FINANCIAL STABILITY FORUM

Issues Paper of the Task Force on Implementation of Standards

Meeting of the Financial Stability Forum

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Preface

At its second meeting on 15 September 1999, the Financial Stability Forum (FSF) established an ad hoc Task Force on Implementation of Standards. Mr. Andrew Sheng, Chairman of the Securities and Futures Commission, Hong Kong, chaired the Task Force.

An issues paper by the Task Force was submitted to the FSF for discussion at its meeting in Singapore on 25-26 March 2000. The Forum endorsed the paper, underscoring the importance of the standard-setting bodies continuing to work actively with the IMF and the World Bank to better leverage resources for assessing observance of standards. It endorsed the set of 12 key standards for sound financial systems identified by the Task Force, which will be highlighted within a revised Compendium of Standards as proposed by the Task Force. The Forum also set in train further work in the area of market and official incentives to help foster implementation of standards.

Subsequent to the Singapore meeting, the issues paper was forwarded to various international groupings and bodies concerned with efforts to foster the implementation of international standards, including the Finance Ministers and Central Bank Governors of the G7 and G20, and the heads of the IMF and World Bank for circulation to their respective executive boards.

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Chairman, Financial Stability Forum

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I. Executive Summary

1. The FSF Task Force on Implementation of Standards was set up to explore key issues and consider a strategy for fostering the implementation of international standards relevant for sound financial systems.

2. Standards help to promote sound financial systems domestically and financial stability internationally. They play an important role in strengthening financial regulation and supervision, enhancing transparency, facilitating institutional development, and reducing vulnerabilities. Standards vary in scope, specificity, and degree of international acceptance. They range from broad principles to specific methodologies. Many of them are functionally overlapping or interdependent. Standards are not ends in themselves but a means for promoting sound financial fundamentals and sustained economic growth. Their implementation must fit into a country's overall strategy for economic and financial sector development, taking account of its stage of development, level of institutional capacity, and other domestic factors.

3. There has been good progress to-date in promulgating and assessing observance of international standards. The standard setting bodies [namely the Basel Committee on Banking Supervision (BCBS), International Association of Insurance Supervisors (IAIS), and International Organisation of Securities Commissions (IOSCO)], the International Monetary Fund (IMF), and the World Bank have promulgated a variety of standards. The standard-setting bodies are also in various stages of developing detailed methodologies for assessing observance of their respective standards. The Fund-Bank experimental *Reports on Observance of Standards and Codes (ROSC)* provide an organising framework for conducting these assessments, including by drawing on assessments conducted through the Fund-Bank *Financial Sector Assessment Programme (FSAP)*. The Fund's *Article IV Consultation* provides a process for discussing individual economies' progress in implementing standards. There is growing political support for these efforts.[1] The experience gained through these efforts points to three key factors for fostering implementation of standards: (a) promoting country ***ownership***; (b) providing a judicious blend of market and official ***incentives***; and (c) mobilising ***resources*** both nationally and internationally through enhanced partnerships.

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[1] At their inaugural meeting in Berlin on 16 December 1999, the Group of Twenty Finance Ministers and Central Bank Governors agreed to undertake the completion of ROSCs and financial sector assessments, within the context of continuing efforts by the IMF and World Bank to improve these mechanisms. Similarly, Western Hemisphere Finance Ministers have encouraged their members to participate in FSAPs and have agreed to participate in ROSCs.

Key Issues

4. ***Ownership.*** Most economies recognize the benefits of adopting and implementing international standards, but their success in doing so depends on their domestic policy priorities, understanding of the implementation process, and capacity to deal with hitherto hidden economic losses made explicit by the application of international standards (e.g. through a more stringent accounting treatment or disclosure requirement). Economies will be more willing to implement standards insofar as they recognise that it is in their national interest to do so, in terms of strengthening financial systems and thereby supporting sustained economic growth domestically while contributing to financial stability globally. While the implementation of standards is a sovereign decision, the international community can encourage it through:

- exchanging experiences on the practical benefits of implementing standards, in international forums like the Group of Twenty (G-20), the International Monetary and Financial Committee (IMFC), IMF and World Bank Executive Boards, the Financial Stability Forum (FSF), and the standard-setting bodies;
- giving a broad range of economies the opportunity to contribute to the standard-setting process;
- helping to align implementation plans with domestic financial sector reform agendas, mainly through the FSAP and technical assistance; and
- encouraging and assisting, where appropriate, self assessments by national authorities of their observance of standards so as to promote better understanding of the standards and their implementation.

5. ***Incentives***. The commitment of economies to implement standards will be reinforced if market participants reflect information on observance of standards in differentiated credit ratings, borrowing spreads, asset allocations, and other lending and investment decisions. The effectiveness of *market incentives* would be enhanced by:

- disclosure of information on assessments of progress in implementing standards;
- improved understanding by market participants of international standards; and
- efforts to encourage market participants to give greater attention to economies' observance of standards in their risk assessments, provide information to others, and apply market discipline through their pricing and allocation decisions.

Efforts in this regard must recognise the diversity of market activities, ranging from banking lending, portfolio investment, foreign direct investment, to assessing credit ratings. Market players differ in their areas of interest, use of information, methods of risk assessment, and factors they affect or influence.

6. *Official incentives* provided by the international community can help complement market incentives if they are applied in a way which takes account of the desirability of maintaining economies' sense of ownership and avoiding adverse effects on economic

development. There is a range of possible official incentives which could be considered (see Box 1 on page 12). Given that assessments of observance of standards are likely to be at least partly qualitative in nature, further work is required to assess if and how they can be effectively linked to official incentives. Official incentives may be more readily applicable for encouraging economies to adopt standards, announce a credible implementation plan, and participate in external assessments than for rewarding actual observance of standards.

7. ***Resources***. Experience to-date suggests that substantial human and financial resources will be required from the *official sector* - national authorities, international financial institutions (IFIs) like the Bank and the Fund, and standard-setting bodies - to support the implementation effort. The two complementary areas where resource needs are most acute and where there is scope for enhanced international co-operation are: (a) capacity building (including technical assistance and training); and (b) assessment of progress in implementation. In both areas, there is a need to more effectively leverage resources through enhanced partnerships among relevant bodies and bolster resources through increased allocation.

8. As a user of information and provider of market incentives, the *private sector* could potentially play a role in supporting the implementation process, e.g. in providing feedback on areas for improvement in implementation and inputs on actual practices vis-à-vis standards. There are, however, a number of issues relating to expertise on standards, data confidentiality, and conflicts of interest, that would need to be addressed before private sector resources can be usefully tapped.

Strategy for Fostering Implementation

9. Ongoing work and existing initiatives by the international community can be framed as a five-stage strategy (see Box 2 on page 17).

10. ***Identifying and forging international consensus on key standards***. There is a broad range of economic and financial standards that are relevant to sound financial systems. It is important to: (a) concentrate efforts on a subset that is likely to make the greatest contribution to reducing vulnerabilities and strengthening the resilience of financial systems; and (b) focus policymakers' attention on a streamlined list of standards for priority implementation depending on country circumstances. Based on prior work which has already established broad international consensus on the critical policy areas for sound financial systems, the Task Force has identified 12 key standards (see Box 3 on page 19). The FSF Compendium of Standards is an effective tool to disseminate information on these key standards as well as provide a one-stop reference for other economic and financial standards relevant for sound financial systems (see Annex I on page 45 for a proposed content and structure of the Compendium).

11. The multiplicity of standards in accounting and auditing, and lack of international standards in the area of insolvency merit attention. The effective application of many standards depends critically on the quality of underlying data and associated accounting practices. Accurate, reliable and timely financial statements are a fundamental for economic efficiency and financial stability. The present quality of financial information on publicly listed companies in many economies falls short of user expectations, leading to poor policies and risk management. Efforts are required to promote further convergence among internationally recognised accounting standards. Economies should be encouraged to (a) adopt high quality internationally accepted accounting standards, (b) clarify which particular standard or set of standards they are following, (c) ensure that its requirements are unambiguous, reliable, transparent and objective, and (d) apply and enforce them in a consistent manner.

12. ***Prioritising standards for implementation taking account of country circumstances***. Prioritisation of standards for implementation must necessarily vary from economy to economy, taking into consideration their current status in observance of standards, economic circumstances, financial structures, legal and institutional frameworks, and policy priorities. A balance would need to be struck between international and domestic considerations. This can be achieved through national authorities working closely with the IFIs and standard-setting bodies.

13. ***Designing and effecting an action plan to implement standards***. National authorities should be encouraged to publicly articulate their adoption of standards and announce an action plan for their implementation. The plan should include targets, a timetable, resource allocations, and technical assistance needs, indicate the legislative or regulatory changes to be effected, and consider how to generate ownership within the domestic community. The drawing up of action plans is a sovereign exercise, taken in consultation with the IFIs and standard-setting bodies where appropriate.

14. ***Assessing progress in observance of standards on an ongoing basis***. Self assessments of progress in implementation are important for promoting country ownership. If based on clear and well-developed methodologies, they can help make more effective use of international resources. But self assessments in themselves are not sufficient; to add credibility and ensure rigour, they need to be complemented by external assessments. These should be partnership efforts between the IFIs and standard setting bodies, building on the Fund-Bank ROSC and FSAP processes. It is important to develop clear assessment methodologies so as to guide the assessment process, help ensure complementarity between self and external assessments, and facilitate comparability across jurisdictions of external assessments.

15. ***Disseminating information on progress in observance of standards***. Dissemination of information is critical if there is to be any prospect of making market or official incentives work. While the decision on a public release of summary assessments rests

ultimately with national authorities (given concerns among some economies of disproportionate market responses to disclosure of assessment results that are perceived negatively), there should be a general presumption in favour of such release. Economies that assess that it would be inappropriate for them to adopt a particular standard or requirement therein should be encouraged to disclose their reasons publicly.

Next Steps

16. The Task Force raises the following for the FSF's consideration.

17. ***Do FSF members agree with:***

- the importance of promoting country **ownership**, employing a judicious blend of market and official **incentives**, and effectively leveraging **resources** through enhanced partnerships, as the key success factors for a strategy to foster implementation of standards;
- the outline for the **5-stage strategy** to foster implementation of standards based on existing initiatives, as set out in Box 2 (page 17);
- the need to give further momentum to the **Fund-Bank ROSC process**, under which the IFIs and standard-setting bodies can take primary responsibility for preparing assessments in their respective areas of expertise;
- the list of **12 key standards** for sound financial systems, as set out in Box 3 (page 19); and
- the proposed content and structure of the revised FSF **Compendium of Standards** covering the 12 key standards on an introductory page and other relevant standards organised separately (as set out in para 57 on page 21 and Annex I on page 45), or an alternative option of a shorter Compendium comprising just the 12 key standards (as outlined in para 58 on page 21).

