International Financial Instability and the Financial Stability Board

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Abstract

The reconstituted Financial Stability Board has made some of the most substantial and significant sets of contributions to the new regulatory reform agenda under construction at the international level following the global financial crisis beginning in Autumn 2007. The various packages of measures adopted cover all of the principal areas of policy revision not dealt with by specific sector technical committees such as the Basel Committee on Banking Supervision and its Basel III capital, liquidity, and leverage program. The number and quality of the papers produced by the Board is a remarkable achievement and testimony to the expertise and commitment of all of the individual participants involved. Further initiatives could nevertheless be undertaken to ensure that this work is as complete, coherent, effective, and accessible as possible.

One of the most significant reform initiatives adopted following the global financial crisis, beginning in autumn 2007,[1] was the establishment of the Financial Stability Board (FSB) in April 2009.[2] The FSB was created through an extension of the mandate and membership of the earlier Financial Stability Forum (FSF),[3] which had originally been set up in 1999 following the earlier Asian Crisis beginning in July 1997.[4] The Asian and global financial crises were ten years and one month apart with the FSB being set up ten years and two months after the original FSF.[5]

The unique nature of the FSF and FSB is principally attributable to the mixed membership and the extended international, regional, and national expertise and experience,

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1. Elliott, Larry, *Global Financial Crisis: Five Key Stages 2007-2011*, THE GUARDIAN (August 7, 2011, 11:49 PM), http://www.guardian.co.uk/business/2011/aug/07/global-financial-crisis-key-stages.

2. Mario Draghi, Chairman, Fin. Stability Forum, Re-Establishment of the FSF as the Financial Stability Board, Prepared Remarks at the London Summit (Apr. 2, 2009), *available at* http://www.financialstabilityboard.org/publications/r_090402.pdf.

3. *Id.*

4. GEORGE ALEXANDER WALKER, INTERNATIONAL BANKING REGULATION LAW, POLICY AND PRACTICE 279 (Joseph Norton ed., vol. 19 2001).

5. *See id.*; Elliot, *supra* note 1.

which the mixed membership has made available.[6] The FSF consisted of the Heads of the Finance Ministries, central banks, and regulatory authorities of each of the G7 countries;[7] This group was later extended to include the full G20 with the replacement of the FSF by the FSB.[8] All of the principal International Financial Institutions (IFIs) and technical standard setting bodies and committees (SSBs) are also represented with the European Commission and European Central Bank (ECB).[9] This brings together all of the key expertise in the financial area at the domestic, European, and international levels.

The initial work program of the FSF appears to have been relatively wide in scope although limited in terms of substantive regulatory content, with the focus on key areas of concern following the Asian financial crisis, including global capital flows, off-shore financial centers (OFCs), and highly leveraged institutions (HLIs).[10] The FSF's most significant single contribution was the establishment of a "Compendium of Standards" governing all of the principal aspects of international financial regulation.[11] As well as increase the membership to include the full G20, the work of the FSF has been extended substantially following the establishment of the FSB and the addition of a number of new areas of vulnerability and response work following the global financial crisis.[12]

The purpose of this paper is to consider the origins of the FSF and its original work program. The need for replacing the FSF with the FSB is examined and its substantially expanded areas of activity reviewed. Each of the key sets of principal reform activity is examined in further detail as well as the revised content of the Compendium of Standards and the separate work undertaken by the FSB in terms of implementation and adherence assessed. A series of provisional comments and conclusions are drawn with regard to the contribution of the FSB to the construction of a new, meaningful, and effective regulatory reform agenda following the recent crises.

I. Asian Financial Crisis and FSF

The FSF had been set up following the Asian financial crisis, which began with the devaluation of the Thai Baht on July 2, 1997, and with the Bank of Thailand having been forced to abandon its peg with the US dollar.[13] The crisis in Thailand quickly spread to other Asian economies including Malaysia, Indonesia, and the Philippines, as well as Taiwan, Hong Kong, and South Korea and then Japan.[14] These Asian "Tiger" economies had

6. WALKER, *supra* note 4 at 308.

7. *Id.*

8. Draghi, *supra* note 2.

9. Financial Stability Board Charter, art. 5, (1)(b)-(c); Annex A., June 19, 2012, *available at* http://www.financialstabilityboard.org/publications/r_120809.pdf [hereinafter, Fin. Stability Bd. Charter (June 2012)].

10. *See* WALKER, *supra* note 4, at 311-13.

11. *Id.* at 317.

12. *See* Draghi, *supra* note 2.

13. The devaluation led to an initial recovery in stock market prices although concerns increased with the effect of the revaluation on financial exposures, continued volatility, and high interest rates. The Thai crisis was triggered by "unsound macroeconomic policy and fundamentally weak banking practices and supervision" accompanied by economic slowdown, a speculative attack on the currency, and political instability. WALKER, *supra* note 4, at 279 n.40.

