

Overview of Progress in the Implementation of the G20 Recommendations for Strengthening Financial Stability

Report of the Financial Stability Board to G20 Leaders

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1. Introduction

In Washington in 2008, the G20 committed to fundamental reform of the global financial system. The objectives were to correct the fault lines that led to the global crisis and to build safer, more resilient sources of finance to serve better the needs of the real economy. National authorities and international bodies, with the Financial Stability Board (FSB) as a central locus of coordination, have taken forward this financial reform programme, based on clear principles and timetables for implementation.

The FSB coordinates and closely monitors the national implementation of these reforms and is responsible for reporting on them to the G20. In order to intensify its monitoring and public reporting on implementation, focusing in particular on designated priority reform areas, the FSB set up in 2011 a framework for implementation monitoring in collaboration with standard-setting bodies (SSBs).

This report details the additional progress made in global policy development and implementation of agreed reforms since the G20 St Petersburg Summit in September 2013. The following sections describe in detail the progress made by the FSB and its members to promote financial stability and strengthen the resilience of the global financial system. The report draws on information from published reports by the FSB, SSBs and other international organisations, as well as surveys conducted by the FSB's Implementation Monitoring Network (IMN).

2. Building more resilient financial institutions

The Basel III package of reforms is the centrepiece of the international community's work to build more resilient financial institutions. The Basel Committee on Banking Supervision (BCBS) has largely completed the design of the reforms and it continues to enhance its implementation monitoring. National implementation of the Basel III framework is on track. Large internationally active banks remain on course to meet the new capital requirements almost four years in advance of the deadline. All FSB members have Basel III risk-based capital rules in force in accordance with the agreed timetable, and most of them have issued final or draft rules on the liquidity coverage ratio (LCR), leverage ratio and systemically important bank (SIB) frameworks. Capital regulations of 7 jurisdictions have already been assessed by the BCBS and deemed consistent with Basel III standards. Over the past year, the BCBS has substantially completed the remaining components of Basel III: it has agreed on the final form of the LCR and on a globally consistent definition of the leverage ratio; issued the final standard for the Net Stable Funding Ratio (NSFR); and has set out its plan to address excessive variability in risk-weighted asset (RWA) calculations.

Work in this area is not confined to the banking sector. The International Association of Insurance Supervisors (IAIS) announced in late 2013 its plan to develop a risk-based group-wide global insurance capital standard (ICS) for internationally active insurance groups (IAIGs) by the end of 2016 (see section 3.2.2). The ICS will be included in the IAIS's comprehensive framework for the supervision of IAIGs (ComFrame).

Implementation of Basel II/II.5/III

Full, timely and consistent implementation of Basel III is fundamental to a sound and properly functioning banking system that is able to support economic recovery and growth on a sustainable basis. Consistent implementation of Basel standards will also foster a level playing field for internationally active banks. In November 2011, G20 Leaders at the Cannes Summit called on jurisdictions to meet their commitment to adopt and implement fully and consistently Basel II and Basel 2.5 by end-2011, and Basel III starting in 2013 and completing full implementation by 1 January 2019.

To monitor progress and assess the implementation of Basel III and its outcomes, the BCBS established the Regulatory Consistency Assessment Programme (RCAP) in 2012. The RCAP consists of two parts: (i) monitoring of the timely adoption of new Basel standards by member jurisdictions and of banks' progress in raising capital and liquidity buffers to meet the new minimum requirements; and (ii) consistency assessments and analytical studies of prudential outcomes. These cover how domestic capital, liquidity, leverage and SIB regulations have incorporated Basel minimum standards, and analytical reviews of banks' calculations of capital ratios, RWAs, and other prudential outcomes. The RCAP is also helping to highlight how effective functioning of the Basel prudential standards depends on complementary and effective supervisory and industry practices.

Member jurisdictions have made considerable progress. In terms of timely adoption, by end-2013 all BCBS/FSB member jurisdictions had adopted and put into force the final set of Basel III-based capital regulations. Work is now underway to adopt Basel III-based regulations for liquidity and leverage ratios, as well as the requirements that apply to firms designated as global systemically important banks (G-SIBs) and domestic systemically important banks (D-SIBs).^{1,2}

In terms of the consistency of national implementation with the agreed Basel III rules texts, the BCBS aims to complete a first round of assessments for all BCBS/FSB jurisdictions by the middle of 2016. Since last year's update, the BCBS has concluded consistency assessments of capital regulations in Australia, Brazil, Canada and China.³ Consistency assessments are underway in the European Union (EU), Hong Kong, India, Mexico, South Africa and the US; the EU and US assessments are expected to be published by end-2014. Assessments of Argentina, Indonesia, Korea, Russia, Saudi Arabia and Turkey will be initiated during 2015.

The RCAP assessments are demonstrably contributing to greater consistency in the national adoption of the Basel III risk-based capital standards: in many cases, jurisdictions are rectifying areas of material inconsistency identified during the assessments. As a result, regulations to adopt and implement Basel III standards are stronger than would have been the case without the BCBS's monitoring and assessments. Member jurisdictions are also

¹ The agreed start date for disclosure of the leverage ratio and the phase-in of the LCR is 1 January 2015. The phase-in of the G-SIB and D-SIB higher loss absorbency requirements is from 1 January 2016.

² See <http://www.bis.org/bcbs/publ/d299.pdf>. As of September 2014, 23 jurisdictions had issued final or draft rules on their G-SIB or D-SIB framework; 26 had issued final or draft rules on the LCR; and 23 had issued final or draft rules on the leverage ratio.

³ All assessments are available at www.bis.org/bcbs/implementation/l2.htm.

reporting that the various elements of the RCAP are fostering peer and industry dialogue on technical aspects of the Basel III framework, helping the quality of implementation and reducing the variations in national regulations. The implementation findings have also begun informing the BCBS's ongoing standard-setting work.

Since 2010 the BCBS has regularly monitored the progress of a sample of banks in its member jurisdictions in adjusting to the minimum Basel III requirements for capital and liquidity. The latest of these quantitative impact studies (QIS) has found that the banking system as a whole continues to build capital and is close to meeting the full set of fully phased-in minimum Basel III capital requirements well ahead of the 2019 deadline.⁴ In the six months to December 2013, the average Common Equity Tier 1 (CET1) capital ratio of large internationally active banks rose from 9.5% to 10.2% of RWAs, mainly as a result of increased amounts of capital. The aggregated capital shortfall of those banks that still have capital ratios below the fully phased-in 2019 CET1 target level of 7% of RWAs continues to decrease: the CET1 shortfall was €15 billion in December 2013 (compared with €115 billion at end-2012). The weighted average Basel III leverage ratio for large internationally active banks was 4.4%, up from 3.7% in December 2012. The weighted average LCR for large internationally active banks was 119%, compared to 114% in June 2013. While these numbers indicate that most banks on average already meet the fully phased-in Basel III minimum requirements, a number of banks still need to take steps to raise capital and liquidity buffers to meet the new minimum requirements.

2.1 Completing the Basel framework

Since the last update, the BCBS has substantially completed the remaining components of the Basel III framework. In January 2014, the BCBS's governing body – the Group of Governors and Heads of Supervision (GHOS) – endorsed the finalised standard for the leverage ratio.⁵ Implementation of the leverage ratio requirements has begun with bank-level reporting to national supervisors of the leverage ratio and its components, and will proceed with public disclosure starting 1 January 2015. The GHOS also endorsed the BCBS's additional work on the LCR, such as LCR disclosure standards, the role of market-based indicators of liquidity within the regulatory framework, and the interaction between the LCR and the provision of central bank facilities (which allows a restricted use of committed central banks' liquidity facilities to be counted as high quality liquid assets subject to a range of conditions and limitations). In October 2014, the BCBS published the final standard for the NSFR.⁶ In line with the timeline specified in the 2010 publication of the liquidity risk framework, it remains the BCBS's intention that the NSFR, including any revisions, will become a minimum standard by 1 January 2018.

⁴ The BCBS QIS is based on a sample of over 200 banks, approximately half of which are large internationally active banks with Tier 1 capital in excess of €3 billion. The most recently published Basel III monitoring report is available at www.bis.org/publ/bcbs289.htm.

⁵ The BCBS will continue undertaking QISs to ensure that the calibration of the Basel III leverage ratio, and its relationship with the risk-based framework, remains appropriate. Any final adjustments to the definition and calibration of the Basel III leverage ratio will be made by 2017, with a view to migrating to a Pillar 1 treatment on 1 January 2018.

⁶ See <http://www.bis.org/bcbs/publ/d295.pdf>.

Over the past year, the BCBS also finalised the large exposures framework; the capital treatment of bank exposures to central counterparties (CCPs); the standardised approach for measuring counterparty credit risk exposures; and capital requirements for banks' equity investments in funds. The BCBS also issued consultative documents on trading book capital requirements; securitisation; Pillar 3 disclosure requirements; and the standardised approach for measuring operational risk capital. These consultative documents will be finalised after considering public comments.

As regards measures to reduce the excessive variation in RWAs across banks, the BCBS is following up on the published RCAP studies of banks' calculations of RWAs in both the banking and trading books. The BCBS is actively considering possible reforms to improve the comparability of outcomes and reduce complexity while maintaining adequate risk-sensitivity of the framework. Its response thus far has centred around three areas:⁷

- **policy measures:** developing prudential proposals related to the use of floors and benchmarks; providing additional guidance on those aspects of the Basel framework that are ambiguous or require clarity; and undertaking a more fundamental review of modelling practices;
- **better disclosure:** strengthening the disclosure requirements related to risk weights by amending Pillar 3 of the Basel framework; and
- **ongoing monitoring:** ensuring proper implementation by monitoring outcomes of RWA variability through hypothetical portfolio exercises under the RCAP.

The BCBS is also undertaking a longer-term review of the structure of the regulatory capital framework. Considerations include the costs and benefits of basing regulatory capital on banks' internal models, the extent to which internal modelling options in the regulatory framework facilitate improved risk and capital management in banks, and alternative approaches for determining regulatory capital that reduce or remove reliance on bank-internal models while maintaining adequate risk sensitivity. The review will consider to what degree effective market discipline is inhibited by ongoing inconsistencies in bank capital ratios and how these inconsistencies can be addressed to facilitate comparability across banks.

2.2 Strengthening risk management

Risk management is a critical first line of defence in the resilience of financial institutions. The FSB, SSBs and national authorities are working to strengthen risk management practices, including through increased regulatory and supervisory focus as well as additional guidance on firms' risk culture and governance practices. Implementation of these reforms is ongoing and will require additional efforts by national authorities and financial institutions.

Although data requests remain a key part of supervision, supervisors are increasingly adding more qualitative indicators to their assessments of risk rather than relying largely on quantitative analysis of risk data. Focusing on qualitative aspects such as risk governance, appetite and culture provides a broader understanding of a firm's risk management framework

⁷ See Basel Committee, *Reducing excessive variability in banks' regulatory capital ratios: A report to the G20*, available at <http://www.bis.org/bcbs/publ/d298.pdf>.

and facilitates discussions around business strategy and business model. Over the past year, the FSB has issued *Principles for an effective risk appetite framework*⁸ and *Guidance on supervisory interaction with financial institutions on risk culture*.⁹ These papers take forward recommendations that were set out in the FSB peer review report on risk governance published in February 2013.¹⁰

Implementation of these FSB principles and guidance will support supervisors' capacity to engage managements and boards on these topics. Assessing risk culture has long been an informal part of supervision. The guidance will help supervisors to form and articulate a view on an institution's risk culture, and to intervene early to prevent behavioural weaknesses from taking root and growing. Enhanced risk awareness and the ability to have meaningful supervisory conversations around an institution's risk culture are powerful preventive tools.

The BCBS continued to engage in initiatives to strengthen risk management at banks. In January 2014, the BCBS finalised *Sound management of risks related to money laundering and financing of terrorism*, which describes how banks should include these risks within their overall risk management framework. It also issued *A sound capital planning process: fundamental elements* to foster overall improvement in banks' capital planning practices. In June 2014, the BCBS issued for consultation an updated version of its *Supervisory guidelines for identifying and dealing with weak banks*, which provide practical guidelines for problem identification, corrective action, resolution techniques and exit strategies. In the same month, the BCBS finalised *Principles for effective supervisory colleges*, which has been revised to reflect observations on best practice¹¹ and aims to strengthen the operation of colleges. In October 2014, the BCBS issued for consultation *Corporate governance principles for banks*, which provide a framework within which banks and supervisors should operate to achieve robust and transparent risk management and decision-making. In the same month, the BCBS issued a *Review of the Principles for the Sound Management of Operational Risk*.

Other SSBs have also issued guidance to strengthen risk management practices by market participants and their oversight by national authorities. The Joint Forum issued a final report on *Longevity risk transfer markets* in December 2013; a final report on *Point of Sale disclosure in the insurance, banking and securities sectors* in April 2014; and a *Report on supervisory colleges for financial conglomerates* in September 2014. The International Organization of Securities Commissions (IOSCO) published in June 2014 a report on *Risk Identification and Assessment Methodologies for Securities Regulators*, which provides a practical overview of the methods, approaches and tools that IOSCO and securities regulators have developed to identify and assess emerging and potential systemic risks.

A number of national authorities have been making efforts to further strengthen the risk management practices of banks in their jurisdiction, particularly on liquidity risk management, measurement and governance given the Basel III liquidity standards. For

⁸ See http://www.financialstabilityboard.org/publications/r_131118.pdf

⁹ See <http://www.financialstabilityboard.org/publications/140407.pdf>

¹⁰ See http://www.financialstabilityboard.org/publications/r_130212.pdf

¹¹ The revisions underscore the importance of continuous collaboration and information-sharing outside the formal college meetings and also incorporate recent supervisory developments, such as the formation of crisis management groups and greater focus on macroprudential considerations.

example, the Australian Prudential Regulatory Authority released a final standard in January 2014 that sets out risk management requirements that are consistent with emerging international consensus on the lessons from the financial crisis, including from the BCBS and the FSB's thematic peer review on risk governance. In the EU, the European Banking Authority adopted guidelines in December 2013 on Pillar 2 capital measures for lending in foreign currencies.

2.3 Enhancing compensation practices

At the 2011 G20 Summit in Cannes, the Leaders called on the FSB to undertake ongoing monitoring and public reporting on compensation practices, focused on gaps and impediments to full implementation of the FSB Principles for Sound Compensation Practices and their Implementation Standards (P&S),¹² as well as to carry out an ongoing bilateral complaint handling process to address level playing field concerns of individual firms.

The FSB's third progress report in this area was published in November 2014.¹³ The report summarises the responses by FSB jurisdictions to the annual monitoring questionnaire, the results of a survey on material risk-takers (MRTs) and malus/clawbacks, and the findings of the second FSB workshop with private sector participants held in April 2014.¹⁴

The report concludes that implementation of the P&S by FSB jurisdictions is essentially completed, with very few remaining exceptions (some of which are due to non-applicability or incompatibility of a few standards with local laws). Several jurisdictions continue to refine their regulatory framework or guidance on compensation practices, the most notable development being the adoption by the EU of the Capital Requirements Directive (CRD) IV, which includes requirements on compensation structures that go beyond those of the P&S. However, there remain significant differences among jurisdictions in the approach to, and implications of, identifying the MRTs to which the remuneration policies apply; these can lead to potential level playing field issues.