18. ***Do FSF members agree to encourage:***

- Standard-setting bodies:
  - ⇨ to continue working actively with the Fund and the Bank within the context of the **FSAP and ROSC processes** to better leverage their resources, existing initiatives, and ongoing efforts in assessing observance of standards;
  - ⇨ to develop **clear assessment methodologies** for the key standards (if they have not already done so) in co-operation with the Fund and Bank where appropriate;
- IMF, World Bank, and standard-setting bodies: to continue working closely with the international and national accounting profession and standard-setters to expedite strengthening **accounting and auditing practices**.

19. ***Do FSF members agree that further work should be done on:***

- promoting **market incentives** by engaging market participants in a dialogue to:
  - ⇨ obtain a better appreciation of their informational needs and potential use of information on standards in their risk assessments;

  - ⇨ enhance their understanding of the role of standards in strengthening financial systems;
  - ⇨ encourage them to give more attention to information on observance of standards; and
  - ⇨ structure official information on observance of standards so that it can be useful for market pricing and allocation decisions.

- evaluating the desirability and feasibility of various **official incentives** and how they can be structured and effectively applied by relevant IFIs and national jurisdictions
- exploring how **resources for capacity building** (technical assistance and training) can be mustered and better co-ordinated to support the implementation of standards.

II. Introduction

Terms of Reference

20. The development and implementation of international standards is an important component of efforts to strengthen domestic financial systems and promote international financial stability. The international community has made considerable progress in developing a range of standards relevant to sound financial systems. The key challenge is to further encourage their adoption and implementation.

21. The IMF, World Bank, and standard-setting bodies have done a significant amount of work in promulgating and assessing observance of standards. Accordingly, the FSF decided at its second meeting in September 1999 to set up a Task Force on Implementation of Standards that would draw on this prior work to *explore key issues* and *consider a strategy* for fostering implementation of international standards relevant to strengthening financial systems. The Task Force was asked to identify a set of international standards most relevant to strengthening financial systems, consider official and market incentives to help promote their implementation, and explore strategies for assisting countries in implementation.[2]

22. The Task Force was asked to provide an issues paper for the Forum to consider future work, rather than make detailed recommendations. This paper:

- discusses the key issues involved in fostering implementation of standards;
- outlines a strategy for implementation based on existing initiatives; and
- sets out next steps for the Forum to consider.

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2 The terms of reference and composition of the Task Force are at Annex A and Annex B respectively. A description of progress to-date in developing and promulgating international standards for sound financial systems is at Annex C; and a description of ongoing work in monitoring the observance of standards is at Annex D.

Objective and Definitions

23. The objective is to *promote sound domestic financial systems and international financial stability* through the implementation of internationally accepted standards for economic, financial and market activities.[3] The development, adoption, and successful implementation of international standards yields both national and international benefits. It helps to:

- strengthen domestic financial systems by encouraging sound regulation and supervision, greater transparency, and more efficient and robust institutions, markets, and infrastructure;[4] and
- promote international financial stability by facilitating better-informed lending and investment decisions, improving market integrity, and reducing the risks of financial distress and contagion.

It is worth noting, however, that the implementation of standards in itself is not sufficient to ensure financial stability.

24. Standards vary in scope, specificity, and degree of formal international acceptance. Many of them are functionally overlapping or interdependent. Standards range from general principles that set out fundamental tenets in a broad policy area to specific methodologies that spell out the practical application of these principles within a more narrowly defined context. The legitimacy or degree of formal acceptance of a standard has an important bearing on the extent to which sanctions can be applied for non-compliance. Successful implementation of standards, which involves a process of interpretation, application, enforcement, and assessment, requires a good understanding of these various distinctions. Further elaboration of these important issues and a taxonomy of international standards is at Annex E.

25. Standards are not an end in themselves but a means for promoting sound financial systems and sustained economic growth. They need to be continually reviewed in order to remain relevant in the face of changing circumstances. The relative importance of different standards to individual economies depends on their financial structure and other domestic circumstances. Their implementation must fit into a country's overall strategy for economic and financial sector development, taking account of its stage of development, level of institutional capacity, and other domestic factors. It is also critical that economies have in place an effective legal framework and infrastructure for enforcement.

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3 While a broad range of political, social, legal, and institutional factors impinge on financial stability, the focus of the FSF is on *economic* and *financial* standards which are generally accepted by the international community as being objective and relatively free of national biases.

4 There is growing recognition that international standards, guidelines, recommendations and benchmarks for good practices can play a major role in the development of institutional frameworks, implementation of sound policies, reduction of vulnerabilities, and promotion of long-term economic development.

26. The focus of the Task Force is on implementation of standards in both industrial and developing economies. The implementation of standards in offshore financial centres (OFCs) is the focus of a separate Working Group of the FSF.[5]

Progress To-Date

27. The international community has made good progress in fostering the implementation of standards, with the IMF, World Bank, and standard-setting bodies at the forefront of these efforts, working closely with national authorities. Considerable experimentation is underway in assisting economies to implement standards, and assessing their observance of standards with a view to identifying areas for improvement and technical assistance needs.

- The Fund and the Bank provide an organising framework for assessing observance of standards and relevant policies:
  - ⇨ The joint Bank-Fund *Financial Sector Assessment Programme (FSAP)* is aimed at assessing financial sector vulnerabilities and identifying developmental priorities, which involves in part an assessment of various financial sector standards. The FSAP is a collaborative effort involving a range of national agencies and standard-setting bodies.
  - ⇨ The experimental *Reports on the Observance of Standards and Codes (ROSCs)* is a vehicle for assembling assessments of standards across a range of areas, including financial sector standards assessed in the context of the FSAP as well as those covering data dissemination, fiscal transparency, and in the future, corporate governance and other standards. ROSC modules provide a description of country practice in a particular area along with an assessment of the extent to which these practices are consistent with the relevant standard in that area.
- The Fund's *Article IV Consultation* provides a process for discussing individual economies' progress in implementing standards of direct operational concern to the Fund.
- The standard-setting bodies are in various stages of developing detailed methodologies that could be used for self assessments or external assessments (which could include peer reviews, or assessments led by the Fund and the Bank). Standard-setting bodies have also been contributing to the Fund-Bank FSAPs and ROSCs.

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5 While many international standards apply equally to OFCs and onshore jurisdictions, some OFCs pose a unique set of issues. Unlike most economies, weak implementation of standards generates larger negative externalities relative to domestic costs in the case of many OFCs; indeed, some OFCs may even profit from weak implementation. This suggests a different approach to OFCs with regard to incentives even if, as a matter of principle, OFCs should not be expected to meet higher standards than onshore jurisdictions.

II. Key Issues

28. The experience gained through the above ongoing efforts points to three key factors for fostering successful implementation of standards: (a) promoting country *ownership*; (b) providing a judicious blend of market and official *incentives*; and (c) mobilising *resources* both nationally and internationally through enhanced partnerships.

Promoting Ownership

29. A strong sense of country ownership - including political commitment - is critical for fostering successful implementation of standards. Implementation can be encouraged but not enforced from outside, and assistance from the international community will only be effective if there is domestic commitment. While most economies recognise the benefits of adopting and implementing international standards, national authorities' commitment or capacity to do so depends on a few considerations:

- There could be inadequate appreciation of the potential vulnerabilities of their domestic financial systems. They may consider "national" standards as being more appropriate for their particular stage of economic development.
- There could be uncertainty about the process of implementation and what it entails, including concerns that disclosure of non-observance of standards may lead to adverse market reactions and reduced access to capital markets or official funds.
- There could be concerns that applying an international standard (e.g. a more stringent accounting treatment or disclosure requirement) could result in an explicit recognition of hitherto hidden economic losses. For example, in some economies, financial institutions and corporates may be solvent according to national accounting standards but could be insolvent if internationally recognised accounting standards are applied. While prompt, corrective action through the application of international standards is important, there is a need for good communication so as not to risk a potential erosion of confidence stemming from the explicit recognition of these economic losses.

30. A key principle for promoting ownership therefore is that implementation of standards must be a sovereign decision taken in the:

- national self-interest of fostering a sound domestic financial system that supports sustained economic growth and development;
- enlightened self-interest of helping to promote a stable global financial system in which the economy has a stake; and
- recognition of the responsibilities attached to participating in the global economic and financial system.

31. ***Ownership from a National Perspective***. This can be fostered in several ways.

- Implementation of international standards should be *aligned with other domestic policy priorities*. The Fund-Bank FSAPs are useful in this regard because they place the implementation of standards within the larger framework of financial sector reform.
- Ownership must *extend beyond governments and central banks* to banking, securities and insurance regulators, accounting authorities, statistical agencies, self-regulated professional bodies, and other domestic standard-setters.
- Dialogue and *exchange of experiences* at international groupings and forums (e.g. the G-20, IMFC, Fund and Bank Executive Boards, FSF, and the standard-setting bodies) on the practical benefits of implementing standards can help foster buy-in.
- Publicly articulating the adoption of standards and *announcing an action plan for implementation* will help strengthen ownership, promote buy-in from broader segments of the economy, and send a powerful signal of the country's commitment.
- Periodic *self assessment* by national authorities of their progress in implementing standards helps promote better understanding of the practical issues and resource implications faced in the implementation process, and thereby build up domestic capacity to carry through the reforms. Making the results of these self assessments public should help enhance credibility as well as accountability. (Self assessments without external verification could suffer from a lack of rigour or credibility or both, and must therefore be complemented by external assessments.)

32. ***Ownership from an International Perspective***. A sense of stakeholdership in the global financial system can be a strong motivation for implementing international standards. An effective way of achieving this would be to *involve a broad range of economies in the standard-setting process*. This should of course be balanced against the need to keep the number of participants involved in the standard-setting process manageable so as not to compromise the quality of the standards and to avoid the risk of undue delay in their formulation. There are two ways in which economies could be involved:

- Where standard-setting bodies have wide representation, all members have an opportunity to comment on and endorse the standards (e.g., the *Code of Good Practices on Fiscal Transparency* by the IMF, and the *Objectives and Principles of Securities Regulation* by IOSCO).
- Where standard-setting bodies have a narrower membership, a consultative process that actively solicits views from many economies and takes into consideration these views when developing standards is important (e.g., the *Core Principles on Effective Banking Supervision* by the Basel Committee). In addition, a broader group of countries could be involved subsequently in preparing the detailed "methodologies". In the case of the *Principles of Corporate Governance* developed by the OECD, the World Bank and OECD have embarked on a joint effort to use the Principles as a basis for dialogue and consultation with developing and transitional economies.

Providing Incentives

33. Official and market incentives, which are often complementary, can help national authorities and domestic players recognise that it is in their interest to promote the implementation of standards.