14. The value of the Malaysian, Indonesian, and Philippine currencies fell by 25-33 percent, with the Taiwan dollar having to be devalued; this led to speculative attacks on the Hong Kong dollar. *Id.* at 279.

enjoyed substantial growth during the earlier 1990s,[15] although international markets had been shocked by the instability in Mexico in 1994;[16] this vulnerability subsequently spread to Japan, Russian, and then Latin America.[17]

The size and severity of the Asian financial crisis attracted significant political attention, with the G7 Heads of Government and Financial Ministers assuming a lead in the response efforts undertaken.[18] The G7 Finance Ministers issued an important report on *Financial Stability* in May 1998,[19] although the G7 had taken an interest in financial markets since the Halifax Summit in 1995 following the collapse of Barings Bank in the UK.[20] Separate papers were issued by the G10,[21] G22,[22] and International Monetary Fund (IMF),[23] with other government and private reform initiatives being announced. UK

15. Average growth was 9 percent between 1992 and 1995, with an average of 5 percent GNP between 1965 and 1990. *Id.* at 278-79.

16. Mexico had to devalue the Peso on December 20, 1994, and then allow it to float following the assassination of the presidential candidate Colosio. Then, $28 billion in short-term government *tesobonos* had to be closed out with the assistance of the United States and International Monetary Fund. *Id.* at 277.

17. Japan issued poor economic figures in the middle of 1998, with Russia defaulting on its debt in August 1998. *Id.* at 279.

18. *Id.* at 282. The G7 was originally set up as the Group of Six in 1975 with France, West Germany, Italy, Japan, the UK, and the US, with the G7 being created the following year with Canada. Stephanie Lee & Alexandra Silver, *The Group of Eight (G8) Industrialized Nations* (March 27, 2009), http://www.cfr.org/global-governance/group-eight-g8-industrialized-nations/p10647#p6. This would be referred to as the G8 with Russian from 1997. *Id.* This would be expanded to form the G20 in September 1999, following the global financial crisis, with South Africa, Mexico, Brazil, Argentina, China, South Korea, India, Indonesia, Turkey, Saudi Arabia, and Australia joining with the European Union. G20, *What is the G20?*, http://www.g20.org/docs/about/about_G20.html (last visited June 7, 2013).

19. Birmingham G8 Summit, May 15-17, 1998, *Strengthening the Architecture of the Global Financial System, Report of G7 Finance Ministers to G7 Heads of State or Government for their meeting in Birmingham May 1998* (May 15, 1998).

20. The G7 considered financial matters at the summits in Halifax in 1995, Lyon in 1996, Denver in 1997, Birmingham in 1998, and Cologne in 1999. *Id.*; Denver G8 Summit, June 20-22, 1998, *Final Report to the G7 Heads of State and Government on Promoting Financial Stability* (June 21, 1997); WALKER, *supra* note 4, at 273 n.10.

21. The G10 had set up a Working Party after the G7 Halifax Summit to consider the orderly management of sovereign liquidity crises, with a separate Working Party on Financial Stability in Emerging Market Economies. Working Party on Financial Stability in Emerging Market Economies, *Financial Stability in Emerging Market Economies: A Strategy for the Formulation, Adoptions, and Implementation of Sound Principles and Practices to Strengthen Financial Systems* (Apr. 1997), *available at* http://www.bis.org/publ/gten02.pdf; The Deputies of the Group of Ten, *The Resolution of Sovereign Liquidity Crises: A Report to the Ministers and Governors Prepared under the Auspices of the Deputies* (May 1996), *available at* http://www.bis.org/publ/gten03.pdf; *see generally* WALKER, *supra* note 4, at 287. The G10 consisted of the eight countries that had agreed in 1962 to participate in the IMF General Arrangements to Borrow (GAB) with Germany and Sweden also agreeing to provide additional resources. *Factsheet: A Guide to Committees, Groups, and Clubs*, INT'L MONETARY FUND (Apr. 4, 2013), http://www.imf.org/external/np/exr/facts/groups.htm [hereinafter *IMF Factsheet*].

22. WALKER, *supra* note 4, at 273. Three working groups have been set up by the G22 on Enhancing Transparency and Accountability, Strengthening Financial Systems, and Managing International Financial Crises. WALKER, *supra* note 4, at 289. The G22 was set up in 1997 to consider reform of the global financial system following the Asian crisis and consisted of the G8 and 14 additional countries. *IMF Factsheet*, *supra* note 21; WALKER, *supra* note 4, at 273 n.14. It was originally referred to as the Willard Group and was expanded to consist of the Group of 33 in 1999. It was then superseded by the G20. *IMF Factsheet*, *supra* note 21.

