subject to amendments by the other European institutions and is likely to be finalised in early 2011. The proposal's objectives are to increase transparency in the OTC derivatives market and reduce counterparty credit risk. To increase transparency, the proposal currently requires that detailed information on OTC derivatives contracts are to be reported to trade repositories and made accessible to supervisory authorities. In addition, it requires that trade repositories publish aggregate positions by class of derivatives. To reduce counterparty credit risk, the proposal introduces stringent rules on prudential, organisational and conduct of business standards for CCPs. It also mandates CCP-clearing for contracts that are eligible and imposes risk management techniques for derivatives that are not cleared by a CCP. The proposal currently provides for some limited exemptions from clearing and reporting requirements for non-financial firms whose positions excluding transactions that are directly linked to commercial activity do not exceed a threshold. Issues concerning trading of OTC derivatives on exchanges or electronic platforms will be dealt within the framework of the review of the Markets in Financial Instruments Directive (MiFID) in 2011. The reform is likely to encompass amendments to require transaction reporting of clearly specified OTC derivatives for market abuse detection purposes to be developed in conjunction with CCPs and trade repositories.
- In May 2010, the Japanese Diet passed a bill amending the Financial Instruments and Exchange Act.²³ Under the new law, CCP clearing will be made mandatory for specific OTC derivatives transactions where the reduction of settlement risk through central clearing would be deemed necessary for the stability of the Japanese market. The exact products included in the central clearing requirement will be specified by Cabinet Office Ordinances. In addition, there will be a mandatory reporting requirement for financial institutions. For trades that are subject to mandatory CCP clearing, the CCP must store the trade information and report it to the regulator. Separately, financial institutions may either submit

²² The European Commission *Proposal for a Regulation of the European Parliament and of the Council on OTC derivatives, Central Counterparties and Trade Repositories* can be found at http://ec.europa.eu/internal_market/financial-markets/docs/derivatives/20100915_proposal_en.pdf.

²³ <http://www.fsa.go.jp/en/refer/diet/174/01.pdf>.

information to the designated trade repository (foreign or domestic), or to the regulator directly. Implementation of the amended law will take place by November 2012.

- In February 2010, the Korean Financial Services Commission organised a task force in cooperation with academia and related agencies to build the infrastructure for OTC derivatives markets, including establishment of a CCP, and make revisions of related laws by 2012.
- The Hong Kong Treasury Markets Association (TMA) has set up a task force to examine issues in connection with the clearing and reporting of OTC derivatives in Hong Kong, including the feasibility to establish a local CCP. A consultation has been conducted to seek industry comments on the subject. The Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) are tasked with the responsibility to determine measures to implement clearing and reporting requirements for OTC derivatives transactions.
- In May 2010 the Singapore Exchange Derivatives Clearing Limited (SGX-DC) ended a public consultation which sought comments on proposed amendments to the SGX-DC Clearing Rules²⁴ that include the introduction of a new trade registration system for the registration of interest rate swaps and Asian foreign exchange forwards.
- In China, the Shanghai Clearing House was established in November 2009, laying the foundation for the centralised clearing of derivatives in the future.
- In addition, several FSB members are analysing the details of US and European legislative changes to ensure they are able to propose harmonising legislative changes in their jurisdictions, or awaiting the outcome of the FSB recommendations to assess whether legislation is required.

V. Strengthening accounting standards

At the Toronto Summit, the G20 Leaders stressed the importance of achieving a single set of high quality, improved global accounting standards, and they called on the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) to increase their efforts to achieve convergence by the end of 2011.²⁵ They also recommended that the IASB institutional framework further increase stakeholder involvement. In addition, at the London Summit in April 2009 the G20 Leaders welcomed the FSB's procyclicality recommendations relating to accounting and called on "accounting standard setters to work urgently with supervisors and regulators to improve standards on valuation and provisioning."

Nearly all FSB member jurisdictions have either adopted IASB standards (International Financial Reporting Standards - IFRS) or have programmes underway to converge with, or

²⁴ <http://www.sgx.com/wps/wcm/connect/145e3800437bb64d876bd75ed7fa9a01/Consultation+Paper+on+DC+Rule+Amendments+for+GCMs%27+Participation+in+OTCF+Clearing.pdf?MOD=AJPERES>.

²⁵ At the Pittsburgh Summit, the G20 Leaders had called on the IASB and FASB to redouble their efforts to complete their convergence project by June 2011.

consider adoption of, IFRS by 2012. The IASB has an extensive programme to further improve the involvement of various stakeholders and dialogue with them, including through enhanced technical dialogue with prudential authorities and market regulators.

In June 2010, the IASB and FASB jointly announced that the Boards had developed a modified strategy that retains the earlier target completion date of June 2011 for most convergence projects but the target completion dates for a few other projects have extended into the second half of 2011. The Boards decided to delay certain project deadlines because stakeholders voiced concerns about their ability to provide high-quality input on the large number of planned major Exposure Drafts (EDs). The SEC Chairman issued a statement that indicated that this action should not impact the SEC's determination in 2011 whether to incorporate IFRS into the financial reporting system for US issuers.

Progress toward FSB recommendations for improved, converged accounting standards can be seen in four main areas.

