

(Slide 1)

IOSCO: Background, Priorities and Challenges

Jane Diplock AO

Chairman, Securities Commission of New Zealand
Chairman, Executive Committee, IOSCO

Presentation to the ASIC Summer School
Melbourne
Thursday 10 February 2005

(Slide 2)

Introduction

- The International Organisation of Securities Commissions (IOSCO) has become the world's leading forum for discussion of securities market issues and for the setting of international regulatory standards. Its peer organisations are the Basel Committee on Banking Supervision and the International Association of Insurance Supervisors (IAIS). These three are the top tier of regulatory forums in the world's financial markets.
- IOSCO's members are predominantly the national securities regulators of over 100 countries (ASIC and the New Zealand Securities Commission among them). The organisation's broad mission is to promote high standards of regulation so that securities markets everywhere are fair, efficient and sound. IOSCO also facilitates information exchange and cooperation between members, especially where this will protect the integrity of markets and make regulatory enforcement more effective.
- IOSCO has two special strengths: First, the breadth of its membership - this encompasses regulators with responsibility for around 90% of the world's securities markets (and membership is still growing). Second, IOSCO is a consensus-based organisation - its principles and standards reflect the collective wisdom of regulators worldwide. IOSCO proceeds on the core assumption that no one regulatory model is best for all countries but that all benefit from adhering to the same broad principles and benchmarks, and from greater transparency and cooperation between jurisdictions.
- IOSCO has two key constituencies: Its member-regulators, and other bodies in the international financial community. The latter include the International Monetary Fund, the International Bank for Reconstruction and Development, the Financial Stability Forum and various others.

- At this stage of its development, IOSCO has clearly defined priorities. It faces substantial challenges from the globalisation and complexity of securities markets in the 21st Century. We will reflect on these through the presentation - but first some background on the organisation.

(Slide 3)

IOSCO - The Organisation

- IOSCO was formed in 1983 when an existing inter-American regional body of regulators opened its membership to regulators worldwide. The first non-Americans to join were the United Kingdom, France, Indonesia and Korea. Then membership grew rapidly.
- The organisation today has 181 members and associate members, from more than 100 countries. Members range from the Albanian Securities Commission to the Securities and Exchange Commission of Zambia. Along the way, they include the UK's Financial Services Authority, the SEC in the United States and the Financial Services Agency in Japan. As noted before, this is an organisation exceptional for its global participation.
- National securities regulators are full members of IOSCO. Other bodies that also have some securities market responsibilities in their respective jurisdictions are associate members. IOSCO has a permanent General Secretariat based in Madrid with a small staff. IOSCO is funded by the subscriptions of members (currently full membership is 8300 euros annually).
- IOSCO's principal working body is the 19 member Executive Committee, comprising the Chairmen of the organisation's other committees and individuals elected from among the membership of those committees. The Executive Committee is effectively the key decision making group.
- I am currently the Executive Committee Chairman (elected for a two year term at the IOSCO annual meeting, May last year). Alan Cameron, the ASIC Chairman through most of the 1990s, was Executive Committee Chairman during 1994-96.
- IOSCO has two other working committees: The 15-member Technical Committee, which leads most standard setting activity, and the Emerging Markets Committee, a forum of 70 or so regulators with a broad mandate to promote the efficiency of emerging securities and futures markets.
- These two committees each have working groups that focus on particular sets of issues - financial disclosure and accounting, the regulation of secondary markets and of intermediaries, enforcement and information exchange, and investment management.
- The committees are elected from among IOSCO's membership (one vote per full member) and their Chairmen are key figures in the organisation. Current Technical Committee Chairman is Andrew Sheng, Chairman of the Securities

and Futures Commission of Hong Kong. (Note: David Knott, then-Chairman of ASIC, was Technical Committee Chairman during 2000-03). The Emerging Markets Committee is chaired by Dogan Cansizlar, Chairman of the Capital Markets Board of Turkey.

