

# FROM CRISIS TO CONFIDENCE: THE ROLE OF GOOD REGULATION

DISCUSSION PRIMER

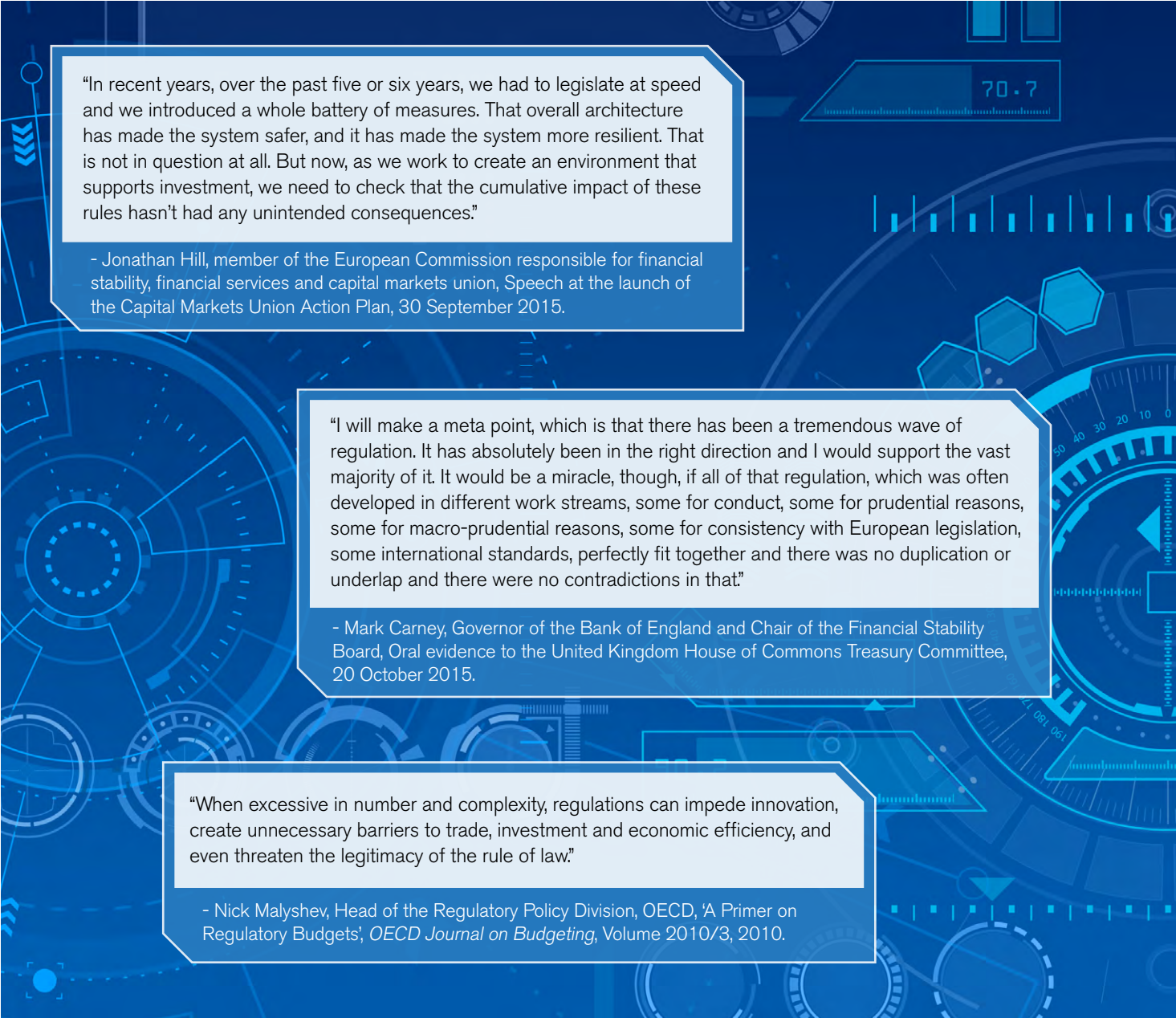
NOVEMBER 2015

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**IFAC**

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"In recent years, over the past five or six years, we had to legislate at speed and we introduced a whole battery of measures. That overall architecture has made the system safer, and it has made the system more resilient. That is not in question at all. But now, as we work to create an environment that supports investment, we need to check that the cumulative impact of these rules hasn't had any unintended consequences."

- Jonathan Hill, member of the European Commission responsible for financial stability, financial services and capital markets union, Speech at the launch of the Capital Markets Union Action Plan, 30 September 2015.

"I will make a meta point, which is that there has been a tremendous wave of regulation. It has absolutely been in the right direction and I would support the vast majority of it. It would be a miracle, though, if all of that regulation, which was often developed in different work streams, some for conduct, some for prudential reasons, some for macro-prudential reasons, some for consistency with European legislation, some international standards, perfectly fit together and there was no duplication or underlap and there were no contradictions in that"

- Mark Carney, Governor of the Bank of England and Chair of the Financial Stability Board, Oral evidence to the United Kingdom House of Commons Treasury Committee, 20 October 2015.

"When excessive in number and complexity, regulations can impede innovation, create unnecessary barriers to trade, investment and economic efficiency, and even threaten the legitimacy of the rule of law."

- Nick Malyshev, Head of the Regulatory Policy Division, OECD, 'A Primer on Regulatory Budgets', *OECD Journal on Budgeting*, Volume 2010/3, 2010.