34. ***Market Incentives.*** Market incentives are applied by market participants when they use information on an economy's observance of standards in their risk assessments and reflect this in differentiated credit ratings, borrowing spreads, asset allocations, and other lending and investment decisions. For market incentives to work, market participants need to:

- be familiar with international standards;
- judge them to be of relevance to their risk assessments;
- have access to information on observance of standards; and
- use that information as a significant input in their risk assessments.

35. The effectiveness of market incentives would thus be enhanced by (a) disclosure of information on assessments of progress in implementing standards; and (b) efforts to encourage market participants to give greater attention to economies' observance of standards in their risk assessments, provide information to others, and apply market discipline through their pricing and allocation decisions. Efforts in this regard must recognise the diversity of market activities, ranging from bank lending, portfolio investment, foreign direct investment, to assessing credit ratings. Market players differ in their areas of interest, use of information, methods of risk assessment, and factors they affect or influence (which act as incentives on economies and institutions).[6]

36. *Further Work*. While market participants cannot be made to integrate information on standards in their risk assessments, it would be useful to engage the various types of market participants in a dialogue aimed at:

- obtaining a better appreciation of their informational needs and potential use of information on standards in their risk assessments;
- improving their understanding of the role of standards in strengthening financial systems and encouraging them to give more attention to information on observance of standards; and
- structuring official information on observance of standards so that it can be useful for market pricing and allocation decisions.

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[6] The Task Force undertook a quick feedback gathering exercise to assess the extent to which the preconditions in para 34 are present. The IMF has also undertaken a small outreach programme to solicit feedback from the private sector and regulatory authorities on its ROSCs. A preliminary assessment based on these limited outreach efforts is presented in Annex F.

37. ***Official Incentives***. Official incentives are measures applied by the official sector to an economy or institutions in that economy conditional on the economy achieving a well-defined milestone in the implementation process, ranging from a commitment to implement standards to observance of standards as verified by an external assessment. The challenges with regard to making market incentives work effectively suggest the need to consider official incentives as complementary measures. Even when market participants start using information on observance of standards in a significant way, there might be a role for official incentives:

- Weak domestic financial systems can impose negative externalities on global financial stability. These externalities may not be fully addressed by market discipline or incentives.
- Markets are focused on end-results and may not recognise progress made by economies in implementing standards. Official incentives could be useful in sustaining the commitment of national authorities and maintaining the momentum of implementation.

38. A menu of possible official incentives, together with a preliminary sketch of the key challenges associated with their application is provided in Box 1. A description of official incentives either currently in use or under consideration is at Annex G.

Box 1: A Menu of Possible Official Incentives

Incentive	**Main Challenges in Application**
Conducting ***surveillance of economic and financial sector vulnerabilities*** and engaging national authorities in a policy dialogue on the role of standards in addressing vulnerabilities and strengthening policies and institutions, e.g. the IMF's Article IV Consultation process and Bank-Fund FSAPs.	• Resource costs are considerable.
Providing ***technical assistance*** to help economies build the capacity to implement standards	• Resource implications on donors could be considerable. • Multilateral grants for technical assistance are limited. • Expertise is scarce.
Providing ***financial assistance*** to help countries finance the implementation effort	• Countries do not like to borrow for such assistance.
Differentiating terms for ***official financing*** conditional on economies achieving progress in implementation, e.g. IMF's Contingent Credit Line, Stand-By Arrangement, and Extended Fund Facility.	• Ultimately for decision by the relevant lending agencies, which have to take account of factors besides observance of standards. • No leverage on economies that do not need such financing.

Linking ***membership in international groupings*** to progress in implementation of standards, e.g. IOSCO, Basel-sponsored bodies, OECD, FATF, etc.	• Ultimately for each body to decide its criteria for membership. • The relevant standards were not formulated as a test for membership. • Exclusion from international organisations of economies lacking in progress in implementation of standards could remove a potential source of peer pressure.
Giving consideration to home supervisory authorities' observance of standards in ***market access*** decisions with regard to foreign institutions, e.g. licenses, branching, acquisitions, new activities, etc.	• Not an effective lever against economies whose institutions already enjoy access to foreign markets. • Requires co-ordination among the major financial centres so as to minimise regulatory arbitrage and protectionism • Requires information on observance of standards to be made available to national regulatory and supervisory authorities.
Differentiating ***risk weights*** within the capital adequacy framework for extensions of credit to counterparties in accordance with the observance of standards in the jurisdictions in which they operate.	• Difficult to apply in an objective manner.
Encouraging banks to consider risks due to weak observance of standards as part of their ***internal credit rating methodologies.***	• Requires co-ordination among the major financial centres so as to minimise regulatory arbitrage and protectionism. • Requires information on observance of standards to be made available to national regulatory and supervisory authorities.
Tightening supervision of foreign subsidiaries or branches of institutions whose home supervisors are in economies with weak implementation of standards, e.g. more frequent examinations, higher reporting requirements, more extensive external audits.	• Requires co-ordination among the major financial centres so as to minimise regulatory arbitrage and protectionism. • Requires information on observance of standards to be made available to national regulatory and supervisory authorities.
Taking ***regulatory actions*** on foreign subsidiaries or branches of institutions whose home supervisors are in economies with weak implementation, e.g. restricting inter-affiliate transactions, issuing informational advisories, etc.	• Requires co-ordination among the major financial centres so as to minimise regulatory arbitrage and protectionism. • Requires information on observance of standards to be made available to national regulatory and supervisory authorities.
Strengthening oversight by central banks with regard to payments systems providers.	• Requires cross-border information exchange on relevant payments data.

39. The preliminary evaluation above suggests that international surveillance of economic and financial sector vulnerabilities and policy dialogues (as is being done through the ROSCs, FSAPs, and Article IV Consultation) is an effective incentive; so is the provision of technical assistance. Market access and regulatory and supervisory actions by other jurisdictions can also be effective but would require co-ordination to minimise regulatory arbitrage or protectionism. Making the availability and terms of financing conditional on progress in implementation is ultimately the prerogative for individual IFIs, multilateral donors or lenders, or capital-providing countries, and requires careful consideration.

40. The following considerations may be appropriate in applying official incentives:

- It is important that official incentives are applied in a way which takes account of the desirability of maintaining economies' sense of ownership and avoiding adverse effects on their economic development.
- While national sovereignty considerations imply that jurisdictions retain the discretion to determine when to apply a particular incentive, its effectiveness will be reinforced by consistent application by all major jurisdictions.
- Given that assessments of observance of standards are likely to be at least partly qualitative in nature and not susceptible to a simple "pass/fail" judgement, the scope for translating them into discrete decisions on whether or not to apply incentives is limited. Most official incentives may thus be more applicable for encouraging countries to adopt standards, announce a credible implementation plan, and participate in independent assessments than for rewarding observance of standards. There may be scope, however, for reflecting economies' observance of standards in a more qualitative way, e.g., in supervisors' overall assessment of the risks associated with loan exposures to jurisdictions that have weak observance of relevant standards.

41. *Further Work*. More focused work is needed in studying the desirability and feasibility of various possible official incentives and the appropriate circumstances for their effective application by relevant IFIs and national jurisdictions.

Mobilising Resources

42. Implementation of standards is very resource-intensive, for national authorities, the IFIs, and standard-setting bodies. Mobilising resources and managing partnerships among the various players involved in the implementation process is critical. The two complementary areas where resource needs are most acute and where there is scope for enhanced international co-operation and partnership are:

- *building capacity*, which includes helping to formulate effective implementation plans, providing technical assistance to build institutional capacity, and providing training opportunities for officials in relevant areas; and

- *conducting assessment* which includes taking stock of economies' status in observance of standards and their ongoing progress, identifying technical assistance needs, and evaluating the effectiveness of technical assistance.

These two areas are closely linked and parts of a seamless process.

43. ***Building Capacity***. Even though a considerable amount of technical assistance is already being provided, the resource requirement for effective implementation of standards should not be under-estimated. Efforts should focus on more effectively leveraging resources as well as augmenting resources.

44. To better leverage existing resources for technical assistance and training, the following approaches might be worth considering:

- *Improving the co-ordination of international technical assistance resources*. There are a number of bodies providing technical assistance and a good amount of co-ordination amongst them. Further improvements in existing modalities for co-ordinating technical assistance could be explored.[7]
- *Publicising training opportunities*. The Directory of Training Opportunities in Financial Supervision, created jointly by the IMF, World Bank, and BIS and available on the FSF website, provides useful information on training opportunities worldwide in banking supervision. Work is currently underway on including in the Directory training courses in insurance. Further work in this direction could take the form of: (a) giving impetus to including in the Directory courses in all the other areas relevant to sound financial systems; and (b) encouraging all training providers to contribute to the Directory and update information on their course offerings on a monthly basis.
- *Co-ordinating training schedules*. There are benefits in enhanced co-ordination of timings and venues of related training courses so as to minimise scheduling conflicts and maximise geographical reach. An annual meeting of key training providers and regular sharing of course schedules among them might be a mechanism for achieving this.

45. ***Conducting Assessment***. The experience of the Fund and Bank in undertaking the FSAPs and ROSCs shows that substantial resources – human and financial – are required. The modular approach for the ROSCs, whereby assessments for different areas are conducted separately as individual "modules" forming a collection over time, allows a more focused use of resources. The cost implications are, however, still considerable.

46. Standard-setting bodies have much expertise in their respective areas such as accounting, banking, securities, insurance, corporate governance, payment and

7 For instance, the G7 Finance Ministers' Report to the Cologne Economic Summit in June 1999 called for exploring the desirability and feasibility of a "clearing house" for technical assistance.

settlement, etc. They have an important role to play in framing and supporting the assessment process. Their involvement is also desirable from the perspectives of:

- ensuring that the most up-to-date expertise is involved in assessments;
- maintaining the integrity of their standards in the course of implementation;
- gaining first-hand experience of the practical issues involved in implementing these standards; and
- reviewing and further improving their standards in the light of this experience.

However, many standard-setting bodies currently do not have the mandate or institutional capacity to carry out assessments.

47. *Strengthening the Ownership Frameworks*. The *shared ownership* framework developed by the Fund/Bank for their ROSCs offers a very useful mechanism to better leverage the resources of the IFIs and standard-setting bodies. Under this approach, the various IFIs and standard-setting bodies can take primary responsibility for preparing assessments in their respective areas of expertise within the context of the Fund-Bank ROSCs. The FSAPs have a *joint ownership* structure whereby the Bank and the Fund are jointly responsible for the report but experts from the standard-setting bodies and national authorities also participate in FSAP missions. Consideration should be given to strengthening these ownership frameworks in the following ways:

- Standard-setting bodies should be encouraged to work more actively with the Fund and the Bank within the context of the FSAP and ROSC processes to better leverage their resources, existing initiatives, and ongoing efforts in assessing observance of standards; and
- More countries should undertake to contribute expertise to assist the FSAP and ROSC processes so as to ensure that more up-to-date and hands-on expertise is brought to bear in the assessment process.