- *Impairment of financial assets* – The FSB recommended that the IASB and FASB incorporate a broader range of available credit information than existing provisioning requirements, so as to improve transparency of information provided to investors while also potentially helping lessen procyclicality. Both the IASB and FASB have proposed alternative loss provisioning approaches that incorporate more information about credit losses into impairment measurements and provide for earlier assessment of expected losses. The proposals have significant differences from each other and the Boards are seeking to converge their provisioning approaches based on comments received, including from an Expert Advisory Panel.
- *Derecognition* – The FSB had also expressed concern that the IASB's proposal on derecognition, which has been subject to consultation, would require repurchase agreements to be treated as sales and forward contracts in certain situations (thus leading to off-balance sheet treatment), instead of as financing transactions on the balance sheet as under IFRS. The IASB has revised its plans and does not intend to move forward with its proposal at this time. Recent amendments to IASB's disclosure standards are designed to enhance information about risk exposures that remain when a financial asset has been derecognised (e.g. securitised) and are broadly aligned to FASB disclosure requirements.
- *Addressing valuation uncertainty in fair value measurement guidance* – Under current standards, valuation adjustments include, for example, adjustments for model deficiencies highlighted through calibration of the model, liquidity adjustments and credit adjustments. In its report to the London Summit, the FSB recommended that standard setters and supervisors explore whether firms should be required to hold valuation reserves or to otherwise adjust valuations to avoid overstatement of income when significant uncertainty about valuation exists, for example, for financial instruments that are not actively traded. Further enhancements to IASB and FASB fair value measurement standards early next year will align requirements about how to measure fair value, including guidance on measurement when markets become less active, and to address valuation uncertainty.

- *Netting/offsetting of financial instruments* – In reporting to the Pittsburgh Summit, the FSB expressed concern that the differences between the IASB and FASB approaches to the netting/offsetting of financial assets and liabilities can result in significant differences in the total assets of large financial institutions. In response to stakeholders' concerns, including those of the FSB and BCBS, the Boards have decided to issue an ED proposing changes that will seek to address differences in their standards on balance sheet netting of derivative contracts and other financial instruments.²⁶

In recommending to the Pittsburgh Summit that the IASB and FASB develop improved converged standards that would simplify and improve the accounting principles for financial instruments and their valuation, the FSB noted that it was particularly supportive of standards that would not expand the use of fair value in relation to the lending activities (involving loans and investments in debt instruments) of financial intermediaries. The IASB issued IFRS 9 in November 2009 which includes an amortised cost category for financial assets such as loans and certain investments in debt securities.

However, there is a potential for divergent accounting standards for lending activities, a subject of importance for financial stability, due to a FASB proposal in May 2010 to use fair value measurement on the balance sheet and through "other comprehensive income" for loans and investments in debt securities. Under this proposal, changes in fair values of lending instruments would affect reported shareholders' equity, but generally would not be included in profit and loss. In response to FASB's request for feedback from interested parties on the ED, and based upon extensive outreach by the FASB, it appears that the majority of investors and other stakeholders do not agree with the fair value measurement recognition aspects of this proposal as it relates to lending activities, deposits, and other liabilities. The FSB welcomes the enhanced outreach and hopes that the accounting boards' consideration of stakeholders' comments will result in improved and converged approaches in their final standards. The FSB encourages the IASB and FASB to continue their efforts to achieve improved converged financial instrument accounting standards by June 2011.

VI. Strengthening adherence to international supervisory and regulatory standards

The FSB has made good progress in the implementation of its *Framework for Strengthening Adherence to International Standards*²⁷ which was put in place in January 2010. Under the *Framework*, the FSB has completed two peer reviews – a thematic review of compensation and a country review of Mexico – and is on track to complete four more by early 2011. In 2011, the FSB plans to conduct three more country peer reviews – of Australia, Switzerland and Canada – and three thematic reviews – of compensation practices, deposit insurance, and a third topic to be determined. Good progress has also

²⁶ In July, the BCBS agreed on certain design and calibration features for the leverage ratio, which would serve as the basis for testing during the parallel run period, including that Basel II netting rules will be used for all derivatives (including credit derivatives). This is intended to provide a simple way of addressing differences between IASB and FASB standards.

²⁷ http://www.financialstabilityboard.org/publications/r_100109a.pdf.

been made on the FSB's initiative to promote global adherence to international cooperation and information exchange standards.

The framework

Under the *Framework*, the FSB seeks to foster a race to the top, whereby encouragement from peers motivates all jurisdictions to raise their level of adherence to international financial standards. This encouragement takes three forms: leading by example, periodic peer reviews, and establishing a toolbox of measures as part of an initiative to encourage global adherence to international cooperation and information exchange standards.

FSB member jurisdictions have committed to lead by example by implementing international financial standards, undergoing an FSAP by the IMF and World Bank every five years, and disclosing their degree of adherence to international standards. They have also committed to undergo periodic peer reviews and publishing their results.

Promoting global adherence to standards

Responding to the call by the G20 Leaders to promote global compliance with international prudential standards, the FSB launched in March 2010 an initiative to encourage improved adherence to international cooperation and information exchange standards in the financial regulatory and supervisory areas.²⁸ All FSB member jurisdictions, as well as other jurisdictions that rank highly in financial importance globally, are having their adherence to these standards evaluated under this initiative.²⁹

Jurisdictions for which, at present, there is not sufficient evidence of strong adherence to the relevant cooperation and information exchange principles have been invited to engage in a confidential dialogue with the FSB to address information gaps, evaluate actions taken to address areas of weakness and identify an action plan to improve adherence using a toolbox of measures that has been developed for this purpose. Most of these jurisdictions contacted have engaged in dialogue with the FSB, and some have demonstrated sufficiently strong adherence to exit the evaluation process. Several countries have taken actions this year to provide additional evidence of their adherence to the relevant standards, including by requesting new assessments of compliance by the IMF and World Bank, or applying to become a signatory to the IOSCO Multilateral Memorandum of Understanding concerning Consultation and Cooperation and the Exchange of Information. As a result, some are close to completing the process of dialogue. The FSB is currently undertaking evaluations for jurisdictions that were assessed recently by the IMF and World Bank and showed weaknesses in adherence, and it is continuing its efforts to engage with a few other jurisdictions that have not yet responded or have not yet taken the encouraged actions.

