

The Global Regulatory Reform Programme

**Jason George
Member of Secretariat**

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Agenda

- Introduction
- Background on the FSB
- The SIFI problem
- Other major workstreams of the FSB

The Challenges of a Globalised World

- How to build an *efficient and safe global financial system*
- How to ensure a reasonably *level playing field*
- How to *promote safety and soundness* without discouraging innovation and market discipline
- How to *reduce systemic risk globally*

...reforms of the international financial architecture are needed

- A global systemic risk regulator?
(Hemerijik, 2010)
- A World Financial Authority?
(Eatwell and Taylor, 1998)
- An international financial regulator?
(Reinhart/Rogoff, 2009)

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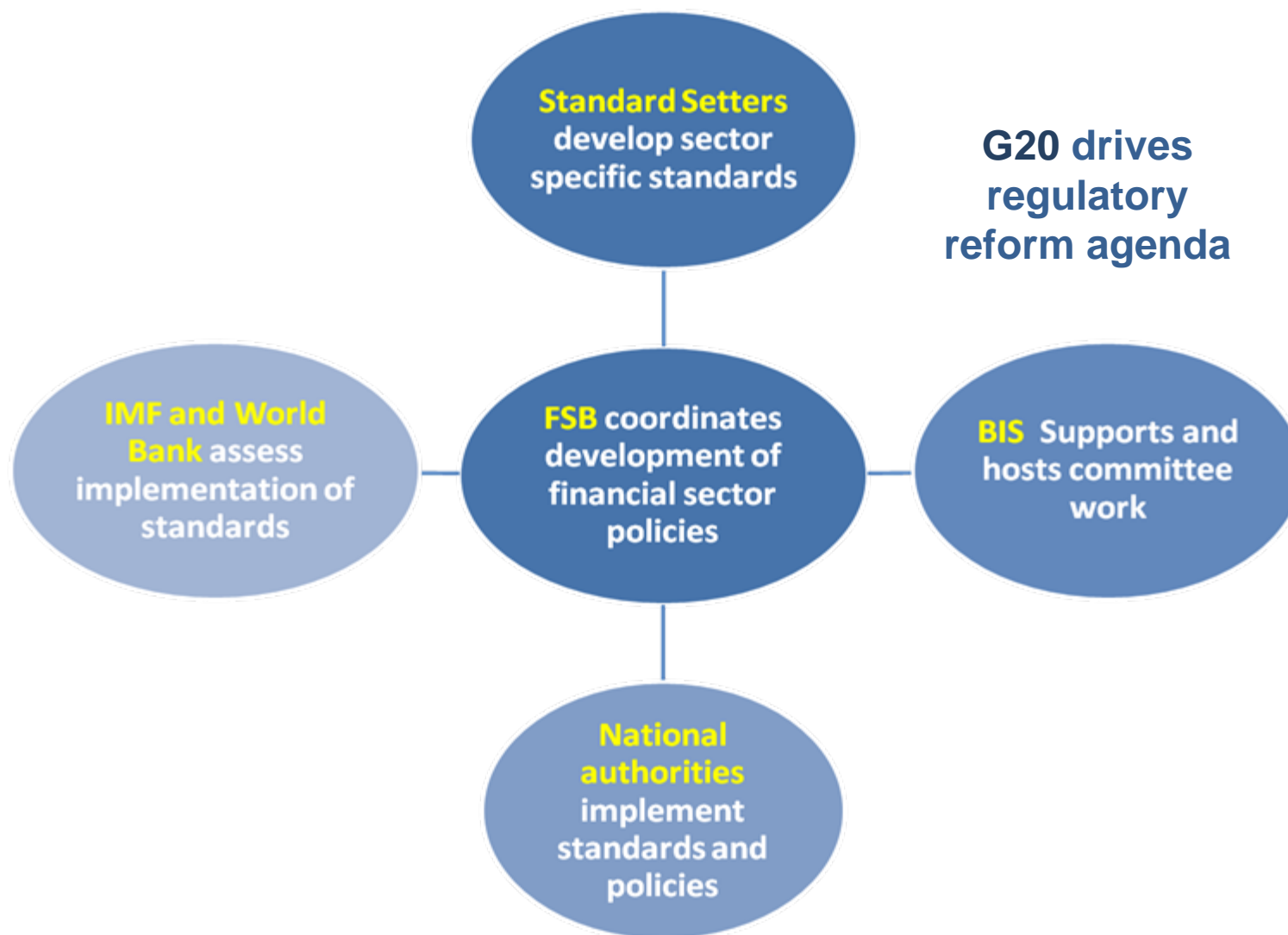
Establishment of the FSB