48. ***A Role for the Private Sector?*** The implementation of standards will have a major impact on the private sector. As a user of financial information and provider of market incentives, the private sector could potentially play a role in the implementation of standards. For instance, some private sector entities, such as domestic standard-setting bodies and self-regulatory associations, could play a useful role in disseminating information on and fostering progress in economies' implementation of standards. Private sector involvement could possibly take the form of providing:

- feedback to the official sector on areas for improvement in implementation procedures and resource allocations, and issues related to prioritisation and sequencing;

- market perspectives, inputs, and assessments on economies' actual practices with regard to standards;[8] and
- technical assistance for implementing certain standards (e.g. with respect to accounting and auditing, some international self-regulatory or professional associations could be involved).

49. While it would be useful to leverage private sector expertise given official resource constraints, there are several issues to be addressed.

- In some areas, the willingness of national authorities to undergo assessments by internationally recognised bodies may not extend to private sector experts or institutions for confidentiality reasons.
- The private sector's ability to assess observance of standards, particularly those dealing with policy transparency, and supervision and regulation, is limited at this stage due to the evolving nature of most international standards and codes.
- Private sector involvement poses difficult issues related to conflicts of interest and privileged access to information that could result in unfair market advantage.

III. Outline of a Strategy

50. Ongoing work and existing initiatives by the international community can be framed as a five-stage strategy as presented in Box 2.[9]

Box 2: Outline of Strategy to Foster Implementation of Standards	
➢ **Identify and forge international consensus on key standards**	
• Identify standards for sound financial systems and highlight gaps	⇨ International community
• Develop methodologies for assessment of observance of standards	⇨ SSBs in co-operation with IFIs where appropriate
• Disseminate information on and promote understanding of standards among national authorities	⇨ International community
• Secure international political commitment to implement standards	⇨ International community
• Engage market participants in a dialogue on the significance of standards	⇨ NAs, IFIs, SSBs

8 For instance, in 1989, the European Commission asked a large accounting firm to carry out a survey in EU countries on the implementation of EU Council directives on own funds and on solvency ratios for credit institutions.

9 The simple linear representation of the various stages in Box 2 is necessarily a simplification of a more elaborate and circular process characterised by feedback between stages.

➢ **Prioritise standards for implementation taking account of country circumstances**	
• Assess country's status in observance of standards, economic circumstances, and financial sector vulnerabilities	⇨ NAs in consultation with IFIs and SSBs
• Prioritise standards for implementation on the basis of this assessment within framework of country's domestic policy agenda or reform programme	⇨ NAs in consultation with IFIs and SSBs
➢ **Design and effect an action plan to implement standards**	
• Publicly articulate adoption of standards	⇨ Nas
• Announce action plan for implementation specifying intermediate targets, time-table, resource allocation, and technical assistance needs	⇨ NAs in consultation with IFIs and SSBs where appropriate
• Provide technical assistance and other official incentives where necessary	⇨ International community
➢ **Assess progress in observance of standards on an ongoing basis**	
• Conduct self or assisted self assessment of progress in observance of standards	⇨ NAs in consultation with IFIs and SSBs
• Verify through external assessment (peer reviews, or assessments led by the Fund and the Bank)	⇨ IFIs and SSBs
• Provide additional technical assistance where necessary	⇨ International community
➢ **Disseminate information on progress in observance of standards**	
• Disseminate information on progress to market participants	⇨ Nas

NAs: national authorities; SSBs: standard-setting bodies; IFIs: international financial institutions.

Identifying and Forging International Consensus on Key Standards

51. ***Identifying Key Standards for Sound Financial Systems***. In accordance with its mandate and drawing on prior work, the Task Force has identified the set of standards it considers the most relevant to strengthening financial systems. Box 3 presents the policy areas relevant for sound financial systems and lists the key standards in these areas.

Box 3: Key Standards for Sound Financial Systems[10]		
Policy Areas[11]	**Key Standards**	**Issued by** [12]
Monetary and financial policy transparency	Code of Good Practices on Transparency in Monetary and Financial Policies	IMF
Fiscal policy transparency	Code of Good Practices in Fiscal Transparency	IMF
Data dissemination	Special Data Dissemination Standard/ General Data Dissemination System[13]	IMF
Insolvency	[14]	World Bank
Corporate governance	Principles of Corporate Governance	OECD
Accounting	International Accounting Standards (IAS)[15]	IASC[16]
Auditing	International Standards on Auditing (ISA)[15]	IFAC[16]
Payment and settlement	Core Principles for Systemically Important Payment Systems	CPSS
Market integrity	The Forty Recommendations of the Financial Action Task Force	FATF
Banking supervision	Core Principles for Effective Banking Supervision	BCBS
Securities regulation	Objectives and Principles of Securities Regulation	IOSCO
Insurance supervision	Insurance Supervisory Principles	IAIS

10 While the key standards are categorised here by policy area, some of them are relevant to more than one area.

11 An additional policy area that could be considered relates to public debt management. The Fund and the Bank have embarked on developing guidance in this area.

12 See Annex C on the status of international endorsement of these standards.

13 Economies with access to international capital markets could be encouraged to subscribe to the more stringent SDDS and all other economies could be encouraged to adopt the GDDS.

14 The World Bank is co-ordinating a broad-based effort, involving relevant institutions and legal experts, to develop a set of principles and guidelines on insolvency regimes. The United Nations Commission on International Trade Law (UNCITRAL), which adopted the *Model Law on Cross-Border Insolvency* in 1997, will help facilitate implementation.

15 The IAS and ISA are used in some jurisdictions but are not endorsed by all jurisdictions. The IAS are currently being reviewed by the BCBS, IAIS, and IOSCO.

16 The International Accounting Standards Committee (IASC) and International Federation of Accountants (IFAC) are distinct from the other standard-setting bodies in that they are private sector bodies.

52. ***Enhancing the Quality of Underlying Accounting Practices***. The practical effectiveness of the key standards relating to data dissemination, banking, securities, and insurance regulation and supervision depends on the quality of underlying data and associated accounting practices. Indeed, accurate, reliable and timely accounting information is a fundamental for economic efficiency and financial stability. Market participants place a great deal of emphasis on the quality of accounting practices, which vary considerably across jurisdictions. The quality of financial information on publicly listed companies in many economies has often been cited as falling short of user expectations. The multiplicity of accounting standards in use has consequences for the effective implementation of other material standards.

53. However, there have been significant efforts by the accounting standard setters and BCBS, IAIS, and IOSCO, and national supervisory and regulatory bodies to expedite the development, convergence, and endorsement of high quality, internationally recognised accounting and auditing standards. These efforts should be strongly pursued. The successful interpretation, implementation, and enforcement of these standards will also depend on the accounting profession, users of financial information, lending institutions, exchanges, and regulatory authorities making significant efforts.

54. Going forward, the Task Force recommends that:

- the relevant standard setters, the accounting profession, and regulatory authorities give high priority to the promotion of convergence, and continue developing and supporting effective implementation of high quality internationally recognised accounting and auditing standards in all jurisdictions;
- the IFIs and key international supervisory and regulatory bodies such as BCBS, IAIS, and IOSCO continue to work closely with the international and national accounting profession and standard setters to expedite strengthening accounting and auditing practices; and
- economies be encouraged to (a) adopt high quality internationally accepted accounting standards, (b) specify which particular standards or set of standards they are following, (c) ensure that the standards' requirements are unambiguous, reliable, transparent and objective, and (d) apply and enforce them in a consistent manner.

55. ***Organising and Disseminating the Standards***. The FSF's Compendium of Standards, available on the FSF website (www.fsforum.org) provides a common, one-stop reference for 43 economic and financial standards relevant for sound financial systems. These standards are no less important than the 12 key standards in Box 3 but are complementary to the key standards, dealing with particular functional areas. The Compendium could thus play the dual role of: (a) focusing attention on the 12 key standards; as well as (b) providing a convenient reference for the larger corpus of related and supporting standards relevant for sound financial systems.

56. There have been proposals from FSF members on including additional standards in the Compendium. These proposals seek to address areas not covered in the current Compendium, such as accounting, auditing, financial conglomerate supervision, market integrity, and market functioning, as well as to include additional standards in insurance and banking (risk management). The additional standards proposed for inclusion in the Compendium, subject to approval by the respective standard-setting bodies and the FSF, are listed in Annex H.[17] The proposed inclusion of these standards will bring the total number of standards in the Compendium to 64 from the current 43.

57. The advantage of a web-based Compendium is that it can accommodate a large number of standards in a user-friendly way as long as the standards are organised sensibly and navigation is easy and efficient. It is therefore proposed that:

- the 12 key standards be listed on an introductory webpage to help focus policymakers' attention; and
- the larger corpus of 64 standards be organised separately in a user-friendly format under: (a) the three *broad headings* of macroeconomic fundamentals, institutional and market infrastructure, and financial regulation and supervision; (b) the various *policy areas* under these headings as set out in Box 3; and (c) specific *functional areas* within these policy areas.[18]

The proposed content and structure of the Compendium is at Annex I.

58. An alternative option would be to reduce the current size of the Compendium from 43 standards so that it comprises only of the 12 key standards. The Compendium would continue to be hyper-linked to the websites of the standard-setting bodies to provide a gateway to the full range of international standards. A smaller Compendium would have the advantage of helping to better focus policymakers' attention on the 12 key standards and facilitating their implementation. It would, however, make it more difficult for users to access the other relevant and complementary standards which should not be presumed to be less important than the 12 key standards. Unlike the Compendium, which is designed as a one-stop reference, the websites of the standard-setting bodies are not uniform in the way they are set up to search for and access these other standards. The IFIs and standard-setting bodies would thus have to establish separate webpages on standards, that could be hyper-linked from the Compendium.

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17 At present, only standards developed by members of the Forum have been included in the Compendium. Since the purpose of the Compendium is to disseminate information on all standards relevant for sound financial systems, it would seem reasonable to include high-quality standards developed by bodies outside the Forum even if some of them have not been endorsed by all jurisdictions.

18 The 43 standards in the Compendium are currently organised under six broad areas: public sector, corporate sector, banking, securities, insurance, and payment and settlement system. While the content of the subject areas of banking, securities, insurance, and payment and settlement is fairly self-evident, it is not readily apparent what the subject area of public sector covers. The classification of standards on corporate governance and accounting under the subject area of corporate sector is also not satisfactory given that they relate to practices that cut across different sectors.

59. ***Securing International Political Commitment***. The respective standard-setting bodies are the most appropriate forums to endorse particular standards at the technical level. However, for successful implementation of these standards, it is important to secure high-level political commitment at both the international and national levels. It might be desirable for relatively broad-based forums with Ministerial-level representation, like the G20 and the IMFC, to provide some political commitment for their implementation.