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"Have the vulnerabilities revealed in the crisis been adequately addressed? Are additional adjustments still necessary? Or, conversely, have we gone too far and created a regulatory Frankenstein's monster that no-one has full control over and that stifles lending and economic growth?"

- Stefan Ingves, Governor of the Sveriges Riksbank and Chairman of the Basel Committee on Banking Supervision, speech at the Federal Reserve Bank of Chicago Annual International Banking Conference, 6 November 2014.

"Following the crisis of 2007, regulatory authorities either are or should be engaging in a fundamental reconsideration of how they approach financial regulation and supervision."

- Gerard Caprio, Jr., 'Financial Regulation After the Crisis: How Did We Get Here, and How Do We Get Out?', *LSE Financial Markets Group Special Paper Series*, Special Paper 226, 2013.

"Don't expect there won't be problems if you're going to unilaterally introduce new rules without regard to what other nations are doing. What we'll end up with is a multilateral environment. There will be problems, and it will only get worse as more and more countries do the same thing. We'll end up with a matrix of great complexity."

- David Wright, Secretary General of the International Organisation of Securities Commissions, cited in Elliott Holley, 'Unilateral regulatory initiatives undermine G20 financial stability goals', *Banking Technology*, 23 October 2015.

# FROM CRISIS TO CONFIDENCE: THE ROLE OF GOOD REGULATION



## FOREWORD

Good regulation is essential to the fairness, efficiency, and effectiveness of economies, and making it work as well as it can is a never-ending mission. Getting regulation right is imperative to strengthening growth, investment, and trade—challenging, crucial objectives in today's global economy.

IFAC wants to spark a focused, frank discussion and debate about how the regulatory responses to financial crises have played out, where the issues stand today, and what the lessons are. During the immediate pressure of crisis decision-making, such reflection is not always possible. Taking stock now is essential. Strengthening the global financial system's capacity to anticipate, respond and collaborate is paramount—especially before the next inevitable shock to challenge the global economy.

The regulatory response to the global financial crisis (GFC) that erupted in 2007 was important in rebuilding trust and confidence across many parts of the global financial system and wider economy. However, as the dust settles, it appears that the response is different in quantum and nature across jurisdictions; that the capacity for regulatory intervention and complexity is now on a scale previously unimagined.

The goal of these discussions is to highlight questions and draw out insights that advance greater understanding of the essential role good regulation plays in economy wide confidence-building. IFAC will use the questions and insights raised in its public policy and regulation activities and further research.

Fayez Choudhury  
Chief Executive Officer, IFAC

**“Strengthening the global financial system’s capacity to anticipate, respond and collaborate is paramount—especially before the next inevitable shock to challenge the global economy.”**

**- Fayez Choudhury**

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# 1. THE CHALLENGE

Eight years after the GFC commenced, global discourse remains dominated by the need for genuine, sustained economic growth and confidence. The purpose of this initiative is to enable broad reflection—without the tension of immediate crisis—on how the financial regulatory environment has evolved, how it is serving economic stability and growth, and what can be learned to better prepare for the next financial shock.

Summarized below, this primer<sup>1</sup> raises questions intended to stimulate discussion and debate. The following sections outline issues that are emerging across multiple jurisdictions, sectors and regulatory streams. The roundtable discussions will identify further issues and questions, and importantly, what issues are urgent, and where they are impacting.

The GFC underscored vulnerability of a globalized economy to rapid contagion, and revealed the need for substantial new financial regulation and reform. Good intentions have prevailed, and significant steps have been taken toward more effective communication, and processes to deal with globally systemic issues and risks.

## CENTRAL QUESTIONS FOR DISCUSSION

### *In the evolving regulatory environment:*

- What has been achieved?
- What is working well?
- Where are problems emerging?

### *What are the main costs and impacts?*

- Compliance costs?
- Broader economic and other aspects?
- Who pays, and who benefits?

### *What is good regulation?*

- Where are aspirations and execution diverging?
- How can recognized principles be better embodied in practice?



**SECTION 2** looks broadly at the evolving regulatory environment. Emerging issues of complexity, fragmentation, and inconsistency, and the clarity of objectives, impacts, and incentives in the regulatory environment warrant attention. What has been achieved? What has worked well, and what has not? And what is causing real problems?

**SECTION 3** queries the costs and impacts of the evolving regulatory landscape, and where the costs and benefits are being felt. The global breadth and depth of post-crisis reforms is greater than the responses to previous crises. Is this reaching a critical mass in terms of its volume and economic impact? Are some sectors being impacted disproportionately?

**SECTION 4** compares regulatory principles and recommendations issued by international organizations. The accord on good financial regulation principles among important players raises important questions about where aspirations and execution are diverging. Vitally, what broad principles and lessons for high-quality financial regulation should be learned? How can they be better implemented?



## SPECIFIC ISSUES PARTICIPANTS MAY WISH TO DISCUSS

Refer also to examples and context outlined in the following sections.



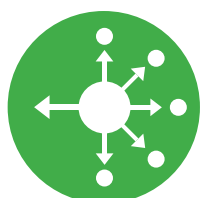
### *Aims and objectives*

- How clear are the objectives of key post-crisis financial regulatory reforms?
- What factors contribute to a lack of clarity or incongruity in policy objectives?
- How can the detail of financial regulatory reforms be better reconciled with objectives?



### *Fragmentation and inconsistency*

- How can international accord and jurisdictional implementation be made more cohesive?
- What factors are leading to regulatory fragmentation and inconsistencies?



