

15 September 2003

Ongoing and Recent Work Relevant to Sound Financial Systems

Note by the FSF Secretariat (with inputs from various bodies) for the FSF Meeting on 10 September 2003

- I. Work Completed Since the Previous FSF Meeting
 - (i) Macroeconomic Management, Surveillance and Transparency
 - (ii) Market Infrastructure
 - (iii) Market Functioning
 - (iv) Prudential Regulations and Supervision

- II. Ongoing Work
 - (i) Macroeconomic Management, Surveillance and Transparency
 - (ii) Identifying Financial System Strengths and Weaknesses
 - (iii) Market Infrastructure
 - (iv) Market Functioning
 - (v) Prudential Regulations and Supervision
 - (vi) Combating Terrorist Financing
 - (vii) Offshore Financial Centres (OFCs)
 - (viii) Highly Leveraged Institutions (HLIs)
 - (ix) E-Finance

- III. Glossary of Agencies and Web Addresses

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I. Work Completed Since the Previous FSF Meeting

(i) Macroeconomic Management, Surveillance and Transparency

1. Financial Sector Assessment Program (FSAP): Review, Lessons, and Issues Going Forward

Agency: IMF

Completion Date: March 2003

Brief Description: The IMF reviewed the experience to date with the the Financial Sector Assessment Program (FSAP). The Board noted that the FSAP greatly increased the depth and breadth of coverage of financial sector issues, by both the IMF and the World Bank. The FSAP has been generally successful in providing a comprehensive and strategic framework to identify countries' financial sector vulnerabilities and strengths; strengthen the analyses of financial stability issues and development needs and priorities; and provide country authorities with appropriate policy recommendations. Notwithstanding these many achievements, however, the Board acknowledged that the program had become increasingly costly, and supported ongoing efforts by IMF and World Bank staffs to make it more efficient and effective through streamlining and prioritization. The next review of the FSAP should take place in 2005.

2. The Foreign Exchange Reserve Management Guidelines: Accompanying Document

Agency: IMF and World Bank

Completion Date: March 2003

Brief Description: Guidances for foreign exchange reserve management were completed in September 2001; they are available at www.imf.org and www.worldbank.org. Related technical assistance for capacity building is expanding. An Accompanying Document to the Guidelines which contains case studies of countries that have developed strong reserve management systems, has been prepared and is also available on the web.

(ii) Market Infrastructure

1. Role of Central Bank Money in Payment Systems

Agency: CPSS

Completion date: August 2003

Brief description: The CPSS published a report on the role of central bank money in payment systems which looks at the issue of competition and cooperation between central banks and commercial banks. Among the practical policy issues dealt with in the report are the following: first, which institutions may have accounts at the central bank; second, the range of services provided by central banks to meet the needs of account-holders; third, when central banks may insist on payment or securities settlement systems settling in central bank money and - when this is not practicable

- what sufficiently safe alternatives are adequate to mitigate credit and liquidity risks; and, fourth, what the possible benefits and risks of the concentration of payments through a few large banks, and how central banks might approach this issue.

2. Market Integrity for Combating Money Laundering

Agency: FATF

Completion Date: June 2003

Brief Description: On 20 June 2003, the FATF issued its *Forty Recommendations* to combat money laundering. The revision makes significant changes, which when combined with the Eight Special Recommendations, create a comprehensive, consistent and substantially strengthened international framework for combating money laundering and terrorist financing.

The major changes that have been adopted include:

- specifying a list of crimes that must underpin the money laundering offence;
- the expansion of the customer due diligence process for financial institutions;
- enhanced measures for higher risk customers and transactions, including correspondent banking and politically exposed persons;
- the extension of anti-money laundering measures to designated non-financial businesses and professions (casinos; real estate agents; dealers of precious metals/stones; accountants; lawyers, notaries and independent legal professions; trust and company service providers);
- the inclusion of key institutional measures, notably regarding international co-operation;
- the improvement of transparency requirements through adequate and timely information on the beneficial ownership of legal persons such as companies, or arrangements such as trusts;
- the extension of many anti-money laundering requirements to cover terrorist financing; and
- the prohibition of shell banks.

The revised Recommendations set a new standard, which FATF members will immediately start working to implement. The FATF encourages other countries and jurisdictions to do likewise. The FATF will also be moving promptly to assess members' compliance with this standard as part of its programme of work for FATF-XV (2003-2004). This will occur through a process of self-assessment, which is then to be followed by a further round of mutual evaluations which could start before the end of 2004.

(iii) Market Functioning

1. Operational Risk Transfer

Agency: Joint Forum (BCBS, IAIS, IOSCO)

Completion date: August 2003

Brief Description: This report, based on interviews carried out with 23 financial institutions in 12 jurisdictions, gives a broad picture of technical issues relating to operational risk transfer. It focuses mainly on risk management issues arising, for both protection buyer and protection seller, when transferring operational risk (extent and effectiveness of transfer, continuity of coverage, proper assessment of risk assumed by the protection seller etc.). But it also considers how insurance can affect capital requirements for both protection buyer and protection seller, leading to arbitrage opportunities. In addition, the report stresses the potential for risk concentration within a limited number of protection sellers.

2. Trends in Risk Integration and Aggregation

Agency: Joint Forum

Completion Date: August 2003

Brief Description: Based on a survey of 31 financial institutions across 12 jurisdictions, this report stresses greater emphasis across sectors on the management of risk on a firm-wide basis (risk integration) and related efforts to aggregate risks through mathematical models, i.e. economic capital methodology (risk aggregation). It also deals with recent trends towards consolidated supervision in many jurisdictions. The main conclusions of the report are that there is no unified model for risk integration, some firms relying more heavily on highly centralised risk management functions, whereas others (particularly in the insurance sector) prefer a decentralised structure. As regards risk aggregation, contacts with industry demonstrate that a large diversity exists in methodologies used to come up with a firm-wide measure of risks. Many institutions are sceptical about economic capital methodologies and even for firms adopting such methods there is little consistency in the way they aggregate risks across risk types and business entities, taking into account correlation effects.

3. Rating Agencies

Agency: CGFS

Completion date: May 2003

Brief description: The Study Group examined the evolving role of the rating industry in the global financial system with particular focus on product dynamics and possible implications for the structure and dynamics of financial markets. The group developed a proposal for a second, working group-stage of the project, which was discussed at the Committee's May 2003 meeting.