23. The IMF produced a framework paper that identified a number of categories of issues considered to be of importance in connection with financial sector reform. DAVID FOLKERTS-LANDAU & CARL-JOHAN LIN-

Chancellor of the Exchequer, Gordon Brown, recommended the establishment of a new permanent Standing Committee for Global Financial Regulation in autumn 1998.[24]

The G7 Finance Ministers and Central Bank Governors agreed to commission a report by Hans Tietmeyer, former President of the German Bundesbank,[25] to consult and consider new structures necessary to enhance cooperation between national and international supervisory bodies and international financial institutions.[26] A formal mandate was issued the same month,[27] with a final report being produced in February 1999.[28] This explained the earlier international financial architecture and split responsibilities with the need for a more integrated approach being highlighted.[29] The report stressed the need to monitor domestic vulnerabilities, which could generate larger systemic threats through evolving global conditions.[30] The report concluded that fundamental institutional change was not required although it was necessary to establish a new "Financial Stability Forum" to meet regularly to identify and assess relevant issues and vulnerabilities concerning the global financial system.[31] This led to the establishment of the FSF by the G7 Ministers and Governors at the Bonn meeting in February 1999, with the FSF holding its first meeting in Washington on February 14, 1999.[32]

The FSF was originally set up with thirty-five representatives from the G7 countries, the IFIs, and the SSBs.[33] Its original Chairman was Andrew Crockett, former General Manager of the BIS.[34] The principal objective "was to create a new contact vehicle through which all of the separate bodies. . . could meet and exchange views on systemically important issues."[35] The initial general activities of the FSF were concerned with "disclosure, training, and standards."[36] Three initial working groups were set up on highly leveraged institutions (HLIs), capital flows, and off-shore financial centers (OFCs),[37] with a separate task force on implementation and a Study Group on Deposit Insurance.[38] The FSF also constructed the first global Compendium of Standards through the collection of the most important papers issued by each of the principal IFIs

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DGREN, INT'L MONETARY FUND, TOWARD A FRAMEWORK FOR FINANCIAL STABILITY (1998), *available at* http://www.imf.org/external/pubs/ft/wefs/toward/.

24. Gordon Brown, Reforming the International Monetary Fund: . . . And Impose New Codes of Conduct, WALL ST. J., Oct. 6, 1998, at A22.

25. HANS TIETMEYER, INTERNATIONAL COOPERATION AND COORDINATION IN THE AREA OF FINANCIAL MARKET SUPERVISION AND SURVEILLANCE (Feb. 11, 1999), *available at* http://www.financialstabilityboard.org/publications/r_9902.pdf.

26. Finance Ministers Meeting, *Statement by the G7 Finance Ministers and Central Bank Governors* (Oct. 3, 1998), *available at* http://www.g8.utoronto.ca/finance/fm100398.htm.

27. *Declaration of G7 Finance Ministers and Central Bank Governors on the World Economy* (Oct. 30, 1998), *available at* http://www.imf.org/external/np/g7/103098dc.htm.

28. TIETMEYER, *supra* note 25, § 1.

29. *See id.* § 3.1.

30. *Id.*

31. *Id.* § 4.

32. WALKER, *supra* note 4, at 307.

33. *Id.* at 308.

34. *Id.* at 307.

35. *Id.* at 309.

36. *Id.* at 316.

37. Press Release, Fin. Stability Forum, FSF Establishes Working Grps. (Nov. 19, 1999), *available at* http://www.bis.org/press/p990511.htm.

38. WALKER, *supra* note 4, at 315.

and SSBs, including on public sector transparency, banking, securities, insurance, corporate governance, and payment and settlement.[39] This was set up as a form of virtual global financial rulebook using html links to all of the original documents on each of the member institution's websites.[40] A sub-set of twelve key standards for sound financial systems was subsequently added to the Compendium.[41]

The creation of the FSF in 1999 was an important development in the construction of a "new international financial architecture."[42] This was the first initiative to attempt to deal with the fundamental global market and local control conflict that arises.[43] A fundamental institutional, organizational, and operational gap exists in terms of international financial market supervision and control, which has to be managed and discharged at the national level.[44] The FSF brought representatives from the national finance ministries, central banks, and supervisory authorities together for the first time with all of the principal IFIs and SSBs.[45] While its initial original research work was fundamentally limited, it was able to draw all of the main international financial standards together for the first time with its Compendium.[46] The earlier inherent advantages of the original FSF model were retained but extended with its replacement by the FSB and with its work load being substantially extended to include all major areas of potential concern following the global financial crisis.[47]

II. Global Financial Crisis

The background causes to the global financial crisis were referred to by the G20 in the first Summit Declaration in Washington in November 2008.[48] The crisis was generally stated to have occurred as a result of a search for yield, vulnerability and policy, regulatory, and supervisory failure.[49] The principal factors behind the crisis had been reviewed

39. *Id.* at 317-18.

40. Fin. Stability Bd., *About the Compendium of Standards*, http://www.financialstabilityboard.org/cos/index.htm (last visited June 9, 2013).

41. *Key Standards for Sound Financial Systems*, FIN. STABILITY BD., http://www.financialstabilityboard.org/cos/key_standards.htm (last visited Aug. 1, 2013).

42. WALKER, *supra* note 4, at 273, 307.

43. *Id.* at 273. A single global market in financial services has been created, although this has to be controlled on a local domestic basis using national regulatory and supervisory systems. *Id.* at 306.

44. *Id.* at 305-06.

45. DOMENICO LOMBARDI, BROOKINGS, THE GOVERNANCE OF THE FINANCIAL STABILITY BOARD 3-4 (Global Economy and Development at Brookings, Sept. 2011), *available at* http://www.banxico.org.mx/sistema-financiero/informacion-general/consejo-de-estabilidad-del-sistema-financiero-stre/%7B831E0646-8590-B54B-91F6-C905F75D4C34%7D.pdf.