- Established in April 2009 by the Leaders of the G20 as successor to the Financial Stability Forum (FSF) with expanded membership, broader mandate and enhanced operating structure to

“to coordinate at the international level the work of national financial authorities and international standard setting bodies in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies”

FSB Charter, September 2009

FSB in the International Financial Architecture



Role of the FSB

- To address financial system vulnerabilities
- To coordinate the development and implementation of strong regulatory and supervisory policies
- Goal: to strengthen financial stability.
- Broad-based agenda for strengthening national financial systems and the stability of international financial system
 - Joint diagnosis of problems
 - Policy development and coordination
 - Monitoring and follow up on implementation

High Level Priorities

- Develop framework and tools for system-wide or macroprudential risks
- Strengthen robustness of the banking system
- Eliminate moral hazard from systemically important financial institutions (SIFIs - 'too big to fail')
- Enhance crisis management capability
- Improve incentives and market functioning
- Consistent implementation - adherence to standards

Who is the FSB?

- The Financial Stability Board (FSB) brings together senior officials of:
 - National financial authorities
 - Ministries of finance
 - Central banks
 - Supervisory and regulatory authorities
 - International financial institutions
 - International regulatory and supervisory groups
 - Committees of central bank experts

Countries and jurisdictions (24):

- Argentina
- Australia
- Brazil
- Canada
- China
- France
- Germany
- Hong Kong
- India
- Indonesia
- Italy
- Japan
- Korea
- Mexico
- Netherlands
- Russia
- Saudi Arabia
- Singapore
- South Africa
- Spain
- Switzerland
- Turkey
- United Kingdom
- United States

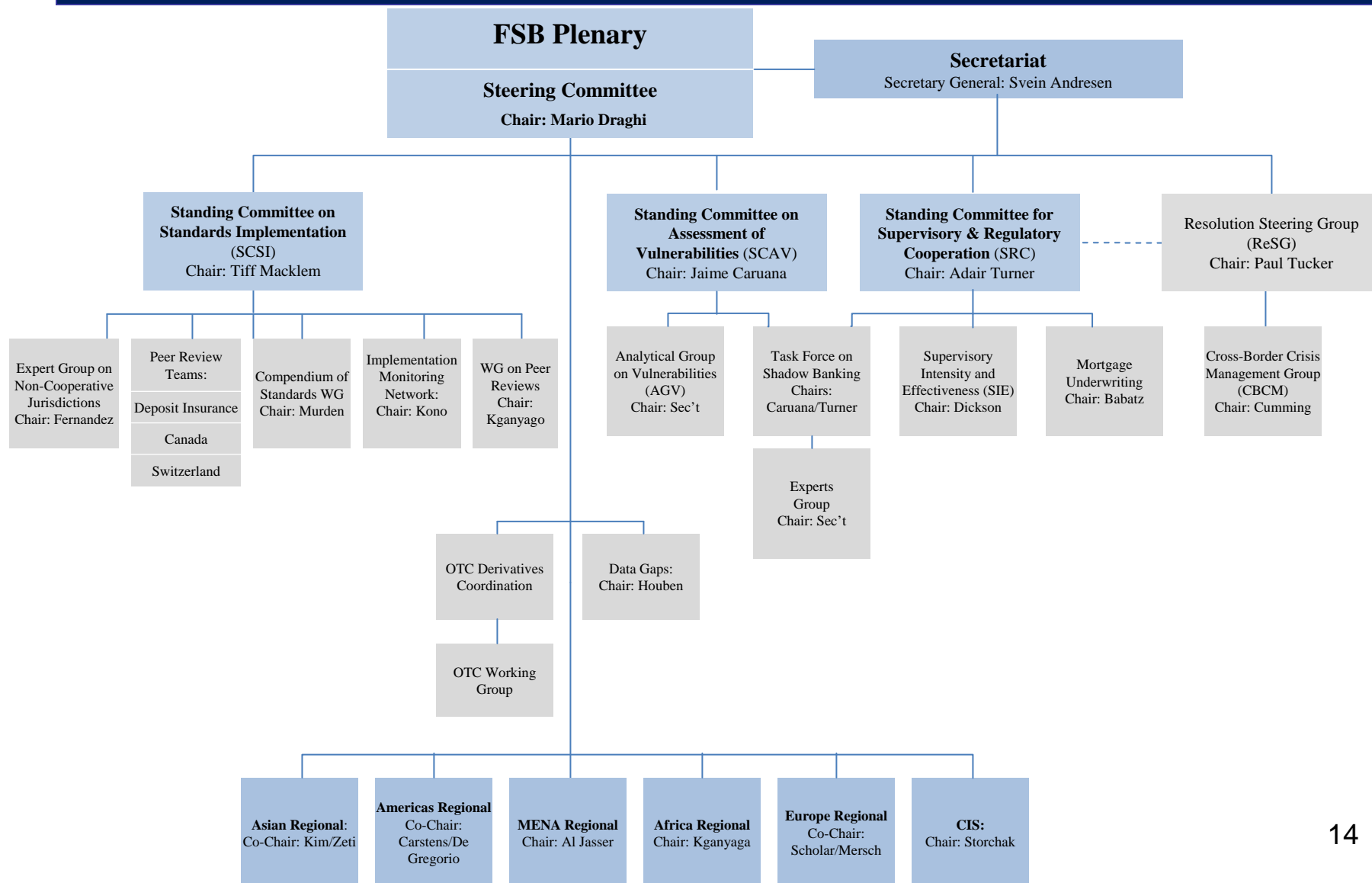
Institutions and bodies:

- BIS
- European Central Bank
- European Commission
- IMF
- World Bank
- OECD
- Basel Committee
- IAIS
- IOSCO
- IASB
- CGFS
- CPSS

- **Plenary**
 - Sole decision-making body (consensus)
 - Meets at least twice a year
- **Steering Committee**
 - To provide operational guidance between Plenary meetings
- **Chair**
 - Presides over the Plenary and the Steering Committee
 - Appointed by the Plenary for a 3 years term renewable
- **Secretariat**
 - Hosted by the BIS in Basel
 - Staff seconded from members



FSB Organisational Chart



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SIFI Framework: Mandate

Today, the Seoul Summit delivers...

...core elements of a new financial regulatory framework, including...measures to better regulate and effectively resolve systemically important financial institutions, complemented by more effective oversight and supervision

The G20 Seoul Summit
Leaders' Declaration
11-12 November 2010

***No firm should be too big to fail or too complicated to fail;
taxpayers should not bear the cost of resolution***

Global and national SIFIs

- Effective and efficient resolution framework
- More intense supervisory oversight
- SIFIs should have a higher loss absorbency capacity
- Robust core financial market infrastructure
- Other supplementary measures

Global SIFIs

- Mandatory international recovery and resolution planning
- Rigorous assessment through supervisory colleges
- Implement cross-border resolution recommendations

SIFI Framework: Rationale

- Negative externalities: Regulatory policies do not fully address the adverse side effects of SIFIs
- Issues:
 - Sub-optimal outcomes (from a system-wide level)
 - Moral hazard (implicit guarantees)
- Objectives of SIFI policies:
 - Reduce the probability of a failure by increasing going-concern capital
 - Reduce the impact of failure by improving recovery and resolution frameworks

- Indicator-based approach to reflect:
 - What generates negative externalities
 - What makes a bank critical for stability of the financial system
- Judgement is used to override the results of the indicator-based approach in exceptional cases (subject to peer review)

SI_B Framework: Indicators

Table 1

Indicator-based measurement approach

Category (and weighting)	Individual Indicator	Indicator Weighting
Cross-jurisdictional activity (20%)	Cross-jurisdictional claims	10%
	Cross-jurisdictional liabilities	10%
Size (20%)	Total exposures as defined for use in the Basel III leverage ratio	20%
Interconnectedness (20%)	Intra-financial system assets	6.67%
	Intra-financial system liabilities	6.67%
	Wholesale funding ratio	6.67%
Substitutability/financial institution infrastructure (20%)	Assets under custody	6.67%
	Payments cleared and settled through payment systems	6.67%
	Values of underwritten transactions in debt and equity markets	6.67%
Complexity (20%)	OTC derivatives notional value	6.67%
	Level 3 assets	6.67%
	Held for trading and available for sale value	6.67%

- Four buckets based upon the score of systemic importance
- Plus one empty bucket
- End 2009 data collected for 73 banks
 - 65% of global banking assets
 - 17 countries

SIB Framework: Buckets

Bucketing approach

Bucket	Score range*	Minimum additional loss absorbency (common equity as a percentage of risk-weighted assets)
5 (empty)	D -	3.5%
4	C - D	2.5%
3	B - C	2.0%
2	A - B	1.5%
1	Cut-off point - A	1.0%

* Scores equal to one of the boundaries are assigned to the higher bucket.