FINANCIAL STABILITY FORUM

4. Credit Risk Transfer: Study on the Insurance Sector

Agency: IAIS

Completion Date: April 2003

Brief Description: The IAIS analyses the issues associated with credit risk transfers with a particular focus on credit derivatives and the possible implications for financial stability. The key problems in this area appear to be less about structure differences in capital adequacy regimes generating regulatory arbitrage and more about problems of opacity about where credit risk has ended up. The IAIS issued a study paper on this topic, which was released on 7 April 2003, and contributes to the work subsequently undertaken by the Joint Forum of BCBS, IOSCO and IAIS.

5. Markets for Bank Subordinated Debt and Equity in G-10 Countries

Agency: BCBS

Completion Date: August 2003

Brief Description: The report consists of a Basel Committee's Research Task Force study of the nature of bank subordinated debt and equity markets in ten Basel Committee countries, and an assessment of the potential for market discipline in these countries. The main conclusions of the report are that the relative size of subordinated debt markets does not correspond to the attention that has been devoted to them: even if subordinated debt issuance is widespread, issuances are not so frequent because instruments generally have long-term maturity. As far as bank equities are concerned, the market has become deeper and more liquid over time. Nevertheless, the scope of the signals and thus potential market discipline is narrower in equity markets, where market activity is more focused on the largest banks, than in subordinated debt markets.

(iv) Prudential Regulations and Supervision

1. Third Quantitative Impact Study for the New Basel Capital Accord

Agency: BCBS

Completion Date: May 2003

Brief Description: The BCBS released two notes outlining the results of its Third Quantitative Impact Study ("QIS3") in May 2003. The study was conducted to assess the potential impact of the proposed New Basel Capital Accord on banks' minimum capital requirements. Over 350 banks in more than 40 countries participated. The results from QIS3 were consistent with the expectations set by the BCBS and suggest that the proposed New Basel Capital Accord will not raise the level of capital overall and will provide incentives for banks to adopt the more advanced risk management approaches for regulatory capital purposes. The study also helped the BCBS to identify a need to reduce some of the capital requirements associated with credit risk in the standardised approach and to offer a choice of modified operational risk requirements for some

banks. The latter would reduce the likelihood of high charges for some traditional banks.

2. Principles for the Management and Supervision of Interest Rate Risk

Agency: BCBS

Completion Date: September 2003

Brief Description: The BCBS has released for consultation a paper on principles for the management of interest rate risk, as part of its on-going efforts to address international bank supervisory issues. The paper is intended to apply to the management of interest rate risk whether in the trading book or reflected in the banks' trading activities. The paper looks at the interest rate risk management process, which includes the development of a business strategy, the assumption of assets and liabilities in banking and trading activities, as well as a system of internal controls. The paper updates previous work by the Committee on this subject and is being issued to support the Pillar 2 approach to interest rate risk in the banking book in the New Basel Capital Accord.

3. Cross-border Implementation of the New Basel Capital Accord

Agency: BCBS

Completion Date: August 2003

Brief Description: The BCBS has released for consultation a set of high-level Principles governing practical cooperation and effective information exchanges between home and host supervisors, and their communication with internationally-active banking groups, in implementing the forthcoming Basel Accord. The document, that is designed to reduce duplication of supervisory rules and retain a necessary degree of flexibility, sets out six basic Principles for practical supervisory cooperation.

4. Cross-border E-banking

Agency: BCBS

Completion date: July 2003

Brief Description: The Basel Committee released two papers titled *Risk Management Principles for Electronic Banking* and *Management and supervision of cross-border electronic banking activities*. The former is a slightly updated version of a consultative paper released in May 2001. It contains fourteen principles aimed at helping banking institutions expand their existing risk oversight policies and process to cover their e-banking activities. The latter is also an updated version of a document first released in October 2002. It has two main areas of focus. The first is to stress the need for banks to integrate their cross-border e-banking into their global risk management systems. The second discusses the role of home country supervisors for cross-border e-banking activities and lays

FINANCIAL STABILITY FORUM

the foundation for continued international cooperation between banking supervisors regarding such activities.

5. Consolidated KYC(“know-your-customer”) Risk Management

Agency: BCBS

Completion Date: August 2003

Brief Description: The Basel Committee on Banking Supervision issued a consultative paper that provides banks with practical guidance on managing their "know-your-customer" (KYC) risks on a consolidated basis. The paper addresses the need for banks to apply the four elements necessary for a sound KYC programme to both the parent bank or head office and all its branches and subsidiaries. These elements consist of customer acceptance policies, customer identification, on-going monitoring of higher risk accounts and risk management.

6. Transparency of Short Selling

Agency: IOSCO

Completion Date: June 2003

Brief Description: Following the report on transparency and market fragmentation (November 2001), IOSCO has published in June 2003 a Report of the Technical Committee which (1) summarises current rules and (2) assesses potential benefits of making short sales transparent and methods of achieving transparency.

7. Use of the Internet in Securities Related Activity

Agency: IOSCO

Completion Date: 2002-2003

Brief Description: IOSCO has hosted a series of roundtable discussions to consider the implications of the use of the Internet in securities related activities. Financial service regulators, consumer groups, financial service firms and relevant information services firms, such as Internet service providers, have been invited. The purpose of the Roundtables was to provide regulators and the industry with an opportunity to discuss existing and emerging practices and risks to consumers and firms and concerns of regulators that arise from the use of Internet-enabled technologies in the securities industry. The first and second Internet Roundtables were held in Hong Kong on 24-25 June 2002 and in Toronto on 25-26 November 2002. The European Roundtable took place in Amsterdam on 4-5 March 2003.

FINANCIAL STABILITY FORUM

8. Insider Trading

Agency: IOSCO

Completion date: May 2003

Brief Description: In May 2003, the Emerging Markets Committee finalized a Report entitled *Insider Trading - How Jurisdictions Regulate it*. The Report aims to survey the regulations prohibiting insider trading in the jurisdictions of IOSCO members and to define guidelines for the creation or amendment of such regulations.