46. *Id.* at 4.

47. *Id.* at 3, 5.

48. Summit on Financial Markets and the World Economy, Washington, D.C., U.S., Nov. 14-15, 2008, *Declaration*, (Nov. 15, 2008).

49. "Market participants [had sought] higher yields with an inadequate appreciation of risk[s]" and failure "to exercise proper due diligence" following a period of strong global growth, capital flow, and stability. Vulnerabilities were created through "weak underwriting standards, unsound risk management practices, increasingly complex and opaque financial products" and excessive leverage. "Policy-makers, regulators[,] and supervisors in some advanced countries[ ] did not adequately appreciate and [manage] the risks building up [within] financial markets, keep pace with financial innovation, or take into account the systemic ramifications of domestic regulatory actions." Excesses and severe market disruption followed from major underlying factors, including "inconsistent and insufficiently coordinated macroeconomic policies [and] inadequate struc-

in further detail by the FSF in its report on *Enhancing Market and Institutional Resilience* in April 2008.[50]

The FSF explained the crisis in terms of market turmoil, underlying weaknesses in risk management and underwriting, and mismanagement by some firms of the originate-to-distribute (OTD) model.[51] Low interest rates and abundant liquidity had increased borrower, investor, and intermediary risk and leverage with the financial system not being able to manage the new risks created through expansion and financial innovation, especially with collateralized debt obligations (CDOs) and mortgage-backed securities (MBSs).[52] A weakening in credit standards within the U.S. subprime mortgage market and household and corporate lending more generally led to a mispricing of risk by banks, investors, and Credit Rating Agencies (CRAs).[53]

The value of subprime-related indices began to fall sharply with rising delinquencies from early 2007, which triggered a wider downturn in market risk-taking and withdrawal of support for off-balance conduits and structured investment vehicles (SIVs).[54] This resulted in a sharp contraction in liquidity and subsequent increased risk aversion, market uncertainty, and deleveraging.[55] The report refers to continuing difficulties being suffered in markets in April 2008, which was eight months after the crisis began,[56] although these problems subsequently continued for five years afterwards.[57]

The report accepts that some market adjustment was inevitable, especially with a turn in the credit cycle and weakening of the U.S. housing market, although this was much more severe due to the scale of the adjustment required, especially through accumulated weak-

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tural reforms" that had "led to unsustainable global macroeconomic outcome." *Id.* The G20 April annex, the *Declaration on Strengthening the Financial System*, contains specific provisions with regard to expanding the FSB, international cooperation, prudential regulation, regulatory scope, compensation, tax havens and non-cooperative jurisdictions, accounting standards, CRAs and follow-up work. G20 London Summit 2009, London, Eng., Apr. 1-2, 2009, *Declaration on Strengthening the Financial System*, 1-2, 4 (Apr. 2, 2009), *available at* http://www.treasury.gov/resource-center/international/g7-g20/Documents/London%20April%202009%20Fin_Deps_Fin_Reg_Annex_020409_-_1615_final.pdf.

50. Fin. Stability Forum, *Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience*, 1 (Apr. 7, 2008), http://www.financialstabilityboard.org/publications/r_0804.pdf [hereinafter *Enhancing Market and Institutional Resilience*].

51. *Id.* at 1.

52. Global low risk premia and "low expectations of future volatility" increased from 2003, especially with the growth in the use of CDOs and perceived higher liquidity through the "pooling and tranching of credit assets," credit enhancement, and increased credit protection through the credit default swap market. This was accompanied by the use of off-balance sheet funding and investment vehicles issuing mortgage-backed securities (MBSs) with low capital and liquidity support. *Id.* at 5.

53. *Id.*

54. Delinquencies produced a fall in index prices, which resulted in losses and margin calls on highly rated subprime products. Multiple downgrades were imposed by CRAs on subprime related structured products with money-market investors refusing to purchase asset-backed commercial paper (ABCP) to roll over conduit and structured investment vehicles (SIV) debt from August 2007. *Id.* at 6.

55. Sponsoring banks had to support conduits and SIVs, which resulted in a sharp contraction in liquidity on interbank markets and rise in term premia or LIBOR rates. Valuation losses were suffered in broad asset classes with fears of fire sales and banks' contingency plans not being able to sustain their continued market losses. Capital levels shrank as banks reabsorbed assets and recorded large valuation losses. *Id.*

56. *Id.* at 6.