### *Complexity and scale*

- What factors are exacerbating regulatory complexity?
- How is complexity impacting capacity to anticipate and respond to emerging risks and future financial shocks?
- How can simplicity be achieved given the complexity of the goal?



### *Clarity of objectives, incentives and impacts*

- How can regulatory compliance and reporting be balanced with the need for forward-looking, risk-focused activities?
- How does the way regulators measure and report performance impact the incentive for forward-looking innovation?



### *What is the cost?*

- How have regulatory compliance and reporting costs changed since the crisis?
- How can the return on compliance expenditure be maximized toward addressing risk?
- Are regulators resourced adequately to match their remit and expectations?



### *Who pays and who benefits?*

- How does regulatory fragmentation and inconsistency impact multinational business decision making?
- What aspects of post-crisis financial regulatory reform are impacting SMEs disproportionately?
- How is the regulatory environment impacting the attractiveness of professional and governance roles?

## 2. THE EVOLVING REGULATORY LANDSCAPE

This section outlines the key post-crisis financial regulatory developments, and queries what is working, and where problems are emerging. Key issues that appear to be developing across multiple sectors and regulatory streams are outlined, including:

- Fragmentation and inconsistency;
- Complexity and scale; and
- Clarity of objectives, incentives, and impacts.

### KEY POST-CRISIS REGULATORY DEVELOPMENTS

The GFC revealed many areas where new, revised, and more extensive financial regulation was needed. The response was swift, extensive, and taken on under “great pressure”.<sup>2</sup> Key aspects include:

- Establishment of the Group of Twenty (G20) Leaders' Summits and substantially enhanced agenda and operation.
- Establishment of the formal Financial Stability Board (FSB), arising from the Financial Stability Forum.
- An extensive post-crisis FSB agenda (Basel III, Liquidity Coverage Ratio, Too big to fail, securitization enhancements, harmonized data collection, over the counter derivatives reforms).
- Audit reforms including, in particular, the European Union (EU) audit quality and United Kingdom (UK) audit market competition reforms.
- Reforms in how and what auditors present in their reports, including in the UK and International Standards on Auditing (ISA).

- International Financial Reporting Standard (IFRS) and United States Generally Accepted Accounting Principles (GAAP) revisions, including around financial instruments, credit losses, leases, and revenue recognition.
- Multiple regional/jurisdictional reform programs, notably including the United States Wall Street Reform and Consumer Protection Act (Dodd-Frank), several important reform initiatives in Singapore, Hong Kong

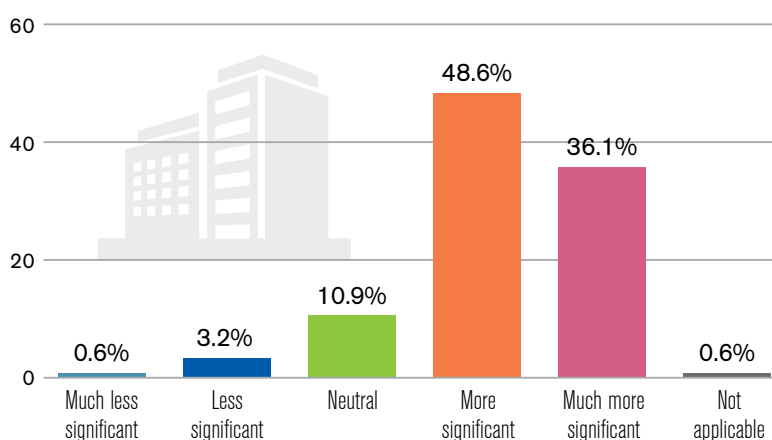
How clear are the objectives of key post-crisis financial regulatory reforms?



and in other areas within the Asian region, and European Banking Union.

In the *IFAC Global Regulation Survey 2015*, 83% of respondents reported that the impact of regulation on their organizations had become more or much more significant over the preceding five years; 84% expect the impact of regulation on their organizations to become more or much more significant in the coming five years.

### GOING FORWARD FIVE YEARS, HOW MUCH MORE OR LESS SIGNIFICANT DO YOU EXPECT THE IMPACT OF REGULATION TO BE FOR YOUR ORGANIZATION OVERALL?



83%

of respondents said the impact of regulation on their organization is **more** or **much more significant** compared to five years ago.





The key post-crisis reforms have a number of central aims. However, in some instances, the objectives are not clear; this is one issue examined below. Generally, the reforms are couched in terms of one or more of the following objectives:

- Stabilizing the financial system and addressing systemic risk;
- Regulating and holding individuals to account for conduct; and
- Enhancing the information available for decision makers in financial markets.



### WHAT IS WORKING?

The regulatory response has addressed many of the specific factors commonly perceived as important in the crisis. Significant steps have been taken toward more effective communication and processes to deal with financial issues and risks that have a globally systemic impact. Mark Carney, Chair of the FSB, said “the financial system today is vastly different from its pre-crisis self. That change didn’t ‘just happen’: it is the intended, positive result of the G-20/FSB reform agenda”; he described the resulting financial system as “safer, simpler and fairer”.<sup>3</sup>

G20 leaders’ summits from 2008 onward, which evolved from former ministerial-level summits has enhanced

focus on key policy developments required after the GFC, and led to the establishment of a more developed cooperative international policy infrastructure to deal with economic and financial matters. The establishment of the formal FSB, has been important in advancing work on many issues that arose during the crisis, and general international regulatory coordination.