- IOSCO has also four Regional Committees for discussion and information sharing on issues of particular interest in each region - the Americas, Europe, Africa and the Middle East, and Asia Pacific. The latter, obviously including Australia and New Zealand, has 21 members and is chaired by Koh Yong Guan, the Managing Director of the Monetary Authority of Singapore. We will look more at the Regional Committees later.
- The Basel Committee and IAIS are important peer organisations. Since 1996, the three have formally cooperated through the Joint Forum. The Forum works on regulatory issues that span securities markets, banking, and insurance - and that is an increasing workload.
- It is important also to take account of the interests and views of Self Regulatory Organisations (SROs). IOSCO has an SRO Consultative Committee, with membership drawn mainly from major securities exchanges worldwide (including the ASX, SFE Corporation, and the Australian Financial Markets Association).
- IOSCO committees and their working groups meet periodically through the year and the organisation has an annual conference - this year to be held in Sri Lanka on 4-7 April. (The year 2000 conference was held in Sydney). The annual conference includes the once-yearly meeting of the IOSCO Presidents Committee, on which sit the presidents of all member regulators.
- The General Secretariat, headed by Philippe Richard, provides some professional support to the research, analysis, and report writing done by the Committees and their working groups. Much support is also contributed by the professional staff of member-regulators. The General Secretariat has 10 staff, who are made available to advise individual members on request. Resourcing is a major issue within IOSCO and we are looking at how to augment this in 2005 - addition of “virtual staff” within member organisations is probably part of the solution.
- It should be clear by now that IOSCO is a busy organisation! To look back at 2004, major work programmes included:
 - A Task Force on strengthening capital markets against financial fraud;
 - A set of fundamental guidelines for the Codes of Conduct of credit rating agencies;
 - A ground-breaking forum in New York with US corporate leaders to explore critical issues like international auditor oversight and the rights of shareholders in the global securities market;
 - Major reports on credit risk transfer, outsourcing of financial services, and financial disclosure standards produced jointly by IOSCO and the Joint Forum.

Various other outputs are in the IOSCO pipeline, all of which can be traced back to IOSCO's core set of Principles for securities regulation - to which we now turn.

(Slide 4)

IOSCO Principles

- All current principles and standard setting relates back to a core piece of IOSCO work during the 1990s, the *Objectives and Principles of Securities Regulation*. This significant document was adopted by IOSCO's annual meeting in May 1998 after a careful process of design and consultation among members.
- The IOSCO Principles establish three core Goals for all regulation:
 - protection of investors from misuse of assets, insider trading and other forms of fraudulent or manipulative practice;
 - ensuring that securities markets are fair, efficient and transparent;
 - reduction of systemic risks.
- Towards achieving these Goals, regulators and others should create structures and follow practices based on 30 Principles, which together cover the these areas:
 - principles relating to regulators and their enforcement of securities regulations;
 - principles for self regulation and cooperation in regulation;
 - principles relating to issuers, collective investment schemes, market intermediaries; and
 - principles relating to secondary markets.
- The Principles establish clear high level benchmarks for the regulatory system in any jurisdiction. Here are four examples:
 - the regulator should be operationally independent and accountable in the exercise of its functions and powers;
 - the regulator should have comprehensive inspection, investigation and surveillance powers;
 - the regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers;
 - there should be full, timely and accurate disclosure of financial results and other information that is material to investors' decisions.
- The IOSCO Principles are available to everyone on the www.iosco.org website. Professional staff in national securities regulatory bodies worldwide should be very familiar with them. Indeed, all IOSCO members have committed to implementing the Principles. There has been a strong expectation since 1998 that members will confirm that their regulatory systems adhere to the Principles and work to close any gaps in adherence.

(Slide 5)

- The IOSCO Principles are obviously useless unless they are actually implemented, i.e. applied in the structures and practices of regulators. The organisation has recognised that by establishing a standard methodology for objectively assessing whether and how well the Principles are implemented in any jurisdiction. The IOSCO annual meeting in October 2003 adopted this Assessment Methodology and it is now a tool for members to pick up and use.
- We also have an IOSCO Principles Assessment and Implementation Program for helping jurisdictions to use the methodology and to design follow up action plans to ensure the Principles are implemented over time. This program is at a pilot stage in four national jurisdictions, one in each of IOSCO's four regions.
- The organisation's focus on practical support for members is one of its strengths. This is largely a matter of information sharing and expertise transfer between jurisdictions, including the transfer from more developed markets to emerging markets. This is particularly important given the diversity among IOSCO members and the difficulties created by differences in language, culture, legal systems and so on.
- Implementation of the IOSCO Principles continues to be IOSCO's highest priority. We are confident the structures and tools are in place to encourage member-regulators to complete assessments and pursue reforms where necessary, although it would certainly help if IOSCO had more resources to assist the process. There are some compelling drivers for implementing the Principles in jurisdictions worldwide.