57. Naoyuki Shinohara, Deputy Managing Dir., Int'l Monetary Fund, Keynote Speech at Bank of Korea International Conference 2013: The Financial Crisis, Capital Flows, and Global Liquidity (June 3, 2013), *available at* http://www.imf.org/external/np/speeches/2013/060313.htm.

nesses in risk management and underwriting standards.[58] Underlying weaknesses arose specifically through poor underwriting standards, failures in firm risk management practices, poor investor due diligence, defective performance by CRAs (especially with regard to structured products), incentive distortions, disclosure weaknesses, and "feedback effects" between valuation and risk-taking.[59]

The report also specifically refers to weaknesses in regulatory frameworks with authorities failing to take effective "countervailing action" having "overestimated the strength and resilience of the financial system."[60] The report accepts that securitization markets and the OTD intermediation model were not defective in themselves, although difficulties arose through increased leverage and complexity with weak credit standards.[61] Some firms were better than others in managing the consequent write-down and restructuring required; a number of specific concerns arose with regard to misaligned incentives, lack of transparency, poor risk management, and the usefulness and transparency of credit ratings.[62]

The FSF proposed that specific action be taken in the five key areas of (1) strengthened oversight of capital, liquidity, and risk management; (2) enhanced transparency and valuation; (3) credit rating adjustment; (4) strengthened official responsiveness to risk; and (5) increased arrangements to deal with financial system stress.[63] A number of provisional recommendations were made to improve regulatory practices in each of these areas.[64] The FSF Chairman issued an Update on the Implementation of the FSF's Recommendations to the G8 Finance Ministers in June 2008,[65] along with other papers being issued on procyclicality and provisioning.[66] The FSB issued a report on Improving Financial Regulation in September 2009, which contained a review of progress achieved and continuing work underway.[67]

58. *Enhancing Market and Institutional Resilience*, *supra* note 50, at 7.

59. This can be understood in terms of cyclic effects with rating downgrades, forced sales, mark to market accounting, margin calls, and further downgrades. *See id.* at 6-9.

60. *Id.* at 9.

61. The OTD model allowed originators "greater capital efficiency, enhanced funding. . . and lower earnings volatility," with investors having increased choice, diversification, and risk matching. Borrowers also benefitted from increased credit availability, product choice, and lower borrowing cost. Difficulties nevertheless arose through increased leverage, maturity, and liquidity risk through conduit and SIV asset holdings (including "through contingent credit lines, reputational links, revenue risks, and counterparty credit exposures"), continuing liquidity exposure, and large retained pipeline exposures. *Id.* at 9-10.

62. *Id.* at 10.

63. *Id.* at 2.

64. *See id.* at 12-62.

65. Fin. Stability Bd., *Update on the Implementation of the FSF's Recommendations: Report by the FSF Chairman to the G8 Finance Ministers* (June 11, 2008), http://www.financialstabilityboard.org/publications/r_0806.pdf.

66. Fin. Stability Forum, *Report of the Financial Stability Forum on Addressing Procyclicality in the Financial System* (Apr. 2, 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904a.pdf [hereinafter *Report on Procyclicality*]; Joint FSF-CGFS Working Group, *The Role of Valuation and Leverage in Procyclicality* (Mar. 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904h.pdf; Joint FSF-BCBS Working Group on Bank Capital Issues, *Reducing Procyclicality Arising from the Bank Capital Framework* (Mar. 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904f.pdf; *see also*, Fin. Stability Forum, *Report of the FSF Working Group on Provisioning* (Mar. 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904g.pdf.

67. The report covered strengthening the global capital framework, making global liquidity more robust, reducing the moral hazard of systemically important institutions, strengthening accounting standards, improving compensation practices, expanding financial system oversight, strengthening the robustness of the

III. Financial Stability Board

The decision to establish the FSB was made at the London G20 Summit in April 2009 hosted by the then-British Prime Minister, Gordon Brown.[68] This set out the core objectives for the FSB[69] with a separate Declaration on Strengthening the Financial System and Declaration on Delivering Resources through the International Financial Institutions attached to the Leaders' Statement.[70] The Leaders' Statement declared that the FSB would consist of all G20 countries, FSF members, Spain, and the European Commission, with the FSB collaborating with the IMF to provide an early warning of macroeconomic and financial risks and to take necessary action.[71] It would "reshape" regulatory systems to allow authorities to identify and take account of macro-prudential risks and "to extend regulation and oversight to all systemically important financial institutions, instruments and markets."[72] The 2009 London Summit followed the initial G20 Summit in November 2008, hosted by then-President George Bush, which examined the initial causes of the crisis and outlined possible areas for reform.[73]

The FSB held its inaugural meeting in Basel on June 26-27, 2009,[74] with a follow-up meeting in Paris on September 15, 2009.[75] The FSB held its third meeting in Basel

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OTC derivatives market, re-launching securitization on a sound basis, and adherence to international standards. Fin. Stability Bd., *Improving Financial Regulation: Report of the Financial Stability Board to G20 Leaders*, 2 (Sep. 25, 2009), *available at* http://www.financialstabilityboard.org/publications/r_090925b.pdf [hereinafter *Improving Financial Regulation*].

68. London Summit, Apr. 2, 2009, London, Eng., London Summit—Leaders' Statement, ¶ 15 (Apr. 2, 2009), *available at* http://www.imf.org/external/np/sec/pr/2009/pdf/g20_040209.pdf [hereinafter *Leaders' Statement*]; Andrew Porter, et al., *G20 Summit: Gordon Brown Announces "New World Order,"* THE TELEGRAPH (Apr. 3, 2009, 6:30 AM), http://www.telegraph.co.uk/finance/g20-summit/5097195/G20-summit-Gordon-Brown-announces-new-world-order.html.