- Criteria
- Ancillary indicators
- Qualitative information
- Process for incorporating supervisory judgement

- Common tier 1 equity
- Bail-in debt (loss absorbency at the point of non-viability)
- Going-concern contingent capital
 - Instruments that convert to capital while the bank is still a going-concern
 - Instruments are untested and can come in many different forms
 - BCBS will continue to review contingent capital; support its use for higher, national loss absorbency requirements

- Phased-in in parallel with capital conservation and countercyclical buffers
 - Between 1.1.2016 and 31.12.2018
 - Fully effective 1.1.2019
 - Legislation and rules by 1.1.2014

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Strengthening Policies

- Develop and strengthen macroprudential policy framework
 - data, analytical techniques, policy toolkit, institutional arrangements
- Implement Basel III
- Address SIFIs
- Establish effective resolution regimes
- Improve incentives and market functioning
 - compensation, transparency, OTC derivatives
- Contain regulatory arbitrage and risks from shadow banking

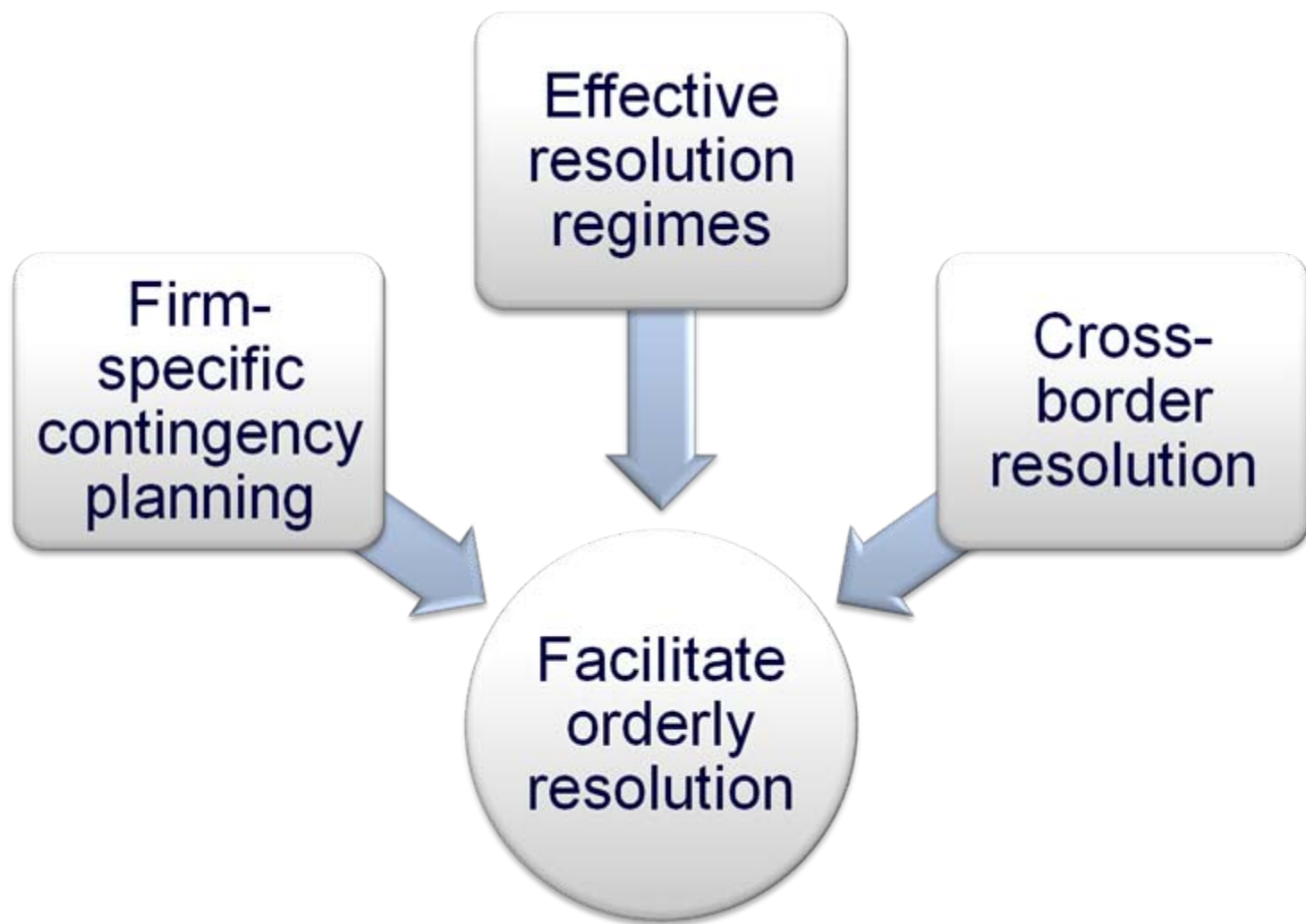
Macprudential Oversight

- Safety and soundness of individual institutions necessary but not sufficient
- System-wide interconnections and behavioural responses under stress are key
- Protect system-wide stability - to deliver core financial services in support of wider economy
- Institutional frameworks for oversight
- Develop tools – both time-series & cross-section that address ‘systemic externalities’
- Collaborate to share lessons and experience, and to limit externalities and arbitrage

Robust banking system

- Strengthen capital framework (Basel III)
 - Higher, more risk sensitive and better quality capital
 - Countercyclical buffers
 - Supplementary leverage ratio as backstop
 - Aim to withstand severe stress without public support
- Common equity up from 2% before regulatory adjustments to 7% (including conservation buffer) after stricter regulatory adjustments
- New international liquidity standard
- BCBS proposals endorsed at Seoul Summit
- To be phased in between 2013 and 2019
- Full and consistent implementation crucial

Improving resolution capacity



Improving incentives and market functioning

- Compensation
- Stronger market infrastructure
 - OTC derivatives (including commodity derivatives)
 - Central counterparties
 - Credit Rating Agencies
- Improve market discipline –
transparency/disclosure/accounting
standards

Shadow banking

- Definition of shadow banking
 - Credit intermediation outside regular banking system
- Developing an improved monitoring framework
 - Gaps in data and disclosure practices