The main focus of national authorities now is on embedding the review of compensation practices in ongoing supervisory processes. Almost all authorities assess the level of implementation by significant banks in their jurisdiction as being medium or high, with notable improvements by significant financial institutions in the governance frameworks for compensation, and better practices in terms of *ex ante* risk adjustment of compensation to reflect risk-taking. Some challenges in this area remain, in particular the application of risk metrics to the business unit or specific product and activity level, as well as at the individual level; a more transparent and consistent application of policies and procedures to guide the use of discretion; and the availability of better data to support the effective alignment of compensation with prudent risk-taking behaviour.

¹² See http://www.financialstabilityboard.org/wp-content/uploads/r_0904b.pdf and http://www.financialstabilityboard.org/wp-content/uploads/r_090925c.pdf.

¹³ See http://www.financialstabilityboard.org/wp-content/uploads/r_141104.pdf.

¹⁴ Officials from FSB member organisations participating in the FSB CMCG and senior executives mainly responsible for remuneration, primarily from global systemically important banks (G-SIBs), participated in the workshop. See http://www.financialstabilityboard.org/wp-content/uploads/r_140627.pdf.

As regards *ex post* performance adjustment, supervisors and firms share the view that proper application of malus and clawback clauses is important for incentivising prudent risk-taking behaviour. Progress is more evident on the use of malus adjustments than clawbacks, which is partly due to legal and tax considerations. There is also scope for enhancement of disclosure of compensation practices.

In light of these findings, the report recommends that FSB jurisdictions undertake more intense and effective supervision of compensation practices, and that they continue to foster the use of malus and clawback mechanisms by their supervised firms. Going forward, the FSB will focus on the link between compensation structures and firms' risk appetite and governance frameworks, and will undertake further work on the identification and treatment of MRTs. As part of this work, the FSB will engage with the industry to exchange views on trends and remaining challenges in this area, extending the focus in 2015 to compensation practices at significant insurance firms.

3. Ending “Too-Big-To-Fail”

At the Seoul Summit in 2010, G20 Leaders endorsed the FSB framework for reducing the moral hazard posed by systemically important financial institutions or SIFIs. This SIFI Framework addresses the too-big-to-fail (TBTF) issue by reducing the probability and impact of SIFIs failing.¹⁵ It comprises requirements for assessing the systemic importance of financial institutions, additional loss absorbency, increased supervisory intensity, more effective resolution mechanisms and stronger financial market infrastructure.

At the St Petersburg Summit, G20 Leaders welcomed the FSB report on *Progress and Next Steps Towards Ending TBTF*¹⁶ and renewed their commitment to make the necessary reforms to national resolution regimes and to ensure that their supervisors have strong mandates, adequate resources and independence to act.

Substantial progress has been made in further developing the SIFI Framework over the past year:

- **Assessment and designation:** An updated list of 30 global systemically important banks (G-SIBs) and 9 global systemically important insurers (G-SIIs) has been designated in 2014 based on assessment methodologies by the BCBS and the IAIS respectively. Higher loss-absorption capacity, more intensive supervision and resolution planning requirements will apply to these institutions. A second consultation paper on the development of assessment methodologies to identify non-bank non-insurer G-SIFIs will be issued around end-2014.
- **Additional loss absorbency:** G-SIBs continue to build up extra capital in order to meet additional going-concern loss absorption capacity. Of the 29 G-SIBs identified in

¹⁵ See http://www.financialstabilityboard.org/publications/r_101111a.pdf. SIFIs are institutions of such size, market importance and interconnectedness that their distress or failure would cause significant dislocation in the financial system and adverse economic consequences. The TBTF problem arises when the threatened failure of a SIFI leaves public authorities with limited options but to bail it out and pass on the costs of failure to taxpayers. The knowledge that this can happen encourages SIFIs to take excessive risks and represents a large implicit public subsidy of private enterprise.

¹⁶ See http://www.financialstabilityboard.org/wp-content/uploads/r_130902.pdf.

2013, the Basel III monitoring exercise found that 21 of them had already reached the CET1 target level plus the surcharge at the end of that year. The IAIS issued in October 2014 a Basic Capital Requirement for G-SIIs as a first step to develop group-wide global capital standards.

- **Supervisory intensity:** Advances in supervisory practices continue to be reported in terms of: greater focus on firms' governance, risk appetite and culture; higher expectations for risk identification and measurement; and more robust stress testing.
- **Effective resolution:** The FSB has issued for public consultation a proposal on the adequacy of G-SIBs' loss absorbing capacity in resolution. The FSB also issued guidance in a number of key areas, including in regard to the resolution of non-bank financial institutions. All G-SIBs identified in 2013 have recovery plans in place, and most home authorities have developed high-level resolution strategies and completed initial operational resolution plans. Cross-border crisis management groups have now been established for all these G-SIBs and for all G-SIIs identified in 2013, and several jurisdictions have introduced legislative reforms aligning their bank resolution regimes more closely with the FSB's *Key Attributes for Effective Resolution Regimes* ("Key Attributes").
- **Addressing data gaps:** Enhancements of datasets to address key information gaps for G-SIBs continue to be made. Work on assessing potential data gaps related to foreign currency exposures, including currency mismatches and leverage in corporate balance sheets, is also underway.
- **Strengthening core infrastructure:** The Committee on Payments and Market Infrastructures (CPMI) and IOSCO are currently in the process of monitoring the implementation of the *Principles for Financial Market Infrastructures* (PFMIs).

National implementation of the SIFI framework is still at an early stage and there is significant additional work to be done in order to embed these reforms, particularly in establishing effective resolution regimes and implementing enhancements to supervisory mandates, powers, tools and resources.

3.1 Improving the capacity to resolve systemic institutions

At the St. Petersburg Summit in September 2013, the G20 committed to make any necessary reforms to implement fully the Key Attributes for all parts of the financial sector that could cause systemic problems and called on the FSB to address the remaining impediments to resolvability. Substantial progress has since been made in taking forward the work detailed in the TBTF Report. The FSB has issued consultative documents on cross-border recognition of resolution actions and total loss absorbing capacity (TLAC) in resolution and finalised its guidance on resolution of non-bank financial institutions and information sharing for resolution purposes. Contractual mechanisms for recognition of temporary stays on early termination rights and cross-default rights have been developed which, if sufficiently widely adopted, could prevent large-scale close-out of financial contracts in resolution. However, further work is needed by jurisdictions to adopt regimes that implement the Key Attributes fully in substance and in scope.

Progress in legislative reforms of resolution regimes

A 2014 monitoring exercise of the implementation of the Key Attributes in the banking sector found continued progress by FSB jurisdictions in adopting resolution regimes for banks, although only a few jurisdictions report having resolution regimes in place that are fully or almost fully aligned with the Key Attributes. In particular, most jurisdictions have not yet adopted resolution powers such as bail-in or the power to impose a temporary stay on early termination rights, or mechanisms to give effect to foreign resolution actions. Moreover, although recovery and resolution planning for G-SIBs is well advanced, fewer than half of jurisdictions have adopted recovery and resolution planning for all domestically incorporated banks that could be systemically significant or critical if they fail.

The FSB will continue to monitor implementation of the Key Attributes and by the end of 2014 will launch a second resolution peer review, focused on banks. It will also, in future years, extend its monitoring exercise to other sectors. In order to support the development of resolution regimes for non-bank financial institutions, the FSB reissued the Key Attributes incorporating guidance on their application to non-bank financial institutions.¹⁷ New Annexes to the Key Attributes set out guidance covering the resolution of Financial Market Infrastructures (FMIs), including CCPs; the resolution of insurers; and the protection of client asset in resolution. The new guidance should assist jurisdictions in implementing the Key Attributes fully, in substance and in scope.

Total loss absorbing capacity (TLAC) in resolution

At the St. Petersburg Summit, the G20 Leaders requested that the FSB develop proposals on the adequacy of G-SIBs' loss absorbing capacity when they fail. In November 2014, in response to this request, the FSB published a policy proposal for public consultation.¹⁸ The proposal, which was developed in consultation with the BCBS, consists of a set of principles that elaborate on the premise set out in the TBTF report that there must be sufficient loss-absorbing and recapitalisation capacity available in resolution to implement an orderly resolution that minimises any impact on financial stability, ensures the continuity of critical functions and avoids exposing taxpayers to loss; and a term sheet that is a concrete proposal for implementing these principles in the form of an internationally agreed standard on the adequacy of TLAC for G-SIBs.

In early 2015, the FSB will, together with the BCBS, undertake a comprehensive quantitative impact study, a cost-benefit analysis and a macroeconomic impact assessment to inform the determination of the Pillar 1 element of the common minimum TLAC requirement for all G-SIBs. In addition, it will carry out a market survey to gauge the depth of markets for eligible TLAC instruments and how these markets and holders of the instruments might be affected. Together, these assessments should provide more information on the impact of the proposal on the broader financial system, financial stability and the real economy. The FSB will submit a final version of the principles and term sheet to the G20 by the 2015 Summit.

¹⁷ See http://www.financialstabilityboard.org/wp-content/uploads/r_141015.pdf.

¹⁸ See <http://www.financialstabilityboard.org/wp-content/uploads/TLAC-Condop-6-Nov-2014-FINAL.pdf>.

Cross-border recognition

The TBTF Report identified legal uncertainties about the cross-border effectiveness of resolution measures as one of the main obstacles to the implementation of resolution strategies. In September 2014, the FSB issued a consultative document on cross-border recognition of resolution actions¹⁹ which proposes a set of policy measures and guidance covering statutory regimes for recognition of foreign resolution actions and contractual approaches. The contractual approaches focus on two particular cases where achieving cross-border recognition is critical for orderly resolution: temporary restrictions or stays on early termination rights (including with respect to cross-defaults); and the write-down, cancellation or conversion of debt instruments in resolution ('bail-in'). The International Swaps and Derivatives Association (ISDA), in consultation with regulators and the FSB, has developed a protocol to the ISDA Master Agreement that, if adhered to by both counterparties, will support the cross-border enforcement of a temporary stay of early termination rights in bilaterally cleared OTC derivatives contracts. FSB members have agreed to act in a concerted manner to promote broad adoption of the ISDA protocol.²⁰ An initial set of eighteen G-SIBs and other large dealer banks have at this point adhered to the protocol.

Information sharing and cooperation for resolution purposes

The TBTF Report identified obstacles to the sharing of information for resolution purposes as a further impediment to effective resolution. In October 2014, the FSB adopted a new Annex to the *Key Attributes* on information sharing for resolution purposes containing principles for the design of national legal gateways and confidentiality regimes and provisions on information sharing that should be included in institution-specific cooperation agreements (COAGs). The development of COAGs to support the cross-border implementation of resolution strategies for G-SIBs and G-SIIs is progressing. To date, only one has been formally signed, although others are close to conclusion. Progress on this front should be assisted by the guidance on information sharing.

In October 2014, the FSB also published for consultation guidance on "Cooperation and Information Sharing with Host Authorities of Jurisdictions Not Represented on Crisis Management Groups (CMGs) where a G-SIFI has a Systemic Presence".²¹ Coordination with such non-CMG host jurisdictions is likely to be important for effective implementation of resolution strategies for G-SIFIs.

G-SIB resolution planning and resolvability assessments

The FSB guidance on recovery and resolution planning published in 2013²² assisted CMGs in their work on resolution strategies and operational resolution plans for G-SIBs. Most home authorities of G-SIBs report that they have developed high-level resolution strategies and

¹⁹ See http://www.financialstabilityboard.org/wp-content/uploads/c_140929.pdf.

²⁰ See FSB press release of 29 September 2014 (http://www.financialstabilityboard.org/wp-content/uploads/pr_140929.pdf).

²¹ See http://www.financialstabilityboard.org/wp-content/uploads/c_141017.pdf.

²² See http://www.financialstabilityboard.org/publications/r_130716b.pdf and http://www.financialstabilityboard.org/publications/r_130716a.pdf.

completed initial operational plans that build on those strategies, and have started to assess the feasibility and credibility of those strategies through technical resolvability assessments.

To promote consistent reporting on the resolvability of G-SIFIs and help determine what should be done to address common obstacles to resolvability, the FSB agreed on a process for reviewing at the level of senior policymakers within CMGs the resolvability of each G-SIFI, drawing on technical resolvability assessments. Such a Resolvability Assessment Process has been carried out for a subset of 10 G-SIBs. The preliminary findings show that good progress has been made in resolution planning, but also identify outstanding legal, operational and financial barriers to resolvability. A number of those barriers relate to issues that are covered by the work on loss absorbing capacity in resolution and cross-border recognition, and may be mitigated as that work is finalised and implemented.

G-SII resolution planning and critical functions in the insurance sector

CMGs have now been established for most G-SIIs, and recovery and resolution planning is progressing. To support resolution planning for insurers, the FSB, with participation of the IAIS, developed draft guidance to assist authorities and CMGs in their evaluation of the criticality of insurance functions.²³ It was published for consultation in October 2014, and will be finalised in 2015.

3.2 Identifying SIFIs and applying higher loss absorbency requirements

The FSB SIFI framework requires that the FSB and national authorities, in consultation with SSBs and drawing on relevant indicators, identify and apply heightened measures to G-SIFIs. The framework recognises that SIFIs vary in their structures and activities, and that systemic importance and impact upon failure can vary significantly across sectors. The methodologies to identify G-SIFIs and the policies that apply to them therefore seek to reflect the nature and degree of risks they pose to the global financial system.

3.2.1 Systemically important banks (SIBs)

The BCBS published its assessment methodology to identify G-SIBs in November 2011. In July 2013, the BCBS published an updated methodology document that adjusted the framework for some technical issues identified during the initial exercises to determine the list of G-SIBs.²⁴ The BCBS also published additional information regarding the G-SIB methodology which enables banks that participated in the G-SIB exercise to calculate their scores and see their positions within the buckets that, from the 2014 exercise onwards, will determine their higher loss absorbency (HLA) requirement.

Based on the assessment methodology, the FSB and the BCBS first identified a list of G-SIBs in November 2011. The list is updated annually based on new data, and published by the FSB each November. The current list, published in November 2014, includes 30 banks²⁵ that are

²³ See http://www.financialstabilityboard.org/wp-content/uploads/c_141016.pdf.

²⁴ See <http://www.bis.org/publ/bcbs255.htm>. The methodology is based on twelve indicators for five drivers of systemic importance: size, cross-jurisdictional activity, interconnectedness, complexity and substitutability/financial institution infrastructure.