A variety of measures have been identified that could be used to promote adherence to international standards under this initiative. The FSB will seek to use positive measures in the first instance, such as policy dialogue and technical assistance. The FSB, in cooperation

²⁸ http://www.financialstabilityboard.org/publications/r_100310.pdf.

²⁹ The three key standards in the regulatory and supervisory area are: the BCBS *Core Principles for Effective Banking Supervision*; the IAIS *Insurance Core Principles*; and the IOSCO *Objectives and Principles of Securities Regulation*. The evaluation focuses on international cooperation and information exchange principles within each of these standards.

with its members and other international bodies, recently completed a review of capacity building initiatives in financial regulation and supervision that helped to identify the scope for reorienting technical assistance to meet countries' requests arising from this initiative. Negative measures are also available as appropriate to promote adherence, including the option of publishing by the end of 2010 the names of non-cooperative jurisdictions in the event that other measures are not achieving sufficient progress.

FSB peer reviews

FSB peer reviews take two forms: thematic and country reviews. Thematic peer reviews focus on the implementation across the FSB membership of specific standards or policies agreed within the FSB. Their aim is to motivate consistent implementation, to learn from cross-country implementation experience, and to assess whether agreed policies have had their intended results.

The first thematic peer review was on compensation practices, and the relevant report³⁰ was published in March 2010. Two thematic reviews are currently underway on risk disclosures and mortgage underwriting practices, and both are scheduled to be published in early 2011. The review on risk disclosures by market participants will follow up on implementation of the recommendations regarding risk disclosures contained in the April 2008 *Report of the FSF on Enhancing Market and Institutional Resilience*.³¹ The review on mortgage underwriting and origination practices will be based on the relevant recommendations made by the Joint Forum in its January 2010 report on the *Differentiated Nature and Scope of Financial Regulation*.³²

The FSB is planning three more thematic peer reviews in 2011. One will be a follow-up review on compensation practices (see Section VII). Another will be on deposit insurance. It will be based on the assessment methodology currently under development for the *Core Principles for Effective Deposit Insurance Systems*.³³ The topic of the third thematic peer review in 2011 is under discussion.

Country peer reviews focus on implementation of relevant standards in a specific member jurisdiction. Country peer reviews follow up mainly on recommendations relating to financial regulation or supervision arising from a recent IMF-World Bank FSAP of the country. The FSB published its first country review in September 2010, on Mexico³⁴, and reviews of Spain and Italy are currently underway. Based on the schedule of recently completed FSAPs, reviews of Australia, Canada and Switzerland are planned for 2011.

Revision of *Compendium of Standards*

A working group has been formed to review the *FSB Compendium of Standards*.³⁵ The Compendium contains both the body of international standards relevant to sound financial

³⁰ http://www.financialstabilityboard.org/publications/r_100330a.pdf.

³¹ http://www.financialstabilityboard.org/publications/r_0804.pdf.

³² <http://www.bis.org/publ/joint24.pdf>.

³³ <http://www.bis.org/publ/bcbs156.pdf>.

³⁴ http://www.financialstabilityboard.org/publications/r_100927.pdf.

³⁵ http://www.financialstabilityboard.org/cos/key_standards.htm.

systems, as well as 12 key standards considered essential to a stable well-functioning financial system. The working group has been tasked with updating the standards featured in the *Compendium*; determining whether any changes should be made to the list of key standards, including in light of the lessons from the crisis; summarising work in progress or plans to update existing standards or develop new ones; and proposing changes to the structure and dissemination of the *Compendium* to improve its visibility and usefulness.

The FSB's key standards and those standards that the IMF and World Bank have endorsed as relevant for their work are identical, and all three bodies are presently reviewing these standards in the light of the crisis.³⁶ The working group will finalise its report in early 2011.

VII. Reforming compensation practices to support financial stability

The FSB launched in December 2009 a review of the steps taken or planned by FSB member jurisdictions to implement the *FSF Principles and Implementation Standards for Sound Compensation Practices* issued in April and September 2009 respectively. The *Principles*³⁷ call for wide ranging private and official sector action to ensure that governance of compensation is effective; that financial firms align their compensation practices with prudent risk taking; and that compensation policies are subject to effective supervisory oversight and engagement by stakeholder. To strengthen adherence and achieve effective global implementation of the principles, the FSB set out specific *Implementation Standards*³⁸ focusing on areas where rapid progress is especially needed and detailing specific proposals on compensation governance, structure and risk alignment, and disclosure.

Thematic review on compensation

The review on compensation³⁹ – the FSB's first thematic review – was published in March 2010 and concludes that considerable progress has been made across the FSB membership in incorporating the FSB *Principles and Implementation Standards* into domestic regulatory and supervisory frameworks. While compensation structures in the major financial firms have changed in a desirable direction, full implementation is far from complete. Sustained efforts by firms and authorities remain necessary to effectively align compensation structures in major financial institutions with prudent risk-taking.

To maintain momentum, the FSB will conduct a further review of implementation in the second quarter of 2011, using more detailed criteria. These criteria will build on work underway in the BCBS, whose Task Force on Remuneration issued in October 2010 a report for consultation on the range of methodologies for risk and performance alignment of compensation schemes.⁴⁰ By that time, more information will be available on which to

³⁶ For background information, see <http://www.imf.org/external/np/sec/pn/2005/pn05106.htm>.

³⁷ http://www.financialstabilityboard.org/publications/r_0904b.pdf.

