

FINANCIAL STABILITY FORUM

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Press release

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Financial Stability Forum urges continued efforts to address vulnerabilities in the international financial system

The Financial Stability Forum (FSF) held its fourth meeting on 7-8 September 2000 at the Bank for International Settlements (BIS) in Basel, Switzerland. Members exchanged views and shared perspectives on vulnerabilities to the stability of the international financial system.

The FSF reviewed progress in implementing the recommendations of the reports on highly leveraged institutions (HLIs), capital flows, and offshore financial centres (OFCs) that were endorsed by the Forum at its previous meeting in Singapore (see FSF press release, 26 March 2000, at www.fsforum.org). It welcomed the considerable progress being made in a wide range of areas, and emphasised the importance of keeping up the momentum in ongoing implementation efforts, including concrete actions by national authorities and the private sector. The FSF will continue to monitor progress in implementation of the reports' recommendations at its future meetings.

The FSF welcomed the IMF Executive Board's decision to undertake the OFC assessment and assistance program proposed following the recommendations of the FSF (see www.imf.org). Although the FSF welcomed the steps announced by certain OFCs to improve supervisory, regulatory, co-operation and information exchange policies and practices, it encouraged OFCs to undertake external assessments of their observance with relevant international standards in these areas, noting that assisted self assessments can play an important preparatory step to understanding the areas in which improvements are necessary. The FSF encourages OFCs to disclose assessment findings as a means of demonstrating progress towards meeting such standards. Forum members reiterated their commitment to provide resources to the IMF for conducting assessments, in conjunction with the World Bank as appropriate, and to assist OFCs in their efforts to strengthen supervisory, information sharing and co-operative practices.

The FSF also:

- endorsed recommendations on market and official *incentives to foster implementation of international standards* to strengthen financial systems put forward by a group headed by Axel Nawrath, Director General, Ministry of Finance, Germany. The key findings and recommendations of the group's report are attached; the full report will be posted on the FSF web site shortly;
- reviewed progress being made in developing international guidance on deposit insurance schemes by the working group headed by Jean Pierre Sabourin, President of the Canada Deposit Insurance Corporation, and welcomed the broad consultative underway;
- discussed implications of e-finance for supervision, regulation and market functioning, and decided to establish a contact group of relevant international groupings and representatives from key financial centres to monitor developments and potential concerns; and

- considered a range of other international financial issues, including consolidation and conglomeration in the financial industry, developments affecting market liquidity, and progress in revising the Basel Committee's Capital Accord.

Note for editors

Initiated in February 1999, the FSF aims to promote international financial stability through enhanced information exchange and co-operation in financial sector supervision and surveillance. It brings together on a regular basis, representatives from national authorities responsible for financial stability in significant international financial centres, international financial institutions, international supervisory and regulatory bodies, and central bank expert groupings. The FSF is chaired by Andrew Crockett, General Manager of the BIS, in a personal capacity.

For further information on the FSF, its membership, working group reports, and previous FSF meetings please, visit the FSF web site at www.fsforum.org.

Report of the Follow-Up Group on Incentives to Foster Implementation of Standards

Key Findings and Recommendations

1. Implementation of international standards is a key component of efforts to strengthen domestic economic and financial systems and promote international financial stability.
2. *Market incentives* can encourage national authorities, and where relevant, the private sector, to implement international standards, provided certain preconditions are met. Consultations with market participants make clear that efforts are needed on many fronts to establish these preconditions.
3. Given their recent origin, most market participants are not very familiar with either the 12 standards recognised by the FSF as key to sound financial systems or the Fund-Bank *Reports on Observance of Standards and Codes (ROSCs)*. Thus, few market participants to-date explicitly take account of an economy's observance of standards in their lending and investment decisions, or use ROSCs directly for risk assessments leading to pricing and allocation decisions. However, there is implicit consideration of information on observance of standards insofar as market participants look at features of the economy covered by the 12 key standards, and interest in making greater use of standards and ROSCs as more information on them becomes available.
 - FSF members should mount a sustained education effort to help raise the general level of awareness of standards in their respective financial centres, drawing on resources and expertise from the international financial institutions (IFIs) and standard-setting bodies,
 - The FSF should encourage the IFIs and standard-setting bodies to enhance further their ongoing efforts to help raise the level of awareness of relevant standards. More active marketing is needed than merely placing information on websites.
 - The FSF should encourage the IFIs, standard-setting bodies, and national authorities to better demonstrate how information on observance of standards can help provide insights on the risk factors that market participants are most interested in. This would include using their outreach programmes to clarify the role of standards in strengthening financial systems, emphasising that standards have been developed in response to past crises and undertaking analytical work on the links between observance of standards and potential vulnerabilities.
 - The FSF should encourage: (a) the IFIs and standard setting bodies to enhance the availability of information on observance of standards; and (b) the IFIs to enhance the presentation of ROSCs taking recent feedback into consideration. FSF members should make a commitment to disseminate information on assessments they might undertake.
4. *Official incentives* can be a powerful means to encourage economies to implement standards and to reinforce market incentives. A three-pronged approach is proposed.
5. First, since achieving observance of all 12 key standards would be very demanding for many economies, emphasis could be placed on incentives that are aimed at *encouraging economies to adopt standards and credible implementation plans*. External assessments of economies' observance of standards are necessary for market incentives and most official incentives to work; self-assessments might be a useful preparation for external assessments. Policy dialogues can provide effective peer pressure and assistance, and impetus for reform. Technical assistance and training can help economies build the capacity to implement standards and foster country ownership and buy-in.

- The FSF should encourage the efforts of the IFIs and standard-setting bodies in enhancing the conduct of *external assessments*, including those standards among the 12 key standards not currently included in the assessment programme. FSF members could demonstrate leadership by undertaking assessments of their own observance with relevant standards.
 - The FSF should encourage the IFIs to consider how the mechanism for *policy advice* could be further enhanced, e.g. through giving greater weight to standards implementation issues within the IMF Article IV consultation process and the Fund-Bank *Financial Sector Assessment Programme (FSAP)*.
 - The FSF should encourage relevant international and regional groupings to promote *peer discussions* of progress in implementing standards, using ROSCs where appropriate.
 - FSF members should make a commitment, and encourage other economies as well, to provide *technical assistance and training* for standards assessments and implementation, co-ordinated either bilaterally or through the IFIs and relevant international groupings, on the basis of assessed needs.
6. Second, incentives aimed at *promoting market discipline and disclosure of assessments* can help raise market participants' awareness of the role of standards, foster market demand for information on observance of standards, and place the onus on market participants to price the risks arising from material gaps in observance.
- FSF members should make a commitment to disseminate information on assessments of observance of relevant standards.
 - FSF members should encourage the voluntary disclosure in prospectuses for international sovereign bond issues of material information on observance of relevant standards in the issuing economy and the use of similar information in financial institutions' risk assessment processes (e.g. in banks' internal credit ratings).
7. Third, market access measures and regulatory and supervisory actions aimed at *encouraging observance of relevant standards and disclosure of assessments* can be enhanced by building on current practice in many jurisdictions.
- FSF members should give greater consideration to a foreign jurisdiction's observance of standards as one of the factors in making *market access* decisions, and in the *supervision and regulation* of (a) subsidiaries or branches of institutions from that jurisdiction; or (b) domestic institutions dealing with counterparties in that jurisdiction.
8. The implementation of the above recommendations will call for the commitment of substantial additional resources from the international community. The FSF should monitor the implementation and effectiveness of these recommendations. It is proposed that members of the Forum report progress in implementation on an ongoing basis.