²⁵ See http://www.financialstabilityboard.org/wp-content/uploads/r_141106b.pdf. Of these banking groups, 8 are North American, 16 are European, and 6 are Asian.

grouped into four buckets of increasing systemic importance, which correspond to increasing levels of HLA, ranging from 1 to 2.5% of risk-weighted assets, with a currently empty bucket of 3.5% to discourage further systemicness.²⁶ The HLA requirement is to be met with CET1, the highest quality form of capital.²⁷

The G-SIB HLA requirements will be phased in commencing in 2016, with a view to full implementation in 2019. The latest BCBS progress report on Basel III implementation indicates that, as of end-2013, most G-SIBs had already met this requirement.²⁸

In October 2012, the BCBS published its framework for dealing with D-SIBs.²⁹ Jurisdictions are proceeding with the implementation of the D-SIB principles and the BCBS continues to provide a forum for information sharing. To help ensure that appropriate and effective frameworks for D-SIBs are in place across jurisdictions, the BCBS will review them as part of its Basel III RCAP starting in late 2015.

3.2.2 Systemically important insurers (SIIs)

In July 2013, the FSB, in consultation with the IAIS and national authorities, identified an initial list of nine life and composite insurers as G-SIIs, using an assessment methodology developed by the IAIS.³⁰ The group of G-SIIs is updated annually based on new data and published by the FSB each November, with the first update in November 2014. The FSB also indicated that in 2014 a decision would be made on the G-SII status of, and appropriate risk mitigating measures for, major reinsurers. Following the IAIS annual assessment exercise based on end-2013 data, the FSB consulted with the IAIS and national authorities and has decided to identify for 2014 the nine G-SIIs identified in 2013 and to postpone a decision on the G-SII status of reinsurers, pending further development of the methodology.³¹

G-SIIs will be subject to a set of policy measures consistent with the SIFI Framework, comprising recovery and resolution planning, enhanced group-wide supervision and higher loss absorbency requirements.

²⁶ If the empty bucket should become populated in the future, a new bucket will be added, in increments of 1% of risk-weighted assets, to maintain incentives for banks to avoid becoming more systemically important.

²⁷ Currently, two G-SIBs are in the fourth bucket, corresponding to a 2.5% additional loss absorbency requirement; 4 G-SIBs in the third bucket (2%); 6 G-SIBs in the second bucket (1.5%), and 18 G-SIBs in the first bucket (1%). On average for these institutions, the additional loss absorbency requirement corresponds to an increase of approximately 20% over the minimum CET1 and buffer capital required under Basel III.

²⁸ See <http://www.bis.org/publ/bcbs289.htm>. Of the 29 G-SIBs included in this exercise, 25 of them had already reached the CET1 target level plus the surcharge by the end of 2013. The other 4 G-SIBs already met the Basel III minimum requirement but would have a shortfall in the additional CET1 required to meet the surcharge.

²⁹ See <http://www.bis.org/publ/bcbs233.pdf>. The D-SIB framework focuses on the impact that the distress or failure of banks will have on the domestic economy. It consists of twelve principles to guide the assessment of systemic importance of domestic banks and the application of higher loss absorbency requirements to identified D-SIBs, in a way that allows for appropriate national discretion to accommodate structural characteristics of domestic financial systems.

³⁰ See <http://www.iaisweb.org/G-SIIs-988>. The assessment methodology to identify G-SIIs is based on industry-specific indicators to reflect the drivers of systemic importance in the insurance sector. The drivers of systemic importance are: size, global activity, interconnectedness, non-traditional/non-insurance activities (NTNI), and substitutability. Higher weight is given to NTNI activities and interconnectedness, the two categories which capture the potential negative externalities of insurance companies on the rest of the system and hence the importance of insurers for financial stability.

³¹ See http://www.financialstabilityboard.org/wp-content/uploads/r_141106a.pdf.

The IAIS published in October 2014 Basic Capital Requirements (BCR) for G-SIIs as a foundation for the HLA requirements.³² The BCR is the first step of the IAIS project to develop group-wide global capital standards. The second step is the development of HLA requirements to apply to G-SIIs, due to be completed by the end of 2015. The HLA requirements will apply as from January 2019 to those G-SIIs identified in November 2017.

The third step is the development of a risk-based group-wide global ICS, due to be completed by the end of 2016, and to be applied to IAIGs from 2019 after refinement and final calibration in 2017 and 2018. The development of the ICS will be informed by the work on the BCR. The ICS, once implemented, will replace the BCR as the foundation for HLA.

3.2.3 Systemically important non-bank non-insurance firms

The FSB and its member authorities continue to extend the SIFI framework to other financial sectors to ensure all SIFIs are covered. The FSB, jointly with IOSCO, published a consultative document on the assessment methodologies to identify non-bank non-insurer (NBNI) G-SIFIs in January 2014.³³ The methodologies comprised a high-level framework for identifying G-SIFIs and implementation approaches that will apply across all NBNI financial entities, and detailed NBNI sector-specific methodologies for (i) finance companies; (ii) market intermediaries (securities broker-dealers); and (iii) investment funds (including hedge funds). The methodologies aim to capture different types of systemic impact posed by a wide range of business models and risk profiles, while maintaining broad consistency with the assessment methodologies for G-SIBs and G-SIIs. They also try to overcome limitations in data availability by allowing a greater role for supervisory judgment in the assessment compared to the G-SIB and G-SII methodologies. The NBNI G-SIFI methodologies will thus rely on detailed analysis conducted primarily by national authorities, which is supplemented by home-host supervisory information-sharing and international coordination.

Based on the analysis of consultative responses, the FSB, jointly with IOSCO, are now revising the methodologies. A second consultative document will be published around the end of 2014. It will include: (a) near-final methodologies for finance companies and market intermediaries; and (b) a revised proposal on methodologies for asset management entities. Following the public consultation period, the FSB and IOSCO will further revise the methodologies with the expectation that they will be completed by the end of 2015. Once the assessment methodologies have been finalised, the FSB, in cooperation with IOSCO and other SSBs where relevant, will begin work to develop within the SIFI policy framework the incremental policy measures needed to address the systemic risks posed by NBNI G-SIFIs.

3.3 Improving the intensity and effectiveness of SIFI supervision

The work to achieve more intense and effective supervision continues. Supervisory attitudes have changed radically since the global financial crisis, with the determination to raise supervisory standards and the expectations for SIFIs. Since then, there has been good progress

³² See http://www.iaisweb.org/view/element_href.cfm?src=1/23741.pdf.

³³ See http://www.financialstabilityboard.org/publications/r_140108.pdf.

in some areas but more remains to be done. Some notable advances in supervisory practices include.³⁴

- *More effective supervisory interactions.* There is now greater supervisory interaction with boards of financial institutions. As a best practice, supervisors should be made aware of board and senior management appointments in advance and have an opportunity to raise any concerns.
- *Greater focus on governance, risk appetite and culture.* There is more supervisory focus on risk governance, including on the development of an institution's risk appetite framework and the assessment of its risk culture, which has been supported by new guidance and principles that aim to strengthen the dialogue with the board and senior management (see section 2.3).
- *Increased understanding of the business.* Supervisors have an increased focus on understanding institutions' business models and the key drivers of revenue, as an approach to understanding an institution's prospective vulnerabilities and risks.
- *More robust stress testing.* There is a wider application of stress testing practices within institutions' risk analyses and capital planning processes, as well as within the supervisory review process. Supervisory expectations have increased for institutions to conduct more rigorous stress testing, while supervisory practices for assessing stress testing models and scenarios have been enhanced.
- *Stronger resolution planning.* Expanded use of recovery and resolution planning has helped to identify new sources of risk and impediments to resolution, such as the complexity of organisational and funding structures, higher operational risk than previously apparent, and complex booking and collateral management practices.
- *Increased oversight of FMIs.* Greater reliance on services such as clearing through CCPs has heightened concerns over banks' exposures to CCPs, in particular the interconnections between banks across CCPs. The CPMI-IOSCO Principles for Financial Market Infrastructures have strengthened the standards for FMIs' risk management, which should be complemented by supervisors enhancing risk management at banks to capture the unique aspects of CCP exposures.

In parallel with implementing changes toward more effective supervision, the work ahead will need to focus on the measurement of supervisory effectiveness, including the search for proper input and output metrics. Assessing supervisory effectiveness is a challenging task and is in its infancy. The ongoing FSB peer review on supervisory approaches for SIFIs, in particular G-SIBs, will take stock of many of the changes being implemented by supervisors, and will be another step in the direction of assessing supervisory effectiveness. The peer review report is expected to be published in the first half of 2015.

To help remedy the gaps in information technology and management information systems highlighted during the crises, the FSB recommended the development of principles for effective risk data aggregation and risk reporting. G-SIBs are required to meet the January

³⁴ See http://www.financialstabilityboard.org/publications/r_140407.pdf.

2013 BCBS *Principles for Effective Risk Data Aggregation and Risk Reporting* by 2016.³⁵ In December 2013, the BCBS issued a report on *Progress in adopting the principles for effective risk data aggregation and risk reporting*, which provides a snapshot of G-SIBs' overall preparedness to comply with the principles as well as the challenges they face. While G-SIBs are increasingly aware of the importance of this topic and have taken steps towards fully implementing the principles, many of them are facing difficulties in establishing strong data aggregation governance, architecture and processes; instead, they resort to extensive manual workarounds.³⁶ The BCBS will continue to monitor their progress towards meeting this deadline, and will publish a progress report in December 2014.

3.4 Addressing data gaps

The FSB has developed a framework that is implementing in incremental and sequenced phases a common data template for G-SIBs to address key information gaps and to provide the authorities with a strong framework for assessing potential systemic risks and to collect and share the data among relevant authorities through a data hub. The second and third phases of the initiative are planned in 2015-2016 after the successful launch in March 2013 of the first phase with the collection of weekly or monthly data on G-SIBs credit exposures (bilaterally by largest counterparties and aggregated by country).

The International Data Hub, hosted by the Bank for International Settlements (BIS) and whose operations are governed by a multilateral framework signed by participating authorities, represents a unique international collaborative process to pool and share consistent firm-level data to assess concentration and interconnectedness among G-SIBs. The Hub's quality checks on data reported by the banks are focused on improving the firms' ability to aggregate and report their counterparty exposures in a consistent, timely, and accurate manner.³⁷

In the second phase, approved by the FSB in March 2014, authorities will collect globally comparable data on G-SIBs' liabilities, their largest fund providers and funding structure. In September 2014, sharing of data has been extended to non-supervisory central banks with a macroprudential mandate.³⁸ Phase 3 of the initiative will involve the aggregation of granular and comparable balance sheet data with country, sector, currency, instrument and maturity

³⁵ See <http://www.bis.org/publ/bcbs239.pdf>. Supervisory programs for G-SIBs now include regular assessments of progress on implementation of these principles, to ensure resources remain committed to this effort through the cycle. In addition, the BCBS strongly suggests that national supervisors apply these principles to institutions identified as D-SIBs three years after their designation. The BCBS believes that the principles can be applied to a wider range of banks, in a way that is proportionate to their size, nature and complexity.

³⁶ Of the 30 banks that were identified as G-SIBs during 2011 and 2012, 10 reported that they will not be able to fully comply with the principles by the 2016 deadline. The main reason reported is large, ongoing, multi-year information technology and data-related projects.

³⁷ The latest Senior Supervisors Group progress report on counterparty data (January 2014, http://www.financialstabilityboard.org/publications/r_140116.htm) highlighted that firms' reporting of top counterparty exposures failed to meet supervisory expectations as well as industry self-identified best practices, with data quality being of particular concern.

³⁸ Collegiate macroprudential authorities (i.e. boards composed of authorities with responsibility to identify, monitor and take action to remove or reduce systemic risks) do not get direct access to the Hub reports, but rely on members that are data receivers (supervisory authorities and central banks) to flag relevant financial stability issues.

break-downs.³⁹ In the event of a crisis, authorities could require more frequent and extended data.

In parallel, work is underway among G-SIB jurisdictions to investigate the legal gateways for extending the sharing of specific reports to international financial institutions. Access of host supervisory authorities in major financial jurisdictions of systemic importance (“systemic hub authorities”) to reports is also under consideration.

This project is one element of a broader Data Gaps Initiative (DGI)⁴⁰ coordinated by the IMF and FSB to address information gaps that were revealed by the global financial crisis. Significant progress on the implementation of 20 recommendations under the DGI has been made but further work is still needed to reap the full benefits for enhancing policy analysis and surveillance, including financial stability and debt analysis, and understanding domestic and international interconnectedness. G20 jurisdictions are enhancing their datasets under this initiative at different paces, primarily reflecting their varying levels of sophistication of statistical systems. Several non-G20 countries also report that they are implementing many DGI statistical requirements.

A second stage of the initiative is currently being defined, for proposal to the G20 in 2015, to strengthen and consolidate the progress to date and promote the regular flow of complete, comparable and high-quality data across G20 countries (with possible extensions to relevant non-G20 jurisdictions). Data collections whose conceptual framework has already been established will start in the next years and a few new data requests could be added as needs arise from policy-makers and other users.

Following a request by G20 Ministers and Governors in April 2014, the IMF, FSB and BIS has advanced work to address potential data gaps related to foreign currency exposures, including currency mismatches and leverage in corporate balance sheets. The three organisations will continue to coordinate their efforts in advancing work in this area and report back to G20 Finance Ministers and Central Bank Governors in late 2015.

3.5 Strengthening core infrastructure

In April 2012, the Committee on Payment and Settlement Systems (CPSS)⁴¹ and IOSCO issued the *Principles for financial market infrastructures* (PFMIs). The principles are designed to ensure that the infrastructure supporting global financial markets is robust and thus well placed to withstand financial shocks. The principles apply to all systemically important payment systems, central securities depositories, securities settlement systems,

³⁹ A QIS, with the participation of the majority of G-SIBs, will be finalised by end-2014 to assess the feasibility and reporting burden for Phase 3 data. The templates should be submitted for approval to the FSB Plenary in March 2015 with a plan to start the data collection by mid-2016.

⁴⁰ Full details on the implementation of the 20 DGI recommendations are included in the annual FSB-IMF progress report to the G20, where benchmarks are provided to determine when to call each recommendation complete and the future work plan is outlined. The fifth progress report was published in September 2014 (http://www.financialstabilityboard.org/wp-content/uploads/r_140923.pdf).

⁴¹ As of 1 September 2014, the BIS’s Committee on Payment and Settlement Systems (CPSS) has been renamed the Committee on Payments and Market Infrastructures (CPMI). See BIS press release, available here: <http://www.bis.org/press/p140901.htm>.

central counterparties and trade repositories (collectively “financial market infrastructures” (FMIs)). These FMIs collectively clear, settle and record transactions in financial markets. CPMI and IOSCO are currently in the process of monitoring the implementation of PFMIs.

4. Transforming shadow banking into resilient market-based finance

Transforming shadow banking into resilient market-based finance is one of the core elements of the FSB’s regulatory reform agenda to address the fault lines that contributed to the global financial crisis and to build safer, more sustainable sources of financing for the real economy.