9. Combating Money Laundering and the Financing of Terrorism

Agency: BCBS, IOSCO, IAIS through the Joint Forum

Completion date: June 2003

Brief Description: The BCBS, IAIS and IOSCO published a joint note: *Initiatives by the BCBS, IAIS and IOSCO to combat money laundering and the financing of terrorism* which provides a record of the initiatives taken by each sector to combat money laundering and the financing of terrorism (AML/CFT). The note provides an overview of the common AML/CFT standards that apply to all three sectors and an assessment as to whether there are serious gaps or inconsistencies in approaches and recommendations. It also covers, for each sector: the relationships between the institutions and their customers focussing on the products or services that are particularly vulnerable to money laundering; how each Committee has sought to address these vulnerabilities; and a description of ongoing and future work.

II. Ongoing Work

(i) Macroeconomic Management, Surveillance and Transparency

1. External Vulnerability Assessments

Agency: IMF

Target Date: Ongoing

Brief Description: In April 2003, the IMFC reiterated the importance it attaches to strengthening the IMF's crisis prevention capacity and to more robust assessments of crisis vulnerabilities, debt sustainability, currency mismatches and other balance sheet and capital account developments.

In July 2003, the Board reviewed the application of the IMF's framework for assessments of external and fiscal sustainability and endorsed some further methodological refinements to the framework. This framework adopted in June 2002 is being applied in the IMF's surveillance and program-related work on countries with significant market access. It introduces greater transparency and discipline to such assessments by clarifying the underlying assumptions and subjecting them to standardized stress tests. The IMF is also working to develop a framework for assessing debt sustainability in low-income countries, including those that have passed their completion points for permanent debt relief under the HIPC Initiative. This work is proceeding in close collaboration with the World Bank and other stakeholders. The IMF Board discussed these issues in July 2003 and will return to consider more concrete proposals later in the year.

Given the need for further work on vulnerabilities arising from public and private sectors' balance sheet structures, the Board discussed in July 2003 a paper on *The Balance Sheet Approach and its Applications at the Fund*. Building on this, a *Liquidity Management Framework* paper is expected to be discussed later in 2003; this paper will aim at integrating existing work on reserves adequacy and debt management.

2. Coordinated Portfolio Investment Survey (CPIS)

Agency: IMF

Target Date: Ongoing

Brief Description: The purpose of the CPIS is to significantly improve the coverage and accuracy of global statistics on cross-border portfolio investment assets and liabilities. It collects comprehensive information, with geographical detail on the country of residence of the issuer, on the stock of cross-border equities, long-term bonds and notes, and short-term debt instruments for use in the compilation or improvement of international investment position (IIP) statistics on portfolio investment capital. The survey was conducted for year-end 1997 and 2001, and is being conducted annually thereafter. Results are published on <http://www.imf.org>.

3. Transparency of IMF Policies and Assessments

Agency: IMF

Target Date: Fall 2003

Brief Description: In 2002 the IMF Board reviewed the experience of the IMF's policies to further enhance the transparency of its operations and the policies of its members. The Board agreed to encourage more systematic release of Article IV and Use of Fund Resources staff reports through continuation of the present policy of voluntary publication. The Board also agreed to move to the presumed publication of policy papers and associated Public Information Notices (PINs). In addition, the public can gain access to Board minutes after a lag of 10 years (compared to 20 years, previously). A progress report on transparency policy, and a statement by the Managing Director, were provided to the fall 2002 International Monetary and Financial Committee (IMFC) meeting, and similar updates went to the spring 2003 IMFC meeting. In June 2003, the IMF Board again reviewed progress under the Fund's continuing transparency and publication policies, and is considering further changes to publication policy. This review is expected to be concluded by end-September 2003.

(ii) Identifying Financial System Strengths and Weaknesses

1. Financial Sector Assessment Program

Agency: IMF and World Bank

Target Date: Ongoing

Brief Description: The Financial Sector Assessment Program (FSAP) provides a coherent and comprehensive framework for identifying financial system strengths, risks and vulnerabilities, assessing development needs and priorities, and helping to develop appropriate policy responses. The FSAP work provides the basis for the IMF's Financial Sector Stability Assessments (FSSAs) which are discussed by the IMF Executive Board within the context of a country's Article IV consultation. It also provides the basis for the World Bank staff's Financial Sector Assessments (FSAs), which are distributed to the World Bank Executive Board for information.

A significant part of the IMF/World Bank work on assessing OFCs and on anti-money laundering and combating terrorist financing is also undertaken under the FSAP. Since the 2003 IMF Board review of the program, AML/CFT issues are included in all FSAPs. The program has envisaged undertaking up to 18 country assessments each year. A total of about 100 countries and economies have undergone, are undergoing, or will soon participate in an FSAP.

FINANCIAL STABILITY FORUM

2. External Assessments of Implementation through Reports on the Observance of Standards and Codes (ROSCs)

Agency: IMF and World Bank

Target Date: Ongoing

Brief Description: Reports on the Observance of Standards and Codes (ROSCs) summarise the extent to which countries observe certain internationally recognized standards and codes. In November 2002, the Financial Action Task Force (FATF) 40 Recommendations on Anti-Money Laundering and 8 Special Recommendations on Terrorism Financing were added to the areas of standards and codes for which ROSCs are prepared, bringing the number of areas to twelve. A 12-month pilot project for anti-money laundering/combating the financing of terrorism (AML/CFT) assessments is underway.

The Executive Boards of the Fund and the Bank reviewed the international standards and codes initiative in March 2003, considering how to build on the initiative's success.

ROSCs are prepared and published at the request of the member country. The ROSCs and FSAPs can be accessed at <http://www.imf.org/external/standards/index.htm> and <http://www.worldbank.org/ifa>.

As of end-May 2003, 410 ROSC modules (for 91 economies) have been completed, of which 292 have been published (for 79 economies).

3. Financial Soundness Indicators

Agency: IMF

Target Date: 1st half 2004

Brief Description: This initiative is aimed at developing further the use of Financial Soundness Indicators (FSIs) to enhance monitoring of financial vulnerabilities. It includes the preparation of a *Compilation Guide on Financial Soundness Indicators (Guide)* to encourage the widespread use and production of FSIs in member countries. A draft *Guide* was posted on the IMF's external website for public comment in March 2003, and a comprehensive progress report was provided to the IMF Executive Board in June 2003. Once revised by IMF staff and reviewed by a group of country and international agency experts, as well as the IMF Executive Board, the *Guide* is expected to be finalized in the first half of 2004. Thereafter, the IMF intends to conduct a coordinated exercise among around 60 countries to support efforts to compile and disseminate FSIs.