³⁸ The FSB Principles for Sound Compensation Practices Implementation Standards can be found at: http://www.financialstabilityboard.org/publications/r_090925c.pdf.

³⁹ The March 2010 FSB *Thematic Review on Compensation* can be found at: http://www.financialstabilityboard.org/publications/r_100330a.pdf.

⁴⁰ <http://www.bis.org/publ/bcbs178.pdf>.

judge ongoing changes in the industry and assess the effectiveness of national implementation measures.

The standard setting bodies have set out guidance for public disclosures around compensation issues. IOSCO issued in February 2010 a set of principles for *Periodic Disclosure by Listed Entities*⁴¹ that provide guidance for annual disclosures to help investors to assess the incentives created by compensation and risk management practices, whether compensation incentives are aligned with investors' interests and how performance may be oriented to the returns generated for shareholders. These principles apply to all listed companies. The BCBS has developed a proposal for *Pillar 3 Disclosure Requirements for Remuneration* which aims to ensure that banks disclose clear, comprehensive and timely information about their remuneration practices with the overarching goal of promoting more effective market discipline. Consistency of disclosure requirements should contribute to a greater convergence of practices and promote a level playing field in the industry.

The IAIS also is working to support consistent implementation of the FSB *Principles and Implementation Standards* across jurisdictions. The IAIS released in March 2010 a draft of its *Standards and Guidance on Remuneration* that support the consistent implementation of the FSB *Principles and Implementation Standards* and highlight remuneration issues that are more specific to the insurance industry, such as the nature and complexity of an insurer's risk profile and the alignment with the longer term interests of policyholders and beneficiaries.

Implementation at the national and regional level

Most G20 members have taken or announced action to implement the FSB *Principles and Implementation Standards* issued at the Pittsburgh Summit in September 2009.

- In the US, bank supervisors have issued final supervisory guidance on incentive compensation practices at banking organisations. The guidance requires banks to have practices that give employees balanced risk-taking incentives, to have sound controls for their incentive compensation systems, and improve corporate governance practices related to compensation.
- The Dodd-Frank Act requires several federal financial regulatory agencies to jointly prescribe rules or guidelines that require certain financial institutions to: i) disclose to the appropriate regulator incentive-based compensation structures; and ii) prohibit incentive-based payment arrangements that encourage inappropriate risks to the institution by providing excessive compensation or that could lead to material financial loss to the firm. These rules must be implemented by April 2011.
- In December 2009, the SEC adopted enhancements to its executive compensation disclosure requirements and all publicly-traded issuers in the US had to follow the new SEC disclosures rule as of 28 February 2010.
- At the European level, the European Commission, the European Parliament and the Council have agreed on amendments to the Capital Requirements Directive (CRD

⁴¹ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD317.pdf>.

III) to reflect new rules on bankers' remuneration. Furthermore, the European Commission updated guidance on directors' remuneration first issued in 2004, with a proposed date for implementation of end-2010 and is also working on additional legislative measures on remuneration in non-banking financial services, which is expected to be finalised in 2011.

- The Committee of European Banking Supervisors (CEBS) published in October 2010 a consultation paper on new guidelines on remuneration policies and practices in order to provide guidance both to supervisors and institutions to ensure the implementation of the new risk-related philosophy on remuneration as required by CRD III, which becomes effective in each member state on 1 January 2011.
- As part of the implementation process, the HKMA is formulating its supervisory plans to include a series of thematic on-site examinations during the fourth quarter of 2010 of major banks operating in Hong Kong.
- Other countries, including Australia, Canada, Germany, France, Italy, India, Japan, Netherlands, Singapore, Switzerland and the UK, have incorporated remuneration aspects into existing requirements on risk management and internal controls, or issued national principles and related guidance in implementation of the FSB Principles.

VIII. Developing macroprudential frameworks and tools

International efforts to develop macroprudential frameworks and tools

The FSB and its members are continuing to develop and examine the application of macroprudential tools. These tools aim to reduce risk in the system by dampening the procyclical build-up and contraction of financial activity and by identifying and addressing common exposures and interconnections as sources of systemic risk. As member jurisdictions are introducing frameworks for macroprudential policies and system-wide oversight (as illustrated below), the FSB will facilitate the sharing of information and experience among its members in areas such as: structures and processes; surveillance analysis and tools; powers to issue recommendations; relations with other authorities; and communication strategies. The FSB, in consultation with the BIS and the IMF, will further consider the scope to develop principles for effective macroprudential policies.

Work is progressing toward developing various tools to monitor and assess the build-up of macroprudential risks in the financial system, and to mitigate such risks on a number of fronts.

- In April 2009, the FSB submitted a report to G20 Leaders setting out a range of policy recommendations for addressing procyclicality in the financial system. The report recommended the development of a countercyclical buffer and a leverage constraint within the bank capital framework; a move from an incurred to an expected loss basis to facilitate earlier loss provisioning within accounting standards; a review of the scope to dampen cyclicality in margining practices; and adjustments for valuation uncertainty in the application of fair value accounting. The follow-up on these recommendations are described below.