- Since the G20 is constituted for promoting informal dialogue rather than making decisions, it could help forge international political consensus by expressing a joint commitment to adopt and implement the key standards where relevant.[19]
- Given the IMF's universal membership and key role as the coordinating body for organising assessments of standards (even if it does not have the main responsibility for conducting assessments in areas outside its direct operational focus), endorsement by the IMFC of the importance of implementing standards and active support for implementation efforts could help generate a sense of collective ownership and peer pressure.

60. The adoption of standards for implementation by individual economies is ultimately a sovereign decision. A process of self-selection may be sufficient to ensure that at least most of the systemically important economies which have a relatively higher stake in sound financial systems will undertake to implement relevant standards. When a critical mass of such economies volunteer themselves for an implementation programme, peer pressure could encourage other economies to also participate.

Prioritising Standards for Implementation

61. Individual economies, in consultation with the IFIs and standard-setting bodies, should be encouraged to prioritise standards for implementation based on an assessment of their current status in observance of standards, economic circumstances, financial structures, legal and institutional frameworks, and domestic policy priorities. Prioritisation can help policymakers focus their efforts, given resource constraints in assessment and technical assistance. Having prioritised the relevant standards, it is necessary to sequence them in a logical manner given the inter-relatedness of many standards and the fact that some standards need to be in place before others can be effectively implemented.

62. The criteria for prioritising standards must necessarily vary from economy to economy, but a few broad principles would seem to apply:

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19 In many cases, the key standards represent minimum requirements which economies should be encouraged to meet or exceed. The G20 has already agreed to undertake the completion of ROSCs and financial sector assessments, within the context of continuing efforts by the Fund and the Bank to improve these mechanisms. Similarly, Western Hemisphere Finance Ministers have encouraged their members to participate in FSAPs and have agreed to participate in ROSCs

- A general review of the economy's current status in the implementation of standards should precede the determination of priorities and sequencing. This could comprise an assisted self-assessment (where national authorities undertake a self-assessment in consultation with experts from the IFIs and standard-setting bodies) and an external assessment (peer reviews or assessments led by the Fund and Bank).
- Prioritisation should not be overly rigid. It may have to be adjusted over time as conditions change or new information becomes available.
- In prioritising standards for implementation, a balance needs to be struck between:
  - ⇨ international considerations in terms of the relevance of the standards and the significance of the economy for global financial stability; and
  - ⇨ domestic considerations in terms of economic and social circumstances.

  This can be achieved through national authorities working closely with the IFIs and standard-setting bodies.

Designing and Effecting an Action Plan to Implement Standards

63. National authorities should be encouraged to publicly articulate their adoption of standards and announce an action plan for their implementation (in consultation with the IFIs and standard-setting bodies where appropriate). Action plans should *inter alia*:

- specify intermediate targets, a time-table, resource allocation, and technical assistance needs;
- consider how to generate ownership among those who are likely to be adversely affected by the changes; and
- indicate the legislative and regulatory changes that would have to be adopted.

The public announcement of action plans serves to signal countries' commitment to implementing standards and enhances credibility.

Assessing Progress in Observance of Standards

64. ***Purpose of Assessments***. Assessment of observance of standards is an integral part of the process of fostering implementation of standards. It can:

- provide an initial stock-take of economies' status with regard to observance of standards and help to set implementation priorities;
- monitor progress towards observance of standards;
- identify areas for improvement and help provide a basis for the allocation of scarce technical assistance resources;
- provide the basis for the application of official incentives where appropriate; and
- provide financial markets with information on observance of standards.

65. ***Modality of Assessments***. Self assessment by national authorities is an important component of the overall assessment process because it helps foster ownership by the economies. If based on clear and well-developed methodologies, they can help reduce the time and resources required for external assessments. But self assessments in themselves are not sufficient. To add credibility and ensure rigour, they must be complemented by external assessments. External assessments also provide an objective basis for applying official incentives, including the provision of technical assistance.

66. The Task Force broadly agrees with the main elements of the modalities for assessment that are currently evolving within the framework of the experimental ROSCs and FSAP. A few key elements of this framework are worth noting:

- *Voluntary Approach*. In line with the principle of promoting ownership, the voluntary approach to undergoing assessments is the most practical given the need for active co-operation between national authorities and external assessors. Economies belonging to the G-20 and the Committee on Hemispheric Financial Institutions have already volunteered to participate in assessments.
- *Narrative Evaluation*. Given the nature of the standards and complexities within the areas being assessed, assessments of standards should evaluate the substance or quality of observance rather than adopt a simple "ticks and crosses" approach. A narrative describing qualitatively the degree of observance with each element of the relevant standard allows for a more nuanced assessment that can highlight progress or backsliding as well as describe the economy's commitment to achieve further improvement.
- *Flexibility*. Assessment of observance with standards should be a means for focusing attention on the underlying objectives of the standards and not an end in itself. Where a country chooses not to observe a particular provision of a standard, it should be encouraged to demonstrate that it has an alternative approach to meet the objectives underlying the standard in question and articulate this publicly.

67. ***Developing Assessment Methodologies***. Given that many standards are rather general and open to different interpretations, it is important to develop clear and specific assessment methodologies, including well-designed questionnaires. This is necessary to ensure that: (a) there is adequate guidance to the qualitative judgements that must inevitably be made in the course of the assessment; (b) there is complementarity between self and external assessments; and (c) external assessments are uniform and comparable across jurisdictions. However, not all standards have such supporting methodologies. Standard-setting bodies that have not already done so should be strongly encouraged to develop methodologies for the key standards to aid the assessment process, in co-operation with the IFIs where relevant.

Disseminating Information on Progress in Observance of Standards

68. ***Purpose of Disclosure***. There are two main objectives for disseminating information on progress in observance of standards:

- to demonstrate to the international community progress in implementation and provide the basis for applying official incentives where relevant; and
- to enable market participants to make better-informed lending and investment decisions thereby improving allocative efficiency and exerting market discipline on economies and institutions to implement standards.

69. ***Considerations in Disclosure***. For accurate and effective external assessments of financial sector vulnerabilities and observance of standards (e.g. in the context of the Fund/Bank FSAPs), economies may need to make available to the team of external assessors proprietary, and possibly commercially sensitive, information. While such information should not be contained in the *summary assessment* that is designed for dissemination to the public (e.g. the Fund/Bank ROSC modules), the judgements included therein must necessarily draw on such information. To do otherwise would reduce the quality and accuracy of the summary assessment and risk misleading the public. While the decision on a public release of these summary assessments rests ultimately with the national authorities concerned, there should be a general presumption in favour of such release. Economies that assess that it would be inappropriate for them to adopt a particular standard or requirement therein should be encouraged to disclose their reasons publicly.

70. ***Addressing Concerns about Disclosure***. Some economies have concerns that public disclosure of assessment results that are perceived negatively by the markets could lead to herding behaviour and disproportionate responses that exacerbate volatility in financial markets. However, a number of market participants surveyed have noted that in the absence of information they usually assume the worst, so that an economy is likely to benefit from disclosing its assessment results even if they are critical. Nevertheless, the existence of these concerns must be acknowledged. The potential risks could be mitigated by:

- ensuring high-quality self and external assessments;
- using the initial assessment of observance of standards solely for purposes of identifying areas of weaknesses and not publishing it;
- disclosing subsequent assessment results on a regular and ongoing basis so as to minimise market surprises;
- balancing information on assessment of observance of standards with information on progress in implementation of standards and positive steps being undertaken to achieve observance; and
- allowing national authorities an opportunity to reflect their views in the reports of external assessors, although the decision to incorporate these views must rest with the external assessors.

IV. Next Steps

71. Having explored the key issues and considered a strategy for fostering the implementation of standards, the Task Force raises the following for the FSF's consideration.

72. ***Do FSF members agree with:***

- the importance of promoting country **ownership**, employing a judicious blend of market and official **incentives**, and effectively leveraging **resources** through enhanced partnerships, as the key success factors for a strategy to foster implementation of standards;
- the outline for the **5-stage strategy** to foster implementation of standards based on existing initiatives, as set out in Box 2 (page 17);
- the need to give further momentum to the **Fund-Bank ROSC process**, under which the IFIs and standard-setting bodies can take primary responsibility for preparing assessments in their respective areas of expertise;
- the list of **12 key standards** for sound financial systems, as set out in Box 3 (page 19); and
- the proposed content and structure of the revised FSF **Compendium of Standards** covering the 12 key standards on an introductory page and other relevant standards organised separately (as set out in para 57 on page 21 and Annex I on page 45), or an alternative option of a shorter Compendium comprising just the 12 key standards (as outlined in para 58 on page 21).

73. ***Do FSF members agree to encourage:***

- Standard-setting bodies:
  - ⇨ to continue working actively with the Fund and the Bank within the context of the **FSAP and ROSC processes** to better leverage their resources, existing initiatives, and ongoing efforts in assessing observance of standards;
  - ⇨ to develop **clear assessment methodologies** for the key standards (if they have not already done so) in co-operation with the Fund and Bank where appropriate;
- IMF, World Bank, and standard-setting bodies: to continue working closely with the international and national accounting profession and standard-setters to expedite strengthening **accounting and auditing practices**.

74. ***Do FSF members agree that further work should be done on:***

- promoting **market incentives** by engaging market participants in a dialogue to:
  - ⇨ obtain a better appreciation of their informational needs and potential use of information on standards in their risk assessments;
  - ⇨ enhance their understanding of the role of standards in strengthening financial systems;

  - ⇨ encourage them to give more attention to information on observance of standards; and
  - ⇨ structure official information on observance of standards so that it can be useful for market pricing and allocation decisions.

- evaluating the desirability and feasibility of various **official incentives** and how they can be structured and effectively applied by relevant IFIs and national jurisdictions
- exploring how **resources for capacity building** (technical assistance and training) can be mustered and better co-ordinated to support the implementation of standards.

Annex A

FSF Task Force on Implementation of Standards

Terms of Reference

1. The Task Force should explore issues related to promoting the implementation of international standards relevant to strengthening financial systems.

2. The Task Force should consider a strategy for implementation of standards that may include:

   - countries announcing their commitment to implement standards and participate in credible assessments of compliance;
   - technical assistance in support of implementation efforts being prioritised;
   - relevant information on progress toward compliance of standards being made available; and,
   - compliance with sound practices being rewarded by market participants and others, thereby reinforcing further efforts at implementation.

3. In support of such a strategy, and taking account of country circumstances, the task force should:

   - identify the set of international standards most relevant to strengthening financial systems and ways of disseminating these standards (e.g. through the Compendium of Standards);
   - explore strategies for assisting countries in the practical implementation of standards;
   - explore official and market *incentives* that could encourage the process of implementation;[20]
   - outline options for generating credible *self-assessments and independent assessments* and for ensuring complementarity between the two;
   - consider how, what kind of, and to whom, information on progress toward compliance with standards could be made available;
   - consider how the *resources* required to support implementation and assessment of standards could best be mobilised.