Related work is ongoing in both the IMF and the World Bank to further develop and refine macro-prudential analysis and stress testing methodologies. Also, to promote more data availability, the IMF and BIS intend to conduct a conference of real estate prices in October 2003.

FINANCIAL STABILITY FORUM

4. Global Financial Stability Report

Agency: IMF

Target Date: Ongoing

Brief Description: The Global Financial Stability Report (GFSR), which, going forward, will be published semi-annually, assesses conditions and risks in global financial markets, including emerging market financing, from a financial market stability perspective.

The latest GFSR, published in March 2003, noted that the gradual improvement of financial conditions in mature markets had reduced the perception of risk and probably the risk itself to global financial stability. U.S. household balance sheets stabilized, corporate balance sheets strengthened somewhat, and financial institutions were showing signs of being less hesitant to take on risk. Easing global financial market conditions in the fourth quarter of 2002 led to a reopening of capital markets to many, but not all, emerging market issuers.

The GFSR highlighted that appropriate expansionary monetary policy in the major economies had contributed to a sizable buildup of cash positions by households and institutions, which could be redeployed into asset markets. The potential for a rebound in financial markets was, however, overshadowed at the time by uncertainty about the prospect of war in Iraq. The report also stressed that improvements in confidence required addressing deficiencies in corporate governance, investment banking practices, and accounting standards. Post-bubble developments had also revealed vulnerabilities in the insurance industry and in corporate defined-benefit pension plans. Encouraged by the steep yield curve, commercial banks and broker/dealers had accumulated considerable, largely unhedged carry trade positions of long-term bonds (including mortgage-backed securities) funded through short-term cash instruments. The report stressed that an unexpected rise in interest rates could spark a rapid unwinding of these positions, resulting in high market volatility. The “feast and famine” dynamics in emerging market financing and persistent credit tiering underscored the need to consistently implement sustainable policies. The GFSR also emphasized that larger local securities markets could eventually provide an alternative source of financing and act as a buffer against changing global financial conditions.

5. Foreign Direct Investment in the Financial Sector

Agency: CGFS

Target date: November 2003

Brief description: The Working Group explores issues related to foreign direct investment (FDI) primarily in the financial sectors of emerging market countries. The project seeks to identify the financial characteristics of foreign direct investment today, to compare them to those of other forms of financing, and to develop policy implications for the effective functioning of financial markets and for financial stability.

(iii) Market Infrastructure

1. Accounting

a) International Financial Reporting Standards

Agency: International Accounting Standards Board (IASB)

Target date: Ongoing

Brief Description: The Financial Accounting Standards Board (FASB) of the United States and the International Accounting Standards Board (IASB) issued a memorandum of understanding in October 2002, agreeing to work together towards convergence of global accounting standards. The IASB also held a meeting with national accounting standard-setters in November 2002 and will hold another meeting in September 2003.

Since 2001, the IASB has been working on completing a platform of standards to be ready for the adoption of IFRSs by companies throughout the world in 2005. The IASB's initial efforts have focused on improvements of existing International Accounting Standards (IASs), providing guidance to those companies adopting IFRSs for the first time, and issuing standards in the areas where current IASB literature is deficient (for example, business combinations and share-based payment). The IASB has pledged to finalise all of the standards to be mandatory for 2005 by 31 March 2004. As one of the projects, the improvements to existing IASs 32 (Financial Instruments: Disclosure and Presentation) and 39 (Financial Instruments: Recognition and Measurement) are expected to complete by Q4 2003, with a potential amendment to IAS 39 on macro-hedging to be finalised by Q1 2004. A number of public discussions for this project were held during March 2003.

The BCBS, IAIS and IOSCO evaluate International Accounting Standards (IASs) developed by the International Accounting Standards Board (IASB) in order to provide supervisory input in the development of existing and new standards in areas of supervisory interest.

b) Banking

Agency: BCBS

Target Date: Ongoing

Brief Description: The BCBS Accounting Task Force is close to finalising a consultative document which is a new and expanded version of the BCBS paper *Sound Practices for Loan Accounting and Disclosure*.

c) Securities

Agency: IOSCO

Target Date: Ongoing

Brief Description: The Technical committee is currently conducting a survey on the accounting review and enforcement mechanisms currently in place in IOSCO member jurisdictions.

2. Auditing Standards

Agency: IFAC

Target date: Ongoing

Brief Description: The International Auditing and Assurance Standards Board (IAASB) of IFAC has published its action plan for 2003 and 2004 (available at www.ifac.org). Its priorities include completion of the audit risk project, updated standards on fraud and the form and content of the auditor's report, developing quality control standards for both audit firms and audit engagements and new standards on group audits and reviews of interim financial information.

To achieve convergence of auditing standards on a worldwide basis, the IAASB is working closely with IFAC member bodies on joint projects and seeking the input of experienced standard setters, international and national regulators, and regional accountancy organizations.

The BCBS, IAIS and IOSCO also evaluate International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Board (IAASB) in order to provide supervisory input.

3. Accountancy Profession

Agency: IFAC

Target date: Ongoing

Brief Description: IFAC is working on achieving lasting reforms that increase confidence in accountants and the credibility of financial information. IFAC standard setting committees – auditing, ethics, education and public sector accounting – consider the views of those affected by their standards and guidance. Increased confidence is possible only if the profession can demonstrate its accountability. IFAC encourages accountability in several ways: through its Code of Ethics, Compliance Program and the Transnational Auditors Committee.

IFAC leadership is working with international regulatory organizations on the creation of a Public Interest Oversight Board to oversee the public interest activities of IFAC.

4. Principles of Corporate Governance

Agency: OECD and World Bank

Target date: Ongoing

Brief Description: In response to the May 2002 mandate by the OECD Ministers for assessments of developments in OECD countries on governance in the corporate and financial sectors, the OECD Steering Group on Corporate Governance has undertaken its assessment with a view to completing it by April/May 2004.

The World Bank and OECD are organising regular Regional Corporate Governance Roundtables across the world, and a multi-donor Global

Corporate Governance Forum has been established for dialogue and support in capacity building. Following the first White Paper on Corporate Governance in Russia released in April 2002, the Asian White Paper was completed in June 2003. Similar White Papers will soon be issued for Latin-America and Southeast Europe. On the basis of these White Papers, the Regional Corporate Governance Roundtables in 2003 and 2004 will focus their work on policy-design, implementation and enforcement.