The FSB has defined shadow banking as “credit intermediation involving entities and activities (fully or partly) outside the regular banking system”, or non-bank credit intermediation in short.⁴² Such intermediation, appropriately conducted, provides a valuable alternative to bank funding that supports real economic activity. However, the global financial crisis exposed significant fault lines in riskier types of shadow banking activities. These centred on heavy reliance on short-term wholesale funding, a variety of incentive problems in securitised and structured finance markets that weakened lending standards, and a general lack of transparency that hid growing amounts of leverage and maturity mismatch, as well as the ultimate bearer of the associated risks.

The FSB has adopted a two-pronged strategy to deal with these fault lines. First, it has created a system-wide monitoring framework to track financial sector developments outside the banking system with a view to identifying the build-up of systemic risks and initiating corrective actions where necessary. Second, the FSB is coordinating and contributing to the development of policy measures in five areas where oversight and regulation need to be strengthened to reduce excessive build-up of leverage, as well as maturity and liquidity mismatch, in the system:

- (i) mitigating risks in banks’ interactions with shadow banking entities;
- (ii) reducing the susceptibility of money market funds (MMFs) to “runs”;
- (iii) improving transparency and aligning incentives in securitisation;
- (iv) dampening pro-cyclicality and other financial stability risks in securities financing transactions such as repos and securities lending; and
- (v) assessing and mitigating financial stability risks posed by other shadow banking entities and activities.

In accordance with the actions and deadlines set by the G20 Leaders in their Roadmap annexed to the St Petersburg Summit Declaration,⁴³ the development of these policy measures has further progressed and will be adopted by FSB members in an internationally-coordinated manner. The FSB, in coordination with the relevant SSBs, will monitor the national

⁴² Based on such features, some authorities or market participants prefer to use other terms such as “market-based financing” instead of “shadow banking”. The use of the term “shadow banking” is not intended to cast a pejorative tone on this system of credit intermediation. However, the FSB is using the term “shadow banking” as this is the most commonly employed and, in particular, has been used in the earlier G20 communications.

⁴³ See <http://en.g20russia.ru/load/782788663>.

implementation of the agreed policies to ensure they achieve the intended objectives. The FSB is publishing an updated Roadmap at the time of the Brisbane Summit.⁴⁴

4.1 Strengthening oversight of the shadow banking system

The FSB began conducting annual monitoring exercises to assess global trends and risks of the shadow banking system in 2011, which now cover jurisdictions representing 80% of global gross domestic product and 90% of global financial system assets. The results of its fourth monitoring exercise were published in October 2014, and reflect data as of end-2013.⁴⁵ In the fourth exercise, the FSB continued to refine the shadow banking measure to produce an estimate that focused more tightly on shadow banking risks, narrowing down the broad Monitoring Universe of Non-Bank Financial Intermediation estimate by filtering out entities that are not involved in credit intermediation and those that are prudentially consolidated into a banking group.

Going forward, the FSB's monitoring will benefit from further improvement in data availability and granularity. In future years, the ongoing work to narrow down the estimate of the shadow banking sector will draw on the results of the information-sharing exercise on shadow banking entities and activities (see below), the initial round of which commenced this year.

Besides the monitoring at the FSB level, the FSB's Regional Consultative Groups (RCGs) for the Americas and Asia, which include non-FSB member authorities, have recently started to conduct their own monitoring exercise modelled on the annual FSB monitoring exercises.⁴⁶ This extension of the FSB's monitoring approach to other jurisdictions where shadow banking entities are often domiciled will help to fill a gap in the current monitoring exercise.

4.2 Strengthening regulation of the shadow banking system

The policy work has focused on the following five areas.

Mitigating risks in banks' interactions with shadow banking entities

To ensure that the spill-over of risks from the shadow banking system to the banking system are addressed, the BCBS has now finalised: (i) risk-sensitive capital requirements for banks' investments in the equity of funds; and (ii) the supervisory framework for measuring and controlling banks' large exposures. The former requirement will be implemented from 1 January 2017, and the latter by January 2019. The BCBS also continues to work on reviewing the scope of consolidation for prudential regulatory purposes with a view to developing guidance for public consultation by end-2015 to ensure that all banks' activities, including interaction with the shadow banking system, are appropriately captured in prudential regimes.

⁴⁴ See <http://www.financialstabilityboard.org/2014/11/Progress-Report-on-Transforming-Shadow-Banking-into-Resilient-Market-Based-Financing>

⁴⁵ See http://www.financialstabilityboard.org/wp-content/uploads/r_141030.pdf.

⁴⁶ The reports by the RCGs for the Americas (http://www.financialstabilityboard.org/wp-content/uploads/r_140822b.pdf) and for Asia (http://www.financialstabilityboard.org/wp-content/uploads/r_140822c.pdf) were published in August 2014.

Reducing the susceptibility of MMFs to “runs”

IOSCO issued policy recommendations in October 2012 that provide the basis for common standards of regulation and management of MMFs across jurisdictions, to address the systemic risks of investor runs on a large segment of MMFs.

Since then, national and regional authorities have been making progress in reforming their regulatory frameworks for MMFs. In the US, the world’s largest MMF market, the Securities and Exchange Commission (SEC) adopted amendments to the rules that govern MMFs in July 2014 to address risks of investor runs while preserving the benefits of those funds.⁴⁷ The new rules will require a floating net asset value (NAV) for institutional prime MMFs so that the daily share prices of these funds fluctuate along with changes in the market-based value of fund assets, and provide non-government MMFs with new tools (e.g. liquidity fees and redemption gates) to address runs. In the EU, the second-largest MMF market, the European Commission issued a proposal in September 2013 that includes, in particular, a 3% capital buffer for constant NAV funds, asset diversification requirements, daily and weekly liquidity requirements as well as a number of other requirements relating to eligible assets, valuation methods, use of external credit ratings, transparency and reporting.⁴⁸

IOSCO is currently undertaking a “level one” peer review (i.e. review of the timeliness of adoption) on the progress of national/regional regulatory reforms for MMFs in the areas covered by the IOSCO recommendations. The review aims to cover all FSB member jurisdictions and those IOSCO members from non-FSB member jurisdictions with significant MMF sectors. The preliminary findings, based on self-assessments, indicate that most FSB jurisdictions have measures in force or are progressing towards the intended outcome. The final report will be published in the second quarter of 2015.

Improving transparency and aligning incentives in securitisation

IOSCO issued policy recommendations in November 2012, based on a stock-take of reforms, especially those related to transparency, standardisation and risk retention requirements. Based on its recommendations, IOSCO is currently undertaking a level one peer review on national/regional approaches to align incentives associated with securitisation, including risk retention requirements.⁴⁹ The preliminary findings, based on self-assessments, indicate that there has been good progress in implementing the adoption measures for the incentive alignment recommendations, with a majority of responding jurisdictions having taken steps to do so. The final report will be published in the second quarter of 2015.

The resumption of orderly securitisation markets is a goal of the wider financial reform programme, and the FSB and SSBs continue to review and address regulatory impediments in this regard. BCBS and IOSCO have established a cross-sectoral working group to identify factors that may be hindering the development of sustainable securitisation markets, and develop criteria to identify and assist in the development by the financial industry of simple and transparent securitisation structures. They are considering the publication of a

⁴⁷ See <http://www.sec.gov/rules/final/2014/33-9616.pdf>.

⁴⁸ See http://ec.europa.eu/internal_market/investment/docs/money-market-funds/130904_mmfs-regulation_en.pdf.

⁴⁹ In relation to this, the US authorities in October 2014 approved a final rule requiring sponsors of securitisation transactions to retain risk in those transactions (<http://www.federalreserve.gov/newsevents/press/bcreg/20141022a.htm>).

consultation paper to identify simple, transparent and comparable securitisations. The document setting out criteria agreed for consultation is expected to be published in late 2014.

Dampening procyclicality and other financial stability risks in securities financing transactions

The FSB published in October 2014 the regulatory framework for haircuts on non-centrally cleared securities financing transactions (SFTs), which includes numerical haircut floors for transactions in which financing against collateral other than government securities is provided to entities other than banks and broker-dealers (or “non-banks” in short).⁵⁰ This Framework is a key part of the FSB’s policy recommendations to address shadow banking risks in relation to SFTs, the rest of which were finalised in August 2013.⁵¹ The Framework aims to limit the build-up of excessive leverage outside the banking system and to help reduce the procyclicality of that leverage.

The FSB has also issued a consultative proposal on the application of numerical haircut floors for non-bank-to-non-bank transactions to ensure shadow banking activities are fully covered, to reduce the risk of regulatory arbitrage and to maintain a level playing field. The FSB plans to complete this work and set out details of how it will monitor implementation of the Framework by the second quarter of 2015. The Framework will be implemented by the end of 2017.

Besides the Framework, the FSB and its members have started to implement the policy recommendations for SFTs that were finalised in August 2013. Based on the recommendations to improve transparency, the FSB has developed, in cooperation with market participants, standards and processes for global data collection and aggregation on securities financing transactions that are relevant for financial stability monitoring and policy responses. The standards were published for public consultation in November 2014 and will be completed in 2015.⁵²

Meanwhile, national and regional authorities as well as market participants have launched legislative and/or data collection initiatives to better understand their securities financing markets and improve market transparency in light of the FSB recommendations. For example, in January 2014, the European Commission adopted a proposal for a Regulation on reporting and transparency of SFTs in the EU, which includes a requirement for SFTs to be reported to a trade repository.⁵³ The European Systemic Risk Board conducted a data collection exercise to gain some initial insights into the structure of the securities financing market and the practices adopted by market participants concerning the re-investment or the re-use of the collateral sourced through SFTs or through equivalent transactions.⁵⁴ In the US, the Office for

⁵⁰ See http://www.financialstabilityboard.org/wp-content/uploads/r_141013a.pdf.

⁵¹ See http://www.financialstabilityboard.org/publications/r_130829b.pdf.

⁵² See <http://www.financialstabilityboard.org/2014/11/fsb-publishes-standards-and-processes-for-global-securities-financing-data-collection-and-aggregation>

⁵³ See <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52014PC0040&from=EN>.

⁵⁴ See https://www.esrb.europa.eu/pub/pdf/occasional/20140923_occasional_paper_6.pdf.

Financial Research, in cooperation with other US authorities, has announced a data initiative to help identify the data gaps with focus on bilateral repo markets.⁵⁵

The FSB has established an expert group to take stock of the current regulatory approaches on re-hypothecation of client assets and examine their possible harmonisation by end-2015. It will also review the financial stability issues regarding the re-use of collateral more generally.

Assessing and mitigating systemic risks posed by other shadow banking entities and activities

Recognising that shadow banking entities and activities take a variety of forms and evolve over time, the FSB has developed a forward-looking high-level policy framework for adoption by authorities to detect and assess the sources of financial stability risks from shadow banking in the non-bank financial space, and apply appropriate policy measures where necessary to mitigate these risks. The framework comprises: (i) an assessment of non-bank financial entity types based on five economic functions;⁵⁶ (ii) the adoption of policy tools to mitigate financial stability risks where necessary; and (iii) information-sharing by FSB member authorities through the FSB process to maintain international consistency in applying the framework, minimise gaps in regulation and detect new adaptations.⁵⁷

Based on the framework, the FSB launched in May 2014 an initial information-sharing exercise to exchange information on national authorities' implementation of the framework and to refine the detailed information-sharing process to prepare for future exercises.⁵⁸ It will conduct a comprehensive exercise next year that will cover all FSB member jurisdictions. The results of next year's exercise will provide the basis for a peer review of member jurisdictions' implementation of the policy framework. Based on the findings, the FSB will evaluate the case for developing further policy recommendations for relevant shadow banking entities and will report the results to G20 Finance Ministers and Central Bank Governors in 2015.

5. Making derivatives markets safer

In response to concerns about systemic risks in OTC derivatives markets, in 2009 and subsequent meetings the G20 Leaders agreed to a comprehensive reform agenda to improve transparency in these markets, mitigate systemic risk, and protect against market abuse. To achieve these objectives, the G20 agreed that by end-2012: all OTC derivative contracts should be reported to trade repositories (TRs); all standardised OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through CCPs; and non-centrally cleared contracts should be subject to higher capital requirements and margining requirements should be developed.

⁵⁵ See <http://www.treasury.gov/connect/blog/Pages/OFR-Teams-with-Fed-to-Fill-Key-Gap-in-Financial-Data.aspx>.

⁵⁶ Each of the five economic functions involves non-bank credit intermediation that poses bank-like systemic risks (e.g. maturity/liquidity transformation and leverage).

⁵⁷ See http://www.financialstabilityboard.org/publications/r_130829c.pdf.

⁵⁸ Fourteen jurisdictions, representing over 80% of the non-bank financial assets of FSB member jurisdictions, participated in the initial exercise. For details, see Annex 3 of the 2014 Global Shadow Banking Monitoring Report.

Implementation of OTC derivatives reforms is uneven and overdue, but progress continues to be made across jurisdictions and further progress is anticipated for 2015. The adoption of legislation, where this has been a necessary first step of the reform process, is nearing completion. The extent of implementation of detailed regulations varies across jurisdictions and reform areas. The greatest progress to date has been in adopting regulations implementing higher capital requirements for non-centrally cleared derivatives and trade reporting requirements, which are each now at least partially effective in more than three-quarters of FSB member jurisdictions. Implementation in other reform areas is also proceeding, though timetables stretch well into 2015 and beyond. Measures to promote trading on exchanges or electronic trading platforms continue to take longer than those in other reform areas.

5.1 Jurisdictional progress and international standards

In each reform area, over half of FSB member jurisdictions have adopted legislation (or legislative changes have not been required) to enable the reform commitment to be implemented. Over three-quarters of FSB member jurisdictions have some trade reporting requirements already in effect and all but one jurisdiction expect to have some trade reporting requirements in effect by end-2015.⁵⁹ Substantial progress has also been made in the implementation of Basel III capital standards for banks' counterparty credit-related derivatives exposures – with close to 90% of the member jurisdictions currently having the relevant requirements fully or partially in effect. While only five jurisdictions have some mandatory central clearing requirements in place currently, by the second half of 2015 it is anticipated that 15 of the 24 FSB member jurisdictions will have mandatory central clearing requirements for some products in effect. Progress to date has been slower on implementing reform measures to promote trading on exchanges or electronic trading platforms, where appropriate. Few jurisdictions report having margin rules for non-centrally cleared OTC derivatives in effect, or in consultation or proposed. Further information on implementation progress is described in the FSB's latest progress report.⁶⁰

International guidance to assist with implementation of reforms is now largely complete. The BCBS issued capital standards for banks' counterparty exposures arising from centrally cleared transactions. CPMI-IOSCO and the FSB have also recently finalised a comprehensive set of guidance on recovery and resolution for FMIs, including CCPs, following a public consultation (see section 3.1). IOSCO released a consultation paper on risk mitigation standards for non-centrally cleared OTC derivatives in September 2014, and plans to issue a final report by the end of 2014. Implementation monitoring of CPMI-IOSCO's PFMI is now underway, covering infrastructure supporting OTC derivatives markets as well as other functions. The FSB has launched a peer review of jurisdictions' actions to meet the G20 commitment that all OTC derivatives transactions should be reported to TRs, and will report on the findings in 2015.

⁵⁹ However, authorities continue to report challenges regarding the access to and usability of data held by TRs.

