



Japan Securities Dealers Association

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Secretariat of the Financial Stability Board
c/o Bank for International Settlements
CH-4002, Basel, Switzerland

RE: Comments to Proposed Framework for Post-Implementation Evaluation of the Effects of the G20 Financial Regulatory Reforms

Dear Sir/Madam:

The Japan Securities Dealers Association (JSDA)¹ appreciates the opportunity to submit comments on the discussion questions in the Financial Stability Board (FSB)'s "Proposed Framework for Post-Implementation Evaluation of the Effects of the G20 Financial Regulatory Reforms" published on April 11, 2017.

1. General Comments

JSDA supports the statement in the Communiqué from the G20 Finance Ministers and Central Bank Governors Meeting in March 2017 that "we will continue to enhance our monitoring of implementation and effects of reforms to ensure their consistency with our overall objectives, including by addressing any material unintended consequences". Further, we welcome that FSB is proceeding with work to establish the framework for post-implementation evaluation of the effects of the G20 financial regulatory reforms.

JSDA understands the importance of eliminating vulnerabilities that exist in the market and the importance of securing financial stability at a global level to prevent any future financial crisis. However, we expect that an appropriate balance will be achieved so as not to impede the contribution by financial and capital markets to the real economy such as smooth fund

¹ JSDA is a self-regulatory organization (SRO) as well as an interlocutor for the securities industry. Its legal status is a Financial Instruments Firms Association authorized by the Prime Minister pursuant to Article 67-2, Paragraph 2 of the Financial Instruments and Exchange Act (FIEA). JSDA comprises around 500 members consisting of securities firms and other financial institutions operating securities businesses in Japan.

provision for growth as an original function of these markets. Accordingly, JSDA hopes that the related parties will thoroughly examine the following items in more detail in future discussions.

2. Comments on the Discussion Questions

(1) Main Elements of the Framework (Question 1-3)

a. Evaluation of the Newly Introduced Regulation

This consultation document only mentions the pre-implementation evaluation of the regulations that “the framework will cover ex ante analysis only to the extent that it is necessary for post-implementation evaluation”. Hence, this framework is basically assumed to cover post-implementation evaluation of regulations that have been implemented or are still ongoing. On the other hand, when considering the introduction of new regulations to cope with emerging issues in the future, careful deliberation should be required to prevent any unintended consequences from occurring due to a combination of various existing regulations as well as other pre-implemented rules such as leverage-ratio requirement and clearing requirement on OTC derivatives transactions. As for the pre-implemented regulation, to ensure consistency in the evaluation approach and analysis method, we hope that guides for the evaluation will be provided in the same framework and give consideration to prevent any unintended consequences as much as possible.

b. Stance for Review of Regulation

This consultation document mentions that “if the findings warrant it, evaluations could provide a basis for possible fine-tuning of post-crisis regulatory reforms, without implying a scaling back of those reforms or undermining the members’ commitment to implement them”. However, the necessity should be judged after relevant evaluation analysis and the scope should not be limited to fine-tuning beforehand. We understand that implementation of this framework could lead to self-denial of FSB’s judgement in the past and conducting a drastic revision would be a significant hurdle. However, we hope that an adequate necessary review will be conducted to achieve an optimal balance for regulation and economic growth.

(2) Challenges and Evaluations (Question 4-6)

a. Balance between Social Benefit and Cost

We appreciate that the consultation document describes that a balance should be achieved between social benefit and cost when evaluating influences. It also describes that the “social benefits include lower probability and lower severity of financial crises and their associated output losses”. However, we are concerned that if once this benefit is overestimated, dilution of cost-consciousness could occur. Additionally, we hope that proper consideration will be given to burdens generated by various requirements including the suppression of transactions and limitation on capital policy causing lower market liquidity and opportunity loss for both intermediaries and users, as well as costs for strengthening disclosure of information and participation in stress tests.

For example, understanding of benefits and costs for each economic entity through qualitative surveys can be considered. In addition, in the capital market, many reforms including those for securities settlement system are ongoing. It is important to verify and consider whether post-crisis regulations impose an indirect burden on such reforms including opportunity loss of innovation such as FinTech and digitalization.

b. Re-evaluation Based on Environmental Changes

This consultation document mentions that “evaluations in a given reform area are not expected to be repeated frequently.” In the meantime, as one of the challenges to conduct evaluation, there is a concern that the results of the evaluation will become obsolete in a short period because the rate of change in the market environment is increasing through the progress of financial technology innovation represented by FinTech which promotes the emergence of new market players. In this regard, we appreciate that this consultation document describes that “monitoring developments in the relevant market segment would help to identify issues and trends”. In addition, it is important to create a mechanism, for example, to establish a public-private forum to facilitate dialogue on a continuous and periodic basis, which could flexibly review the result of past evaluations.