Concerning financial governance, the OECD endorsed new guidelines on governance of pension funds in October 2002 and, in co-operation with the IAIS, is currently working on guidelines on governance of insurance companies.

5. Principles and Guidelines for Effective Insolvency and Creditor Rights Systems

Agency: World Bank

Target Date: Q4 2003

Brief Description: In April 2001, the World Bank Board approved a first set of Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, for use in ROSC assessments. The Principles, now under review, are expected to be released later this year in a final form, taking into account further feedback and lessons from insolvency assessments conducted under the ROSC initiative, is expected in 2003 (see www.worldbank.org/firm).

The Bank is also working on a paper discussing comparative practices and developmental experience in areas covered by the Principles, and is collaborating with other organisations to develop a survey of practices to strengthen institutional capacity and regulatory frameworks.

A Global Insolvency Law Database (GILD) has been developed as a companion piece to the initiative (www.worldbank.org/gild). Building upon the work done by other international institutions (including the World Bank, IMF and the Asian Development Bank), UNCITRAL is currently preparing a legislative guide for commercial insolvency law. The World Bank is working with UNCITRAL to ensure consistency between the Principles and the guide.

6. Bank Insolvency Initiative

Agency: World Bank and IMF

Target Date: End 2003

Brief Description: The project, closely related to the work on effective insolvency described above, seeks to identify an appropriate legal, institutional and regulatory framework to deal with bank insolvency (the Framework), including in the context of systemic crisis and to develop the international consensus regarding that framework. Significant attention is devoted to participation of the highest possible number of countries. The initiative is being coordinated with other international efforts in related areas .

FINANCIAL STABILITY FORUM

A number of global and regional seminars, as well as a series of consultation meetings with supervisory/legal authorities in different areas of the world, have been conducted or will take place in the next 12 months. A Core Consultative Group with participation of 17 systemically important countries and the international agencies participating in the Initiative has been actively cooperating in the preparation of the Main Document under the Initiative. The Main Document will be presented to the Executive Boards of the World Bank and the IMF before the end of 2003. It is expected that the document and its supporting and complementary papers will serve as benchmarks for the conduction of voluntary country evaluation of their Framework. A small number of pilot country evaluations will start shortly after Board consideration of the Main Document.

7. Forum for Asian Insolvency Reform

Agency: OECD

Target Date: Ongoing

Brief Description: Organised by the OECD, and sponsored by AusAID and the ADB, in partnership with the World Bank Group and Government of Japan, the 2nd Forum for Asian Insolvency Reform took place in Bangkok, Thailand, in December 2002. 120 participants from 20 countries met to discuss informal workouts and cross-border insolvency. Based on conference proceedings, an article appeared in the February 2003 edition of the International Financial Law Review, detailing priority steps for reform in the region. These steps include: (i) putting in place credible liquidation procedures and efficient secured-transaction processes; (ii) moving from balance-sheet to cash-flow tests for insolvency; (iii) providing for independent review by qualified experts of the debtor's business, its prospects and options for restructuring; (iv) requiring that restructuring "fix the business;" (v) reforming lending practices; and (vi) instituting corporate governance practices that help prevent bankruptcy. The third meeting of the Forum is scheduled to be held in Seoul on 10-11 November 2003. The meeting will inter alia focus on the performance of regional asset management companies and experience in bulk sales of non-performing loans.

8. Legal and Institutional Underpinnings of Global Financial Markets

Agency: G-10

Target Date: Ongoing

Brief Description: This project collected and analysed comparative information on the bank resolution procedures, contract enforceability and insolvency arrangements in the principal international financial jurisdictions. A report, *Insolvency Arrangements and Contract Enforceability*, was released as a consultative document in December 2002 (available at www.bis.org/publ/gten06.htm). A symposium on these issues will take place at the ECB on 30 September and 01 October 2003 (Insolvency Symposium 2003). The focus is on current legal, economic and

FINANCIAL STABILITY FORUM

supervisory issues in cross-border insolvencies of larger financial institutions.

9. Model Contractual Clauses

Agency: G-10
Target Date: Ongoing
Brief Description: Monitoring of draft model contractual clauses in sovereign bonds that will facilitate communication and promote orderly and predictable debt restructuring. The work is taking place in close collaboration with market participants. The G10 had earlier released work by legal experts to ensure collective action clauses' compatibility in major jurisdictions.

10. Code of Good Conduct (COGC)

Agency: G-10
Target Date: Ongoing
Brief Description: The G-10 is currently collecting information that might facilitate the process of establishing a COGC (the information is stored under <https://e.bis.org>; to access contact g10@bis.org). The aim of the COGC might be to strengthen policy principles and to develop operational principles and to help (sovereign) debtors and creditors in a more timely, orderly and predictable resolution of a financial debt crisis. The contours of such a COGC are being debated by the private and official sector.

11. Enhancing Information Exchange among Securities Regulators

Agency: IOSCO
Target Date: Ongoing
Brief description: Following the event of Sept. 11th, a special Project Team on Cooperation worked on the development of a draft multilateral MOU (Memorandum of Understanding) that would enhance information exchange among the signatory securities regulators and facilitate financial crime investigation. The President's Committee of the Organization endorsed the IOSCO MOU during its May 2002 annual meeting. The MOU builds on the many previously existing IOSCO Resolutions and Principles to establish an international benchmark for cooperation and information sharing. Prior to signing the IOSCO MOU, member regulators must establish through a fair and transparent process that they have the legal capacity to fulfil its terms and conditions. The process adopted for the implementation of the MOU provides incentives for members that do not have the legal capacity to sign the MOU to raise their respective national standards. IOSCO is committed to assisting them in this process and a framework for assistance is being developed. As a follow up to the endorsement of the MOU, a screening group was set up. This group prepared an operational procedure to review the applications sent by

FINANCIAL STABILITY FORUM

members. The MOU signatory process was officially opened in August 2002.

12. Oversight of Payment and Settlement Systems

Agency: CPSS
Target date: Summer 2005
Brief description: The CPSS will map and compare the objectives central banks have for their oversight work and the methodologies they use to achieve these objectives. The analysis will be carried out from both a national and an international perspective.

