Understanding and adapting to the regulatory environment: An IOSCO perspective

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CHECK AGAINST DELIVERY

Introduction

I've been invited to speak to you today as Chairman of the International Organization of Securities Commissions (IOSCO).

In that capacity, I want to discuss three main topics:

- IOSCO and its role in financial regulation
- IOSCO's work on securitisation since the global financial crisis (GFC) – here I will focus on the reports we released in 2009 and 2012, and
- IOSCO's current work with the Basel Committee on Banking Supervision (Basel Committee). Here I'd like to provide:
  - background on why we are working with the Basel Committee on securitisation, and
  - details on an upcoming consultation paper we are releasing to help improve investor trust and confidence in securitisation transactions.

Afterwards, I'm happy to take questions.

Before I start, it is worth noting that although I'm wearing a different hat to the one I have worn at many previous conferences both here and in the United States – and Europe and Asia – my message has not really changed.

My message has three elements. The first is recognising the integral role securitisation has in financing the real economy globally. It has done so in the past. It has the potential to do so again – but only if we build sustainable securitisation markets.

The second is recognising that building sustainable securitisation markets is a joint project – between industry, regulators and policy makers. Our role as regulators and for policy makers is to develop the right regulatory settings. But what we cannot – and should not – do this on our own. We need to work with you to make sure the settings we have are the right ones and do not have unintended consequences.

The third element – and I say this having sat on both sides of the fence – is the need for all of us to focus on investors, particularly real money investors – what they need and want – in building sustainable securitisation markets.

IOSCO and its role in financial regulation

Now on to my first main topic – IOSCO and its role in financial regulation. I'd like to describe IOSCO, who we are and what we do.

IOSCO brings together financial services and markets regulators from 115 jurisdictions. Together our members account for 95% of global capital markets (valued at in excess of $US 200 trillion) of the world's securities markets.

The Board I have chaired since 2013 – and will continue to Chair until 2016 – now comprises the leaders of 34 regulators, drawn from every continent.

The strength of our Board lies in the breadth and diversity of our membership. It includes the leaders of authorities in every major capital market and from the largest growth and emerging economies, including China, Brazil, India and frontier economies

Collectively our objectives are the same – to enable markets to allocate capital to the real economy by ensuring investors have trust and confidence in using them and by ensuring they operate in a fair, orderly and transparent way.

My vision for IOSCO has been for us to be proactive, forward-looking and to be seen by regulators, policy makers and industry as the key global reference point for capital markets regulation.

We have worked towards this under my Chairmanship by:

- identifying emerging risks to the markets we regulate
- developing standards and guidance to address emerging issues and risks. If we are not ahead of the game, individual jurisdictions will develop their own approaches, and
- supporting global implementation, including by building the regulatory capacity of our members.

Working with industry has been a key part of our work.

I'd like to now expand on these first two points:

- identifying emerging risks, and
- developing standards and guidance.

On emerging risks we have highlighted:

- the real risks posed by weaknesses in cyber security and in corporate governance
- the need to use behavioural science to build a more effective regulatory tool kit, and

- how growth and emerging markets should go about attracting patient capital to support their growth agenda.

On standard setting, we have developed guidance in key areas, including financial benchmarks, financial market infrastructure and over-the-counter derivatives.

We are also working on initiatives to improve audit quality, improve cyber resilience in the firms we regulate and reduce regulatory barriers to cross-border capital markets.

Our aim is for our guidance to be the basis for consistent global approaches to regulation – because it is timely, granular and clear about what it is intended to achieve. Our guidance should facilitate mutual recognition between markets.

I should also say that we have been very active in highlighting the role capital markets can play in supporting sustainable economic growth.

A great example of this is a report we published in early-October which highlighted, to the Group of Twenty (G20) Leaders and the Financial Stability Board (FSB), twenty examples of capital markets being used to successfully finance infrastructure and small to medium-sized enterprise activity. Securitisation figured very significantly in these examples.

IOSCO's work on securitisation since the GFC

Now, I'd like to move on to the second topic – the work IOSCO has done on securitisation since the GFC.

We have had the regulation of securitisation activities and markets on our agenda since late 2008. We have published two reports, one in 2009 and one in 2012.

Both have influenced global thinking on regulation. Both have recognised the need for industry, policy makers and regulators to work together. Both have emphasised that non-bank investors hold the key to building sustainable securitisation markets.

Let me touch briefly on these reports.

2009 IOSCO report

The first report was our 2009 report, *Unregulated financial markets and products*.[1]

This report was IOSCO's immediate response to the events of 2007 and 2008, and set out what IOSCO thought was needed at the time to rebuild trust and confidence in securitisation markets.

Its focus was on realigning incentives across the securitisation value chain, improving disclosure to investors about the underlying asset pool, and the independence of service providers.

It built heavily on work done by McKinsey & Company for the global securitisation forums on disclosure and standardisation.[2]

Importantly, the report recognised that restoring confidence was a joint industry-regulatory project. The report made it clear that industry initiatives alone would not be enough to restore confidence in the market. It recommended a measured response from policy makers by helping the market develop.

The report was widely endorsed and set the tone for discussions in the global regulatory community

2012 IOSCO report

Our second report, which was published in 2012, was prepared at the request of the FSB.[3] Its main focus was on coming to grips with why global markets were not recovering and on what was impeding cross-border activity.

This work – which I led – was supported by roundtables and discussions with industry to understand their perspectives.