⁶⁰ See http://www.financialstabilityboard.org/wp-content/uploads/r_141107.pdf.

5.2 Progress towards resolving cross-border issues

To ensure that implementation achieves the underlying G20 goals, the remaining cross-border regulatory issues need to be resolved. With many jurisdictions now well underway in their implementation of reforms, clarity over the cross-border application of regulations and regulatory coordination in applying rules is increasingly important. Accordingly, bilateral and multilateral discussions addressing outstanding cross-border issues have intensified over the course of 2014. The OTC Derivatives Regulators Group – a group of market regulators from jurisdictions with large OTC derivatives markets – has been working to address identified cross-border issues and has provided a report to the Summit providing more concrete information on how it has addressed or intends to address identified cross-border issues.⁶¹

Deference – in part or in full – to another jurisdiction's derivatives regulatory regime, where appropriate, is an important tool for addressing some of the cross-border issues arising from differences in the regulatory reforms. The FSB encourages jurisdictions and regulators to defer to each other when it is justified, in line with the St. Petersburg G20 Leaders' Declaration.⁶² To provide more information about existing deference processes and arrangements, the FSB published in September 2014 a report summarising the status of each FSB member jurisdiction's capabilities and processes to defer to another jurisdiction's OTC derivatives regulatory regime.⁶³ The report noted that most jurisdictions have established or are establishing frameworks and processes for applying deference where justified. This information, together with the forthcoming IOSCO report on cross-border regulatory tools, can help to inform any further work done to better understand the circumstances under which deference and other regulatory tools could be used most effectively. The OTC Derivatives Regulators Group, in the context of its work to implement understandings in the area of equivalence and substituted compliance, is continuing to consider how deference to foreign regimes will work in practice.

5.3 Global aggregation of TR data

While a majority of jurisdictions have introduced trade reporting obligations, the usefulness of this data in supporting monitoring of financial stability risks is limited by data quality issues (including the formatting, completeness and accuracy of data). Authorities continue to face challenges regarding the accessibility and usability of data held by TRs; resolving these issues is a priority. The FSB and the OTC Derivatives Regulators Group have expressed concern about legal barriers to the reporting of counterparty information to TRs, and stressed the importance of rapid action by jurisdictions to remove those barriers.

Aggregation of the data being reported across the various TRs operating in different jurisdictions is necessary to ensure that authorities are able to obtain a comprehensive global view of the OTC derivatives market and activity. The FSB published in September 2014 a

⁶¹ See http://www.cftc.gov/ucm/groups/public/@internationalaffairs/documents/file/oia_odrgreportg20_1114.pdf.

⁶² Paragraph 71 of the September 2013 G20 Leaders' St Petersburg Declaration; available at: https://www.g20.org/sites/default/files/g20_resources/library/Saint_Petersburg_Declaration_ENG.pdf.

⁶³ See http://www.financialstabilityboard.org/wp-content/uploads/r_140918.pdf.

study of the feasibility of various options for a mechanism to produce and share globally aggregated TR data.⁶⁴ Acting on the recommendations of the study, the FSB:

- has asked CPMI and IOSCO to develop global guidance on harmonisation of data elements that are reported to trade repositories and are important to aggregation by authorities.
- will work with CPMI and IOSCO to provide official sector impetus and coordination for the further development and implementation of uniform global UTIs and UPIs.
- will, with the involvement of CPMI and IOSCO, study in more detail and address the legal and regulatory changes that would be needed to implement a global aggregation mechanism that would meet the range of authorities' data access needs, and the appropriate governance structure for such a mechanism.⁶⁵

6. Creating continuous markets – other market reforms

6.1 Reforming financial benchmark-setting

Over the course of recent years, serious concerns and allegations have been raised regarding the integrity and manipulation of various benchmarks used internationally in the banking industry and financial markets. The post-crisis decline in liquidity in some interbank unsecured funding markets has also reduced confidence in these benchmarks. In response to these concerns, in 2013 IOSCO published *Principles for Financial Benchmarks*, and the FSB established an Official Sector Steering Group (OSSG) to coordinate work on reforms of financial benchmarks. G20 Leaders in their St Petersburg Declaration endorsed the IOSCO Principles, and supported further reforms as necessary of international benchmarks.

Since then, the FSB has published reform proposals both for key interest rate benchmarks and for key FX rate benchmarks, with IOSCO undertaking complementary reviews of how well these benchmarks meet the relevant principles. The FSB has recommended that IOSCO conducts a further review of the three interest rate benchmarks in mid-2015, reporting back to the OSSG on its findings by the fourth quarter of 2015. The FSB will produce an interim report in 2015 and a final report in 2016 on how these reform proposals have been implemented by the industry.⁶⁶

Interest rate benchmarks

In July 2014 the FSB published a report, prepared by the OSSG, with proposals, plans and timelines for the reform and strengthening of existing major interest rate benchmarks (such as LIBOR, EURIBOR, and TIBOR) and for additional work on the development and introduction of alternative benchmarks.⁶⁷ This report included IOSCO's review of these

⁶⁴ See http://www.financialstabilityboard.org/wp-content/uploads/r_140919.pdf

⁶⁵ See http://www.financialstabilityboard.org/wp-content/uploads/pr_140919.pdf.

⁶⁶ These international workstreams have been separate to any ongoing conduct investigations being undertaken in different jurisdictions by specific authorities.

⁶⁷ See http://www.financialstabilityboard.org/wp-content/uploads/r_140722.pdf.

benchmarks against the IOSCO Principles,⁶⁸ as well as a report by private sector experts identifying alternative benchmark rates and analysing the transition issues arising in the event of a move to an alternative benchmark rate.⁶⁹

The report's main recommendations involved: (i) strengthening the existing interest rate benchmarks referenced above, as well as other potential reference rates based on unsecured bank funding costs, by underpinning them to the greatest extent possible with transaction data; and (ii) developing alternative, nearly risk-free rates to meet the principles of encouraging market choice, recognising that certain financial transactions, including many derivative transactions, may be better suited to reference rates that are closer to risk-free.

While there is widespread support for the multiple-rate approach, there will necessarily be heterogeneity across currencies in terms of how this approach is implemented. There are several reasons for this heterogeneity, including differing availability of underlying transactions data necessary to produce enhanced benchmark rates based on unsecured bank funding costs, different markets for near risk-free rates, and different levels of willingness and scope to use supervisory or other means to encourage markets participants to adapt to the multiple-rate approach.

Currency subgroups formed by the OSSG will work with and guide the private sector to: implement new designs and methodologies for existing benchmarks; and, where currently absent, identify and develop viable near risk-free rates supported by robust methodologies. By end-2015, administrators of the major benchmarks should have publicly consulted on any recommended changes, while the currency subgroups will work to develop transition strategies and address any legal obstacles and risks. In respect of risk-free rates, where suitable, central banks and supervisory authorities should encourage the industry or work with the administrators to implement at least one IOSCO-compliant risk-free rate by the second quarter of 2016.

FX benchmarks

In September 2014 the FSB published a report on FX benchmarks, which set out a number of reform recommendations both for these benchmarks and around market practices.⁷⁰ As with interest rate benchmarks, this report had benefited from a review undertaken by IOSCO of the observance by the dominant FX rate provider of the IOSCO Principles.⁷¹ The FSB report analysed the FX market structure and incentives that may promote particular types of trading activity around benchmark fixings.

The report recommended changes to the calculation methodology of the key FX benchmarks – in particular, that the calculation window for these fixings be widened – and that the administrator of these benchmarks make enhancements to address findings in IOSCO's review. The report also made recommendations in relation to the publication of reference

⁶⁸ See http://www.financialstabilityboard.org/wp-content/uploads/r_140722a.pdf.

⁶⁹ See http://www.financialstabilityboard.org/wp-content/uploads/r_140722b.pdf.

⁷⁰ See http://www.financialstabilityboard.org/wp-content/uploads/r_140930.pdf.

⁷¹ See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD451.pdf>. The IOSCO report recommends a subsequent review of FX rate providers' implementation of the IOSCO Principles be conducted, which IOSCO intends to do in mid-2015.

rates produced by central banks, the market infrastructure in relation to the execution of trades associated with benchmark fixings, and the behaviour of market participants around the time of the major FX benchmark fixings. The FSB believes that all the recommendations above can and will be accepted and implemented by relevant entities.

6.2 Building a global legal entity identifier

A global legal entity identifier (LEI) system is now effectively functioning and actively used by a number of companies and authorities around the globe to uniquely identify participants in financial markets. The transition to the steady state, with a fully functional central operating unit, will take place in the course of 2015. Progressing towards adoption of the LEI by legal entities worldwide is essential to fully reap the collective benefits of this innovation. The use of the LEI by authorities for a wider range of regulatory purposes, as encouraged by G20 Leaders in Los Cabos, will help to further promote the adoption of the LEI by market participants. The system should also progressively develop its capacity to record additional reference data on the direct and ultimate parent(s) of legal entities, as envisaged by the FSB's LEI High Level Principles and Recommendations of 2012. This will further enhance the ability of authorities and market participants to manage more reliably and cost-efficiently complex financial market data and better identify and mitigate financial risks.

The Regulatory Oversight Committee (ROC) of the Legal Entity Identifier,⁷² established in January 2013 to oversee the Global LEI System in the broad public interest, took over full responsibility from the FSB for the implementation of the system, with the FSB continuing to provide active support. The ROC includes members and observers from more than 70 authorities.

The ROC approved in 2013 an interim endorsement process for the system, whereby the ROC endorses local operating units (LOUs) as issuers of globally compatible codes after meeting the conditions set out by the ROC. As of end-September 2014, over 300,000 legal entities from 189 countries had obtained LEIs from 18 operational LOUs endorsed by the ROC. In addition to assigning LEIs, LOUs also validate and maintain the associated reference data, and make these data available to the public and regulators free of charge and on a continuous basis.

The Global LEI Foundation (GLEIF), overseen by the ROC, was established by the FSB in June 2014 and is in the process of setting up its operations. The GLEIF will support the maintenance of a logically centralised database of identifiers and corresponding reference data and, over the course of 2015, will take over all responsibilities towards LOUs to ensure the application of uniform global operational standards and protocols.

⁷² See <http://www.leiroc.org/>.

6.3 Reducing reliance on credit ratings and improving oversight of credit rating agencies (CRAs)

6.3.1 Reducing reliance on CRA ratings

The FSB issued in 2010 *Principles for Reducing Reliance on CRA Ratings* and is closely monitoring the implementation of the principles. The goal of the FSB's Principles is to end mechanistic reliance on CRA ratings by banks, institutional investors and other market participants by reducing the "hard wiring" of CRA ratings in standards, laws and regulations and by providing incentives for firms to develop their own capacity for credit risk assessment and due diligence. As demonstrated during the financial crisis such reliance can be a cause of herding behaviour and of abrupt sell-offs of securities when they are downgraded ("cliff effects"), which can in turn amplify procyclicality and cause systemic disruption. However, by 2012, authorities in most G20 countries had made only slow progress to reduce reliance across the different financial sectors, and G20 Leaders in their Los Cabos Declaration called for accelerated progress by national authorities and SSBs in ending the mechanistic reliance on credit ratings. In response to this call, the FSB published a roadmap⁷³ in October 2012 with timelines to accelerate implementation of the FSB Principles.

The FSB undertook a thematic peer review to assist national authorities in fulfilling their commitments under the roadmap. The review was structured in two stages: the first stage, published in August 2013⁷⁴ comprised a structured stock-taking of references to CRA ratings in national laws and regulations, and the second and final stage focused on the action plans developed by national authorities to implement the roadmap.⁷⁵

The peer review found that progress toward the removal of references to CRA ratings from standards, laws and regulation has been uneven across the financial sectors. Reliance on such ratings persists, particularly in private contracts, investment mandates, internal limits, and collateral agreements. Reliance on ratings also remains to some extent in existing risk-based prudential frameworks for banks and insurers, where such frameworks are largely based on international standards. Central banks continue to rely on ratings in their eligibility criteria for collateral for lending facilities and in investment guidelines and mandates for foreign reserves operations.

The key challenge is developing alternative standards of creditworthiness and processes so that CRA ratings are no more than an input to credit risk assessment. National authorities and financial entities should guard against the temptation to adopt a small number of alternative measures for assessing creditworthiness in place of CRA ratings, which can result in substituted procyclicality and herd behaviour.

While good progress has been made toward removing references to CRA ratings from laws and regulations, mechanistic reliance can also come from market practices and contracts. Authorities should encourage market participants to review provisions within their private contracts which represent mechanistic reliance on CRA ratings (e.g. ratings triggers).

⁷³ See http://www.financialstabilityboard.org/publications/r_121105b.pdf.

⁷⁴ See http://www.financialstabilityboard.org/publications/r_130829e.pdf.

⁷⁵ The action plans can be found at http://www.financialstabilityboard.org/publications/c_140429.htm.

The stock-taking exercise and development of action plans across the FSB membership represent a significant step toward reducing reliance on CRA ratings in standards, laws and regulations, but more work is needed to implement fully the agreed roadmap. More work in the design of action plans is needed on the development of alternative standards of creditworthiness, the ways authorities will incentivise or promote own credit assessment processes, and the establishment of clear timelines for taking action. The challenges of identifying alternative standards of creditworthiness and the time required to build-up or enhance own credit risk assessment capabilities (especially for smaller entities) are hindering progress. National authorities need to intensify efforts to address these gaps in their action plans in order to meet the timelines set out in the roadmap.

Over the coming year, the FSB will monitor progress toward implementing the recommendations set out in the peer review to address some of the challenging hindering progress toward implementing the roadmap. To facilitate this, the FSB will hold a workshop with national authorities in early 2015.

Work by SSBs to reduce reliance on CRAs

The BCBS published in December 2013 a second consultative paper on revisions to the Basel securitisation framework, which seeks to reduce the mechanistic reliance on external ratings embedded in the existing framework.⁷⁶ The revised securitisation framework is expected to be finalised by the end of 2014. In addition, the BCBS has set up a Task Force on Standardised Approaches, one of whose objectives is to reduce or remove, where possible, the reliance on external ratings. This includes developing supplementary measures for risk classification and encouraging stronger supervisory practices to promote alternative measures for risk assessment. In considering potential alternatives to use of CRA ratings, the BCBS is taking account of the challenges that also exist with respect to reliance on banks' internal models, the large variations in risk-weights that cannot be explained by underlying risks, the potential procyclicality of market-based indicators and the need for sufficient reliable in-house capacity to assess credit risks. A public consultation on revisions to the standardised approach is expected by the end of 2014.

An IOSCO consultation report on *Sound Practices at Intermediaries regarding Alternatives to the Use of Credit Ratings to Assess Creditworthiness* is expected to be published in the first half of 2015 and a final report is expected to be published later that year. A consultation report on *Good Practices on Reducing Reliance on CRAs*⁷⁷ was published in June 2014, and the final report is expected to be published by the end of this year. In addition, CPMI and IOSCO are conducting a survey of CCPs regarding their use of CRA ratings. The survey seeks to understand whether and how CRA ratings are currently used at CCPs and to identify good practices for how to reduce reliance on CRA ratings.