Drivers for Principles Implementation

- First, there is genuinely strong commitment to the Principles among IOSCO members. This is a reflection of their origins in the collective wisdom of members and the care taken not to make the Principles overly prescriptive. IOSCO's internal constituency recognises that these are a fundamental set of international benchmarks to which all should aspire.
- Second, IOSCO and its members face strong expectations from the organisation's external constituency, that is, other bodies in the international financial community looking for progress on Principles implementation as part of the solution to problems in the global economy. The World Bank and the IMF have, for example, picked up the Principles as part of a benchmarking framework in their Financial Sector Assessment Program.
- We are very aware of the focus put on implementation of the Principles by the Financial Stability Forum and others. To some extent, tangible progress with implementation in more of the jurisdictions covered by IOSCO is an acid test for the organisation. The Principles have been applauded but there is no room for IOSCO to rest on its laurels. Retention of the organisation's high status as a standard setter will depend on further progress with implementation. If we are seen to falter, other organisations who share a stake in the same issues

might well decide to start standard setting themselves. IOSCO faces a healthy competitive pressure of this sort.

- The underlying driver for the IOSCO Principles is, of course, the growth of global securities markets, accompanied by an increasing incidence of financial wrongdoing among market participants and the appearance of international regulatory failure. Everyone accepts that regulators, working within their domestic jurisdictions and cooperating across borders, must keep abreast of the challenges posed by, for example, complex international corporate structures and accounting vehicles. The Parmalat Group collapse in late 2003 is the most recent high profile case to bring these issues to the fore internationally.
- Parmalat was the catalyst for IOSCO's Technical Committee to form the Task Force looking at the threat of fraud to capital markets. Investigation and legal proceedings over what exactly happened in the Italian food group will continue for a while yet but the allegations include systematic falsification of accounts, the misuse of international corporate structures, lapses in audit oversight and inadequate disclosure of risks to Parmalat investors. The latter have lost billions of Euros.
- The allegations of wrongdoing are international and touch major names in world banking and auditing. Parmalat will galvanise regulatory reform in Europe, as the Enron collapse did in the United States. Such crises give additional impetus to implementation of the IOSCO Principles and to other current IOSCO initiatives.
- We are now looking at risk assessment to try to anticipate problems before they occur and ensure that standard setting outcomes are timely and relevant. For example, our standard setting in particular areas like Credit Rating Agencies and auditor oversight and independence (principles endorsed in 2003).
- IOSCO has a strong focus on encouraging greater cooperation between regulators especially for enforcement purposes. Our work in this area has a particularly high priority for pulling the Principles into the structures and practices of members.

(slide 6)

IOSCO MMOU and Cross Border Cooperation

- The *IOSCO Multilateral Memorandum of Understanding concerning Consultation and Cooperation and the Exchange of Information* (the IOSCO MMOU) was endorsed at IOSCO's annual meeting in May 2002. It is a comprehensive response to the growth in financial wrongdoing across borders. The IOSCO MMOU has certainly proved useful already in some of the work of the Securities Commission in New Zealand.

- The IOSCO MMOU defines the legal authority that individual regulators must have in order to engage in efficient and timely cross-border cooperation and information exchange. It sets down the conditions under which these exchanges should occur.
- We expect the IOSCO MMOU to create an expanding network of regulators who cooperate as a matter of routine for seamless international enforcement of securities laws and regulations.
- To date, 26 IOSCO members have become signatories after a rigorous screening and approvals process under the direct oversight of a group comprising the Chairmen of the Executive, Technical, and Emerging Markets Committees. Application for signatory status starts with completion of a detailed questionnaire - the questions look closely at the legal authority and operating capabilities of the applying regulator.
- Signatories are indeed making regular use of the IOSCO MMOU. Experience to date has made us confident that it is a highly effective tool for promoting international cooperation and effective enforcement.
- However, more IOSCO members must join the IOSCO MMOU. Like all networks, it becomes more powerful when there are more participants. In addition to the 26 (Australia and New Zealand included), a further 25 members have applied for signatory status. Most of the applications are at various stages of the screening process. In four cases, regulators have been listed as under appendix B of the IOSCO MMOU which means they are formally committed to removing the legal obstacles that prevent them becoming signatories.
- The rate of applications and approvals has slowed over the past year. In 2005, we are injecting a sense of urgency into expansion of the IOSCO MMOU network. In April, the annual meeting will look at proposals to establish a deadline for all IOSCO members to become signatories or to at least commit themselves to meeting the criteria and to listing under appendix B. It is also proposed that the IOSCO MMOU gain explicit recognition as the international standard for enforcement related cooperation and information exchange.
- Various members face impediments in terms of their existing legal authority and organisational capabilities to obtain, hold, and pass on financial information. In respect of some signatories, the existence of the IOSCO MMOU has itself been sufficient for the national legislature to endow its regulator with sufficient additional powers. But IOSCO recognises the extent of change that the IOSCO MMOU requires in other jurisdictions.
- An IOSCO MMOU Assistance Program was introduced in late 2003 to provide individual members with expert support in completing the questionnaire and in taking the steps necessary to remove impediments to their becoming signatories over time.