Our report highlighted issues with implementation of reforms in areas touched on in our 2009 recommendations. For instance, jurisdictions had taken different approaches – or were still developing different approaches – to incentive alignment and disclosure.

These differences – and uncertainty about where reform was heading – made issuers and investors reluctant to return to securitisation markets.

We made recommendations intended to address these problems, including:

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[1] IOSCO, *Unregulated financial markets and products*, final report, September 2009.
[2] American Securitization Forum (ASF), Securities Industry and Financial Markets Association (SIFMA), Australian Securitisation Forum (AuSF), and European Securitisation Forum (ESF), *Restoring confidence in the securitization markets*, 3 December 2008.
[3] IOSCO, *Global developments in securitisation regulation*, final report, 16 November 2012.

- more detailed guidance on incentive-alignment approaches and transparency
- recommendations that incentive-alignment approaches be implemented – with an implementation review to be conducted during 2014, and
- recommendations about standardisation.

We also identified a number of other issues, including prudential treatment of securitised and collateralised products and accounting issues, which we thought needed to be addressed.

Early indications are that some progress has been made across G20 jurisdictions in implementing our recommendations, but further work is needed.

IOSCO’s current work with the Basel Committee

I’d now like to turn to my third and final topic, IOSCO’s current work with the Basel Committee.

I had hoped to be able to share with you the consultation paper we are working on, but the document is currently going through the approval processes of the Board of IOSCO.

We expect it to be issued in early-December with a consultation period of around two months. I would encourage you all to carefully consider and comment on the consultation paper.

In talking about IOSCO’s work with the Basel Committee I’d like to provide:

- background on why we are working with the Basel Committee, and
- some indication about what you can expect to see in the consultation paper.

Background

Let me first provide some background. We were asked to do this work by the FSB late last year. An important driver was concern that some securitisation markets had been slow to recover in some regions.

The concern was strongest in Europe, where economic recovery has been slow and authorities have been looking to encourage diversification of funding of the real economy through market-based financing.

The mandate we were given had two elements:

- The first was to understand and identify potential impediments to the development of sustainable securitisation markets, with a particular focus on the participation of non-bank investors.
- The second was to develop criteria to identify and assist the industry to develop simple and transparent securitisation structures.

Our work to date has involved discussions with industry at a roundtable in London – which a number of you attended – followed by a survey of over 100 market participants, including a significant number of non-bank investors, and 30 regulators and supervisors.[4] These were supplemented by interviews with market participants in eight jurisdictions.

Two points are worth noting about our work. The first is that it was cross-sectoral. This reflects our belief that the design of solutions will benefit from the insights from regulators in each sector, including banking, insurance, securities and accounting.

The task force draws its members from 40 jurisdictions, including securities regulators, banking supervisors and insurance supervisors. It has representatives from standard setters from each of these sectors, including accounting standard setters. I chair the task force with David Rule from the Bank of England, representing the Basel Committee.

The second is the focus on understanding how to get more real-money investors into securitisation markets. Getting these investors into markets we believe is the key link to developing sustainable securitisation markets.

The consultation paper

Let me now turn to what you can expect to see in the consultation paper.

Our survey and interviews with industry have pointed to three main impediments to investors participating in securitisation markets on an ongoing basis:

- The first, which is not a surprise, is the negative perception of securitisation as an asset class. The post-GFC stigma remains.
- The second is that investors, particularly non-bank investors, are looking for three things – certainty, neutrality and consistency in regulatory treatment.
- The third is the challenges investors say they face in assessing the risks of the products they are being offered.

[4] Following the survey questions used by McKinsey & Company, commissioned by ASF, SIFMA, AuSF, and ESF, *Restoring confidence in the securitization markets*, 3 December 2008.

Investors want greater comfort and confidence when doing their due diligence on potential securitisation investments.

Based on the survey and discussion with investors, the consultation paper addresses these concerns by describing the criteria or features of securitisation structures which we believe will address investors' concerns.

The consultation paper will set out criteria around three themes which are considered a good basis for trust and confidence:

- simplicity ('S')
- transparency ('T'), and
- comparability ('C').

The consultation paper will focus on three categories of risks and the type of features securitisation structures that might meet the STC criteria:

- asset risks
- structural risks, and
- fiduciary and servicer risks.

I should emphasise that the proposed criteria are not of themselves a prescription for regulatory action and reform. This was outside the scope of our mandate. They reflect a consensus based on feedback from real-money investors.

Instead, they are intended to assist industry in developing securitisations which will support sustainable markets underpinned by ongoing real-money investor participation.

The key take-away for industry from our work will be the need to focus on real-money investors – and to do so in two ways.

The first is about focussing on products real-money investors want. Our sense from the surveys and discussions with non-bank investors is that they are looking for simplicity and comparability. Many are more likely to be attracted, for instance, to products with characteristics which mean they can be included in the underlying indexes against which they are measured.

The second is the information investors should get about what is being offered. This is a key focus of the consultation paper. The criteria we set out in the consultation paper are about investors having greater access to:

- comprehensive and reliable performance information
- information about the underlying asset profile, including its performance during the life of the transaction, and
- information about the structure.

Conclusion

I'd like to conclude by re-iterating that, from IOSCO's perspective, we see sustainable securitisation markets as making an important contribution to global economic growth.

We believe that our work to date, particularly our current work with the Basel Committee, is laying a foundation for building sustainable securitisation markets.

Thank you.

I would be happy to take any questions you may have.