69. Leaders' Statement, *supra* note 68, at ¶ 4.

70. London Summit, *Declaration on Strengthening the Financial System*, *supra* note 49; London Summit, Apr. 2, 2009, London, Eng., *Declaration on Delivering Resources through the International Financial Institutions*, (Apr. 2, 2009), *available at* http://www.treasury.gov/resource-center/international/g7-g20/Documents/London%20April%202009%20Fin_Deps_IFI_Annex_Draft_02_04_09_-_1615_Clean.pdf.

71. Leaders' Statement, *supra* note 68, ¶ 15.

72. The leaders agreed to implement the FSF's principles on pay and compensation, to improve the quality, quantity, and international consistency of banking in the financial system "once recovery is assured," "to take action against non-cooperative jurisdictions," including tax havens, to improve global accounting valuation and provisioning standards and to "extend regulatory oversight and registration to Credit Rating Agencies" (CRAs). *Id.*

73. *The G20 Summit in Washington D.C.: Not a Bad Weekend's Work*, ECONOMIST (Nov. 16, 2008), http://www.economist.com/node/12623258/print; *Declaration Summit on Financial Markets and the World Economy*, WASH. TIMES (Nov. 15, 2008), http://www.washingtontimes.com/news/2008/nov/15/declaration-summit-financial-markets-and-world-eco/?page=all.

74. The FSB revised FSF internal structures and considered risks and challenges facing the international finance system. The FSB also considered the progress of the FSF/FSB and G20 recommendations on strengthening financial systems. Press Release, Fin. Stability Bd., Financial Stability Board Holds Inaugural Meeting in Basel, 28/2009 (June 27, 2009), *available at* http://www.financialstabilityboard.org/press/pr_090627.pdf.

75. The FSB considered risks, vulnerabilities, and responses to the international financial system, and progress towards implementing reforms. It also addressed further work that is required to improve financial regulation with specific reference to strengthening the global capital framework, making global liquidity more robust, reducing moral hazard and strengthening cross-border resolution capacity, strengthening accounting standards, improving compensation practices, expanding oversight of the financial system, strengthening the OTC derivatives markets, re-launching securitization on a sound basis, and adhering to

on January 9, 2010.[76] The FSB set up a plenary of full members[77] with a steering committee[78] and three standing committees, including the Committee on the Assessment of Vulnerabilities (SCAV),[79] the Committee for Supervisory and Regulatory Co-operation (SCSRC),[80] and the Committee for Standards Implementation (SCSI).[81] The Secretariat is located at the Bank for International Settlements (BIS).[82]

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international standards. Press Release, Fin. Stability Bd., Financial Stability Board Meets in Paris, 37/2009 (Sept. 15, 2009), *available at* http://www.financialstabilityboard.org/press/pr_090915.pdf.

76. The FSB examined relevant financial conditions, improving market regulation (including sound compensation practices, bank capital and liquidity, moral hazard and cross-border resolution, perimeter and regulatory consistency, and accounting standards), and strengthening adherence to international standards. Press Release, Fin. Stability Bd., Financial Stability Board Meets on Financial Reform Agenda, 03/2010 (Jan. 9, 2010), *available at* http://www.financialstabilityboard.org/press/pr_100109a.pdf.

77. These included the finance departments, central banks, and regulatory agencies (where separate) of its member countries, which consist of Argentina, Australia, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Indonesia, Italy, Japan, Korea, Mexico, Netherlands, Russia, Saudi Arabia, Singapore, South Africa, Spain, Switzerland, Turkey, the United Kingdom, and the United States. Relevant International Financial Institutions (IFIs) included the International Monetary Fund (IMF), the Bank for International Settlements (BIS), the World Bank, and the Organization for Economic Co-operation and Development (OECD). Relevant technical committees consisted of the Basel Committee, International Association of Insurance Supervisors (IAIS), and the International Organization of Securities Commissions (IOSCO), as well as the International Accounting Standards Board (IASB). Committees of central bank experts consisted of the Committee on Payment and Settlement Systems (CPSS) and the Committee on the Global Financial System (CGFS). Representatives also attended from the European Central Bank (ECB) and the EU Commission. Fin. Stability Board Charter, Annex A (Sept. 2009), *available at* http://www.financialstabilityboard.org/publications/r_090925d.pdf [hereinafter Fin. Stability Bd. Charter (Sept. 2009)].

78. *Id.* arts. 6, 12-13. The Steering Committee provides "operational guidance between . . . Plenary meetings" and is headed by the FSB Chair. *Id.* arts. 12-13. The FSB is chaired by Mark Carney, the Governor of the Bank of Canada. Press Release, Fin. Stability Bd., Appointment of Chairman and Vice-Chairman of the Financial Stability Board, 60/2011 (Nov. 4, 2011), *available at* http://www.financialstabilityboard.org/press/pr_111104bb.pdf [hereinafter Appointment of Chairman]. The FSB Charter sets out the responsibilities of the plenary, representation and attendance, convocation, seat assignments, and standing committees and working groups. Fin. Stability Bd. Charter (Sept. 2009), *supra* note 77, arts. 7-11. The FSB Charter also addresses the composition, appointment, responsibilities, and authorities of the Steering Committee. *Id.* arts. 12-13. The appointment and responsibilities of the FSB Chair are stated in Article 14 of its Charter. *Id.* art. 14. The Secretariat is dealt with in Article 15 of the FSB Charter. *Id.* art. 15.