The work of the Organisation for Economic Co-operation and Development (OECD) in this area has included a review of the OECD principles for occupational pension fund regulation, consultations with pension regulatory bodies and workshops, and a 2013 survey of the pension fund industry. All of the surveyed pension funds use CRA ratings in their risk

⁷⁶ See at www.bis.org/publ/bcbs269.htm.

⁷⁷ See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD442.pdf>.

management or asset management, and often in a mechanistic manner. Pension regulatory frameworks do not, in most countries, discourage the mechanistic use of CRA ratings in an explicit, systematic manner. The lack of suitable alternative approaches was indicated as the main hindrance to the removal of references to CRA ratings.

For the insurance sector, the FSB's thematic peer review noted that the use of CRA ratings in regulation and legislation in FSB jurisdictions is not considered mechanistic as these ratings are generally supplemented with an internal assessment of creditworthiness. Starting in early 2015, the IAIS will undertake a comprehensive Self-Assessment and Peer Review on the thematic topic of Solvency and Solvency-Related Issues, which will cover these issues. Based on the findings from this assessment, the IAIS will consider whether insurance supervisors require additional guidance on the use of CRA ratings.

6.3.2 Improving oversight of CRAs

Almost all FSB jurisdictions report having put in place requirements for the registration of CRAs. Only Russia and Saudi Arabia have indicated that they are still developing their CRA regulations. Most jurisdictions report that their code for CRAs and/or their regulatory oversight framework is consistent with the IOSCO *Statement of Principles Regarding the Activities of Credit Rating Agencies* and the IOSCO *Code of Conduct Fundamentals for Credit Rating Agencies*.⁷⁸

The IOSCO Code of Conduct is currently under revision. IOSCO published in February 2014 a consultation report⁷⁹ with proposed amendments to the Code. After analysing the consultation responses IOSCO aims to publish the final revised Code by early 2015.

Several jurisdictions (e.g. Australia, Canada, Hong Kong, Mexico, US) have signed Memorandums of Understanding for appropriate sharing of information. In the EU, the European Commission has taken an Equivalence Decision (allowing for endorsement of third-country ratings and equivalence of third-country regimes) on the regulatory frameworks of a number of non-EU FSB jurisdictions, such as Argentina and Hong Kong.

Following recommendations that IOSCO made in its July 2013 *Final Report on Supervisory Colleges for Credit Rating Agencies*, CRA supervisors established supervisory colleges for globally active CRAs (Standard & Poor's, Moody's and Fitch), which held their inaugural meetings in November 2013 in New York.

6.4 Enhancing market functioning

6.4.1 Hedge funds

The G20 at its Seoul Summit in November 2010 recommitted itself to work in an internationally consistent and non-discriminatory manner to strengthen regulation and supervision of hedge funds. Considerable progress has been reported in registration, appropriate disclosures and oversight of hedge funds over the past year. This includes adoption of the EU's Alternative Investment Fund Managers Directive (AIFMD) by relevant

⁷⁸ See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf>.

⁷⁹ See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD437.pdf>.

FSB members. Only South Africa reports that it is still implementing reforms, while hedge funds are not permitted in Argentina and no hedge funds are currently domiciled in Indonesia. Most of the other FSB jurisdictions have in place an oversight framework that includes registration of hedge funds or their managers and enhanced disclosure of information to investors and regulators on an ongoing basis. IOSCO is currently implementing the third iteration of its global hedge fund survey, with results and reporting due in 2015.

Progress has been made in the establishment of international information sharing arrangements for hedge funds, but more work is needed in this area. A number of jurisdictions (Australia, France, Hong Kong, Italy, Turkey) report an increase in the number of bilateral supervisory cooperation agreements with foreign counterparts. IOSCO's 2013 Hedge Funds Survey also indicated that jurisdictions were taking measures to overcome legal limitations concerning data sharing. Over the past year, two of the three FSB jurisdictions (Argentina and Indonesia) that were still listed in Appendix B of IOSCO's Multilateral Memorandum of Understanding (MMoU) have become full signatories, while the third member (Russia) reports that it has undertaken legislative reforms to promote international cooperation and information exchange and has recently applied to be a full signatory to the MMoU. China and South Africa report that they are yet to complete the reforms in this area.

6.4.2 Market integrity and efficiency

Structural change in financial markets brought about by technological developments and the risks posed by financial innovation and ongoing globalisation necessitate continuous efforts to enhance the regulation and surveillance of market participants. In this regard, IOSCO published in December 2013 its final report on *Regulatory Issues Raised by Changes in Market Structure*,⁸⁰ which makes recommendations that seek to promote market liquidity and efficiency, price transparency, and investors' execution quality in a fragmented environment.

The G20 at its Cannes Summit in 2011 committed to implement initial recommendations by IOSCO on market integrity and efficiency, including measures to address the risks posed by high frequency trading (HFT) and dark liquidity. Some jurisdictions (EU, Hong Kong, Russia, Switzerland) report making progress in this area over the past year. In the EU, this has been achieved with the entry into force of legislative initiatives⁸¹ that will take effect in early 2017 following national transpositions. In Hong Kong, an enhanced regulatory framework for electronic trading came into effect in January 2014 and the consultation concerning the regulation of alternative liquidity pools closed in April 2014. The Swiss Federal Council launched a reform package in December 2013, which also contains elements on market integrity to implement the G20 commitments on OTC derivatives and to bring FMI regulation in line with international standards.

HFT and dark pools represented more than 10% of the total equity trades for 2012 in thirteen FSB jurisdictions. Of these, seven jurisdictions (Australia, Canada, Hong Kong, Japan, Korea for HFT, Mexico for HFT, USA) report that they have already implemented market integrity and efficiency reforms; four (France, Germany, Spain, UK) will implement the new EU

⁸⁰ See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD431.pdf>.

⁸¹ These include the revised Markets in Financial Instruments Directive (MiFID II), the Markets in Financial Instruments Regulation and Market Abuse Directive II, and some provisions of Market Abuse Regulation.

legislative measures; and the remaining one (Switzerland) reports that it is in the process of implementing the reforms. By contrast, such practices are not relevant in several other jurisdictions either because they are prohibited or because of their limited scope.

6.4.3 Regulation and supervision of commodity derivatives markets

Responding to the G20 request for monitoring on a regular basis the implementation of the IOSCO Commodity Derivatives Principles, IOSCO published an *Update to the Survey on the Principles for the Regulation and Supervision of Commodity Derivatives Markets* in September 2014.⁸² The report notes that a majority of respondents were broadly compliant with the Principles and where commodity derivative markets exist⁸³ and market authorities acknowledged non-compliance, many of those authorities have proposed or enacted initiatives aimed at achieving full compliance over time. Because a number of the initiatives remain under development or in various stages of implementation, a more definitive analysis of those initiatives will be provided by IOSCO that will be conducted when the majority of the most significant initiatives reach key milestones.

Progress in the regulation of these markets was made in the EU where MIFID II was published in July 2014. This legislation comes into force in January 2017, and EU member states will adapt their national laws and regulations upon completion of the European texts. It is important to note the linkages of the Commodity Derivative Principles to OTC derivatives market reforms in creating a robust framework. Several FSB jurisdictions have not yet adopted reforms to implement the Principles given the non-existent or relatively small size of their commodity derivatives markets. However, available information indicates that there remain some non-EU FSB jurisdictions (Argentina, Canada, India, Singapore, South Africa) that are still implementing the reforms. A significant industry development has been a trend for the withdrawal of investment banks from the commodities sector and an increase in the activities of the generally unregulated specialist commodity trading firms; the regulatory implications of this change are being considered.

7. Improving accounting, auditing and disclosures

7.1 Enhancing and aligning accounting standards

The convergence work that was set in train by the G20 London Summit in April 2009 is now nearing completion, but the outcome will be two different models (produced by the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB)) for financial instruments and for insurance contracts. The FSB will work with standard setters, supervisors and regulators and other stakeholders to discuss how to further promote consistency of implementation.

⁸² See <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD449.pdf>.

⁸³ Available data on the size and location of commodity derivatives markets is limited. The thirteen countries that contribute to the BIS semi-annual derivatives survey (Australia, Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Spain, Sweden, Switzerland, UK, USA) account for the large majority of outstanding OTC commodities contracts.

In July 2014 the IASB published the final version of its revised standard (IFRS 9 Financial Instruments), bringing together the classification and measurement, impairment and hedge accounting phases of the project. This will reflect how an entity manages financial assets to realise cash flows, its expectations of credit losses and the effect of its risk management activities, and is effective from 1 January 2018, with early application permitted.

The FASB, after considering stakeholder feedback on its proposed model for classification and measurement, has decided to finalise the portion of its proposal related to equity investments and to retain existing GAAP for debt investments and hybrid financial instruments.

On loan loss impairment, IASB and FASB have been developing expected loss impairment standards that will incorporate a broader range of available credit information so as to recognise credit losses in loan portfolios at an earlier stage. The two boards' proposals are a significant improvement on the existing incurred loss approach, and should lead to similar provisions for poorly performing loans, but they are not fully converged and the provisions will be partly different for performing loans.

The IASB, in IFRS 9, requires entities to account for a portion of expected credit losses when financial instruments are first recognised and to recognise full lifetime expected credit losses on a more timely basis. The new model also results in a single impairment model being applied to all financial instruments, thereby removing a source of complexity associated with previous accounting requirements.

The FASB has developed an expected credit loss model which requires an entity to recognise at each reporting date an allowance for credit losses on financial assets equal to its current estimate of the total expected credit losses over the life of the assets. This will apply to financial assets measured at amortized cost (including debt securities classified as held-to-maturity), with debt securities classified as available-for-sale subject to existing guidance with some revisions. The FASB expects to issue a final standard in 2015.

The Boards' insurance projects have significantly different scopes, and there will not be a converged outcome. The IASB standard for insurance contracts is not comprehensive, whereas the FASB is proposing improvements to its long-standing insurance model. The IASB expects to issue the Standard on Insurance Contracts in 2015, but is currently considering the most difficult and contentious of the issues on which it sought input i.e. those relating to the accounting for contracts with participating features. In doing so, the IASB is conscious of the need to balance completing the project with the need to maintain the quality of its decision-making process in dealing with these challenging technical issues. After considering stakeholder feedback on the 2013 exposure draft, the FASB decided to make targeted recognition and measurement improvements to the model for long duration contracts. For short-duration contracts, the FASB decided to retain existing GAAP, but to make enhanced disclosures to improve transparency to investors.

The FSB has welcomed the standard setters' work and reaffirmed the continuing relevance of the objective of achieving a single set of high-quality global accounting standards.⁸⁴ The FSB

⁸⁴ According to the jurisdictional profiles prepared by IFRS Foundation (<http://www.ifrs.org/Use-around-the-world/Pages/Analysis-of-the-G20-IFRS-profiles.aspx>) to assess progress toward the goal of global accounting standards,

encouraged the IASB and FASB to monitor the consistent implementation of their respective standards and to continue to seek opportunities for further convergence. The FSB plans to hold a roundtable in early 2015 for standard setters, supervisors and regulators, and other stakeholders to discuss how to further promote consistency of implementation of the accounting standards for financial instruments.

7.2 Improving audit quality

The International Forum of Independent Audit Regulators (IFIAR) in April 2014 released a follow up to its first survey of its membership regarding findings from their inspection programs, conducted in 2012. The initial survey, released in December 2012, was designed to identify common inspection findings on a global basis. The survey was designed to gather information in response to a request by the FSB to IFIAR to obtain information on challenges and problems that members have identified in their inspection programs relating to external audits of financial institutions.

The IFIAR survey of 2012 and 2013 audit inspections indicated that the leading areas of deficiency in audits of systemically important financial institutions, including global systemically important banks, relate to auditing of allowance for loan losses and loan impairments; internal control testing; and auditing of the valuation of investments and securities. The FSB has been encouraging the work of IFIAR and the major accounting firms through their Global Public Policy Committee to identify root causes for these deficiencies and enhance audit quality in the audits of G-SIFIs. IFIAR is conducting a further survey in 2014, to be published in 2015, of findings from inspections completed 2013-14.

The BCBS in March 2014 published its revised *Guidance on External Audits of Banks*.⁸⁵ This document sets out the Basel Committee's greater supervisory expectations regarding audit quality and how that relates to the work of the external auditor and of the Audit Committee in a bank. Implementation of the principles and the explanatory guidance is expected to improve the quality of bank audits and enhance the effectiveness of prudential supervision, which is an important element of financial stability.

As part of the global effort to improve audit quality, IOSCO has identified three areas for potential action to improve audit quality: i) enhancing its cooperation with IFIAR; ii) assessing whether and how to strengthen the role of audit committees; and iii) improving the robustness of audit-related standard-setting governance.

14 of the G20 jurisdictions have adopted IFRSs for all or most companies in their public capital markets. Of the remaining 6 jurisdictions, three permit IFRSs on a limited voluntary basis for domestic and/or foreign issuers (India, Japan, United States); one (Saudi Arabia) requires IFRSs on a limited basis (banks and insurance companies only); one (China) has substantially converged its national standards to IFRSs; and one (Indonesia) has adopted some IASs/IFRSs but has not announced a plan or timetable for full adoption.

⁸⁵ See <http://www.bis.org/publ/bcbs280.pdf>.

7.3 Enhancing financial institutions' disclosures

In March 2012, the FSB facilitated the formation of the private sector Enhanced Disclosures Task Force (EDTF) to develop principles for enhanced disclosures. The EDTF report, 'Enhancing the Risk Disclosures of Banks', was published in October 2012. It contains principles and recommendations for improved bank risk disclosures and leading disclosure practices that are designed to provide timely information useful to investors and other users and can contribute, over time, to improved market confidence in financial institutions. The FSB views the principles and recommendations as a valuable step to improve the quality of risk disclosures, and a number of FSB jurisdictions (France, Italy, Netherlands, Singapore, South Africa, Spain, Switzerland, UK) report taking steps to encourage the adoption of the EDTF recommendations.

At the FSB's request, the EDTF has produced a second progress report in September 2014 on the level and quality of the implementation of the recommendations in their October 2012 report, based on a survey of major banks' 2013 annual reports.⁸⁶ The survey results confirm that significant progress has been made towards implementing the EDTF recommendations in 2013 disclosures. The banks' self-assessment is that they have disclosed 73% of the information set out in the EDTF Recommendations, a substantial increase from 2012, with particular improvement in quantitative disclosures, where the implementation rate increased from 40% to 70% on an aggregate basis.

As in the 2013 survey, investors and analysts (the so-called 'User Group') within the EDTF undertook a further review of the disclosures. This assessment confirmed that banks have made substantial progress in implementing the EDTF recommendations over the past year, although there is still a gap between the users' assessment and the banks' own self-assessment. The User Group assessed 50% of the recommendations reviewed as being fully implemented and 29% partly implemented. They also noted that levels of implementation were highest in countries where regulators have been most active in promoting adoption.