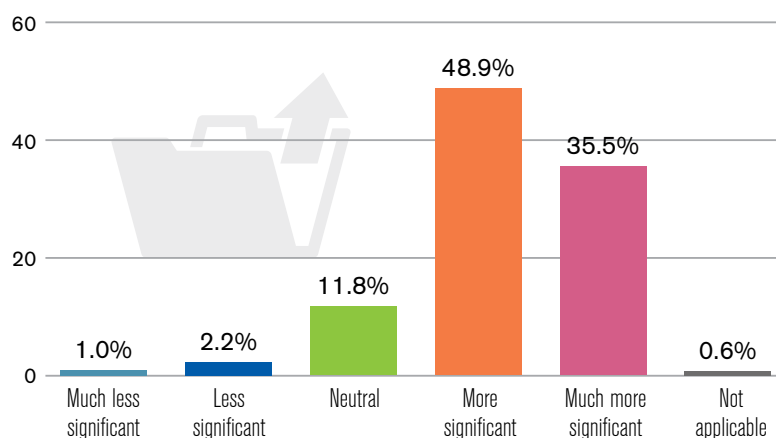
There has been good progress in many areas toward the adoption of consistent international standards, such as the establishment of the compendium of standards recognized by the FSB as “key for sound financial systems and deserving of priority implementation”. Notably, this includes the adoption and implementation of IFRS and ISA.

However, significant work remains to achieve global convergence and consistency, and the challenges and implications of this issue are examined below.

As institutions prepare for the next crisis, significant work remains to achieve consistent regulatory frameworks that will facilitate a rapid, cohesive global response. The challenges and implications of this issue are examined on the next page.



### COMPARED TO FIVE YEARS AGO, HOW MUCH MORE OR LESS SIGNIFICANT IS THE IMPACT OF REGULATION FOR YOUR ORGANIZATION OVERALL?



## 2. THE EVOLVING REGULATORY LANDSCAPE

### WHERE ARE PROBLEMS EMERGING?

#### *Fragmentation and inconsistency*

Fragmentation and inconsistency pose increasing challenges, despite enhanced processes for communication and international coordination. The international accord on policy intentions reached on many important issues contrasts with considerably divergent detail and implementation, and nationally focused regulatory agendas.

The extent to which nationally focused regulation leads to inconsistency and fragmentation raises important questions. To what extent is this due to the need for greater clarity on policy objectives, or other factors such as arbitrage or politicization?

These issues are important to both the regulators, charged with administering and enforcing regulation, and to the citizens impacted by it.

Some commentators observing the immediate post-crisis environment argued that “growing politicization is generating more ambitious regulatory agendas” domestically, making international coordination more difficult and increasing the prospect of fragmentation.<sup>4</sup> More recently, commentators have observed that “a rise in new forms of transnational regulation is

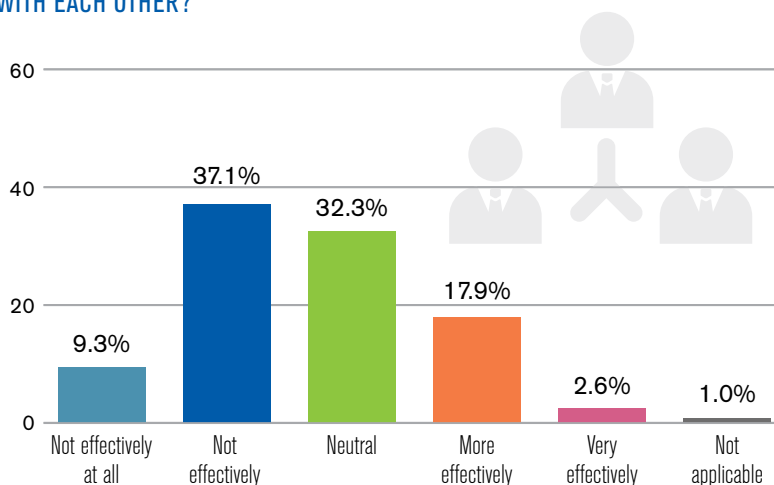
being driven by a range of global and institutional forces including the globalization of the professions, the globalization of professional bodies, the activities of various multilateral organizations such as the World Bank and various United Nations organs, and others.”<sup>5</sup> The Organisation for Economic Cooperation and Development’s Regulatory Policy Outlook in 2015 indicated “countries display a fragmented approach to regulatory policy”.<sup>6</sup>



How can international accord and jurisdictional implementation be made more cohesive?

More than one-third (36%) of respondents to the *IFAC Global Regulatory Survey 2015* said the approach to regulation between different regions in which their organizations operate is not consistent or not at all consistent, while 30% called it consistent or very consistent; 25% took a neutral view. Almost half (48%) of respondents said that different regulators collaborate with each other not effectively or not effectively at all, while 20% cited effective or very effective collaboration; 32% were neutral. One respondent—representative of many—stated: “We need to review the regulatory agenda to have a more consistent and aligned framework. Currently, the approach is often piecemeal in nature and contradictory at times.”

