

Public statement Steven Maijor IOSCO Beijing 2012, 16 May

Ladies and gentlemen,

I would first like to thank our Chinese colleagues for organizing the 2012 annual IOSCO event. I am very impressed by the warm hospitality and smooth organisation of the conference and it is great that we all have the opportunity to spend a few days in the wonderful city of Beijing. In addition, and probably more importantly, holding the annual event here reflects the importance of China, and Asia more generally, for current international financial markets.

ESMA

As ESMA is for the first time formally represented at an annual IOSCO meeting I feel obliged to briefly introduce my organisation. ESMA's mission is to enhance the protection of investors and promote stable and well-functioning financial markets in the European Union (EU). As an independent institution, ESMA achieves this aim by building a single rule book for EU financial markets and ensuring its consistent application across the EU. ESMA contributes to the regulation of financial services firms with a pan-European reach, either through direct supervision or through the active coordination of national supervisory activity. To briefly illustrate some of our activities, we have already made technical standards for Credit Rating Agencies (CRAs) and short-selling and now we are drafting technical standards for OTC derivatives. In addition, CRAs are under our direct supervision and we will participate in the supervisory colleges of CCPs.

To achieve our mission, we extensively cooperate with the 27 national EU securities regulators who are all represented in our Board of Supervisors.

On the international side, we foster dialogue and cooperation with supervisors outside the EU. We are empowered to develop contacts and enter into administrative arrangements with the supervisory authorities and administrations of so-called 3rd countries and with international organisations. For example, we are currently coordinating the negotiation of memoranda of

understanding between the EU and non-EU authorities for the supervision of alternative investment funds managers that operate on a cross-border basis and we have frequent bilateral and multilateral contacts relating to the regulation of OTC derivatives. Also, ESMA intends to become an active member within IOSCO in the fields of its direct competence.

Let me conclude on this brief description by emphasising that ESMA also has, in addition to the traditional objectives of transparency and investor protection, financial stability as an objective. This is consistent with the increased focus by securities markets regulators across the world on stability concerns in response to the financial crisis. Essential elements of achieving this objective are identifying stability risks and conducting stress tests of market players. For us, like for other securities regulators, this is a relatively new area, and exchanging experiences with other securities regulators across the world would be highly beneficial. This exchange should not be limited to possible models, frameworks, and methodologies, but also the exchange of identified stability risks. It is difficult to think of stability risks that have no cross-border implications. IOSCO has started work on the stability objective and I strongly support further work in this area.

The rationales for broadly common regulation of international financial markets

Let me now move on to the subject matter of this panel. Why is it so important to aim for broadly common regulation of financial markets at world-wide level? In the middle of this ongoing worldwide financial crisis it would be foolish not to support broadly common regulation of international financial markets. Still, I would like to give you my views on the main reasons for common regulation as we need to continuously keep them in mind when reforming international financial markets.

First, many market participants, both on the investor side and the industry side, operate on a global level. Therefore, to achieve the same level of investor protection and to minimise the extra costs of doing business at the international level, common regulation is desirable.

Second, financial markets are very sensitive and responsive to regulatory differences, and this holds especially for wholesale financial markets. Differences in regulation will affect where financial activities are conducted. To avoid regulatory competition, where regions are undercutting each other with laxer but also more risky regulation, we need to cooperate to achieve the same level of robust regulation. Competition is the right model for markets, not for regulation and supervision. Common regulation also increases the acceptance by the financial industry in our local markets of the far-reaching consequences of regulatory reforms. The additional costs of new regulations are more palatable when the industry knows that their international competitors are confronted with the same costs. I should also mention here that the committee that laid the foundations for the establishment of ESMA, the De Larosiere committee, considered regulatory competition to be one of the most important causes of this financial crisis.

Third, the performance of financial markets in countries and regions across the world is strongly linked. No financial market can isolate itself from the performance of other markets across the world. Hence, the value of a well-regulated home market is constrained by the potential risks of lax regulated markets abroad. Therefore, we all have a strong interest that not only our own financial market is well-regulated, but also all other foreign markets to which our home market is exposed. This also goes back to my earlier point that we need to exchange information on stability risks.

Achieving common international regulation

Let me now move on to how we can achieve broadly common regulation of financial markets across the world. That achieving this objective is difficult and hard work needs no further explanation at this event. IOSCO is the most experienced organisation in this respect and its members are well aware of all the difficulties involved in international cooperation but also that in the end we do progress. I would like to comment on two specific issues relating to achieving broadly common regulation of international financial markets. The first issue concerns the regulation of internationally active market players by various national regulators. The second issue concerns the relationship

between securities markets regulators and our governments who decide on the core regulation with which we have to work.