The EDTF noted the proposed changes to the Basel Committee's Pillar 3 and the implementation of the new IASB and FASB financial instrument standards as steps that will lead to further changes in disclosures, and suggested that a review and updating of the EDTF recommendations may be necessary in the future. The EDTF is an important driver for continuing improvement in risk disclosures, and the FSB has asked the EDTF to undertake another survey in 2015, of the level and quality of disclosures in 2014 annual reports.

8. Building and implementing macroprudential frameworks and tools

A number of FSB jurisdictions (Brazil, China, EU, France, Germany, India, Mexico, Turkey, UK, US) have established committees that have explicit mandates for assessing systemic risk and maintaining financial stability/macroprudential oversight. For example, China established the Joint Ministerial Conference on Financial Regulatory Coordination in August 2013 upon the approval of the State Council, which will serve as the macroprudential authority. The

⁸⁶ See http://www.financialstabilityboard.org/wp-content/uploads/r_140930a.pdf.

formal inaugural session of the French macroprudential authority was held in June 2014. In the EU, most member states have already established their competent national authorities.

Most jurisdictions have also strengthened their monitoring mechanisms, including the powers to gather information from financial institutions, and have been using a wide range of prudential tools in pursuit of financial stability during the past year. These included *inter alia* loan-to-value limits, higher risk weights and loan loss provisions for specific sectors, differentiated reserve requirements, dynamic provisioning, leverage ratios, countercyclical capital and systemic risk buffers, SIFI capital surcharges.⁸⁷ Some jurisdictions also report improvements in cooperation and information sharing across authorities over the past year.⁸⁸

Given these developments, the majority of FSB jurisdictions report that they are at an advanced stage of implementation of these reforms. However, as recent FSB country peer reviews and work by other international bodies makes clear, macroprudential frameworks differ substantially in terms of structure and they continue to evolve, such as via the creation of inter-agency financial stability committees (FSCs). For example, the FSB peer reviews of Germany and the Netherlands, which examined the institutional arrangements for systemic oversight in those jurisdictions, included the following main findings on FSCs:

- **Germany** – The October 2012 Financial Stability Act delineates statutory responsibilities for financial stability in Germany; establishes an FSC and mandates the Bundesbank to provide it with substantial analytical support; specifies arrangements for cooperation and information exchange between the Bundesbank and BaFin; and provides for backstop powers to collect additional information from financial institutions. The authorities emphasise that the FSC has played an instrumental role in strengthening cooperation and formalising information sharing arrangements between its member agencies. The peer review notes that the framework underpinning the FSC will need to be clarified and fine-tuned as processes crystallise and as more experience is gathered, and that the FSC will need to develop a macroprudential strategy that is comprehensive and addresses aspects of the FSC's institutional design that remain unclear. These include, for example, a communication strategy; the conditions for triggering warnings and recommendations; and the approach to assessing the impact of policy actions. The peer review also recommended that the FSC should develop a comprehensive macroprudential toolkit on an *ex ante* basis to ensure timely application of relevant tools if the need arises.⁸⁹
- **Netherlands** – Under the amended Banking Act, the central bank has explicit responsibility for financial stability and has formulated a comprehensive risk assessment and decision making process for operationalising macroprudential policy. In addition, an FSC was created in November 2012 via a Ministerial Decree as a

⁸⁷ For example, Switzerland increased the countercyclical capital buffer to 2% of risk weighted assets for residential mortgages in June 2014; Turkey applied loan-to-value limits for car loans and maturity limits on consumer loans; and Russia increased risk weights and loan loss provisioning rates for unsecured consumer loans.

⁸⁸ These included, for example, China, EU (adoption of CRD IV/CRR provides for stronger information gateways between national supervisors and central banks in EU member states), Indonesia (MoU between BI and OJK), Mexico (enhanced powers to share information under recent reform), and UK (changes to Bank of England's organisational structure).

⁸⁹ See http://www.financialstabilityboard.org/publications/r_140409.pdf.

forum to identify and discuss potential risks and ways to mitigate them, including by making recommendations with respect to those risks. The peer review found that cooperation and information exchange has been strengthened via the creation of the FSC. The authorities emphasise that the FSC has played a useful role as a forum for discussing cross-sectoral issues and key risks to the financial system, and that it has given impetus to some joint project work. The peer review noted that ongoing efforts to analyse and address housing market vulnerabilities will be an instructive test of the FSC's effectiveness and level of ambition. It recommended further clarifying the role of the FSC within the macroprudential framework, including by specifying and publicly setting out the nature of its involvement in systemic risk assessment and macroprudential policy. It also recommended that the authorities should consider embedding the FSC's role and institutional standing in primary legislation to improve its effectiveness and enhance its credibility; and strengthening accountability for FSC recommendations via the establishment of a formal 'comply or explain' mechanism.⁹⁰

Work on macroprudential policy frameworks/tools and their interaction with other sets of policies is also ongoing at the international level. In particular, the IMF has published a number of working papers and policy notes on this topic over the past few years.

9. Strengthening adherence to international financial standards

The FSB, through the Standing Committee on Standards Implementation, coordinates and oversees implementation monitoring under the Coordination Framework for Implementation Monitoring (CFIM).⁹¹ This includes reporting on members' commitments and progress in implementing international financial standards and other policy initiatives; conducting peer reviews of FSB members (which are an obligation of membership); and encouraging global adherence to prudential regulatory and supervisory standards.

The CFIM distinguishes between priority and other reform areas in terms of the depth of information required for implementation monitoring to satisfy G20 reporting requirements.⁹² Monitoring of the Basel II/II.5/III framework, OTC derivatives market reforms and compensation practices is well underway, while a new process to monitor the implementation of the *Key Attributes* was initiated this year (see section 3). Starting in 2015, the FSB will begin detailed reporting on implementation progress of shadow banking reforms, drawing on monitoring and peer review work by relevant bodies.

In order to help focus G20 discussions on progress and challenges in implementing reforms, the FSB has created an implementation monitoring dashboard. The dashboard presents: an overview of implementation progress for priority reform areas; a summary of key implementation issues and challenges requiring senior-level attention; and a colour-coded table indicating the status of implementation by jurisdiction and reform area. The focus of the

⁹⁰ See <http://www.financialstabilityboard.org/wp-content/uploads/Netherlands-peer-review-report.pdf>.

⁹¹ See http://www.financialstabilityboard.org/publications/r_111017.pdf.

⁹² The current list of priority areas agreed by the FSB comprises the Basel II/II.5/III framework; OTC derivatives market reforms; compensation practices; policy measures for G-SIFIs; resolution frameworks; and shadow banking.

dashboard at this stage of the reform process is on the timeliness of implementation and not on the extent to which implementation is consistent with the international standard or is effective in achieving the reform objectives. Future iterations of the dashboard will include further information on measuring and assessing the consistency and effects of reforms in line with the FSB's plans, commencing in 2015, to prepare a consolidated annual report on the implementation of reforms and their effects. The FSB will also undertake work to address other monitoring challenges, such as optimising the use of scarce monitoring resources. In this regard, the dashboard notes that it is important for national authorities to be adequately resourced for full and timely implementation of reforms as well as for supporting their effective monitoring.

The FSB's IMN is tasked with collecting information from national authorities and reporting on the implementation of financial reforms in areas not designated as priority areas under the CFIM. The IMN also serves as the FSB's information collection "hub" and portal on overall national progress in implementing the G20/FSB recommendations on financial regulatory reform.⁹³ Over the course of the past year, the IMN has further streamlined the information collection process on non-priority areas to provide more clarity and ensure greater consistency.⁹⁴ In addition, to improve implementation dissemination efforts, the IMN has created a query function on the FSB website to enable the public to quickly extract information by selecting a combination of the following three filters: (i) year of reporting; (ii) area of reform; or (iii) jurisdiction.

In addition to periodic progress reports, the FSB monitors the implementation and effectiveness of international financial standards and policies via its peer review programme. Peer reviews are an important institutional mechanism to promote complete and consistent implementation and are a means of fostering a race to the top by FSB member jurisdictions. They provide an opportunity for FSB members to engage in dialogue with their peers and to share lessons and experiences. Over the past year, the FSB has completed the thematic peer review on reducing reliance on CRA ratings (see section 6.3) and has launched peer reviews on: the supervisory frameworks and approaches to SIFIs, focusing in particular on G-SIBs; reporting of OTC derivatives transactions to trade repositories; and resolution frameworks. These three peer reviews will be completed and the final reports published by the time of the next G20 Summit. The FSB has also completed the country peer reviews of Germany, Indonesia and the Netherlands. Four more peer reviews – China, Russia, Saudi Arabia and Turkey – are underway and will be completed by mid-2015. All completed peer review reports are available on the FSB website.⁹⁵

FSB members' adherence to international standards is essential to reinforce the credibility of the FSB's efforts to strengthen adherence by all countries and jurisdictions. To lead by example, member jurisdictions have agreed to publish information on the commitments they

⁹³ See http://www.financialstabilityboard.org/activities/implementation_monitoring/index.htm.

⁹⁴ See http://www.financialstabilityboard.org/implementation_monitoring/other-query.htm. The information on implementation progress in non-priority areas is based on self-reporting by FSB jurisdictions. The IMN has not undertaken an evaluation of those responses to verify the status or assess the effectiveness of implementation. As a result, the responses and the cross-country comparative tables do not allow straightforward comparisons between jurisdictions.

⁹⁵ See <http://www.financialstabilityboard.org/publications/peer-review-reports/>.

made under the *FSB Framework for Strengthening Adherence to International Standards*.⁹⁶ These commitments include undergoing an assessment under the Financial Sector Assessment Program (FSAP) every five years and disclosing their degree of adherence to international standards, and undergoing periodic FSB peer reviews. South Africa, which is the only FSB jurisdiction with an FSAP older than five years – presently interpreted as completed in 2009 – is undergoing an FSAP Update assessment, while several other FSB jurisdictions are also undergoing such assessments. Almost all FSB jurisdictions that completed their FSAP and sectoral compliance assessments have already published the results.⁹⁷ In terms of country peer reviews, the schedule of all remaining country reviews is now finalised, and the first round of these reviews is expected to be completed by end-2017.

In March 2010, the FSB launched an initiative to encourage the adherence of all jurisdictions to regulatory and supervisory standards on international cooperation and information exchange. The FSB published in December 2013 the third Status Update on progress made by this initiative. The report showed that since the publication of the previous update in November 2012 an additional jurisdiction – India – had demonstrated sufficiently strong adherence to the relevant regulatory and supervisory standards in the areas of banking supervision, insurance supervision and securities regulation, thus taking the total number of adherent jurisdictions to 45 out of a total of 61 in the FSB’s evaluation pool. Of the two jurisdictions that were listed as “non-cooperative jurisdictions” in the first Public Statement in November 2011, Venezuela continues to remain in that category while Libya is still temporarily suspended from the evaluation process.⁹⁸ The remaining jurisdictions in the evaluation pool are yet to demonstrate sufficiently strong adherence to the relevant standards, and therefore remain under the FSB’s evaluation.

The FSB has updated the ranking of financial importance used in 2010 to select a priority pool of about 60 jurisdictions that would be evaluated as part of this initiative, with a view to select additional jurisdictions for evaluation starting in 2015. The FSB expects to publish in the next Status Update in December 2014 the results of this work, together with additional information on the progress of this initiative.

10. Other issues

10.1 Assessing structural banking reform initiatives

Responding to a call from the G20, the FSB, in collaboration with the IMF and the OECD, published a report in October 2014 on cross-border consistencies and global financial stability implications of structural banking reforms.⁹⁹

⁹⁶ See http://www.financialstabilityboard.org/leading_by_example/index.htm.

⁹⁷ Turkey is the only FSB member that has not published the assessments from its 2011 FSAP, while Argentina has not published its 2013 FSAP report.

⁹⁸ On 19 June 2014, the FSB issued a notice advising financial institutions to be aware that Venezuela had been determined by the FSB to be a non-cooperative jurisdiction and therefore to exercise appropriate caution in conducting business in Venezuela or with financial institutions supervised by the Venezuelan authorities. See http://www.financialstabilityboard.org/wp-content/uploads/pr_140616.pdf.

⁹⁹ See http://www.financialstabilityboard.org/wp-content/uploads/r_141027.pdf.

Such reforms have recently been implemented or proposed in a number of jurisdictions (which account for a material share of global banking assets). The most far-reaching reforms are in jurisdictions that are home to G-SIBs, as well as host to substantial operations of G-SIBs. The recent financial crisis highlighted concerns around the complexity and resilience of banking group structures. A broad aim of many structural banking reforms is therefore to introduce a separation between certain ‘core’ banking activities – such as payments and retail deposit-taking – and the risks emanating from investment banking and capital market activities. The reforms are designed to reduce risks to banking groups stemming from trading activities and simplify legal and operational structures of complex banking groups, in order to enhance their supervisability and resolvability with a view to reducing systemic risk, enhancing depositor protection and limiting fiscal exposures. The reforms have mostly taken the form either of functional separation of types of financial activities through outright prohibitions, ‘ring-fencing’ or subsidiarisation; or of geographical separation via local subsidiarisation requirements for domestic operations of foreign banks.

Jurisdictions implementing structural banking reforms emphasise that the reforms support the international reform agenda and promote global financial stability by reducing systemic risks as well as the implicit government guarantee to TBTF institutions, resulting in more efficient market pricing of risk and more efficient allocation of capital.

Authorities in other jurisdictions generally support the overall objectives of the structural banking reforms, as being consistent with the shared goal of ending TBTF. At the same time, such authorities have also identified a number of potential negative cross-border implications, including possible impacts on the efficiency of cross-border groups and complications to their crisis management and resolvability, decreased liquidity of financial markets, regulatory arbitrage and leakage to the shadow banking system. To date they have not observed instances where structural banking reforms being implemented elsewhere have had a material adverse impact on their domestic financial systems. They also note, however, that in many cases the details of reforms are yet to be fully specified or put into effect.

As implementation of structural banking reforms progresses, the FSB, in collaboration with the IMF and OECD, will provide an update of this assessment, expanding the analysis with data where available, to G20 Ministers and Governors in 2016, as part of the FSB’s ongoing work to monitor the implementation and impact of post-crisis reforms.

10.2 Promoting long-term investment finance

Over the past two years, the FSB undertook a series of surveys and studies into regulatory reforms that may affect the provision of long-term investment finance. The FSB’s monitoring continues to find little tangible evidence or data to suggest that global financial regulatory reforms have had adverse consequences on the provision of long-term finance. The reforms are intended to be proportionate to risks and to support financial stability. They are not designed to encourage or discourage particular types of finance.

The FSB’s 2014 report¹⁰⁰ to the G20 Ministers and Governors draws on: i) a survey of FSB members to collect inputs on any specific regulatory reform areas that may have had material

¹⁰⁰ See http://www.financialstabilityboard.org/wp-content/uploads/r_140916.pdf.

unintended consequences on the provision of long-term finance; ii) engagement with practitioners in long-term finance from the private sector to understand and assess whether and how regulatory reforms are affecting the provision of long-term finance for investment; iii) consultation with FSB RCGs on the potential impact of financial regulation on long-term investment; and iv) work by the FSB Secretariat together with the staff of the IMF, World Bank and OECD to develop a set of key quantitative indicators that summarise the main developments in the provision of long-term finance across different types and regions.