#### HOW EFFECTIVELY DO DIFFERENT REGULATORS COLLABORATE WITH EACH OTHER?



Major jurisdictional differences exist in key aspects of bank capital and liquidity regulation. This includes, for example, how capital is defined, as well as the approach and timing of regulatory implementation. Deutsche Bank Research has indicated that “divergent rules on capital, liquidity, derivatives and banking structures are threatening to fragment the financial markets.” Dialogue within the international regulatory community also indicates preferences for alternative approaches to certain aspects of Basel III, for instance Thomas M. Hoenig, Director, Federal Deposit Insurance Corporation argues “the poor record of Basel I, II and II.5 is that of a system fundamentally flawed...Basel III is a continuation of these efforts, but with more complexity”, and proposes an alternative, simpler approach.<sup>7</sup>

The approach to post-crisis auditing reform generally, and the European Union reforms in particular, present a microcosm of how fragmentation and inconsistency are potentially being built into cross-border regulation. EU auditing reforms introduced in 2014 include more than 80 options, presenting the potential for significant inconsistency between member states. Options include fundamental definitions on the scope of entities included, length of auditor tenure, and restrictions on non-audit services. The Federation of European Accountants notes that “disruption due to different rotation timeframes could lead to additional audit procedures and inefficiencies in the coordination of audits with potential effects on the quality and cost of audits.”<sup>8</sup>

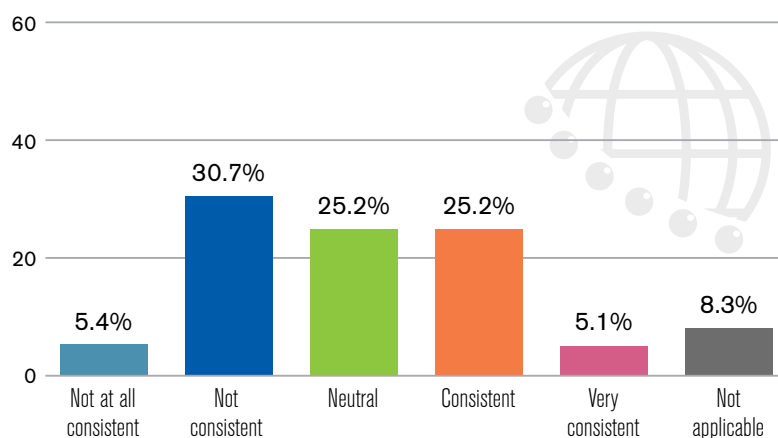
What factors are leading to inconsistencies and fragmentation in the regulatory environment?



Genuine convergence of financial reporting and auditing standards remains an ongoing journey - “Business and capital markets have ‘gone global’, whereas relevant laws, regulations and standards remain predominantly national in nature.”<sup>9</sup>

In addition to existing gaps between IFRS and US GAAP, IFRS appears to be becoming increasingly nuanced in different jurisdictions. Although progress has been achieved in outcomes aimed at converging IFRS and US GAAP, some of the post-GFC responses have led to substantial differences in views, such as financial instruments, credit losses, and leases.

#### HOW CONSISTENT IS THE APPROACH TO REGULATION BETWEEN THE DIFFERENT REGIONS IN WHICH YOUR ORGANIZATION OPERATES?



## 2. THE EVOLVING REGULATORY LANDSCAPE

### COMPLEXITY AND SCALE

Response to the GFC is distinguished by a capacity for rule-making on a scale and complexity far greater than previously thought possible. 79% of respondents to the *IFAC Global Regulatory Survey 2015* perceived that regulation impacting their organizations had become complex or very complex. One respondent stated “the problem is that legislatures are micromanaging government, not-for-profit, and business,” and another that “we would regularly feel that regulations are missing key areas of risk and focusing on areas which are over regulated.”

Important questions surround what general factors are exacerbating regulatory environment complexity, and to what extent it is undue or inappropriate—for instance, a more interconnected and complex financial system and the role of enhanced technological and institutional capacity. When incubated in silos, policies and rules across sectors and regulatory streams may affect complexity from the perspective of both regulated populations, and the system as a whole.

Research has indicated that “incentives for persons that impact drafting and implementation of financial regulation produce a bias towards excessive complexity”.<sup>10</sup>

What factors are exacerbating complexity in the regulatory environment?

While recognizing the benefits of the Basel III reforms, such as enhanced financial system safety and preservation of risk-sensitivity in the capital framework,<sup>11</sup> the complexity of its evolution has been used as an example to highlight the evolving regulatory environment. The first Basel Accord, introduced in 1988, had seven risk categories and required seven calculations; Bank of England Chief Economist Andrew Haldane has remarked that Basel III results in more than 200,000 risk categories, and more than 200,000,000 calculations.

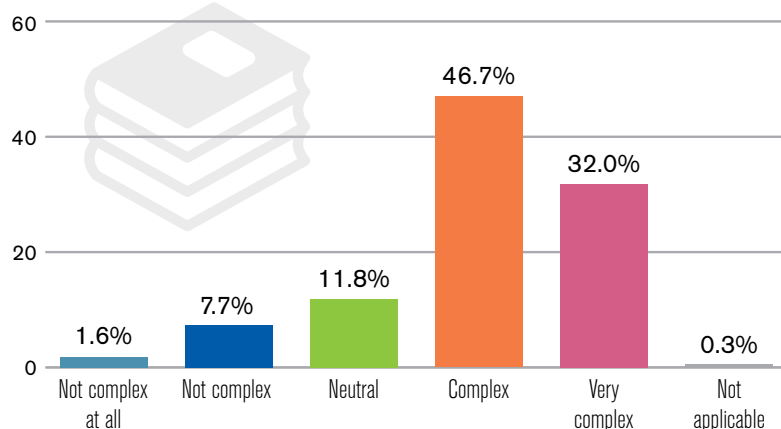


How is complexity impacting capacity to anticipate and respond to emerging risks and future financial shocks?

