ICSA
INTERNATIONAL COUNCIL of SECURITIES ASSOCIATIONS

23 May 2012

Mark Carney, Chairman
Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Re: Importance of multilateral global coordination

Dear Mr. Carney:

The International Council of Securities Associations (ICSA) is the global forum for trade associations and self-regulatory organizations that represent and/or regulate firms active in the securities industry.[1] We are writing to you because ICSA members are increasingly concerned that regulations being put in place in different G20 jurisdictions are creating conditions that will lead to fragmentation, increased protectionism and regulatory arbitrage, ultimately risking a reduction in the ability of regulators to effectively regulate an increasingly globalized capital market. ICSA members support both the G20's goals of developing a globally consistent regulatory framework as well as the practical regulatory repair process that has been taking place under the leadership of the Financial Stability Board. Our concerns reflect the risk that the various financial sector reforms being enacted around the world are not consistent with one another and, as a result, the ambitious goals set by the G20 in the aftermath of the financial crisis are not likely to be met.

In order to develop a more globally consistent regulatory framework, we believe that the work being done by international standard setters such as the Financial Stability Board, the Basel Committee, IOSCO and the CPSS in aligning regulatory approaches should be supplemented by operational arrangements that would help to make the new global financial architecture more coherent on a cross-border basis. As a first step, ICSA members urge the FSB to foster an active and ongoing multilateral dialogue involving regulators and market participants from a broad range of jurisdictions focused on specific areas of regulatory policy, such as OTC derivatives regulation, where there are significant divergences between the regulations being considered or

[1] ICSA is composed of trade associations and self-regulatory organizations that collectively represent and/or regulate the vast majority of the world's financial services firms on both a national and international basis. ICSA's objectives are: (1) to encourage the sound growth of the international securities markets by promoting harmonization in the procedures and regulation of those markets; and (2) to promote mutual understanding and the exchange of information among ICSA members. More information about ICSA is available at: www.icsa.bz

implemented in different jurisdictions. The intention of this dialogue would be for the FSB to encourage regulators in different jurisdictions to recognize as 'equivalent' or mutually compatible specific aspects of the regulatory framework in other jurisdictions that are sufficiently comparable to their own, based on an objective set of criteria. This process, we believe, would be much more efficient than the current approach, which involved lengthy and involved bilateral negotiations.

As a result of that dialogue, ICSA members suggest that the FSB could promote the development of a multilateral mutual recognition framework that would allow regulators in different jurisdictions to coordinate their regulations in a relatively efficient manner with a large number of other jurisdictions. A multilateral mutual recognition framework could help regulators improve the overall soundness and efficiency of the global financial markets by eliminating regulatory overlaps and loopholes while at the same time avoiding excessive regulatory burdens on markets participants and ensuring a level-playing field between different jurisdictions. We are writing to you because we believe that the FSB would be the appropriate body to oversee the development of these types of agreements, given its global responsibilities.

G20 commitments for consistent global standards not being met

As we are all well aware, because of the absence of any effective global framework for addressing the global financial crisis when it erupted in 2008, the immediate legislative and regulatory responses to the crisis have been resolutely national or, at best, regional. This approach to regulatory repair has impacted on regulatory and supervisory authorities as governments have become more closely involved in setting their agendas and policy priorities. Although some convergence in approaches has been facilitated by the governing principles and standards for post-crisis regulatory repair set by the international standard-setting bodies, national implementation has generated not just the emergence of differently-paced timetables for regulatory reforms but also substantial differences in the manner in which global standards are being or will be implemented.

In particular, practical problems are starting to multiply as new regulatory reforms are being implemented with extensive extraterritorial consequences. For example, the European Union is making increasing use of the concept of 'equivalent' regulation, which in practice requires that regulators from all other jurisdictions must engage in extensive discussions with EU regulators in order to demonstrate that their own regulatory regimes are 'equivalent' to the European regulations being put in place so that their market participants have access to European markets. This has been the case with the EU Credit Rating Agency Directive as well as the Alternative Investment Fund Managers Directive, both of which require regulators in other jurisdictions to demonstrate equivalence of their regulation in a slow, cumbersome, country-by-country process.

Similarly in the U.S. both the Foreign Account Tax Compliance Act (FATCA) and the proposed Volcker rule could have extensive extraterritorial consequences, as you pointed out in your recent letter regarding the proposed Volcker rule.[2] As you are aware, regulators and government

[2] Comment letter from Mark Carney, Governor, Bank of Canada to Board of Governors, U.S. Federal Reserve, 13 February 2012.

form a number of other jurisdictions, including Japan and the U.K. along with the European Commission, also expressed their strong concerns regarding the likely adverse impact of the Volcker rule on the ability of foreign financial institutions to make markets for their own government's sovereign bonds. The U.S. has already moved to mitigate the extraterritorial impact of FATCA by developing bilateral agreements with a number of other jurisdictions that will allow the U.S. Treasury and IRS to receive the information that they were seeking through FATCA without directly imposing regulations on foreign financial institutions. We are hopeful that the recent announcement by the U.S. regarding a delay in the implementation of the Volcker rule means that they are also working to eliminate the extraterritorial implications of that regulation.