4. The Task Force should consider how the various elements of the implementation strategy could best reinforce each other, and what the roles and responsibilities of various bodies in implementing it should be.

5. In all of the above, the Task Force should draw upon the work already done by the IMF, World Bank, standard-setting bodies, and others with respect to encouraging implementation of sound practices.

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20 Such incentives might include, *inter alia*, making access to certain types of official sources of financing conditional on compliance (as in the case of the CCL), preferential risk weights in the capital adequacy framework, consideration in market access decisions by key financial centres, more generous offers of technical assistance to enhance the capacity of countries to implement sound practices

Annex B

Members of the Task Force on Implementation of Standards

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Annex C

Current State of Development of International Standards

Area	**Monetary and Financial Policy Transparency**
Standard	***Code of Good Practices on Transparency in Monetary and Financial Policies***
Agency	International Monetary Fund (IMF)
Status	Endorsed by the IMF Interim Committee in September 1999.
Guidance for Implementation	A supporting document to guide members seeking to implement the Code is being developed in consultation with national authorities and other international organisations and groupings.
Area	**Fiscal Policy Transparency**
Standard	***Code of Good Practices on Fiscal Transparency***
Agency	IMF
Status	Adopted by the IMF Interim Committee in April 1998.
Guidance for Implementation	A manual to guide economies seeking to implement the Code has been developed and approved by the IMF Executive Board. The Fund has also produced a questionnaire and a self-assessment report to allow countries to assess their practices against those set out in the Code.
Area	**Debt, Liquidity, and Reserve Management**
Standard	-
Agency	IMF, World Bank
Status	The Fund and the Bank are jointly developing a manual of best practices in sovereign debt and risk management. They have also been asked to prepare in the next stage a set of principles for debt and reserve management.
Guidance for Implementation	-
Area	**Data Dissemination**
Standard	***Special Data Dissemination Standard (SDDS)***
Agency	IMF
Status	Approved by the IMF Executive Board in March 1996. There have been two significant reviews since then.
Guidance for Implementation	To-date, 47 countries, representing a mix of industrial, emerging market, and transition economies, have voluntarily subscribed to the SDDS and established websites containing the data disseminated under the SDDS.

Area	**Data Dissemination**
Standard	***General Data Dissemination System (GDDS)***
Agency	IMF
Status	Approved by the IMF Executive Board in December 1997.
Guidance for Implementation	The GDDS is being implemented in two phases. Phase I, completed in November 1999, focused on information and training. Phase II, beginning in 2000, is a period of intensive country work that will take a number of years to complete.
Area	**Insolvency**
Standard	-
Agency	United Nations Commission on International Trade Law (UNCITRAL), IMF, World Bank
Status	UNCITRAL adopted the *Model Law on Cross-Border Insolvency* in May 1997. It was negotiated among more than 40 countries representing a broad spectrum of differing legal systems and is now under consideration in a number of countries. The IMF published a report *Orderly and Effective Insolvency Procedures* in 1999 that discusses the major policy choices to be addressed by countries when designing an insolvency system. The World Bank is providing information to governments on good practices for reform of insolvency systems and institutional development, including the role of specialist bankruptcy courts. Discussions are underway with the International Bar Association and multilateral organisations on an initiative to develop guidelines for sound insolvency law in developing countries and incentives for debtors and creditors to utilise insolvency mechanisms.
Guidance for Implementation	-
Area	**Corporate Governance**
Standard	***Principles of Corporate Governance***
Agency	Organisation for Economic Cooperation and Development (OECD), World Bank
Status	Endorsed by the OECD Ministerial Meeting in May 1999.
Guidance for Implementation	A co-operative framework has been established between the OECD and the World Bank to promote a sustained, global policy dialogue and co-ordinate the provision of technical assistance as needed, including expert advice on best practices. The framework is structured around a Global Corporate Governance Forum and several regional Round Tables which will produce white papers on corporate governance reforms in the regions using the OECD Principles as a point of reference.

Area	**Accounting**
Standard	***International Accounting Standards (IAS)***
Agency	International Accounting Standards Committee (IASC)
Status	A total of 39 IAS have been promulgated by the IASC to-date. The BCBS has identified and is evaluating in its Accounting Task Force the standards of interest for bank supervisors. IOSCO is evaluating whether a set of core IAS can be used by issuers undertaking cross-border securities offerings and listings. The IAIS is reviewing the suitability of IAS for the insurance industry. The International Federation of Accountants (IFAC) is formulating accounting standards for the public sector based on the IAS. This is expected to be completed by 2001.
Guidance for Implementation	
Area	**Auditing**
Standard	***International Standards on Auditing (ISA)***
Agency	International Federation of Accountants (IFAC)
Status	ISA and Audit Practice Statements have been formulated by IFAC through its International Auditing Practices Committee (IAPC).
Guidance for Implementation	
Area	**Payment and Settlement**
Standard	***Core Principles for Systemically Important Payment Systems***
Agency	Committee on Payment and Settlement Systems (CPSS)
Status	A consultative document was issued by the CPSS in December 1999.
Guidance for Implementation	The CPSS is working on how the principles can be interpreted and applied in different contexts.
Area	**Financial Crime and Money Laundering**
Standard	***The Forty Recommendations of the Financial Action Task Force (FATF)***
Agency	FATF
Status	Issued by FATF in April 1990 and modified in 1996.
Guidance for Implementation	During the period 1990-95, FATF has elaborated various *Interpretive Notes* designed to clarify the application of specific Recommendations.

Area	**Banking Supervision**
Standard	***Core Principles for Effective Banking Supervision***
Agency	Basel Committee on Banking Supervision (BCBS)
Status	Issued by the BCBS in September 1997 and endorsed by the international financial community during the annual meeting of the IMF and World Bank in October 1997.
Guidance for Implementation	A *Core Principles Methodology* that provides detailed criteria for assessing observance of the Core Principles was released in October 1999.
Area	**Securities Regulation**
Standard	***Objectives and Principles of Securities Regulation***
Agency	International Organisation of Securities Commissions (IOSCO)
Status	Issued by IOSCO in September 1998.
Guidance for Implementation	A detailed self-assessment methodology is being developed by IOSCO with inputs from international financial institutions; it is expected to be completed in May 2000.
Area	**Insurance Supervision**
Standard	***Insurance Supervisory Principles***
Agency	International Association of Insurance Supervisors (IAIS)
Status	Issued by IAIS in September 1997.
Guidance for Implementation	A *Core Principles Methodology* is being developed by IAIS in collaboration with international financial institutions; it is expected to be completed by April 2000.
Area	**Financial Conglomerate Supervision**
Standard	***Supervision of Financial Conglomerates***
Agency	Joint Forum on Financial Conglomerates(BCBS, IOSCO, IAIS)
Status	Issued by the Joint Forum in February 1999.
Guidance for Implementation	-

Annex D

Progress on Assessment of Observance of Standards

1. This annex provides an overview of ongoing efforts by the international financial institutions (IFIs) and standard-setting bodies to assess observance of international standards.

International Monetary Fund (IMF)

2. The IMF has developed an assessment framework for observance of standards and has accumulated the most experience in this area.

- The joint Bank-Fund *Financial Sector Assessment Programme (FSAP)* is the primary vehicle for the assessment of financial sector standards in the Fund and the Bank. It is aimed at assessing financial sector vulnerabilities and identifying developmental priorities, which involves in part an assessment of various financial sector standards. The FSAP is a collaborative effort involving a range of national agencies and standard-setting bodies.. The FSAP pilot programme has already finalised assessments for four economies and eight more are close to completion.

- The experimental *Reports on the Observance of Standards and Codes (ROSCs)* assemble assessments of standards across a range of areas, including financial sector standards assessed in the context of the FSAP as well as those covering data dissemination and fiscal transparency. ROSC modules provide a description of country practice in a particular area along with an assessment of the extent to which these practices are consistent with the relevant standard in that area. Several ROSCs are undertaken in collaboration with the World Bank and in consultation with other standard-setting bodies. Nearly 50 ROSC modules covering 15 economies have been completed to-date, covering a range of industrial, emerging market and developing economies. Between one and seven standards have been assessed in each economy. In addition, more than 60 modules involving 18 economies are currently underway. Publication of these assessments remains voluntary, but the bulk of the completed assessments have been released and are available on the IMF's website.

3. ***Financial Sector Assessment Programme (FSAP)***. The objective of the FSAP is to help countries identify likely vulnerabilities within their financial systems and assist them in developing appropriate policy responses. It provides the Bank and the Fund with a common platform for policy advice and technical assistance, and national authorities with a strategic framework within which to undertake measures to strengthen their financial systems.

4. The FSAP has been set up to operate for a year from May 1999, during which approximately 12 country assessments are to be carried out. The pilot FSAP has involved voluntary participation by countries in the context of the Fund's *Article IV Consultation* process. The issue of whether the FSAP should become a fixed part of the Article IV process will be considered at the time of completion of the pilot stage.

5. Each FSAP mission provides a detailed aide-memoire which is left with the national authorities, covering the mission's assessment of the strengths, weaknesses, risks, and vulnerabilities in the financial systems, including an assessment of the extent to which a country observes and is progressing towards implementation and observance of international standards relevant for sound financial systems. This report is confidential.

6. The FSAP report provides useful inputs to other assessments within the Fund and Bank. These include the:

- Fund's *Reports on Observance of Standards and Codes (ROSCs),* discussed below;
- Fund's *Financial System Stability Assessments (FSSAs)*, which will contain less specific institutional information than the FSAP report and instead focus on financial system issues of significance for macroeconomic performance and policies, and will become part of the Fund's staff papers presented for discussion by the Executive Board; and
- the financial sector component of the Bank's *Social and Structural Reviews (SSRs).*

7. ***Reports on Observance of Standards and Codes (ROSCs)***. The ROSCs, previously called *Transparency Reports*, were instituted in response to the G22 proposal that the IMF, in the context of its Article IV surveillance process, should prepare and publish reports that summarise the extent to which economies observe internationally recognised standards. Efforts to-date have concentrated on standards within the direct operational focus of the IMF, namely data dissemination; fiscal, monetary and financial policy transparency; and banking supervision. The World Bank has joined the Fund in this exercise and has begun to experiment with the preparation of ROSC modules. To-date, modules prepared have comprised two elements: (a) a description of country practice; and (b) a commentary by IMF staff on the extent to which these practices are consistent with the relevant standard.