(3) Engagement with Stakeholders (Question 11)

- Extensive Input and Considering Characteristics of Each Country’s Market

JSDA appreciates that the consultation document emphasizes the importance of collecting relevant information, and the conduct of the analysis, thereby leveraging expertise from

outside experts, including academics, think-tanks, industry and others. It is desirable that stakeholders can be involved at the stage of drafting evaluation other than public consultation, which enables opinions to be reflected properly from an external source.

When conducting evaluation, influence by implementation can differ in each country because the status of implementation is substantially different in the US, Europe and other countries. In this regard, we request that the characteristics of each market is adequately considered and analysis of the US and European markets are not directly applied to other markets.

(4) Approaches and Priorities for Evaluation (Question 1, 4, 7, 12)

a. Simulation Assuming Crisis

The consultation document mentions mainly three challenges as follows.

(1) Did the reform “cause” an outcome? (Attribution)

(2) Did the reform have broadly similar effects across relevant markets, states of world, or jurisdictions and regions? (Heterogeneity)

(3) Did the reform achieve its overall objective? (Aggregation/general equilibrium)

In any of these challenges, we hope that sufficient simulation will be conducted from the standpoint of whether each regulation can perform effectively as intended originally during a crisis.

For example, disclosure of liquidity profile of open-end funds may be useful information for investors in normal conditions. However, at the time of a financial crisis, there is a risk that it may become an unintended alert disclosing that liquidity has fallen and encourage investors to seek further redemptions. Also level 2 relationship data added on the LEIs impose a heavy burden on participants in the OTC derivatives market. However, there is the question of whether this system can properly trace participants’ capital relationship which could rapidly change in a critical situation. It is important that each regulation can perform its expected function under a crisis.

b. Urgency of addressing Unintended Consequences

This consultation document seems to lack the awareness of urgency of addressing unintended consequences. This document insists that social benefit and a set of reforms can only be evaluated through long-term analysis that includes a full financial cycle. However, if it takes a long time to analyze, there is rather a risk of making the financial system unstable through unintended consequences which will have a harmful impact on the system.

It is important to judge the necessity of measures to mitigate this risk at an early stage and temporary evaluation, as a base for the countermeasures, would be the most prioritized work.

Regarding problems which can not only generate short-term cost but also increase the probability of a financial crisis occurring over the long term, such problems could carry a high risk by waiting for a full financial cycle without reviewing regulations. For example, decreasing market liquidity by leverage-ratio requirement, dysfunction of short-term money market, collapse of arbitration in the credit market and shrinking of OTC derivatives transactions including client clearing should be taken into consideration.

The countermeasures based on these evaluations can be reconsidering the implementation schedule and scope of the regulation, and also suspending existing regulations. In particular, dysfunction and non-stabilization of the financial system could be avoided by suspending regulations globally, deepening analysis in the interval and taking measures. Also, through observing influences by the suspension, it will be possible to identify the effects of the regulation, which enables more appropriate regulations to be designed. The US has postponed the implementation of the countercyclical capital buffer based on theoretical and practical challenges because if implementation of the policy is forced, there is concern that procyclicality will actually increase.

c. Importance of Qualitative Analysis

It should be noted that the mechanism of interaction between regulations is still not clear. That is why severe unintended consequences occur. Considering this situation, quantitative models should not be excessively emphasized and surveys and hearings should be rather emphasized as information sources. In particular, for the evaluation of interaction and overall effects, it should be reconsidered that this consultation document recognizes general equilibrium analysis based on the model as an effective way and puts qualitative analysis at a lower position.

3. Conclusion

JSDA would like to pay tribute to FSB's effort for this proposal and expects further cooperation will be promoted among international standard setters.

In recent years, against the global financial regulation led by G20, some countries add their own regulation on the international standard and exercise extraterritorial application to other countries. This adding and extraterritorial application could possess an element of danger that makes regulation more complicated and causes distortion and fragmentation in markets. On the other hand, when authorities of large markets such as the US and EU start to consider suspension or phased implementation of globally agreed regulations, it is desirable for FSB to reexamine the rationality of the agreement in a timely manner to mitigate the impact of market

fragmentation. To ensure that evaluation under this framework functions effectively, we expect national authorities to promote cooperation and respect the regulations of other countries to achieve consistent implementation of international standards.

Best regards

Handwritten signature of Koichi Ishikura in blue ink, consisting of the characters '石倉 宏一' followed by a horizontal line.

Koichi Ishikura

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