It is important to recognize complex problems often demand complex solutions, and that inappropriate simplicity can have negative consequences, as can inappropriate complexity. The Institute of International Finance argues that proposals currently being contemplated, which would lead to a reduction of risk-sensitivity as a result of seeking simplicity, could “stand to penalize banks for holding low-risk assets while favoring high-risk exposures”.<sup>12</sup>

How can simplicity be achieved given the complexity of the goal?

### HOW COMPLEX IS THE REGULATION THAT IMPACTS YOUR ORGANIZATION?



The metrics informing broader decision makers in financial markets have also become gradually more complex. To what extent is this arising due to increasingly complex financial markets and businesses? To what extent are responses to regulatory and standards issues exacerbating complexity? This includes financial reporting, where complexity has been increasingly recognized as an issue. For example, the International Accounting Standards Board (IASB) is currently examining increasingly complex financial reporting disclosures. The response to some issues highlighted by the crisis has led to greater complexity and volume of information, with respect to measurement and disclosure, in financial reporting.



## CLARITY OF OBJECTIVES, INCENTIVES, AND IMPACTS

Starting with clear policy objectives, and then building complementary requirements, is generally recognized as essential to good regulation (see also Section 4). The links between post-GFC policy reform objectives and the detail, incentives and intended impacts, have not always been clear.



How can the detail of financial regulatory reforms be better reconciled with objectives?

Research has indicated that banks' responses to capital and liquidity regulation "might create unintended evil: a reduced supply of bank loans, incentives to securitize assets, and adverse incentives on bank risk monitoring".<sup>13</sup> These possible impacts have recently received substantial international interest. However, during the GFC and its immediate aftermath, comprehensive contemplation of impacts was less obvious.

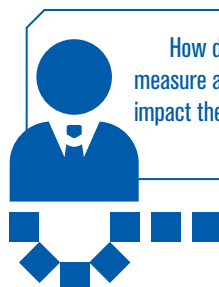
Regulatory approaches taken in many areas are characterized by detailed requirements which create the need for significant investment in, and attention to, routine compliance. Policy aspirations toward accountability, stronger governance, and dealing with emerging risks may not always be synonymous with compliance.



What factors contribute to a lack of clarity or incongruity in policy objectives?

The *Thomson Reuters Annual Cost of Compliance Survey 2015* found "regulatory matters are consuming disproportionate amounts of board time, from correcting non-compliance and preventing further sanctions to implementing structural changes to meet new rules". *IFAC Global Regulatory Survey 2015* respondents agreed, highlighting the impact on scarce time and resources for forward-looking, risk-focused activities.

Corporate treasurers play a critical strategic role in financial risk management. In a 2015 survey, the Association of Corporate Treasurers found they "overwhelmingly feel that financial services regulation has a negative impact on what they do".<sup>14</sup>



How does the way regulators measure and report performance impact the incentive for forward-looking innovation?

Audit file inspection programs help identify issues and promote continuous audit quality improvement. The remit of audit oversight bodies often necessarily

focuses on a subset of quality and documentation, and inspections have led to constructive efforts to improve audit quality.

However, since the GFC these programs received wide public attention, as a proxy for general audit quality, and the auditing profession. Given the importance of innovation in rapidly

How can regulatory compliance and reporting be balanced with the need for forward-looking, risk-focused activities?



evolving financial markets and business environments, it's important to consider how this impacts incentives for auditors to think holistically about their role and new ways of addressing risk.

Some post-GFC auditing regulation provides further significant examples unclear policy objective-setting. Objectives related to audit market competition, audit quality, and financial market confidence have been used interchangeably in a number of regions to support regulatory proposals. In some instances, detailed regulatory proposals appear to precede formulation of clear objectives. What factors have led to these incongruities? How have structures designed to ensure clarity of regulatory reform objectives performed?

### 3. WHAT'S THE COST, WHO PAYS AND WHO BENEFITS?

This section queries the evolving regulatory landscape's cost and benefits, and where they are being felt. A focused discussion about which groups are advantaged or disadvantaged most sharply is important to understanding the lessons and ramifications of the post-GFC regulatory environment.

While on a stand-alone basis, G-20 reforms appear logical, the total impact of all the reforms, including measures undertaken locally without international mandate, need to be examined for their impact on markets, sectors, and overall global growth.

#### COMPLIANCE COSTS

Assessing the cost of regulatory compliance and administration in the post-GFC environment is challenging. However, there are indications of a substantial increase.

In the *IFAC Global Regulation Survey 2015*, 80% of respondents indicated that regulation was having a significant or very significant impact on the cost of doing business. In relation to accounting and financial services, respondents pointed to substantial cost increases in keeping up and complying with new regulation. One respondent

said, "The regulatory burden seems to have been materially increased with no consideration of the cost to the real economy of industry and commerce, hence to society".

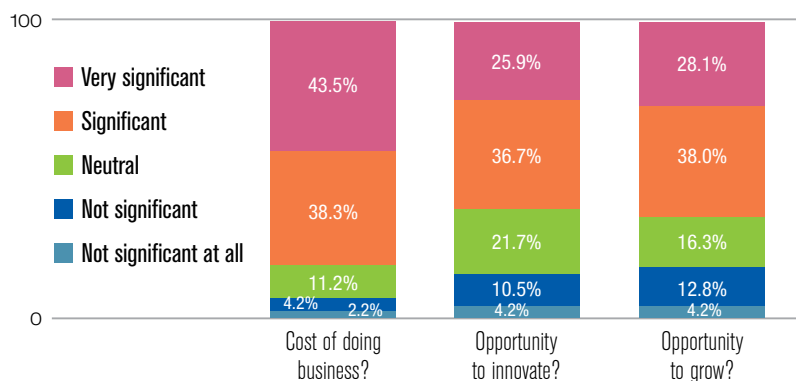
The *Thomson Reuters Annual Cost of Compliance Survey 2015* found that demand for skilled compliance staff was driving up costs, and more than two thirds of respondents expected a compliance budget increase in 2015. Trends in large financial institutions show consistent increases in head count and spending on post-GFC compliance.