8. A *modular approach,* whereby each standard is assessed separately, is being used to prepare assessments, recognising that attempting to simultaneously assess a range of standards is too resource-intensive for all parties involved, and can give rise to co-ordination problems. This modular approach will allow assessments to be prepared sequentially for a range of standards, thereby building up over time a picture of an economy's observance of standards. It also allows efforts to be better focused on priority areas within and across economies. In addition, outreach programmes directed at private market participants have also been undertaken to assess the format and value of the published summary assessments.

9. The Fund has looked to the Bank and other standard-setting bodies to prepare assessments in areas beyond the Fund's mandate, envisioning a *shared ownership framework* whereby different international institutions take primary responsibility for preparing assessments in different areas, consistent with their mandates and expertise. It has been agreed that the Bank will experiment with undertaking assessments of accounting, auditing, corporate governance, and possibly, insolvency regimes, in a range of countries. There has also been regular contact with the BCBS, CPSS, IAIS, and IOSCO on issues related to the development, implementation, and observance of standards in their respective areas.

10. Thus far, two rounds of experimental assessments have been completed and there has been encouraging feedback from a number of participating national authorities and market participants on the value of these exercises. A third round of experimental assessments has already commenced and a number of IMF members have volunteered to participate.

World Bank

11. The most important initiatives of the World Bank in assessing observance of standards are the two programmes being undertaken in collaboration with the IMF: the joint FSAP and the ROSC. As a complement to these efforts, the Bank is also expanding its efforts on corporate governance, accounting and auditing, and insolvency regimes.

12. With respect to corporate governance, the Bank has developed a template for corporate governance assessments building on earlier work, which is being discussed with the OECD, IMF and others, and which will be used for a pilot programme of assessments as part of the joint ROSC exercise with the IMF. The templates focus on equity markets, and, in particular, on shareholder rights and the role of boards in publicly traded corporations.

13. The Bank is refining its *Country Financial Accountability Assessments* to cover both private and public sector accounting and auditing more thoroughly. Once finalised, these assessments will be used for a pilot programme of assessments in collaboration with others. As more country assessments are completed, their results will be more systematically incorporated in the Bank's *Country's Assistance Strategies* including technical and financial support.

14. In the area of insolvency regimes, priority is being given to developing a set of principles and guidelines to underlie successful systems. An initial draft will be issued shortly, which will be revised to reflect the outcome of regional workshops planned over the next six months, as well as wider international consultation. In parallel, an assessment matrix is being developed for subsequent use in a series of pilot assessments.

Basel Committee on Banking Supervision (BCBS)

15. The BCBS initiated in April 1998 a self-assessment survey on observance of the *Core Principles for Effective Banking Supervision*. The questionnaires were completed by 124 jurisdictions, but the quality of responses was uneven. Based on a review of this self-assessment exercise as well as preliminary external assessments of countries' observance of the Core Principles carried out by the IMF and World Bank, the BCBS has developed a *Core Principles Methodology*. The Methodology is designed for use in multiple contexts: (a) self-assessments by bank supervisors themselves; (b) peer review conducted for instance within regional groupings of bank supervisors; (c) reviews conducted by private third parties such as consulting firms; and (d) reviews performed in the context of IMF surveillance or World Bank lending operations.

16. The BCBS will invite jurisdictions to re-assess their observance of the Core Principles based on the Methodology. It has also requested the IMF, World Bank, and regional supervisory groups to undertake external assessments of jurisdictions' observance of the

Core Principles using the Methodology. These assessments are currently being carried out in separate missions or as part of technical assistance, but could eventually be part of the Fund/Bank's FSAP.

International Asssociation of Insurance Supervisors (IAIS)

17. Following the adoption of the *Insurance Core Principles* by the IAIS' membership, a self-assessment survey was carried out, to which half the membership responded. The IAIS has since established a task force to develop a Methodology for assessing observance of the Core Principles. This is targeted for completion by April 2000.

18. The IAIS works with international financial institutions like the IMF and World Bank to develop modalities for using the Methodology for assessing observance with the Core Principles. The IAIS also supports regional training programmes to foster implementation, develops text books and case materials to help insurance supervisors implement the Core Principles, and draws up a list of qualified insurance experts who could become part of the external assessment teams under the shared ownership framework of the Fund's ROSC initiative.

International Organisation of Securities Commissions (IOSCO)

19. Following the promulgation of its *Objectives and Principles of Securities Regulation,* IOSCO has established a task force to promote their implementation and is preparing a handbook on the methodology for assessing observance of the Principles. To-date, the task force has conducted three self-assessment surveys in this respect: a general survey on the level of observance in broad terms and two detailed surveys for securities regulators and issuers respectively. Results of these surveys are expected by April 2000. The task force is also developing a practical mechanism for providing assistance and co-operation to the IMF, World Bank, and OECD in using the Principles in their programmes for assessing economies' financial systems. It is also evaluating the efficacy of self-assessments vis-à-vis peer reviews.

Organisation for Economic Co-operation and Development (OECD)

20. The OECD has been working with the World Bank to use the *Principles of Corporate Governance* as a framework for dialogue and consultation with emerging market and transition economies with a view to improving corporate governance practices. In this connection, Round Table meetings have been organised in various regions.

Annex E

A Taxonomy for International Standards

1. The relevance of a standard depends on the nature of the problems to be measured or benchmarked. The relevance of some standards may also depend on varying circumstances, including the stage of development of market economies. Standards are also interdependent. For example, capital adequacy standards depend on the legal and accounting standards that measure economic value.

2. Standards can be classified in many different ways. Conceptually, it may be helpful to classify standards by scope, specificity and degree of formal international acceptance. The taxonomies presented here are necessarily simplifications for helping to understand the nature of standards. In practice, the distinctions are not as sharp and many of the standards are interrelated. It is also worth noting that in rapidly changing markets, standards are continually evolving and that implementing obsolete standards could impede financial innovation and development.

3. ***Scope***. The scope of standards may be divided along two axes:

   - _Sectoral_. These cover the economic and institutional sectors, for which many standards have been developed, such as the government and central bank, the banking, securities, insurance and other financial intermediaries sectors, and the corporate sector.
   - _Functional_. Within each sector, standards have generally been developed along functional lines, covering areas such as governance, accounting, disclosure and transparency, capital adequacy, regulation and supervision, information sharing, risk management, payment and settlement, business ethics, etc.

   This taxonomy reveals that there are gaps in standards which may impact on financial stability, such as in areas of public sector accounting, governance and legal standards for insolvency. In view of resource constraints, policymakers must consider prioritisation and sequencing when implementing standards. The order of priority can be represented on a third axis.

4. ***Specificity***. From a practical implementation perspective, a useful distinction among standards is in terms of their degree of specificity:

   - _Principles_: These are fundamental tenets pertaining to a broad policy area. Principles are usually set out in a general way and therefore offer a degree of flexibility in implementation to suit country circumstances, e.g. the Basel Committee's *Core Principles for Effective Banking Supervision*, IOSCO's *Objectives and Principles of Securities Regulation*, IAIS' *Insurance Supervisory Principles*, and CPSS' *Core Principles for Systemically Important Payment Systems*.
   - _Practices_: These are more specific and spell out the practical application of the principles within a more narrowly defined context, e.g. the Basel Committee's *Sound Practices for Loan Accounting*, IOSCO's *Operational and Financial Risk Management Control Mechanisms for Over-the-Counter Derivatives Activities of Regulated Securities Firms*, and IAIS' *Supervisory Standards on Licensing*.

- <u>*Methodologies*</u>: These provide detailed guidance on steps to be taken or requirements to be met and are specific enough to allow a relatively objective assessment of the degree of observance, e.g. the IMF's *Special Data Dissemination Standard*.

5. ***Formal International Acceptance or Legitimacy***. Standards can also be classified into:

- those which most jurisdictions have endorsed under various international institutional arrangements, e.g. the IMF's codes of good practices on fiscal transparency and transparency in monetary and financial policies, the core principles by the BCBS, IOSCO and IAIS; and
- those which have not as yet gained widespread international acceptance or endorsement, e.g. accounting, legal and public governance standards.

<u>Annex F</u>

Some Preliminary Feedback on Market Incentives

1. The Task Force undertook a quick feedback gathering exercise to assess the extent to which: (a) market participants were familiar with standards; (b) they were interested in observance of standards; and (c) used information on observance of standards in their risk assessments. The IMF has also undertaken a small outreach programme to solicit feedback from the private sector and regulatory authorities on its ROSCs. The assessment presented below is based on a very narrow sample and is preliminary but could be indicative of the challenges with making market incentives work. It should also be noted that the promulgation of most standards is fairly recent and it would take time for them to be fully disseminated and their significance understood by the private sector.

2. ***Is the Market Familiar with Standards?*** Market participants appear to lack familiarity with many international standards. The standards that they seem to be aware of were limited to the IMF's Special Data Dissemination Standard (SDDS) and Codes of Good Practices on Fiscal Transparency and Transparency in Monetary and Financial Policies, and the Basel Committee's Capital Accord and Core Principles on Banking Supervision. This is not surprising as many standards were developed only recently and some are still in the final stages of gaining general acceptance.

3. ***Is the Market Interested in Standards?*** Market participants have indicated they welcome the general promulgation of standards and policies which encourage their implementation and transparency of information. However, standards do not seem to figure very prominently in the range of factors that private sector market participants are specifically interested in. The following points emerged from the limited feedback to-date:

   - *<u>Economic and financial fundamentals</u>* are the most important considerations for market decisions. Implementation of standards cannot, in itself, eliminate risks and therefore would not necessarily raise an economy's sovereign rating or increase its attractiveness as an investment destination.

   - The relevance of individual standards to market participants is a function of the *<u>particular problems facing an economy</u>*. To the extent that problems were predominantly macroeconomic in nature, standards like the SDDS seem to matter. If the problems were mainly in the banking industry, the Basel Core Principles are relevant.

   - There is relatively stronger interest in *<u>accounting and disclosure</u>* standards since the value of much of the data that market participants analysed depended on underlying accounting and disclosure practices. The absence of standards for the quantification of the potential exposures of derivatives was cited as a significant problem.

4. ***Does the Market Use Information on Observance of Standards?*** In general, market participants that Task Force members spoke to do not appear able to evaluate the specific costs of non-observance of standards nor how to measure them analytically and

use them in a transparent manner in their risk assessments. The following points were made in this regard:

- Market participants use a range of economic and financial indicators – mostly *quantitative* – in their risk assessments. They expressed less interest in using information on observance of standards *per se* which is only a means to achieving sound financial systems as reflected in the more quantitative indicators they monitor. While market participants (in particular credit rating agencies) did take account of qualitative factors in their risk assessments, these pertained mainly to factors like political stability, rule of law, predictability of policymaking, and degree of state intervention in markets, rather than observance of standards.