13. Developments in Large-value Payment Systems

Agency: CPSS
Target date: Summer 2005
Brief description: The CPSS will analyse recent developments in large-value payment systems including the introduction of new settlement algorithms designed to save liquidity in systems that provide intraday finality and the emergence of offshore payment systems. In addition to liquidity and other benefits, the risks and costs that arise from these new systems will be considered.

14. Risk Management Standards for Central Counterparties

Agency: CPSS-IOSCO Task Force
Target Date: end-2004
Brief Description: The CPSS-IOSCO Task Force intends to develop standards for CCP (Central Counterparty) risk management. This initiative reflects the growing interest in developing CCPs and expanding the scope of their services as well as the lack of clear international standards in this area.

15. Crisis Resolution

Agency: IMF
Target Date: Ongoing
Brief Description: The Spring 2003 IMFC meeting, while recognizing that it is not feasible now to move forward to establish the Sovereign Debt Restructuring Mechanism, urged the Fund to continue work on issues that are of general relevance to the orderly resolution of financial crises. In response, the Fund's current efforts on crisis resolution are focused on improving the process of restructuring sovereign debt within the existing legal framework. This includes promoting the inclusion of collective action clauses (CACs) in international sovereign bonds in jurisdictions where they are not yet the market standard, and contributing to initiatives aimed at formulating a voluntary code of conduct for sovereign debtors and their creditors.

FINANCIAL STABILITY FORUM

In addition, the Fund has clarified the conditions under which it is willing to extend support in the context of a crisis for a member's adjustment program and the scale of such support (February 26, 2003), along with adopting a more comprehensive framework for making judgments on debt sustainability. The Executive Board has also reviewed recently the application of the criterion concerning good-faith negotiations between sovereign debtor and its creditors in the context of the Fund's lending into arrears policy (September 4, 2002). Staff have also examined the usefulness of a balance sheet approach to crisis resolution.

(iv) Market Functioning

1. Credit Risk Transfer

a) Supervisory perspective

Agency: Joint Forum

Target Date: March 2004

Brief Description: The objective of the work will be to take stock of supervisory knowledge about institutional participation in the CRT market and to make an assessment of how supervisors can obtain further information about CRT activity. This will also involve a review of how different financial institutions book CRT transactions (in particular credit derivatives and CDOs) and how they manage the associated risks. The output of the group's work will be a report dealing with key issues such as: the principal participants involved in the CRT market and their respective roles; the scale and scope of activities in this market; the main risks incurred by these participants and the way they are managed; how typical transactions are structured and used; disclosure of the risks associated with CRT transactions; and supervisory rules and reporting requirements associated with CRT transactions.

b) Reporting on Credit Default Swaps in the Semi-annual Central Bank Survey on OTC derivatives

Agency: CGFS

Target date: Ongoing

Brief description: Following up on the report on *Credit Risk Transfer*, the CGFS Working Group on credit risk transfer has begun a process with the objective to incorporate reporting on credit default swaps in the semi-annual Central Bank survey of OTC derivatives published by the BIS.

2. Rating Agencies

a) Regulatory perspective

Agency: IOSCO

Target Date: 2003

FINANCIAL STABILITY FORUM

Brief Description: In February 2003 IOSCO Technical Committee decided to assess and analyse issues related to rating agencies, and to look in particular at regulation, functioning, transparency and potential conflicts of interest. The Committee of Chairs has been commissioned to develop guidelines that state high-level objectives, for which rating agencies, regulators and issuers should strive in order to improve investor protection and the fairness, efficiency and transparency of the securities markets which rely on rating agencies opinions.

b) Ratings in structured finance

Agency: CGFS

Target date: End 2004

Brief description: A working group has been established with to explore the role of rating agencies in the rapidly evolving markets for structured finance instruments and the implied new requirements for the ratings process, the rating agencies and for participants in structured finance markets. The group will seek to develop an understanding of various methodological and organisational challenges involved in rating structured finance products.

3. Disclosure and Transparency of the Reinsurance Industry

Agency: IAIS

Target Date: 2003 or 2004

Brief Description: The IAIS is developing a framework to enhance the transparency of the global reinsurance market and will propose measures to improve risk-oriented disclosure by individual reinsurance firms.

4. Stock Repurchase Programs

Agency: IOSCO

Target Date: 2003

Brief Description: The objective of the project is to focus on the market impact of stock repurchase programs (SRPs). IOSCO is developing a descriptive analysis of the existing main SRPs mechanisms and is currently surveying the related regulatory provisions in the jurisdictions of members.

(v) Prudential Regulations and Supervision

1. Revision of the Basel Capital Accord

Agency: BCBS

Target Date: 2003

Brief Description: On 29 April 2003 the BCBS released the third consultative document for the New Basel Capital Accord. The New Accord, which will replace the 1988 Basel Accord, is intended to align more closely regulatory capital requirements with the underlying risks that banks face and to provide

incentives for banks to improve their management of risk. It establishes three pillars to achieve these goals, namely: (1) developing more risk-sensitive capital requirements for the treatment of credit and operational risk; (2) recognising the importance of supervisory review in evaluating the adequacy of banks' internal capital allocation processes; and (3) promoting effective market discipline through enhanced financial disclosure. The first, quantitative, pillar allows a choice between three principal methods of calculating credit and operational risk.

The third consultative document represents the near final draft of the proposed framework. Its content reflects both extensive consultation with the banking industry and other interested parties as well as the findings of the third quantitative impact study the BCBS conducted with the assistance of over 350 banks worldwide. Public comments to the BCBS were due on 31 July 2003 and, at the time of writing, the BCBS had received some responses. The BCBS is currently reviewing the public responses in order to determine what final clarifications or revisions of its proposals are necessary. It plans to issue the final text of the New Accord by the end of 2003 and its member countries have agreed on a common implementation date of end-2006.

Members of the BCBS intend to apply the New Accord on a consolidated basis to the internationally active banks in their jurisdictions and other significant banks as national supervisors deem appropriate. Many G-10 members intend to apply the New Accord to their entire banking system. Hence, the BCBS has deliberately sought to ensure that the Accord's provisions are suitable for a wide range of banks in different countries. However, the wording of the consultative proposal envisages some flexibility as to the timing of implementation in the non-G-10.