- Policy options
 - Regulation of shadow banking entities and activities
(*conduits/SIVs, money market funds, other entities, securitisation, repos and securities lending*)
 - Regulation of banks' interactions with shadow banking (indirect regulation)

Implementation of standards

- FSB members commit to implement agreed international standards
- Lead by example to promote wider application
- Peer reviews
 - Thematic (eg compensation, mortgage underwriting, risk disclosures)
 - Country (FSB members, following up on FSAPs/ROSCs)
- Network to monitor implementation of FSB & G20 recommendations
- Strengthen global adherence to co-operation and information standards
- Establish FSB regional consultative groups in 2011

FSB regional consultative groups

- Broadening input to FSB policy-making
- Same institutional mix – ministries of finance, central banks, supervisors, IFIs
- Forum for FSB members and mid-sized other financial markets in their region
- Consultation during the policy formulation stage
- Six regions, including the Americas
- Additional outreach to a wider group of jurisdictions will take place

Financial stability issues in emerging market and developing economies

- Joint report from FSB, IMF, World Bank being prepared for November G20 Summit
- Task force of FSB members and other emerging market & developing economies
- Five proposed areas for recommendations:
 - Application of international standards
 - Cross-border supervisory cooperation
 - Expanding the regulatory & supervisory perimeter
 - Managing FX risks
 - Developing domestic capital markets

Areas for EMDE recommendations

- Application of international standards
 - Legal underpinnings, supervisory capacity
 - Guidance on adoption of Basel II/III, financial conglomerates
 - Promoting technical assistance
- Cross-border supervisory cooperation
 - Encouraging host participation in supervisory colleges, crisis management groups
 - Alternatively, bilateral or regional information sharing

Areas for EMDE recommendations

- Expanding the regulatory & supervisory perimeter
 - Strengthening regulation and supervision of small-scale, non-bank institutions (e.g. microfinance, savings cooperatives)
- Managing FX risks
 - Enhancing capacity to identify build-up of FX risks
 - Information sharing
 - Guidance on prudential regulation of risks

Areas for EMDE recommendations

- Developing domestic capital markets
 - Promoting domestic investor base
 - Making infrastructure more robust
 - Systemic risk mandate for securities regulators
- EMDEs paper to be finalised by October

Contact Details

Jason George
Member of Secretariat
Financial Stability Board

jason.george@bis.org