



Credible Deterrence

IOSCO Committee 4 on
Enforcement and Information Sharing



Purpose of the report

To **identify** and **promote** awareness of those factors that may **credibly deter misconduct** in securities and investments **markets**.

A successful credible deterrence strategy can:

- modify behaviour;
- reduce securities law violations;
- increase investor protection;
- create an environment in which fair and efficient markets can thrive.

However: the report is **not an assessment tool** but a **think piece**.

Enforcement focus

- While other regulatory activities may help deter misconduct, enforcement plays a central role.
- The paper focuses primarily on those factors that are within the remit of enforcement programmes.
- **Credible Deterrence is a key component of any effective enforcement strategy.**

Who will find the report useful

- This report is an important tool to help regulators design, develop, review and consider their enforcement strategies.
- It is of interest to both emerging market regulators and regulators in developed markets.
- The report draws on the collective experience and expertise of Committee 4 members.
- It is unique in that it offers real life examples of Credible Deterrence in action.

Tailored deterrence

Credible Deterrence cannot be one size fits all.

Regulators need to decide what it means for them in the context of:

- their strategic objectives;
- their powers and responsibilities;
- their local economic, financial and market context.

What makes deterrence credible

Deterrence is **credible** when:

- A. would-be wrongdoers perceive that the **risks** of engaging in misconduct **outweigh** the **rewards**, and;
- B. when **non-compliant attitudes** and behaviours are **discouraged**.

Deterrence **occurs** when individuals and entities who are contemplating engaging in misconduct are dissuaded from doing so because:

- A. they have an **expectation of detection** and;
- B. that detection will be rigorously **investigated, prosecuted and punished**.

Key Factors to a Credible Deterrence strategy

The report recognises that despite the need for specific jurisdictional tailoring, there are certain general key factors that apply to Credible Deterrence strategies generally:

- 1. Legal certainty;**
- 2. Detecting misconduct;**
- 3. Regulatory co-operation and collaboration;**
- 4. Investigation and prosecution of misconduct;**
- 5. Sanctions;**
- 6. Public messaging;**
- 7. Regulatory governance.**

Legal certainty

- The quality of legal and regulatory frameworks and the laws that underpin them play a prominent role in shaping behaviour by creating and enforcing a system of incentives and disincentives.
- Frameworks that provide legal certainty:
 - Inspire confidence in the administration of justice and regulation;
 - Establish a platform upon which individuals and entities can organise their affairs in a lawful manner; and
 - Allow individuals and entities to understand that if they act in a manner that is outside the law they will be held accountable.

Detecting misconduct

- Using mechanisms to detect misconduct in a timely way will create an environment in which those contemplating or involved in misconduct have an expectation that they will be caught.
- Well connected regulators with access to sources of intelligence providing real time information will be more likely to detect misconduct before it causes harm to investors or markets.

Regulatory co-operation and collaboration

- Potential wrongdoers may be deterred from engaging in misconduct when they know that securities regulators are working with criminal authorities and other domestic, national and international agencies to strengthen their detection, investigation, prosecution and sanctioning capabilities.
- Wrongdoers will understand that they cannot hide behind borders.
- **No safe havens.**

Investigation and prosecution of misconduct

- Potential wrongdoers may be deterred from engaging in misconduct when:
 - They realise that regulators will hold wrongdoers accountable for their actions;
 - They will be swiftly investigated, prosecuted, and sanctioned.
- Timely enforcement interventions prevent misconduct crystallising into investor detriment and harm to market integrity.

Sanctions

- Sanctions can be a deterrent to wrongdoing and recidivism when they are consistently and reliably applied and have a meaningful correlation to:
 - The gravity of the misconduct;
 - The economic and social impact of the misconduct;
 - The unjust enrichment of the wrongdoer;
 - The cost to investors.
- When the cost of engaging in misconduct is greater than the reward, potential wrongdoers may be dissuaded from engaging in it.
- Regulators who have and use an array of regulatory responses and sanctions are more likely to deter potential wrongdoers' involvement in misconduct.

Public messaging

- Public messaging and understanding of regulatory mandates strengthens deterrence by informing wrongdoers that:
 - Misconduct will be detected, investigated and sanctioned;
 - Regulators are working together to enforce the law and hold individuals and entities accountable.
- Regulators who communicate their objectives, mandates and outcomes enhance the deterrent impact of enforcement activities.
- Public messages send a clear signal as to what behaviour is unacceptable and thereby help to set industry standards.

Regulatory governance

- To be more organisationally agile and more responsive to emerging risks, regulators should continually evolve their enforcement strategies by:
 - **Regularly reviewing** their governance arrangements;
 - **Prioritising** and allocating resources;
 - Ensuring that enforcement **tools are fit for purpose.**
- When regulation is well designed and regulators have well developed enforcement strategies then the risk of engaging in misconduct will outweigh the benefit.

Closing remarks

- ❖ The factors referred to previously and explained in detail in the paper are not weighted or ordered in any priority – each can contribute to deterrence in different ways.
- ❖ Jurisdictions and regulators seeking to maximise deterrence within their regulatory frameworks may find some or all of the factors worthy of further consideration.
- ❖ The effectiveness of the factors may be influenced by:
 - The unique legal and regulatory characteristics of each jurisdiction;
 - The political and economic framework;
 - The specific facts, circumstances and nature of the conduct to be deterred, and;
 - The social, cultural, and economic environment.