79. Fin. Stability Bd. Charter (Sept. 2009), *supra* note 77, Annex B. The SCAV assesses vulnerabilities within the financial system and makes recommendations on vulnerability deliberations, including Early Warning Exercises. *Standing Committee on Assessment of Vulnerabilities*, FSB WATCH, http://www.fsbwatch.org/index.php/fsb/84-program/83 (last visited July 29, 2013). The Chairman is Jaime Caruana, BIS General Manager. *Id.*

80. Fin. Stability Bd. Charter (June 2012), *supra* note 9, Annex B. The SCSRC considers coordination and policy development issues including regulatory standards, supervisory issues, and cross border management. *Standing Committee on Supervisory and Regulatory Cooperation*, FSB WATCH, http://www.fsbwatch.org/index.php/fsb/84-program/82 (last visited July 29, 2013). It is chaired by Daniel Tarullo, Chairman, Board of Governors of the Federal Reserve System. *Members of Standing Committee on Supervisory and Regulatory Cooperation*, FIN. STABILITY BOARD (April 2, 2013), http://www.financialstabilityboard.org/about/scsrc.pdf. The Standing Committee also has a Cross Border Crisis Management working group under Paul Tucker, Deputy Governor of the Bank of England. *Standing Committee on Supervisory and Regulatory Cooperation*, *supra*.

81. Fin. Stability Bd. Charter (June 2012), *supra* note 9, Annex B. The SCSI manages members' peer reviews and reports on standards implementation. *Standing Committee on Standards Implementation*, FSB WATCH, http://www.fsbwatch.org/index.php/fsb/84-program/81 (last visited July 29, 2013). It is chaired by Ravi Menon, Managing Director, Monetary Authority of Singapore. *Members of Standing Committee on Standards Implementation*, FIN. STABILITY BOARD (April 2, 2013), http://www.financialstabilityboard.org/about/scsi.pdf.

Sixty-four agencies are represented on the FSB, with the Plenary having seventy members and the Steering Committee forty members.[83] A Standing Committee on Budget and Resources was subsequently formed as well.[84] The FSB also operates through six Regional Consultative Groups (RCGs) for (1) the Americas, (2) Asia, (3) the Commonwealth of Independent States, (4) Europe, (5) the Middle East and North Africa, and (6) Sub-Saharan Africa.[85]

An original Charter came into effect on September 25, 2009,[86] although it was subsequently replaced by an extended Charter in June 2012,[87] following agreement at the G20 Cannes Summit in November 2011 to strengthen the FSB's capacity, resources, and governance through the creation of an enduring organizational basis.[88] The FSB is required under its Charter to coordinate the alignment of activities between the SSBs and to develop standards to address any regulatory gaps not "fall[ing] within the functional domain of another" SSB.[89] The FSB is to consult widely among members and other stakeholders and to maintain "a structured process for public consultation on policy proposals."[90] Accountability and transparency are to be maintained through the publication of reports and periodical progress updates to the G20.[91] Membership eligibility is specified in Article 5 of the Charter, and members must commit to maintain financial stability, to maintain financial sector openness and transparency, to implement international financial standards, to undergo periodic peer reviews, and to participate in implementation monitoring of agreed commitments, standards, and policy recommendations.[92] The Charter specifies the organizational structure of the FSB, as well as the responsibilities of each of its operations.[93] While the FSB is to have legal personality, the Charter is specified as not being

82. Fin. Stability Bd. Charter (Sept. 2009), *supra* note 77, art. 15(7).

83. *Members of the Financial Stability Board*, FIN. STABILITY BOARD (Apr. 4, 2013), http://www.financialstabilityboard.org/about/plenary.pdf; *Links to FSB Members*, FIN. STABILITY BOARD (Apr. 2, 2013), http://www.financialstabilityboard.org/members/links.htm (last visited Aug. 5, 2013); *FSB Steering Committee*, FIN. STABILITY BOARD (Apr. 2, 2013), http://www.financialstabilityboard.org/about/steeringcommittee.pdf.

84. Press Release, Fin. Stability Bd., FSB Appoints New Chairs of its Standing Committees, 19/2003 (March 20, 2013), *available at* http://www.financialstabilityboard.org/press/pr_130320.pdf.

85. *Regional Consultative Groups*, FSB WATCH, http://fsbwatch.org/index.php/regional-participation (last visited July 30, 2013).