- There are indications, however, that non-observance of standards is *used indirectly* in credit assessments. For example, to the extent that firms or banks do not provide financial statements in line with internationally accepted accounting standards, they might have less access to funds or face higher risk premiums. If an economy does not subscribe to the SDDS, it raises the suspicion that it has something to hide, with similar implications for the availability and pricing of funds.

- Not surprisingly, market participants generally seem to welcome any information on economies' observance of standards. They found the IMF's experimental ROSCs a useful reference document and particularly liked the independent assessment and commentary. However, they were less enthusiastic about the value of these reports to their risk assessments because the reports did not sufficiently analyse the *definition and quality* of the information provided.

- Market participants also expressed a strong preference for *easy-to-use summary documents* which are less detailed and shorter than the experimental ROSCs.

Annex 7

Official Incentives Currently in Place and Under Consideration

Incentives Currently in Place

1. The Executive Board of the International Monetary Fund decided in April 1999 that among the factors that the Fund will consider in committing financing to a member of the Fund under the *Contingent Credit Line (CCL)* facility, it will take into account the extent of the member's adherence to relevant internationally-accepted standards and, in particular, whether the members have subscribed to the *Special Data Dissemination Standard* and are judged to be making satisfactory progress towards meeting its requirements.[21]

2. Steps to implement and observe specific standards have been included in some recent IMF country programmes.

Incentives Under Consideration

3. The Basel Committee on Banking Supervision has proposed in its *A New Capital Adequacy Framework* – a consultative paper issued for comments by 31 March 2000 – the following incentives with regard to observance of standards:

   - To be eligible for claims on a sovereign to receive a risk weighting below 100%, the sovereign must subscribe to the IMF's *Special Data Dissemination Standard*.
   - Claims on a bank will only receive a risk weighting of less than 100% if the banking supervisor in that country has implemented, or has endorsed and is in the process of implementing, the BCBS' *Core Principles for Effective Banking Supervision*.
   - Claims on a securities firm may only receive a risk weighting of less than 100% if that firm's supervisor has endorsed and is in the process of implementing IOSCO's *Objectives and Principles of Securities Regulation*.

   These proposals will be discussed by the BCBS in end-March 2000.

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21 To-date, the CCL has not been drawn by any economy. Proposals to use assessments of standards as input for assessing eligibility for financial assistance (e.g.the CCL) has triggered a number of concerns among some IMF members.

Annex 8

Additional Standards Proposed for the Compendium of Standards

Data Dissemination

- IMF Manual of Monetary and Financial Statistics (5th Edition)
- IMF Balance of Payments Manual

Accounting

- International Accounting Standards

Auditing

- International Standards on Auditing

Market Integrity

- The Forty Recommendations of the Financial Action Task Force on Money Laundering
- Ten Key Principles for the Improvement of International Co-operation Regarding Financial Crime and Regulatory Abuse

Market Functioning

- How Should We Design Deep and Liquid Markets

Banking

- Sound Practices for Banks' Interactions with Highly-Leveraged Institutions
- Principles for the Management of Credit Risk
- Operational Risk Management
- Risk Management for Electronic Banking and Electronic Money Activities
- Principles on the Management of Interest Rate Risk
- Risk Management Guidelines for Derivatives
- Recommendations for Public Disclosure of Trading and Derivative Activities of Banks and Securities Firms

Insurance

- Principles for the Conduct of Insurance Business
- Guidance on Insurance Regulation and Supervision for Emerging Market Economies
- Model Memorandum of Understanding
- Supervisory Standard on Asset Management by Insurance Companies

Financial Conglomerates

- Supervision of Financial Conglomerates
- Intra-Group Transactions and Exposure Principles
- Risk Concentration Principles

Annex 9

Proposed Content and Structure of the Compendium of Standards

PART 1: KEY STANDARDS FOR SOUND FINANCIAL SYSTEMS

Policy Areas	**Key Standards**[22]	**Issued by**
Macroeconomic Fundamentals		
Monetary and financial policy transparency	Code of Good Practices on Transparency in Monetary and Financial Policies	IMF
Fiscal policy transparency	Code of Good Practices in Fiscal Transparency	IMF
Data dissemination	Special Data Dissemination Standard/ General Data Dissemination System[23]	IMF
Institutional and Market Infrastructure		
Insolvency	[24]	World Bank
Corporate governance	Principles of Corporate Governance	OECD
Accounting	International Accounting Standards (IAS)[25]	IASC[26]
Auditing	International Standards on Auditing (ISA)[25]	IFAC[26]
Payment and settlement	Core Principles for Systemically Important Payment Systems	CPSS
Market integrity	The Forty Recommendations of the Financial Action Task Force	FATF
Financial Regulation and Supervision		
Banking supervision	Core Principles for Effective Banking Supervision	BCBS
Securities regulation	Objectives and Principles of Securities Regulation	IOSCO
Insurance supervision	Insurance Supervisory Principles	IAIS

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22 While the key standards are categorised here by policy area, some of them are relevant to more than one area.

23 Economies with access to international capital markets could be encouraged to subscribe to the more stringent SDDS and all other economies could be encouraged to adopt the GDDS

24 The World Bank is co-ordinating a broad-based effort, involving relevant institutions and legal experts, to develop a set of principles and guidelines on insolvency regimes. The United Nations Commission on International Trade Law (UNCITRAL), which adopted the *Model Law on Cross-Border Insolvency* in 1997, will help facilitate implementation.

25 The IAS and ISA are used in some jurisdictions but are not endorsed by all jurisdictions. The IAS are currently being reviewed by the BCBS, IAIS, and IOSCO.

26 The International Accounting Standards Committee (IASC) and International Federation of Accountants (IFAC) are distinct from the other standard-setting bodies in that they are private sector bodies

PART 2: STANDARDS FOR SOUND FINANCIAL SYSTEMS

[Standards currently not in the Compendium are in italics.]

MACROECONOMIC FUNDAMENTALS

Monetary and Financial Policy Transparency

- Code of Good Practices on Transparency in Monetary and Financial Policies

Fiscal Policy Transparency

- Code of Good Practices on Fiscal Transparency

Data Dissemination

- Special Data Dissemination Standard (SDDS)
- General Data Dissemination System (GDDS)
- *IMF Manual of Monetary and Financial Statistics (Fifth Edition)*
- *IMF Balance of Payments Manual*

INSTITUTIONAL AND MARKET INFRASTRUCTURE

Insolvency

[Standards in this area are currently being developed.]

Corporate Governance

- Principles of Corporate Governance

Accounting

- *International Accounting Standards*

Auditing

- *International Standards on Auditing*

Payment and Settlement

General

- Core Principles for Systemically Important Payment Systems

Banking

- Settlement Risk in Foreign Exchange Transactions
- Real Time Gross Settlement Systems
- Report of the Committee on Inter-Bank Netting Schemes of the Central Banks of the Group Of Ten Countries (“The Lamfalussy Report”)

Securities

- Delivery Versus Payment in Securities Settlement Systems
- OTC Derivatives: Settlement Procedures and Counterparty Risk Management
- Clearing Arrangements for Exchange-Traded Derivatives

Market Integrity

- *The Forty Recommendations of the Financial Action Task Force on Money Laundering*
- *Ten Key Principles for the Improvement of International Co-operation Regarding Financial Crime and Regulatory Abuse*

Market Functioning

- *How Should We Design Deep and Liquid Markets*

FINANCIAL REGULATION AND SUPERVISION

Banking Supervision

General Supervision

- Core Principles for Effective Banking Supervision
- *Sound Practices for Banks' Interactions with Highly-Leveraged Institutions*

Capital Adequacy

- International Convergence of Capital Measurement and Capital Standards
- Overview of the Amendment to the Capital Accord to Incorporate Market Risks
- Amendment to the Capital Accord to Incorporate Market Risks
- Supervisory Framework for the Use Of "Back-Testing" in Conjunction with the Internal Models Approach to Market Risk Capital Requirements

Cross-Border Supervision

- Principles for the Supervision of Banks' Foreign Establishments (The "Basel Concordat")
- Minimum Standards for the Supervision of International Banking Groups and their Cross-Border Establishments
- The Supervision of Cross-Border Banking

Disclosure and Transparency

- Enhancing Bank Transparency
- Sound Practices for Loan Accounting and Disclosure
- *Recommendations for Public Disclosure of Trading and Derivatives Activities of Banks and Securities Firms [see also under Disclosure and Transparency within Securities Regulation]*

Risk Management

- Framework for Internal Control Systems in Banking Organisations
- *Principles for the Management of Credit Risk*
- *Operational Risk Management*
- *Risk Management for Electronic Banking and Electronic Money Activities*
- *Principles on the Management of Interest Rate Risk*
- *Risk Management Guidelines for Derivatives*

Securities Regulation

General Regulation

- Objectives and Principles of Securities Regulation
- IOSCO Resolution: Principles for Record Keeping, Collection of Information, Enforcement Powers and Mutual Co-operation to Improve the Enforcement of Securities and Futures Laws

Capital Adequacy

- Methodologies for Determining Minimum Capital Standards for Internationally Active Securities Firms which permit the Use of Models under Prescribed Conditions

Cross-Border Information Sharing

- Guidance on Information Sharing
- Report on Co-operation Between Market Authorities and Default Procedures
- Principles of Memoranda of Understanding

Disclosure and Transparency

- International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers
- *Recommendations for Public Disclosure of Trading and Derivatives Activities of Banks and Securities Firms [see also under Disclosure and Transparency within Banking Supervision]*

Risk Management

- Operational and Financial Risk Management Control Mechanisms for Over-the-Counter Derivatives Activities of Regulated Securities Firms
- Risk Management and Control Guidance for Securities Firms and their Supervisors
- Client Asset Protection

Market Functioning

- Securities Activity on the Internet
- Co-ordination between Cash and Derivative Markets: Contract Design of Derivative Products on Stock Indices and Measures to Minimise Market Disruption
- The Application of the Tokyo Communique to Exchange-Traded Financial Derivatives Contracts
- Principles for the Supervision of Operators of Collective Investment Schemes
- Report on Investment Management Principles for the Regulation of Collective Investment Schemes and Explanatory Memorandum

Insurance Supervision

General Supervision

- Insurance Supervisory Principles (“Core Principles”)
- *Principles for the Conduct of Insurance Business*
- Supervisory Standard on Licensing
- Supervisory Standard on On-Site Inspections

- *Guidance on Insurance Regulation and Supervision for Emerging Market Economies*

Cross-Border Supervision

- Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations ("Insurance Concordat")
- *Model Memorandum of Understanding*

Risk Management

- Supervisory Standard on Derivatives
- *Supervisory Standard on Asset Management by Insurance Companies*

Financial Conglomerate Supervision

General Supervision

- *Supervision of Financial Conglomerates*

Risk Management

- *Intra-Group Transactions and Exposures Principles*
- *Risk Concentrations Principles*