- In November 2009, the IMF, FSB, and BIS submitted a paper⁴² to G20 Finance Ministers and Central Bank Governors setting out guidance for assessing the systemic importance of financial institutions, markets, or instruments. The paper has provided a useful identification framework for the work on the “too big to fail” (TBTF) problems associated with SIFIs and also provides a foundation for continuing work on assessing the systemic importance of financial institutions at the FSB and the BCBS.
- In July 2010, the BCBS issued proposals to introduce countercyclical capital buffers that are built up in good times and that can be released in economic downturns. The proposal complements the capital conservation buffer in the new capital framework, the primary objective of which is to ensure that banks that approach the minimum do not pay out capital and further deplete their reserves.
- As described in Section V, both IASB and FASB have issued exposure drafts for expected loss provisioning approaches that will facilitate earlier recognition of credit losses, and thus, help to dampen procyclicality.
- The CGFS conducted a stock-taking exercise to review the issues and experience related to the design and implementation of macroprudential policy. The results⁴³ were published in May 2010. The CGFS also published a report⁴⁴ in March 2010 on the role of margin requirements and haircuts in contributing to procyclicality in the financial system. The report sets out policy options directed at margining practices to dampen the build-up of leverage in good times and soften the systemic impact of the subsequent deleveraging.
- The IAIS has conducted an analysis of the characteristics of systemic risk for the insurance sector. On the basis of this analysis, the IAIS is promoting macroprudential monitoring of potential build-up of systemic risk and planning to develop measures for national authorities to assess degrees of systemic risk.
- The IOSCO published in June 2010 revised *Objectives and Principles of Securities Regulation*⁴⁵ to incorporate eight new principles, based on the lessons learned from the recent financial crisis and subsequent changes in the regulatory environment. The new principles recognise the need for regulators to be conscious of systemic risk and the role they play in relation to it.
- Initiatives to strengthen core financial infrastructures will lower the risks of contagion in the event of financial institution’s failure. The work outlined in Section IV to improve the infrastructure for the trading and clearing of OTC derivatives markets is an essential element.

⁴² The October 2009 FSB, IMF and BIS paper *Guidance to Assess the Systemic Importance of Financial Institutions, Markets, and Instruments: Initial Considerations* can be found at http://www.financialstabilityboard.org/publications/r_091107d.pdf?frames=0.

⁴³ The May 2010 CGFS report *Macroprudential Instruments and Frameworks: A Stocktaking of Issues and Experiences* can be found at <http://www.bis.org/publ/cgfs38.pdf?frames=0>.

⁴⁴ The March 2010 CGFS report *The role of Margin Requirements and Haircuts in Procyclicality* can be found at <http://www.bis.org/publ/cgfs36.pdf>.

⁴⁵ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD323.pdf>.

Considerable work is also underway to improve the information base for macroprudential analysis of the risks in the financial system. The IMF and FSB have collaborated to produce a report on *The Financial Crisis and Information Gaps*⁴⁶ in response to a recommendation from the G20 Working Group on Reinforcing International Cooperation and Promoting Integrity in Financial Markets. The report sets out priorities and offers twenty recommendations for strengthening data collection, with the goal of improving the ability of policymakers and market participants to assess emerging systemic risks and to develop effective responses. The report also emphasises the importance of flexibility and prioritisation to take account of each jurisdiction's level of statistical development and resource constraints. The IMF and FSB reported to the G20 Finance Ministers and Central Bank Governors in June 2010 on their progress, with a concrete plan of action including a timetable to address each of the outstanding recommendations. The next progress report to the G20 is due in June 2011.

System-wide oversight arrangements at national, regional and international levels

Efforts to strengthen system-wide oversight and macroprudential policy arrangements are taking place at national, regional as well as the international levels.

- In the US, the Dodd-Frank Act established the FSOC, which will provide comprehensive oversight over the stability of the US financial system and is charged with identifying threats to the financial stability of the US. Stricter prudential standards will be applied to firms that are judged to be systemically important.
- In the EU, the ESRB is being created, with responsibility for the macroprudential oversight of the EU financial system as a whole. The ESRB will provide early warning of risks, recommend actions to address them and monitor compliance with its recommendations. European authorities to whom recommendation are addressed will need to provide information on the actions undertaken or explain why no action has been taken.
- In France, the recently adopted bill on financial and banking regulation has created a Financial Regulation and Systemic Risk Council with all sectoral regulators and the Banque de France under the presidency of the Minister for Finance, responsible for identifying systemic risks and facilitating the cooperation between authorities.
- In the UK, the government has announced plans to give the Bank of England (BoE) control of macroprudential policies and of prudential supervision.
- In May 2010, the Japanese Diet passed a bill amending the Financial Instruments and Exchange Act which includes: introducing regulation and supervision on a consolidated basis for securities companies above a certain scale; and introducing prudential standards on a consolidated basis for insurance groups.
- National frameworks have been reviewed in the number of other jurisdictions and amendments have been made or planned. For example, in India a high-level Financial and Stability and Development Council has been announced with

⁴⁶ http://www.financialstabilityboard.org/publications/r_091107e.pdf.

responsibility for macroprudential supervision. The Financial System Stability Council was set up in Mexico to identify risks that may disrupt the functioning of the financial system, assess the macroprudential policies to mitigate their impact and identify the vulnerabilities of the financial system and the economy that may eventually have a significant negative impact on the development of the financial system. The Systemic Risk Coordination Committee has been established in Turkey.

- Powers of national authorities to gather relevant information on all material financial institutions, markets and instruments in order to assess the potential for failure or severe stress that contribute to systemic risk have been strengthened. In Australia, for example, legislation was amended to provide Australian Prudential and Regulatory Authority (APRA) with the power to collect data from any entity providing financial services for the purposes of enabling any financial sector agency to perform its functions or exercise its powers. In the UK, the Financial Services Authority (UKFSA) was granted new information gathering powers by the Financial Services Act 2010. In the US, the new US Treasury Office of Financial Research may require reporting from any financial company to assess the extent to which it poses a threat to financial stability.
- Internationally, the IMF and the FSB have put in place a joint Early Warning Exercise, presented twice yearly to senior policy makers and covering economic, macro-financial and financial system risks.