International market participants and national regulators

When regulating national or, in the case of the EU, regional financial markets, the issue needs to be addressed of how international market players are regulated. To illustrate this with the European perspective, and also the European terminology: How do we for example regulate market players like CRAs, hedge funds, private equity firms, and CCPs from 3rd countries doing business in the EU? To provide EU investors with the same level of protection, and to create a level playing field with EU market players, these 3rd country market players need to meet the same EU requirements. This automatically raises the potential problem of market players becoming subject to multiple regulatory regimes. These potential problems can be controlled under two conditions. The first one is that the regulatory requirements of the 3rd country and EU are broadly similar. More common regulations between home and host countries obviously limit the potential problems facing cross-border entities and activities. I will discuss achieving broadly common regulation later in my contribution. Secondly, we must avoid circumstances where market players are subject to two, or even more, sets of day to day regulatory demands.

In this context, I believe that the easiest and most efficient option is a system based on equivalence and relying on mutual recognition. Without mutual recognition, entities operating on a cross-border basis would be subject to different requirements and to the jurisdiction of different authorities. This exposes them to potentially conflicting requirements and to higher compliance costs. Of course, I fully understand that before you rely on a foreign regulatory system its robustness needs to be assessed. Hence, the equivalence needs to be assessed of the home country regulation and supervision of the foreign market player. However, when the home country regulation and supervision achieve similar outcomes, we will need to rely on mutual recognition and co-operation with the home country regulator. This cooperation with the home country regulator is essential to ensure that when needed and in response to

specific risks you can supervise the 3rd country market participant in the same way as domestic market participants.

Governments and securities regulators

Much of the regulation with which we have to work as securities regulators depends on decisions by our governments. As we are all aware, there is no governance mechanism at worldwide level which ensures that governments take coordinated decisions regarding the regulation of financial markets. The EU has developed such a mechanism after many decades: the European Commission, Council, and EU Parliament can decide on Directives and Regulations, and ESMA now has the powers to write technical standards.

While we should obviously respect the sovereignty of governments, I have already made clear what the benefits are of broadly common regulation of international financial markets. Not achieving broadly common regulation will inevitably lead to different levels of investor protection, as well as an uneven playing field and extra costs for market players. Hence, sovereign governments can obviously deviate locally, but such deviations come at a high price.

I should now qualify my statement that there is no governance mechanism at world-wide level ensuring that governments take coordinated action regarding financial market regulation. One of the few positive results of the financial crisis is the G20 commitments on financial market reform and the new role of the Financial Stability Board. As a result of these G20 commitments, the regulatory developments in the main financial centres of the world are broadly similar on such issues as CRAs, hedge funds and OTC derivatives. Of course, we all know the complaints by industry on differences in regulation across the world. While we should not deny these differences and be complacent, I would like to be positive on what the G20 commitments have achieved.

The key of the success of the G20 commitments is that they have driven the law making by governments and this has resulted in relatively common laws with which we have to work as securities regulators. It is clear that the financial crisis has provided the catalyst for the G20 commitments. However, we should not need a crisis to let this system work. How can we help as the

international community of securities regulators to ensure that the process above runs well? We should not only cooperate *after* our governments have taken decisions on financial market regulation, we also should influence policy making by governments at the international level *at an early stage*.

I am very much in favour of a strong international community of securities markets regulators driving the international policy debate on financial market regulation. In popular words “we need to be ahead of the curve”. We need to identify possible future areas of regulation and offer possible regulatory frameworks. For example, an area where this has worked well is CRAs where IOSCO published its first principles in 2003. The actual IOSCO Code of Conduct Fundamentals for Credit Rating Agencies has been largely incorporated in legislation in many countries in response to the financial crisis.

The policy debates that I have just mentioned should not only be amongst colleagues, but also with various stakeholders and especially governmental representatives. IOSCO has a clear role here already and I would like to wholeheartedly support the organisation and facilitation of these policy debates by IOSCO. I am convinced that when we are successful in this area, there is a much higher chance that our governments will establish financial market regulation which is broadly aligned. While my brief intervention here is not intended to start these policy debates and identify possible new areas of regulation, examples of important topics for the months and years ahead include shadow banking issues like money market funds and securities lending, and more intrusive regulation and supervision of financial products and their innovation.

An additional argument for a more active role of securities regulators in international policy debates is that the interest in many of the current important topics are shared with other regulators and specifically banking regulators. The latter group has strongly influenced the current regulatory reforms in response to the crisis. While this is to some extent logical considering that the current crisis is in essence a banking crisis, we need to ensure that for topics that have the joint interest of banking and securities regulators, our perspective gets the right attention.

To conclude

Let me conclude by stating the obvious: regulating international and interconnected financial markets from a national perspective is a mismatch. However, despite this difficult starting point, the community of international securities regulators should do its utmost to achieve broadly common regulation of international financial markets. Important ingredients to achieve this are cooperation both before and after our governments decide on the regulation of financial markets. It is essential that we drive the international policy debates on future areas of financial market regulation and possible solutions. Once regulation is in place which is broadly similar, we need to move to a model of equivalence, mutual recognition, and cooperation between regulators.

Thank you for your attention.