- In 2005, we expect to see additional IOSCO resources channelled into the Assistance Program. We are also looking for members to help expedite applications and approvals by sharing their experience and advice on a bilateral or multilateral basis. The organisation's Regional Committee structure is especially important in this regard.

(Slide 7)

The Importance of Regional Committees

- IOSCO has four Regional Committees. These committees have increasing importance in the context of Principles implementation, expanding the IOSCO MMOU network, and our work programmes generally. The Committees have particular value because of the additional level of common interest and concern that exists between members in each region.
- The Asia-Pacific Regional Committee, for example, includes the Securities and Exchange Commission of India, the China Securities Regulatory Commission, and the Financial Services Agency of Japan, as well as 18 other bodies (among them ASIC and the New Zealand Securities Commission). This is a unique forum for discussion and cooperation between a diverse set of regulators who have increasingly common interests as their national securities markets evolve together.
- The Committees are well positioned to facilitate information exchange and expertise transfer, especially between developed and emerging markets. We see this is as especially important to encouraging and supporting more national regulators to apply under the IOSCO MMOU and to undertake the reforms that might be necessary for signatory status. It is, after all, likely that the greatest need for enforcement-related cooperation will be between neighbouring jurisdictions or at least between those in the same region.
- We should not underrate the importance of informal contact between the personnel of different regulators when it comes to increasing their willingness to cooperate across borders. The Committees are an excellent vehicle for such relationship building.
- IOSCO's mission encompasses the early detection of emerging market trends and problems. This is necessary if the organisation is to be proactive in raising awareness of issues and setting relevant standards. The regions are an excellent location for IOSCO to be collecting intelligence from the markets and from the front line of regulation, and to be feeding it through to the Technical Committee for further research, consultation, and international action.

(Slide 8)

The Challenges Facing IOSCO

- To sum up, we will review the challenges facing IOSCO now and into the future. There are three areas of challenge, each touched on already.
- *First, organisational effectiveness.* We need to ensure the organisation remains the world's principal forum on securities regulation because it has a high level of engagement from members and because the most pressing international issues are on top of its agenda. The challenges include:
 - increase the quality and timeliness of response when market crises occur;
 - promote the organisation's ability to detect emerging market trends and problems;
 - protect and enhance the organisation's reputation with external constituents (loss of standing would weaken IOSCO's ability to be effective);
 - optimise members' input of information and wisdom to process for setting new principles and standards;
 - enhance assistance to members;
 - develop the role of Regional Committees in facilitating cooperation and expertise transfer between members; and
 - to be proactive on these.
- Any global organisation faces constant challenges to its effectiveness, especially one with such a comprehensive coverage (90% of the world's securities markets) and diversity of membership. Members are separated by historical, legal and structural, and cultural differences (although IOSCO has thus far been remarkably successful at overcoming such potential barriers).
- *Second area of challenge* is progress on IOSCO Principles implementation and the IOSCO MMOU. Principles and standards must be implemented through the structures and practices of regulators. For this, IOSCO needs to encourage and support members to overcome their own particular challenges. More progress is required in 2005 and beyond, especially with the IOSCO MMOU and the expansion of an effective cross-border network of information exchange and cooperation between members. Progress is also required in dialogue with those jurisdictions which have not yet taken steps to build active cooperative mechanisms with other regulators.
- *The third challenge* is the globalisation and complexity in securities markets. New issues and imperatives are constantly being added to the agenda. We need to constantly increase our understanding of threats to the fairness, efficiency, and soundness of markets and tailor IOSCO's response to actual and emerging need.

//