IX. Expanding and refining the regulatory perimeter

Gaps in the scope of regulations

The Joint Forum published a report⁴⁷ in January 2010 which analysed key issues arising from the differentiated nature of financial regulation in the international banking, insurance and securities sectors. It also addressed gaps arising from the financial regulation in order to help ensure that the scope and the nature of financial regulation are appropriate and as consistent as possible. As a follow-up to the report, the FSB is currently conducting a review of mortgage origination and underwriting practices, covering regulated and unregulated entities. For the insurance sector, the IAIS is developing a guidance paper on the treatment of unregulated entities which will take into account lessons learned from the crisis in this area.

A number of initiatives are also undertaken at the national level to review the adequacy of domestic regulation and fill regulatory gaps, including as part of broader financial sector reform proposals. In France, for example, the banking and insurance authorities were merged to establish the Prudential Supervisory Authority (ACP) in January 2010 notably to strengthen financial stability by creating a supervisory authority capable of monitoring risks across the financial sector and eliminating “blind spots” in the monitoring. South Africa has also formed an interagency working group to review the current scope of regulation and make proposals to change regulations.

⁴⁷ The January 2010 Joint Forum report *Review of the Differentiated Nature and Scope of Financial Regulation Key Issues and Recommendations* can be found at <http://www.bis.org/publ/joint24.pdf>.

Drawing on these works at the international and national level, the FSB will assess the appropriateness of the regulatory scope, and expand the regulatory perimeter to activities outside the banking sector, namely the shadow banking sector. In particular, as regulatory requirements on the banking system tighten, the need intensifies for more systematic attention to activities in the shadow banking sector. This sector remains a large part of our financial system and continues to play an important role in credit intermediation and liquidity transformation, but resides outside the rigorous capital and liquidity regulatory framework that applies to banks.

Hedge Funds

In February 2010, IOSCO published a template⁴⁸ for the global collection of hedge fund information to enable the collection and exchange of consistent and comparable data among regulators and other competent authorities, and facilitate international supervisory cooperation in identifying possible systemic risks posed by this sector. The first data gathering exercise is being carried out on a best efforts basis (given the status of legislation in many jurisdictions) reflecting the situation as of September 2010. IOSCO is also conducting a broad review of implementation of its principles for the regulation of hedge funds adopted in June 2009 and is developing a methodology for assessing their implementation. IOSCO's revised *Objectives and Principles of Securities Regulation*⁴⁹ published in June 2010 include a new principle that "(r)egulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight."

Legislation to establish registration, reporting and oversight arrangements for hedge funds/advisers has advanced in most G20 jurisdictions. Importantly, dialogue between the EU and the US should continue – bilaterally and through the FSB and IOSCO – to achieve an appropriate level of consistency across national and regional initiatives and avoid regulatory arbitrage or disadvantaging cross-border participants, while respecting the principles of non-discrimination.

- The US Dodd-Frank Act eliminates the "private fund investment adviser" exemption and subjects nearly all advisers to private funds to registration and record-keeping requirements. It also requires hedge fund advisers with assets under management above a certain threshold to register with the SEC. Fund advisers are required to report on funds' leverage, counterparty exposure and other such information as deemed necessary by the supervisors for the assessment of systemic risk. As discussed above, the Dodd-Frank Act also provides for prudential safeguards for any hedge fund that may be identified as systemically relevant.
- The European Commission proposed a Directive on Alternative Investment Fund Managers⁵⁰ in April 2009 to improve macroprudential oversight of the sector, increase transparency and strengthen investor protection. The proposed Directive, which has been agreed in the Council of Ministers is expected to be formally approved by the European Parliament in November, will require managers to be

⁴⁸ The 25 February 2010 IOSCO press release *International Regulators Publish Systemic Risk Data Requirements for Hedge Funds* can be found at <http://www.iosco.org/news/pdf/IOSCONEWS179.pdf>.

⁴⁹ <http://www.compliance-exchange.com/governance/library/ioscoprinciples2010.pdf>.

⁵⁰ http://ec.europa.eu/internal_market/investment/alternative_investments_en.htm.

authorised and supervised, to report regularly to competent authorities on their major exposures and use of leverage, and to comply with a series of ongoing operational and organisational requirements. Once adopted, the Directive will require transposition into the national legal systems of the Member States.

- In Japan, the Financial Services Agency (JFSA) published in January 2010 the *Development of Institutional Frameworks Pertaining to Financial and Capital Markets*⁵¹, which includes policy guidance on collaboration with other countries with regard to the reports made by hedge fund managers to the JFSA. In addition, in March 2010, the JFSA revised and enforced *Guidelines for Supervision* in order to expand operators and items for the fund monitoring survey to strengthen the collecting of fundamental information on various funds.
- The Monetary Authority of Singapore (MAS) is reviewing the regulatory regime for fund managers. In April 2010, the MAS issued a *Policy Consultation on Review of the Regulatory Regime for Fund Management Companies and Exempt Financial Intermediaries*⁵² detailing new proposals aimed at enhancing supervisory oversight over fund managers and raising the quality of new entrants to the industry. The MAS has received industry feedback and issued a response in September 2010, and will effect the changes to the regulatory regime through legislation in 2011.
- A small number of G20 countries reported that they do not have a specific regulatory framework for hedge funds, largely because hedge funds are not of systemic importance in their domestic financial systems. Other factors may be that they do not see a need for a specific regulatory framework for the protection of professional investors.