How have regulatory compliance and reporting costs changed since the crisis?



Public sector expenditure on financial regulation administration has faced the same significant pressures as other government priorities in a current climate of slow economic growth. With reduced budgets, there are signs that some regulators are struggling to perform the functions expected of them. In some cases, steps toward levies and 'user pays' funding, rather than funding out of general government revenue, are being taken in an effort to increase and provide more stable funding.

#### HOW SIGNIFICANT IS THE REGULATION THAT IMPACTS YOUR ORGANIZATIONS...

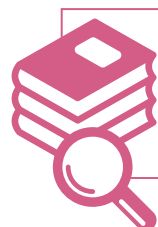


How can the return on compliance expenditure be maximized toward addressing risk?

## ECONOMIC AND BROADER ASPECTS

While experts disagree on the broader economic cost and impact of post-GFC regulatory reforms, the impact of regulatory fragmentation and inconsistency could be significant. The Organisation for Economic Co-operation and Development (OECD) found that the “recent economic crisis has underscored the power of globalization but has also shown the vulnerability of the global economic system”,<sup>15</sup> pointing to the “economic interdependence between countries”. The OECD Economic Outlook in June 2015 points to important impacts of regulatory uncertainty, and harmonization or lack thereof, in terms of foreign direct investment and trade across multiple major OECD countries.<sup>16</sup>

Are regulators resourced adequately to match their remit and expectations?



What aspects of post-crisis financial regulatory reforms are impacting SMEs disproportionately?

The Atlantic Council, TheCityUK, and Thomson Reuters, which have studied regulatory divergence, highlight a range of costs: “divergent practices help enable regulatory arbitrage that can undermine the effectiveness and stability of the global financial system, as well as undermine the ability of transatlantic financial authorities to export their regulatory approaches and best practices to the rest of the world [and] can introduce duplicative or inefficient practices for both providers and users of capital, thereby undermining global economic growth and, by extension, job creation”.<sup>17</sup>

How does regulatory fragmentation and inconsistency impact multinational business decision making and investment?



Respondents to the *IFAC Global Regulatory Survey 2015* working in Multinational Entities (MNE) described cross-border operations challenges, including with different and sometimes conflicting regulatory approaches. Understanding how these conflicts impact planning, decision making, and the outlook of MNEs seeking to grow and increase their multinational presence is critical.

Small- and medium-sized entities (SMEs) may be impacted disproportionately in the evolving regulatory environment. The challenges facing SMEs in terms of investment, financing, and growth are widespread, and included in the *Turkish G-20 Presidency Priorities for 2015*.

How is the evolving regulatory environment impacting the attractiveness of professional and governance roles?



In contrast with periods after previous recessions, Goldman Sachs found that United States-based SMEs have underperformed larger entities since the GFC. SMEs have traditionally been central to recovery. Goldman's 2015 report, *The Two Speed Economy*, states “the most widely-cited and perhaps the most likely explanation for much of the split that we observe between the performance of large and small businesses is the cumulative impact of the new regulations and related policy actions that have been taken since the crisis”.<sup>18</sup>

More stringent banking capital requirements have been raised as an impediment to the provision of longer-term funding for governments and infrastructure development. The importance of significant medium-term infrastructure development is well documented, with developing countries particularly in need.

Strong governance, ethics, and professionalism are increasingly highlighted as vital to addressing the issues and failures that emerged in the crisis. Understanding how the regulatory environment is impacting the attractiveness of crucial professional and governance roles is important.

## 4. WHAT IS GOOD REGULATION?

This section compares recognized regulatory principles and recommendations issued by key international organizations involved in post-crisis financial regulatory reforms, including IOSCO, IFIAR, BCBS, OECD, and IFAC.

### PRINCIPLES OF GOOD REGULATION

The following table sets out nine commonly cited themes, with relevant statements from key international organizations and recognized regulatory policy frameworks.

Key players in the development of post-GFC financial regulatory reforms are noticeably consistent on principles of good regulation.

It is highly relevant to consider why divergence from these principles occurs at implementation stage. How have time and resource pressures during and since the crisis impacted the capacity for clear objectives, an evidence basis, and adequate consultation in financial regulatory reforms? What lessons can be learned and applied on an ongoing basis? How can good regulation help anticipate and respond to future financial shocks?