As the FSB noted in its initial report in February 2013, the most important contribution of financial regulatory reforms to long-term investment finance is to promote a safer, sounder and therefore more resilient financial system. If implemented in timely and consistent manner, these reforms will help rebuild confidence in the global financial system and reduce procyclicality, which will enhance the system's ability to intermediate financial flows through the cycle and for different investment horizons. For this reason, the G20 regulatory reform programme is supportive of long-term investment and economic growth.

With most regulatory reforms still at an early stage of implementation, it remains too early to fully assess their impact on the provision of long-term finance or changes in market behaviour in response to these reforms. Authorities and market participants both note that regulatory reforms need to be finalised and fully implemented in order to reduce uncertainty in the market and achieve the intended effects. The FSB's monitoring has also highlighted a shortage of consistent data on long-term investment finance for analysing the impact of regulatory reforms. This illustrates the potential merits of the project to develop standardised definitions for quantitative indicators of long-term investment finance, which could be collected in a comparable fashion across countries.

The FSB will continue to monitor impacts in order to identify potential financial regulatory impediments to the promotion of market-based financing, the development of new instruments to finance long-term investment,¹⁰¹ or the supply of long-term financing by domestic or foreign intermediaries. The impact of financial regulation on the provision of long-term finance for investment will be incorporated in the FSB's monitoring framework to ensure broad coverage and enable monitoring in this area to be an ongoing rather than a stand-alone exercise.

10.3 Effects of regulatory reforms on EMDEs

In response to the G20 Leaders' request in the Los Cabos Summit Declaration, the FSB, in collaboration with SSBs and international financial institutions (IFIs), has initiated monitoring, analysis and reporting on the effects of financial regulatory reforms on emerging market and developing economies (EMDEs). The first FSB report was published in September 2013, while the latest one was published in November 2014 and provides an update of monitoring developments since last year, drawing upon discussions in FSB work streams and in RCGs.¹⁰²

¹⁰¹ The IOSCO research note "Market-Based Long-Term Financing Solutions for SMEs and Infrastructure" (<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD452.pdf>), published in September 2014, examines recent innovative examples of capital market solutions in developed and emerging markets that have contributed to the financing of SMEs and infrastructure projects.

¹⁰² See <http://www.financialstabilityboard.org/wp-content/uploads/Monitoring-the-effects-of-reforms-on-EMDEs.pdf>.

The main findings from the FSB's monitoring over the past year are as follows:

- EMDEs continue to express strong support for the G20/FSB reform agenda to enhance the resilience of the global financial system. Those EMDEs that are members of the G20/FSB are in the process of adopting the reforms in accordance with their commitments and the agreed implementation timetable, while a number of other EMDEs report that they are also implementing some of these reforms.
- Findings on impacts continue to be predominantly of a qualitative nature, reflecting the still early stage of implementation and challenges in separating the effects of reforms from broader conjunctural macroeconomic and financial system developments. To date, EMDEs have not reported major unintended consequences in their economies from the implementation of internationally agreed reforms.
- The implementation of reforms is bringing about changes to the business models and structures of financial market participants. In this regard, a number of EMDEs have noted that the overall effects of reforms on global financial intermediation need to be monitored carefully since they could potentially hinder the ability of EMDEs to disperse risk efficiently. Other effects, such as potentially higher costs of credit, are often an expected outcome of reforms to restore more prudent business practices and provide more sustainable finance over the economic and financial cycle. The FSB will continue to monitor for any signs that the areas of reform about which concerns have been raised are having an unduly large effect on EMDEs.
- EMDEs express concerns about specific aspects of the G20/FSB reforms and about the impact of structural banking reform initiatives in some advanced economies. Some of these concerns have been taken up in relevant bodies and are being addressed in subsequent modifications and guidance on implementation. However, other concerns remain, notably regarding the suitability and spill-overs of OTC derivatives reforms in smaller markets, implementation challenges given capacity constraints, and the need for enhanced home-host coordination to resolve cross-border issues.
- Given their different starting points, EMDEs will need to continue to make appropriate use of the flexibility in international policy frameworks (e.g. using observation and phase-in periods, calibrating parameters, undertaking impact assessments, and applying national discretions and proportionality) and the technical assistance by IFIs and SSBs to develop strategies that enable them to implement the reforms in a way that is appropriate to their particular circumstances.
- Progress has been made by the FSB and the SSBs to introduce more inclusive policy development processes (particularly with non-members that may be affected by those reforms) and to expand implementation support through various means. Further steps can be taken, such as the creation of additional EMDE-specific guidance and identification of good practices to facilitate implementation, and stronger coordination among international bodies in the provision of technical assistance and capacity-building.
- The FSB, drawing on input from its members and RCGs, will continue to monitor and report on the effects of agreed regulatory reforms on EMDEs. The results of this monitoring will be incorporated in the consolidated annual report to the G20 on the

implementation of reforms and their effects, which the FSB will prepare starting in 2015. This will help to facilitate the mitigation of unintended consequences.

The FSB, drawing on input from its members and RCGs, will continue to monitor and report on the effects of agreed regulatory reforms on EMDEs. The results of this monitoring will be incorporated in the consolidated annual report to the G20 on the implementation of reforms and their effects, which the FSB will prepare starting in 2015. This will help to facilitate the mitigation of unintended consequences.

10.4 Strengthening deposit insurance

The majority of FSB jurisdictions indicate that their national deposit insurance system is broadly compliant with international standards such as the BCBS-International Association of Deposit Insurers (IADI) *Core Principles for Effective Deposit Insurance Systems*. In this regard and following a public consultation process, IADI is expected to issue by the end of 2014 revised *Core Principles*, which incorporate lessons from the financial crisis, significant developments in the regulatory landscape and policy development, and enhanced guidance by IADI to address recommendations from the FSB's 2012 thematic peer review on deposit insurance systems.

A number of FSB jurisdictions also report reforms to their deposit insurance system over the past year. For example, a new Deposit Guarantee Schemes Directive in the EU entered into force in July 2014 and will now be transposed by member states. Hong Kong revised its guidelines to make member banks under the Deposit Protection Scheme report depositor information more comprehensively and on a more timely basis, while the entry into force of legal amendments in Russia has expanded deposit insurance coverage for some classes of depositors and work is underway to introduce differentiated risk premiums. However, none of the jurisdictions identified in the 2012 FSB peer review on deposit insurance systems as not having an explicit system (China, Saudi Arabia, South Africa) have established one thus far.

10.5 Enhancing consumer finance protection

In the G20 meeting at Cannes in November 2011, the Leaders agreed that integration of financial consumer protection policies into regulatory and supervisory frameworks contributes to strengthening financial stability and decided to pursue the full application of the G20/OECD High-Level Principles on Financial Consumer Protection (G20/OECD Principles) in their jurisdictions.

A number of FSB jurisdictions (Argentina, Australia, Brazil, Canada, China, France, Germany, Hong Kong, India, Indonesia, Italy, Japan, Mexico, Netherlands, Russia, Saudi Arabia, Singapore, UK and the USA) report that their existing framework for financial consumer protection are in line with the G20/OECD Principles. Other jurisdictions, including Korea, South Africa and Switzerland, are still in the process of implementing legislative/regulatory initiatives to enhance consumer protection in order to align their

frameworks more closely with the principles. Several jurisdictions within the EU are working to transpose European Directives, relating to the G20/OECD Principles, into national law.¹⁰³

A first update report on effective approaches to support the implementation of the G20/OECD Principles was published in September 2013, and it focused on the three priority principles of disclosure and transparency; responsible business conduct of financial services providers and their authorised agents; and complaints handling and redress. The OECD has submitted a report to the G20 Brisbane Summit on effective approaches to support the implementation of the remaining principles,¹⁰⁴ drawing on information gathered by the G20/OECD Task Force on Financial Consumer Protection.

11. FSB Regional Consultative Groups

The FSB established RCGs in 2011 for six regions: Americas, Asia, Commonwealth of Independent States, Europe, Middle East and North Africa, and Sub-Saharan Africa. These bring together ministries of finance, central banks and supervisory authorities in 65 FSB non-member jurisdictions and their counterparts in FSB jurisdictions. Collectively, the RCGs have held 35 meetings since their inception, of which 15 were held since the St Petersburg Summit, to discuss a range of financial stability issues.

Several RCGs have established working groups to study financial stability issues of interest to their region, with the RCGs presenting their analysis and findings to the FSB Plenary. Four reports prepared by RCG working groups were published on 22 August 2014 on the FSB's website; these covered, in the case of the RCG for the Americas, shadow banking, and the effects on host countries of balance-sheet consolidation and risk management practices by global banks; and, in the case of the RCG for Asia, shadow banking, and the impact of the SIFI framework on the Asian region and measures in response. In addition, several RCGs have held workshops to explore specific financial stability issues in greater depth, including resolution of financial institutions and long-term investment financing.

12. Review of the structure of representation in the FSB

At the St Petersburg Summit, the G20 Leaders supported the FSB's intention to review the structure of its representation and asked the FSB to report on this review to the Brisbane Summit.¹⁰⁵ The FSB is publishing on its website its report to the Brisbane Summit on the completed review, including the measures agreed by the FSB. The measures seek in particular

¹⁰³ The current EU financial consumer protection reforms cover a number of sectoral issues; some of the key priorities include the Mortgage Credit Directive; the Payments Account Directive; the updated rules for MiFID II; the Regulation on Packaged Retail and Insurance Based Investment Products (PRIPS); and the Insurance Mediation Directive.

¹⁰⁴ These are: legal, regulatory and supervisory framework; role of oversight bodies; equitable and fair treatment of consumers; protection of consumer assets against fraud and misuse; protection of consumer data and privacy and competition.

¹⁰⁵ See paragraph 64 of the St Petersburg G20 Leaders' Declaration (September 2013), available at https://www.g20.org/sites/default/files/g20_resources/library/Saint_Petersburg_Declaration_ENG_0.pdf

to strengthen the voice of EMDEs in the FSB while also preserving the effectiveness of its decision-making process. The agreed measures include:

- allocating to the five EMDE jurisdictions that currently have a single seat each in the Plenary – Argentina, Indonesia, Saudi Arabia, South Africa and Turkey – a second Plenary seat each. In order to keep the size of the Plenary at the current level of 70 seats, the five international organisations that currently have two Plenary seats each - BCBS, IAIS, IOSCO, the IMF and the World Bank - have agreed that their allocation be reduced to one Plenary seat each, with their second attendee being an observer.
- the FSB making greater use of the existing flexibility in the FSB's Charter to enable non-member authorities (either from or beyond the member jurisdictions) to be involved in the work of the FSB's Committees and working groups, either through membership of these bodies or attendance at individual meetings, to strengthen and broaden engagement in the work of the FSB and to widen the pool of expertise available, including that of EMDEs and securities market regulators;
- the FSB extending to the non-FSB member co-chairs of the RCGs a standing invitation to attend Plenary meetings, in order to better integrate the discussions at the six RCGs with the work of the FSB and enhance communication with the RCGs;
- the FSB continuing to seek to identify policy and implementation issues of most relevance to EMDEs and ensuring that they are addressed as part of the FSB's global work. The FSB will hold an Emerging Market Forum in early 2015 to identify and discuss issues of importance to EMDEs that the FSB should address.

The FSB will carry out future reviews of the structure of its representation at five-yearly intervals.

Annex: List of Abbreviations

| | |
|-------|----------------------------------------------------------------------------------------------------------------------|
| AIFMs | Alternative Investment Fund Managers Directive (EU) |
| BCBS | Basel Committee on Banking Supervision |
| BCR | Basic Capital Requirement (for G-SIIs) |
| BIS | Bank for International Settlements |
| CCP | Central counterparty |
| CET1 | Common Equity Tier 1 (capital adequacy ratio) |
| CFIM | Coordination Framework for Implementation Monitoring |
| CMG | Cross-border Crisis Management Group |
| COAG | Institution-specific cooperation agreement |
| CPMI | Committee on Payments and Market Infrastructures – previously the Committee on Payment and Settlement Systems (CPSS) |
| CRA | Credit rating agency |
| CRD | Capital Requirements Directive (EU) |
| DGI | Data Gaps Initiative |
| D-SIB | Domestic systemically important bank |
| EDTF | Enhanced Disclosures Task Force |
| EMDEs | Emerging markets and developing economies |
| EU | European Union |
| FASB | Financial Accounting Standards Board (US) |
| FMI | Financial market infrastructure |
| FSAP | Financial Sector Assessment Program |
| FSB | Financial Stability Board |
| FSC | Financial Stability Committee (Germany, Netherlands) |
| FX | Foreign exchange |
| GHOS | Group of Central Bank Governors and Heads of Supervision |
| GLEIF | Global LEI Foundation |
| G-SIB | Global systemically important bank |
| G-SII | Global systemically important insurer |
| HFT | High frequency trading |
| HLA | Higher loss absorbency |
| IADI | International Association of Deposit Insurers |
| IAIG | Internationally Active Insurance Group |
| IAIS | International Association of Insurance Supervisors |
| IASB | International Accounting Standards Board |
| ICS | Insurance Capital Standard (for IAIGs) |
| IFI | International Financial Institution |
| IFIAR | International Forum of Independent Audit Regulators |
| IMF | International Monetary Fund |
| IMN | Implementation Monitoring Network |
| IO | International organisation |
| IOSCO | International Organization of Securities Commissions |
| ISDA | International Swaps and Derivatives Association |
| LCR | Liquidity Coverage Ratio |
| LEI | Legal entity identifier |

| | |
|-------|----------------------------------------------------------------------------|
| LOU | Local Operating Units (LEI) |
| MiFID | Markets in Financial Instruments Directive (EU) |
| MMFs | Money market funds |
| MMoU | Multilateral Memorandum of Understanding |
| MPG | Market Participants Group |
| MRTs | Material risk-takers |
| NAV | Net asset value |
| NBNI | Non-bank non-insurance (G-SIFIs) |
| NTNI | Non-traditional/non-insurance (activities) |
| OECD | Organisation for Economic Cooperation and Development |
| OSSG | Official Sector Steering Group |
| OTC | Over-the-counter |
| P&S | FSB Principles & Implementation Standards for Sound Compensation Practices |
| QIS | Quantitative impact study |
| RCAP | Regulatory Consistency Assessment Programme (BCBS) |
| RCG | Regional Consultative Group (FSB) |
| ROC | Regulatory Oversight Committee (LEI) |
| RWAs | Risk-weighted assets |
| SEC | Securities and Exchange Commission (US) |
| SFTs | Securities financing transactions |
| SIB | Systemically important bank |
| SIFI | Systemically important financial institution |
| SSB | Standard-setting body |
| TBTF | Too-big-to-fail |
| TLAC | Total loss absorbing capacity |
| TR | Trade repository |
| UK | United Kingdom |
| US | United States |