OTC derivatives regulation is an area that particularly demonstrates the pressing need for global action in order to ensure that there is consistency and coordination between the regulations being put in place in different jurisdictions. In the light of regulations that have been proposed and in some cases approved, banks and other financial institutions which undertake significant cross-border activities in OTC derivatives are concerned that they may be subject to overlapping and contradictory regulatory requirements in different jurisdictions and may need to comply with two or more different regimes. Areas of concern include duplication of registration and licensing requirements, clearing obligations, transaction and position reporting, collateral and margining requirements, and prudential obligations.

The effect of divergent regulations for OTC derivatives would be to cause competitive imbalances in the international derivatives markets with market participants structuring their businesses and making decisions in relation to dealings in particular jurisdictions or with particular counterparties based on regulatory considerations rather than normal commercial grounds. Such imbalances are also likely to have an effect on counterparty and ultimately consumer choice and lead to increased costs. If differences are material, many firms are likely to gravitate away from an integrated global approach to business and structure their businesses around specific products with local counterparties in the relevant jurisdiction.

Need for a multilateral approach

To date much of the attention placed on addressing overlapping and contradictory national and regional regulation has involved bilateral negotiations between the U.S. and the EU. While it is extremely important that the U.S. and EU reach convergence or at least a high level of consistency in terms of their regulatory reforms, ICSA members suggest these negotiations alone are too limited and therefore do not adequately serve the goals of the G20 from a global perspective.

One major problem with the bilateral approach to global regulatory convergence is that it ignores the rest of the world. Which means that most jurisdictions in the world will need to prove that their own regulations are 'equivalent' to the regulations established in the U.S. and/or the EU. ICSA members suggest that a more effective and efficient approach would be for the FSB to take a more active role in fostering an active and ongoing multilateral dialogue between regulators

and market participants on a broad range of issues in order to ensure that any 'convergence' that is ultimately achieved between different national and regional regulations is truly global.

As part of this process, we urge the FSB to also consider its possible role in developing a framework for multilateral mutual recognition agreements between financial market regulators. Prior to the emergence of the global financial crisis, regulators in the U.S., Australia, Canada, the EU and elsewhere had begun to explore the concept of "mutual recognition" as a way to facilitate cross-border financial transactions. A mutual recognition agreement was actually signed between the U.S. and Australia in August 2008 and negotiations between the U.S. and Canada on a similar agreement was also quite far advanced.[3] These efforts, quite understandably, were abandoned once the extent of the financial crisis became clear, both because regulators had more pressing problems and because of a general aversion toward any policy changes that could appear to loosen regulations on financial sector participants rather than tighten them.

Although the idea of mutual recognition lost a great deal of its appeal for regulators in the immediate aftermath of the financial crisis, the concept remains valid and potentially quite useful since, as noted above, there are significant and wide divergences between some of the regulations that are being developed in a number of jurisdictions. Given the urgency of the issue at the current time, ICSA members believe that work in achieving mutual recognition needs to be done on a multilateral as opposed to bilateral basis. This is necessary since the process of achieving bilateral mutual recognition determinations would require a huge amount of resources, take an extended period of time, could be delayed by disputes over latent protectionism and could unduly favor the interests of the larger economies over all other economies. A multilateral approach would also result in a higher level of global consistency between national and regional regulatory policies than would be likely with a bilateral approach.

In order to address the limitations inherent with the bilateral approach to mutual recognition, ICSA members suggest that the FSB could work toward developing a framework for multilateral mutual recognition agreements in particular areas of regulatory policy. A multilateral mutual recognition agreement could, for example, set out parameters for the recognition of "functional equivalence" of regulation between jurisdictions as well as parameters for exemptive relief in specific areas of regulatory policy.[4] For example, given the critical importance of the issue, a multilateral mutual recognition agreement could be developed for OTC derivatives regulation. The aim of such an agreement would be to achieve coordination and consistency between the divergent regulations for OTC derivatives regulation that are in place or being contemplated in the U.S. and EU while also providing a framework for OTC derivatives regulation in other jurisdictions.

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[3] The mutual recognition arrangement signed in August 2008 provided a framework for the SEC, the Australian government, and ASIC to consider regulatory exemptions that would permit U.S. and eligible Australian stock exchanges and broker-dealers to operate in both jurisdictions, without the need for these entities (in certain aspects) to be separately regulated in both countries.

[4] Any multilateral mutual recognition agreement will need to be designed so as to not adversely impact on the efficient flow of capital between jurisdictions that are signatory to the agreement and those that are not.

The FSB is clearly the appropriate body to oversee the effort to develop multilateral mutual recognition agreements, given its global responsibilities. We also suggest that consideration could be given to how the FSB's peer review process could contribute to regulatory policy convergence and the development of efficient multilateral mutual recognition arrangements.

In closing, we reiterate ICSA's members' commitment to the goals of global regulatory repair, including most importantly the goal of creating globally consistent regulations which encourage capital mobility and economic growth. ICSA members stand ready to engage with the FSB to expand on our ideas regarding both the importance of multilateral mutual recognition agreements and how they could be made to work in practice. We look forward to hearing from you about this proposal at your earliest convenience.

Sincerely,

Jong Soo Park, Chairman
International Council of
Securities Associations (ICSA)

Duncan Fairweather, Chairman
ICSA Standing Committee on
Regulatory Affairs

cc: Svein Andresen
Secretary General
Financial Stability Board