Credit rating agencies (CRAs)

Increased transparency

The revised *IOSCO Code of Conduct Fundamentals for Credit Rating Agencies (IOSCO Code of Conduct)*⁵³ has been substantially implemented by the major rating agencies. It asks CRAs to make clear, in a prominent place, the limitations of ratings of financial products with limited historical data upon which to base the rating. It also requires credit rating agencies (CRAs) to: i) adopt reasonable measures so that the information they use in assigning a rating is of sufficient quality to support a credible rating; ii) establish a review function to examine the feasibility of rating new products that are materially different from those already rated; and iii) refrain from rating where the complexity or structure of a new structure products or the lack of robust data on underlying assets raise serious questions as to whether CRAs can determine a credible rating. In addition, it calls for CRAs rating structured products to provide information about their analysis to allow investors to understand the basis for the rating and calls upon CRAs as an industry to encourage structured finance issuers and originators to publicly disclose all relevant information

⁵¹ <http://www.fsa.go.jp/en/news/2010/20100122-3/01.pdf>.

⁵² http://www.mas.gov.sg/resource/publications/consult_papers/2010/Policy_Consultation_on_Review_of_the_Regulatory_Regime_for_Fund_Management_Companies_and_Exempt_Financial_Intermediaries_edit.pdf.

⁵³ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf>.

regarding these products in order to allow investors and other CRAs to conduct their own independent analyses.

At the London Summit, G20 Leaders agreed that the regulatory oversight regime of CRAs, consistent with the *IOSCO Code of Conduct*, should be established by end-2009. Following this commitment, national and regional initiatives have been taken or are underway to strengthen oversight of CRAs:

- In the US, the SEC approved rules implementing a regulatory oversight regime for nationally recognised statistical rating organisations (NRSROs) in June 2007 that established registration, recordkeeping, financial reporting and oversight rules for CRAs that apply to be registered with the SEC. These rules are consistent with the *IOSCO Code of Conduct*. The SEC adopted amendments to its NRSRO rules twice in 2009 and has proposed an additional set of amendments. In addition, the Dodd-Frank Act includes a number of provisions designed to strengthen the SEC's regulatory oversight of NRSROs and to foster accountability, transparency, disclosure, and competition in the credit rating industry as well as to address conflicts of interest at NRSROs.
- In the EU, regulation introducing oversight and supervision of CRAs entered into force in December 2009 broadly based on the *IOSCO Code of Conduct*. This requires all CRAs established in the EU, and those based in third countries who wish their ratings to be used for regulatory purposes in the EU, to be subject to registration and supervision within the EU. The Committee of European Securities Regulators (CESR) has also issued guidance on various topics including the registration process and supervisory practices for CRAs. With the framework of the EU supervisory and regulatory reform underway, the new European Securities and Markets Authority would be in charge of the registration and supervision of CRAs in the EU.
- In Japan, the new CRA regulations became effective in April 2010.⁵⁴ The new regulations, consistent with the *IOSCO Code of Conduct*, introduced a registration regime for CRAs and include an operational control system requirement to ensure adequate quality control and address conflicts of interest, as well as disclosure requirements for registered CRAs. Registered CRAs are also under a supervision and inspection programme of the JFSA. Furthermore, in order to facilitate implementation of a new requirement for broker-dealers to provide explanations when soliciting customers using ratings by unregistered CRAs, a Designated CRA-Group Supervisory System will become effective in January 2011, which enables investors to access sufficient information through registered CRAs within a designated CRA-group.
- The Canadian Securities Administrators published a rule for comment that proposes a regulatory oversight framework for CRAs, which will include a reliance on the *IOSCO Code of Conduct*. Legislative amendments will be required in this regard.

⁵⁴ <http://www.fsa.go.jp/en/news/2010/20100331-4.html>.

- Effective 1 January 2010, CRAs in Australia were licensed. As a condition for its license, CRAs were required to comply with the *IOSCO Code of Conduct*.
- A new law became effective in Korea in October 2009 to impose on CRAs duties of establishing and complying with internal control standards, including an internal process to ensure appropriateness of credit ratings and strengthened duty of preventing conflicts of interest.

While these regulatory programs are each consistent with the *IOSCO Code of Conduct*, attention is needed to avoid requirements coming into place in different jurisdictions that fragment rating markets or impose unnecessary burdens on CRAs. At the request of the FSB, the US, EU and Japan have been continuing their discussions to identify conflicts between CRA regulatory regimes and seek appropriate resolutions consistent with the IOSCO principles. In May 2010, IOSCO issued for public consultation a report⁵⁵ reviewing CRA supervisory initiatives in several of its member jurisdictions in order to evaluate whether, and if so how, these regulatory programs implement the *IOSCO Statement of Principles regarding the Activities of Credit Rating Agencies (IOSCO CRA Principles)*.⁵⁶ The report concluded that although the structure and specific provisions of CRA regulatory programs may differ, the objectives of the *IOSCO CRA Principles* are embedded into each of the programs and appear to be the building blocks upon which the CRA regulatory programs have been constructed.

Reducing reliance on CRAs

At the Toronto Summit, the G20 Leaders built on their commitment at the London Summit and agreed to reduce reliance on external ratings in rules and regulations. Work is underway both at the FSB and the BCBS to reduce, where possible, the use of external ratings by the official sector.

The FSB has developed high-level principles to reduce reliance on external ratings in central bank operations; prudential supervision of banks; internal limits and investment policies of investment managers; private sector margin agreements; and disclosures by issuers of securities. The FSB high level principles were submitted to the G20 Finance Ministers and Central Bank Governors in October 2010.⁵⁷ The goal of the principles is to reduce the cliff effects from changes in CRA ratings that can amplify procyclicality and cause systemic disruption. The principles aim to catalyse a significant change in existing practices, setting out in broad terms the direction of change needed and asking standard-setters and regulators to follow up with defining the more specific actions that will be needed to implement the changes.