A number of BCBS member countries have issued national consultation documents as part of their domestic rule-making procedures. The comment timetable on these proposals is on a separate track from the BCBS documents.

Now that the process for revising the New Basel Accord is nearly complete, attention is shifting toward preparing for its implementation. In that regard, the BCBS has created the Accord Implementation Group ("AIG") to serve as a forum for sharing information on supervisors' experiences with the adoption and implementation of the New Accord. The AIG, whose membership mirrors that of the BCBS, is already engaging in dialogue with non-member supervisors through the BCBS's Core Principles Liaison Group (which contains senior representatives of fifteen non-G10 countries) and with the banking industry.

2. Policy Guidance for Banks' Compliance Functions

Agency: BCBS

Target Date: 2003

Brief description: The BCBS is developing policy guidance on banks' compliance functions, including their organisation of, management oversight over

and responsibility for the compliance function. A document for public consultation is expected in Autumn 2003.

3. Insurance Principles, Standards and Guidelines

Agency: IAIS

Target Date: Autumn 2003-Autumn 2004

Brief Description: a) Revised Insurance Core Principles:

A Task Force is working to revise the *Insurance Core Principles* and accompanying methodology taking into account comments of members (particularly arising as a result of their experience with the self-assessment exercise), the IMF and World Bank experience in conducting assessments, the Joint Forum work on comparing the Core Principles of the IAIS, IOSCO and the BCBS, and comments from relevant IAIS subcommittees. The revised Core Principles are to be submitted to the IAIS Annual Meeting in October 2003.

b) Insurance Supervisory Standards:

The IAIS is developing supervisory standards, guidelines, or issues paper on (1) insurance liabilities, (2) the use of actuaries, (3) control solvency levels, (4) stress testing, (5) insurance securitisation (6) disclosure of non-life insurers and reinsurers, (7) reinsurance companies, (8) investment risk management, (9) forms of capital, (10) disclosures concerning technical performance and risks for non-life insurers and reinsurers. The papers from (1) to (7) are planned to be adopted in October 2003. The papers (8) to (10) are intended to be adopted in autumn 2004.

The IAIS is developing insurance laws and regulation database. The database covers not only jurisdiction specific insurance regulatory and supervisory information but also comparative analyses of different insurance systems. The database will enhance mutual understanding of insurance supervisory systems among insurance supervisors and facilitate implementation of insurance supervisory standards. The database will also help exchanges of information among insurance regulators and supervisors.

4. Insurance Regional Seminars and Training

Agency: IAIS and FSI

Target date: Ongoing

Brief Description: IAIS and FSI organise in collaboration with national insurance supervisory authorities and other bodies around 15 regional seminars annually to assist insurance supervisors implement IAIS principles and standards.

FINANCIAL STABILITY FORUM

5. Core Curriculum for Insurance Supervisors

Agency: World Bank, IAIS, and FSI
Target date: Ongoing
Brief description: World Bank, IAIS, and FSI, in collaboration with insurance supervisory authorities, are developing the core training curriculum for insurance supervisors. The programme will cover development of implementation materials and various tools to deliver training programmes (case study, video presentation, web

6. Securities Analysts

Agency: IOSCO
Target Date: 2003
Brief Description: IOSCO is currently assessing the actual and perceived conflicts that confront analysts and the firms that employ them in light of the varying roles played by analysts and the manner in which analysts are employed in the jurisdictions of IOSCO members. Work is currently focused on the conflicts that confront analysts employed by brokerage and investment banking firms (so-called "sell-side" analysts), as a significant proportion of the inherent conflicts appear to involve this group of analysts. The Subcommittee of Chairs is developing high level principles related to potential conflicts of interest.

7. Principles for Regulation and Supervision of Private Pensions

Agency: OECD and International Network of Pensions Regulators and Supervisors (INPRS)
Target Date: Ongoing
Brief Description: Principles for regulation of occupational private pensions were endorsed by the OECD in December 2000 and the INPRS in April 2001 (see www.oecd.org and www.inprs.org). In May 2001, the OECD Ministers mandated the OECD to develop further principles. In October 2002, the OECD Working Party on Private Pensions endorsed a set of new guidelines for the governance of pension funds. The OECD is in the process of finalising guidelines on rights of beneficiaries. The OECD and INPRS are also finalizing a template for assessing the implementation of the OECD/INPRS Principles for the regulation of private pensions, to be used by the IMF and the World Bank in parallel with the FSAP exercise.

(vi) Combating Terrorist Financing

1. Implementation of the Plan of Action to Combat Terrorist Financing

Agency: FATF
Target Date: Ongoing

FINANCIAL STABILITY FORUM

Brief Description: (1) Since June 2002, an FATF Working Group has been established for, among other things, developing further guidance on the individual Special Recommendations. In October 2002, the FATF published a Best Practices Paper on preventing the misuse of non-profit organisations by terrorists (Special Recommendation VIII). The FATF has continued to take steps to counter the financing of terrorism in developing further guidance to implement the 8 Special Recommendations. At its February 2003 Plenary, the FATF issued an Interpretative Note to Special Recommendation VI to prevent informal transfer systems and funds from being misused by terrorists. It also issued an interpretative note on Special Recommendation VII which focuses on the abuse of wire transfers by terrorist and their financiers. At the June 2003 Plenary, FATF released a Best Practices Paper on alternative remittance systems (Special Recommendation VI).

(2) The FATF has also begun developing a process to identify weaknesses in the world-wide efforts to combat terrorist financing. During 2002 – 2003, FATF members have continued their efforts to implement the Eight Special Recommendations, and these changes have been reflected in the updated information contained in this year's annual report (available at <http://www.fatf-gafi.org>). In addition, there has been a collaborative effort between the FATF, the United Nations and other international organisations, to encourage all countries to implement the Special Recommendations. The Recommendations have now been endorsed by many non-FATF members and international organisations and bodies, and 130 jurisdictions are participating in the FATF self-assessment exercise. This will enable FATF to assist the IMF, World Bank, UN and other donors, including the recently-created Counter Terrorism Action Group, to prioritise their offers of technical assistance with respect to implementing the Eight Special Recommendations on Terrorist Financing.