<b>CLEAR OBJECTIVES IN THE PUBLIC INTEREST</b>	<p><b>IOSCO:</b><sup>19</sup> “The responsibilities of the Regulator should be clear and objectively stated.”</p> <p><b>IFIAR:</b><sup>20</sup> “The responsibilities and powers of audit regulators should serve the public interest and be clearly and objectively stated in legislation.”</p> <p><b>BCBS:</b><sup>21</sup> “An effective system of banking supervision has clear responsibilities and objectives for each authority involved in the supervision of banks and banking groups.”</p> <p><b>OECD:</b><sup>22</sup> “Policy should have clear objectives and frameworks for implementation.”</p> <p>“Clearly identify policy goals, and evaluate if regulation is necessary and how it can be most effective and efficient in achieving those goals.”</p> <p>“Role clarity is essential for a regulator to understand and fulfil its role effectively.”</p>
<b>PROPORTIONATE AND BALANCED</b>	<p><b>IFAC:</b><sup>23</sup> To meet the public interest, regulation must be proportionate.”</p> <p><b>OECD:</b> “to ensure that, if regulation is used, the economic, social and environmental benefits justify the costs, the distributional effects are considered and the net benefits are maximized.”</p> <p>“Consider means other than regulation and identify the trade-offs of the different approaches analyzed to identify the best approach.”</p> <p>“As appropriate apply risk assessment, risk management, and risk communication strategies to the design and implementation of regulations to ensure that regulation is targeted and effective.”</p>
<b>EVIDENCE BASED</b>	<p><b>IFAC:</b> “The benefits of regulation to the economy and society should outweigh the costs of that regulation.”</p> <p><b>OECD:</b> “Integrate Regulatory Impact Assessment (RIA) into the early stages of the policy process for the formulation of new regulatory proposals.”</p>



<b>APPROPRIATELY RESOURCED</b>	<p><b>BCBS:</b> “The supervisor possesses operational independence, transparent processes, sound governance, budgetary processes that do not undermine autonomy and adequate resources, and is accountable for the discharge of its duties and use of its resources.”</p> <p><b>IOSCO:</b> “The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.”</p> <p>“The Regulator should be operationally independent and accountable in the exercise of its functions and powers.”</p>
<b>COOPERATIVE</b>	<p><b>BCBS:</b> “Laws, regulations or other arrangements provide a framework for cooperation and collaboration with relevant domestic authorities and foreign supervisors.”</p> <p><b>IFIAR:</b> “Audit regulators should make appropriate arrangements for cooperation with other audit regulators and, where relevant, other third parties.”</p> <p><b>OECD:</b> “In developing regulatory measures, give consideration to all relevant international standards and frameworks for co-operation in the same field and, where appropriate, their likely effects on parties outside the jurisdiction.”</p>
<b>CONSISTENT AND COHERENT</b>	<p><b>IOSCO:</b> “The Regulator should adopt clear and consistent regulatory processes.”</p> <p><b>OECD:</b> “Where appropriate promote regulatory coherence through co-ordination mechanisms between the supranational, the national and sub-national levels of government.”</p>
<b>TRANSPARENCY AND OPEN CONSULTATION</b>	<p><b>IOSCO:</b> “In exercising its powers and discharging its functions, the regulator should adopt processes which are...transparent to the public”.</p> <p><b>IFIAR:</b> “Audit regulators should be transparent and accountable.”</p> <p><b>IFAC:</b> “Transparency is particularly important as it enables the public to know and understand how the profession is being regulated and what the regulator is doing.”</p> <p><b>OECD:</b> “Adhere to principles of open government, including transparency and participation in the regulatory process to ensure that regulation serves the public interest and is informed by the legitimate needs of those interested in and affected by regulation.”</p> <p>“Regularly publish reports on the performance of regulatory policy and reform programs and the public authorities applying the regulations.”</p>
<b>ACTIVE OVERSIGHT</b>	<p><b>IFAC:</b> “Regulatory bodies should have robust governance arrangements and publicly disclose details of their activities.”</p> <p><b>OECD:</b> “Establish mechanisms and institutions to actively provide oversight of regulatory policy procedures and goals, support and implement regulatory policy, and thereby foster regulatory quality.”</p>
<b>SYSTEMATIC REVIEW</b>	<p><b>IOSCO:</b> “The Regulator should have or contribute to a process to review the perimeter of regulation regularly.”</p> <p><b>IFAC:</b> “To meet the public interest, regulation must be...subject to regular review”.</p> <p><b>OECD:</b> “Conduct systematic program reviews of the stock of significant regulation against clearly defined policy goals”</p>

## 5. CONTRIBUTING TO THIS INITIATIVE

### COMMENTS AND RESEARCH

IFAC welcomes written comments on the issues and questions raised in this document, as well as engagement with the academic community on relevant research. These inputs along with views raised in the roundtable discussions will further inform IFAC's public policy agenda.

Please submit comments to Amir Ghandar (Principal Author), Senior Policy Advisor, Public Policy and Regulation, IFAC, at [amirghandar@ifac.org](mailto:amirghandar@ifac.org), by March 31, 2016.



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David Schraa Regulatory Counsel, Regulatory Affairs Department, Institute of International Finance.

## ENDNOTES

1. This document is not intended as a policy position or comprehensive research paper.
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17. Atlantic Council, The City UK, Thomson Reuters, 'The Danger of Divergence: Transatlantic Financial Reform & the G-20 Agenda Report', 14 February 2014.
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19. Throughout this table "IOSCO" refers to International Organization of Securities Commissions, 'The Objectives and Principles of Securities Regulation', 2003.
20. Throughout this table "IFIAR" refers to International Forum of Independent Audit Regulators, 'Core Principles for Independent Audit Regulators'.
21. Throughout this table "BCBS" refers to Basel Committee on Banking Supervision, 'Core Principles for Effective Banking Supervision', 2012.
22. Throughout this table "OECD" refers to Organisation for Economic Cooperation and Development, 'Recommendation of the Council on Regulatory Policy and Governance', 2012.
23. Throughout this table "IFAC" refers to International Federation of Accountants, 'Policy Position Paper 1 Regulation of the Accountancy Profession', 2011.

The IFAC logo is a blue hexagon with a white geometric pattern inside, resembling a stylized 'A' or a network of lines.

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