The BCBS is working to address a number of negative incentives arising from the use of external ratings in the regulatory capital framework. It is especially focusing on i) review of hierarchy of approaches for securitisation that currently favours external ratings; ii) cliff effects in the capital requirements associated with the use of external ratings; and iii) due diligence when using external ratings.

⁵⁵ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD319.pdf>.

⁵⁶ <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD151.pdf>.

⁵⁷ http://www.financialstabilityboard.org/publications/r_101027.pdf.

National and regional authorities have also taken steps to lessen undue reliance on ratings in rules and regulations or are considering ways to do so. For example, in the US, the Dodd-Frank Act removes references to credit ratings from certain US statutes and requires each federal agency to the extent applicable, to review any regulation issued by the agency that requires the use of an assessment of the creditworthiness of a security or money market instrument, modify the regulations to remove any reference to or requirement of reliance on external credit ratings and substitute a standard of credit-worthiness as appropriate. Each agency is required by July 2011 to submit a report to the Congress describing any modifications made to the regulations. As part of the ongoing initiative to reduce reliance on credit ratings, Japan removed the requirement of credit ratings for the Shelf Registration System in April 2010, and also requires issuers since January 2011 to provide, in their disclosure documents at the time of offering, explanations regarding credit ratings in the case where credit ratings are obtained from registered CRAs. Meanwhile, the pension fund system reform of 2008 in Argentina reduced pension fund regulators' reliance on external credit ratings, particularly for investments in production and infrastructure that contribute to long-term growth. Challenges nonetheless remain in this area, not least in identifying objective alternatives to CRA ratings.

Securitisation

Re-establishing securitisation on a sound basis remains a priority in order to support provision of credit to the real economy and improve banks' access to funding in many jurisdictions. Numerous initiatives by regulators, central banks and the private sector to improve market practices have been undertaken with the aim of rebuilding investor confidence, and there are now mixed signs of recovery, but progress remains slow. Understanding whether, and what kind of, additional action may be needed is critical to restoring capacity and liquidity in securitisation markets.

International efforts to improve transparency and the alignment of incentives in the area of structured finance are ongoing. The BCBS issued in July 2009, *Enhancement to the Basel II Framework*⁵⁸, that introduced higher risk weights for complex securitisation exposures to better reflect the risk inherent in these products and has also required banks to conduct more rigorous credit analyses of securitisation exposures especially if externally rated. It also strengthened disclosure requirements for banks under the Pillar 3 in several key areas including securitisation exposures in the trading book; sponsorship of off-balance sheet vehicles; resecuritisation exposures; and pipeline and warehousing risks. The new enhancements will be implemented by the end of 2011. The FSB thematic review on risk disclosures will also examine the steps taken by FSB member jurisdictions on implementing the enhanced Pillar 3 disclosures by the end of 2011.

Meanwhile, in April 2010, IOSCO, which published recommendations on enhancing securitisation practices in September 2009⁵⁹, published disclosure principles for asset-backed securities.⁶⁰ The Joint Forum is also undertaking a study analysing the potential

⁵⁸ <http://www.bis.org/publ/bcbs157.pdf>.

⁵⁹ The September 2009 IOSCO final report *Unregulated Financial Markets and Products* can be found at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD301.pdf>.

⁶⁰ The April 2010 IOSCO final report *Disclosure Principles for Public Offerings and Listings of Asset-Backed Securities* can be found at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD318.pdf>.

impact of current and proposed regulatory reform proposals on the incentives of those participating in securitisation markets. The study seeks to contribute to the development of a co-ordinated suite of policy responses and indicate possible areas for regulatory action. The Joint Forum plans to submit a report to its parent committees (BCBS, IAIS, and IOSCO) by mid-2011.

National and regional measures have also been introduced to improve securitisation markets. It is important that these initiatives are harmonised wherever possible. Measures include changes confirmed by the European Central Bank (ECB) in April 2010 and similar changes proposed by the BoE in March 2010 to their collateral eligibility rules requiring greater transparency, including loan-level data and reporting of information in a standardised format. The BoE has further proposed that cash-flow models be made publicly available. Similarly, in the US, the SEC proposed rules in April 2010 that would require publishing computer programs of contractual cash-flow provisions as well as asset-level disclosure and changes to the offering process. The FDIC has also adopted a rule with conditions on securitisation structures in order for such transactions to receive safe harbour treatment in the event of bank insolvency. The proposal is designed to complement the proposal put forth by the SEC.

Legislative and regulatory measures in major jurisdictions have been proposed or implemented that would require originators of securitisations to retain a minimum level of ownership with the aim of better aligning incentives such as in the EU and the US. In the US, the Dodd-Frank Act requires that securitizers retain certain credit risk. In October 2010, the Federal Reserve Board of Governors published its report to the Congress analysing the impact of various risk retention and incentive alignment practices for individual classes of asset-backed securities both before and after the recent financial crisis.⁶¹ Also as required by Dodd-Frank Act, the SEC proposed implementing rules in October 2010 that would require issuers of ABS and the CRAs that rate them to provide new disclosures about representations, warranties and enforcement mechanisms⁶² as well as rules that would require issuers of ABS to conduct a review of underlying assets and make public any asset review reports produced by third parties.⁶³

Despite the substantial efforts to improve these markets, securitisation issuance volumes remain significantly below pre-crisis levels. The FSB continues to monitor developments in this area and consider what further actions could assist the development of more robust securitisation markets, including what could be done to encourage the return of a stable investor base.

⁶¹ <http://federalreserve.gov/boarddocs/rptcongress/securitization/riskretention.pdf>.

⁶² <http://www.sec.gov/rules/proposed/2010/33-9148.pdf>.

⁶³ <http://www.sec.gov/rules/proposed/2010/33-9150.pdf>.