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The views expressed in this presentation are those of the author and do not necessarily represent the position of the CVM
Topics

• Introduction

• Process: identifying risks, prioritizing entities and defining supervisory actions

• Lessons learned/benefits realized

• Future enhancements
Introduction

• Risk based supervision (RBS) model implemented in 2009
  • The National Monetary Council (CMN) Resolution no. 3.427 provided the mandatory adoption of RBS
  • The CVM Deliberation no. 521/07 established general procedures and responsibilities

• On a semi-annual basis, the CVM reports the activities, findings, and assessments to CMN/COMOC

• The semi-annual written report is made available at our website
Most categories of entities subject to the CVM’s regulation are covered either directly by CVM’s supervision and/or indirectly by self-regulatory bodies’ supervision

- Public companies
- Independent auditors
- Investment funds and asset managers
- Market intermediaries
- Self-regulatory bodies (BVMF – stock exchange; CETIP – trade repository; ANCORD – for autonomous investment agents)

Supervision is handled either by off-site activities and/or on-site inspections

Thematic supervision complements routine supervision on an as-needed basis
Identifying which risks - focus

Determining which entities to prioritize: criteria

Setting the supervisory intensity: sample size and type of supervisory action

• The pertinent supervision offices propose risks, entities and actions, which are approved by the CVM’s Board
1. Essential risks relative to disclosure and conduct requirements set down by law or regulation

• Example: public companies
  • Risk: elaboration and disclosure of financial information not in accordance with the regulation and statutory provisions
  • Supervision focus – ensuring the consistency of financial information with IFRS and with CVM’s rules
2. Risks caused by new circumstances or innovative instruments and practices

• The pertinent offices during their regulatory activities
• Committee on Risk Identification (CIR), created in 2011: systemic or emerging risks
• As a rule, in terms of supervision, potential risks are turned into a thematic supervision prior to routine supervision
In general, the concept of a probability-impact matrix is applied to ranking groups of entities (for each risk/focus):

- First step: entities are clustered in different groups according to their effects (impact) on investors/markets – criteria: entity’s size, number of investors, distribution channels etc.
- Second step: it is assigned probabilities of failure to each group – criteria: history of non-conformities, portfolio composition etc.
**Examples – public companies**

**Risk**
- Irregularities in relation to:
  - proposals and decisions of management;
  - decisions of general meetings; and
  - conducting of business by management and controlling shareholders

**Supervision focus**
- M&A transactions
- Related parties transactions
- Capital increase by private subscription
- Capital reduction
- Shares conversion

**Criteria for grouping**
- Whether the entity’s shares comprise the main stock indexes
- Number of shareholders
- Company’s net worth
- Number of complaints from investors
- History of sanctions
- Others
Examples – independent auditors

Risk

• Failure of auditor's opinion in reflecting the non-compliance of financial statements (funds and public companies) with IFRS

Supervision focus

• Inadequacy of auditor’s reports that contain unmodified opinion

Criteria for grouping

• Number of public companies clients
• Size of audited companies
• History on continuing professional education
• History of sanctions
• Others
Examples – investment funds and asset managers

Risk
- Improper valuation of portfolio’s assets

Supervision focus
- Modified opinion in the auditor’s report
- Valuation (selected investment funds and selected asset classes):
  - Market value
  - Manager’s policy on pricing

Criteria for grouping
- Number and profile of quotaholders
- Acquisition of assets issued by related parties to the manager
- Proportion of illiquid assets
- Others
Process – supervisory actions intensity

- Regular approach

  Risks Focus

  Priority groups

  Intensity varies:
  - number of entities supervised within each group;
  - type of off-site supervision; and
  - on-site inspections

- Another approach (risk nature and immediate data availability)

  All entities are submitted to supervision:
  - some cases - risk indicators are used as filters

  Off-site supervision and On-site inspection
Lessons learned / benefits realized

• Better targeting at riskier entities/practices – more effective allocation of CVM’s scarce human resources

• From fear of red tape to disciplined approach (methods)

• Cultural changes – the CVM and market participants
  • From ex-post posture to ex-ante posture: preventing the risks from materializing

• Better understanding of regulated entities modus operandi: expedite identification of new risks

• Flexibility of the regular process to fit new situations, recognizing that risks evolve and have different features
The CVM is preparing the next 2 years plan for RBS

- Introducing activities, such as public offerings
- Reinforcing and extending the role of on-site inspections

- Deepening the understanding of risks faced by regulated entities and the interaction of said risks with our mandate

- Enhancement of data collection and development of risk metrics
Thank you!

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