2. Intensification of the IMF/World Bank's Contribution to Combating Terrorist Financing

Agency: IMF and World Bank

Target Date: Ongoing

Brief Description: The Executive Boards of the IMF and World Bank approved in November 2002 a 12-month pilot project that significantly enhances the institutions' contributions to the international efforts to combat money laundering and the financing of terrorism (AML/CFT) by adding the FATF 40 Recommendations on an effective AML framework, and the 8 Special Recommendations on Terrorism Financing to the list of areas and associated standards and codes that are incorporated into their operational work. AML/CFT assessments of the FATF 40+8 and accompanying ROSCs will now be undertaken by the Bank and Fund in all countries undertaking an FSAP assessment, and in the Fund's Offshore Financial Center Assessments.

A voluntary questionnaire on the anti-money laundering/countering terrorist financing policies and institutions is being circulated to countries in the context of Article IV discussions with full coverage of the

FINANCIAL STABILITY FORUM

membership expected by end-2004. The Fund and the Bank have also conducted a study of informal funds transfer systems, initially focused on the Hawala system.

The Fund and Bank are delivering AML/CFT technical assistance directly to individual countries. The Fund and Bank are also conducting numerous regional programs, seminars and workshops, including Global Policy Dialogues via video conference with more than 500 policy makers from 42 countries. Finally, the Bank in collaboration with the Fund published the first comprehensive Reference Guide to AML/CFT (client handbook).

3. Terrorism Insurance

Agency: OECD

Target Date: 2004

Brief Description: In May 2002, the OECD Ministers mandated the OECD to develop policy analysis and recommendations on how to define and cover terrorism risks and to assess the respective roles of the insurance industry, financial markets and governments, including for the coverage of "mega-terrorism" risks. To carry out the work, the OECD Insurance Committee has set up a special Task Force on Terrorism Insurance. The Task Force is expected to complete its work in 2004.

(vii) Offshore Financial Centres (OFCs)

1. Offshore Financial Centre Assessments (OFCA)

Agency: IMF

Target Date: Ongoing

Brief Description: The IMF has been assessing financial regulation and supervision in OFCs, focusing on assessments of banking supervision relative to the *Basel Core Principles* and of the anti-money laundering/countering terrorist financing regime based on the methodology endorsed by the FATF and the Fund's Board in October and November, 2002, respectively. The assessment program was accelerated in 2002 and some 22 jurisdictions (including FSAPs) were assessed. The Fund plans to assess a further 10 jurisdictions in 2003, and provide technical assistance to another two. This will virtually complete the current phase of the program. In August 2003 the IMF Board received a report on progress and staff's plans for the future direction of the program whose details will be discussed at a Board meeting at a future date to be determined.

2. Statistics on OFCs

Agency: IMF

Target Date: Ongoing

FINANCIAL STABILITY FORUM

Brief Description: The IMF is helping OFCs to improve their statistics, primarily by encouraging them to participate fully in international statistical collections such as the Co-ordinated Portfolio Investment Survey (CPIS), but also by helping them to improve their national macroeconomic statistics.

(viii) Highly Leveraged Institutions (HLIs)

1. Disclosure: Follow-up of the MWGED Recommendations

Agency: Joint Forum

Target Date: 2003

Brief Description: In 2002 the Joint Forum created a working group to follow up the recommendations contained in the April 2001 report of the Multidisciplinary Working Group on Enhanced Disclosure (MWGED). The working group began its work by surveying firm compliance with the specific recommendations by the MWGED. The group has met with relevant end users of financial reports to gain knowledge about their disclosure needs and with a number of firms including hedge funds to hear their views on the MWGED recommendations. The group expects to produce an interim report in 2003.

(ix) E-Finance

1. Implications for Developing Countries of Electronic Finance

Agency: World Bank

Target Date: Ongoing

Brief Description: In-depth work is being undertaken on specific applications of technology to delivery of financial services and on e-security.

2. E-Finance and Debt Management

Agency: OECD

Target Date: Ongoing

Brief Description: The OECD Working Party on Public Debt Management discusses on a regular basis the implications of information and communications technology on debt management practices. An interim report on this work is now available as chapters 4 and 5 in the OECD publication *Public Debt Management and Government Securities Markets in the 21st Century*.

3. Management of outsourced IT activities and electronic banking security issues

Agency: BCBS

Target date: Spring 2004

FINANCIAL STABILITY FORUM

Brief description: The Electronic Banking Group of the BCBS will carry out a stock-taking exercise to collect input from members on electronic security and IT outsourcing developments in their respective countries. The exercise is aimed at getting a better sense of the current landscape of IT outsourcing and cybersecurity. It will also raise the main risk issues and supervisory concerns associated with these topics, summarising relevant supervisory rules, policies and guidance. The stock-taking exercise will be used as a basis for a report presenting recommendations to be released in Spring 2004.

4. Insurance Activities on the Internet

Agency: IAIS

Target Date: 2004

Brief Description: The IAIS is developing risk management principles for electronic commerce in insurance products. The paper intends to address how the risks can best be managed when monitoring and inspecting companies that use electronic distribution channels for product sales.

III. Glossary of Agencies

BCBS	Basel Committee on Banking Supervision (www.bis.org/bcbs)
BIS	Bank for International Settlements (www.bis.org)
CGFS	Committee on the Global Financial System (www.bis.org/cgfs)
CPSS	Committee on Payment and Settlement Systems (www.bis.org/cpss)
FATF	Financial Action Task Force on Money Laundering (www.fatf-gafi.org)
FSF	Financial Stability Forum (www.fsforum.org)
FSI	Financial Stability Institute (www.bis.org/fsi)
G-10	Group of 10 (A group of industrial countries)
IAIS	International Association of Insurance Supervisors (www.iaisweb.org)
IASB	International Accounting Standards Board (www.iasc.org.uk)
IAASB	International Auditing and Assurance Board (www.ifac.org/iaasb)
IFAC	International Federation of Accountants (www.ifac.org)
IMF	International Monetary Fund (www.imf.org)
IMFC	International Monetary and Financial Committee
INPRS	International Network of Pensions Regulators and Supervisors (www.inprs.org)
IOSCO	International Organization of Securities Commissions (www.iosco.org)
MWGED	Multidisciplinary Working Group on Enhanced Disclosure
OECD	Organisation for Economic Co-operation and Development (www.oecd.org)
UNCITRAL	United Nations Commission on International Trade Law (www.uncitral.org)
World Bank	International Bank for Reconstruction and Development (www.worldbank.org)