86. Fin. Stability Bd. Charter (Sept. 2009), *supra* note 77, art. 17.

87. Fin. Stability Bd. Charter (June 2012), *supra* note 9, art. 24.

88. Cannes Summit, Nov. 3-4, 2011, *Final Declaration*: Building Our Common Future: Renewed Collective Action for the Benefit of All, ¶ 38 (Nov. 4, 2011), *available at* http://www.g20civil.com/documents/Cannes_Declaration_4_November_2011.pdf. The FSB would be strengthened following Chairman Mark Carney's recommendations by conferring on the FSB legal personality and greater financial autonomy and by reconstituting the Steering Committee to include the executive branch of governments of the G20 Chair, of the larger financial systems and geographic regions, and of centers not currently represented. *Id.* ¶ 38; Appointment of Chairman, *supra* note 78. Its coordination role would also be strengthened with other standard setting bodies (SSBs) "on policy development and implementation monitoring" without functional overlap and while preserving the independence of the SSBs. Cannes Summit Final Declaration, *supra*.

89. Fin. Stability Bd. Charter (June 2012), *supra* note 9, art. 2(2)-(3).

90. *Id.* art. 3.

91. *Id.* art. 4.

92. The FSB is to report periodically on member adherence, and standard setting bodies (SSBs) will report to the FSB on implementation. The international financial institutions (IFIs) will work with the FSB in accordance with their specific legal frameworks and policies. *Id.* art. 6.

93. *Id.* arts. 7, 9-22.

intended to create any legal rights or obligations.[94] The revised Charter came into effect on June 19, 2012.[95] Formal Articles of Association were also adopted at a plenary meeting in January 2013.[96]

IV. Financial Stability Board Reform Program

The FSB has supported a large number of initiatives since its formation in 2009.[97] Its principal areas of work include Market Resilience and Financial Regulation, Compensation, Global Systemically Important Institutions (G-SIFIs), Crisis Management, and Macro-Prudential Oversight.[98] It has also been working in the areas of shadow banking, disclosure, supervision, financial derivatives, and legal identifiers, as well as credit risk transfer and service regulation.[99] It has subsequently been involved with continuing work on standards implementation in each of these other functional areas.[100]

A. Improving Financial Regulation

The FSF issued a follow-up report on Enhancing Market and Institutional Resilience in October 2008 and then again in April 2009[101] in advance of the G20 London Summit, which reviewed wider international initiatives following the crisis.[102] The FSB issued its first principal report to the G20 Leaders on Improving Financial Regulation in September 2009, which outlined the achievements made to date and critical work underway.[103]

The G20 Leaders had confirmed their determination to implement fully and consistently the reforms agreed to at the national level to secure a level playing field and to avoid protectionist pressures.[104] They were anxious to dispel any expectation that the private financial sector would be allowed to return to its pre-crisis position.[105] The "objective [was] to create a more disciplined and less procyclical financial system that better support[ed] balanced sustainable economic growth."[106] Leverage had to be limited and individuals not allowed to extract profit with "ultimate losses [being] borne by governments

94. *Id.* art. 23.

95. *Id.* art. 24.

96. Fin. Stability Bd., *Articles of Association of the Financial Stability Board*, (Jan. 28, 2013), *available at* http://www.financialstabilityboard.org/publications/r_130128aoa.pdf [hereinafter *FSB Articles of Association*]. *See* Section 7(2) below.

97. *See generally* Fin. Stability Bd. Charter (Sept. 2009), *supra* note 77.

98. *About the FSB*, Fin. Stability Board, http://www.financialstabilityboard.org/about/overview.htm (last visited Aug. 5, 2013).

99. *Id.*

100. *Key Standards for Sound Financial Systems*, *supra* note 41.

101. Fin. Stability Forum, *Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience: Update on Implementation*, at 2 (Apr. 2, 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904d.pdf; Fin. Stability Forum, *Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience: Follow-Up on Implementation*, at 4 (Oct. 10, 2008), *available at* http://www.financialstabilityboard.org/press/pr_081009f.pdf.

102. *See*, Leaders' Statement, *supra* note 68, ¶ 20.

103. *Improving Financial Regulation*, *supra* note 67 at 1, 2-12.

104. *Id.* ¶¶ 3, 53.

105. *Id.* ¶ 4.

106. *Id.* ¶ 5.

and the wider public."[107] The Leaders were committed to resolving the problems of moral hazard stemming from large institutions that were too complex to resolve and too big to fail (TBTF).[108] Profits arising from the extraordinary official measures had to be retained to strengthen institutions, and restrictions were imposed on dividend payments, share buy-backs, and compensation rates.[109]

The substantial progress achieved to give effect to the measures recommended in the FSF's April 2008 and 2009 Reports, the G20 Washington Action Plan, and the London Summit Statement were reviewed and the critical work underway was outlined.[110] The G20 Leaders also confirmed the need for perseverance and consistent national implementation over time, in particular, to maintain a level playing field.[111]

The FSB issued a parallel Report to the G20 Leaders in September 2009 titled *Overview of Progress in Implementing the London Summit Recommendations for Strengthening Financial Stability*.[112] The establishment of the FSB was referred to and its general structure and operation. The paper outlined the action taken in connection with securing international co-operation (including through supervisory colleges, cross-border crisis management and deposit insurance, and carrying out an Early Warning Exercise), prudential regulation (including capital, risk management, and liquidity), macro-prudential frameworks and tools, regulatory scope (including hedge funds, OTC derivatives and other unregulated markets and products), compensation, adherence, accounting standards, and credit rating agencies.[113]

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107. *Id.*

108. *Id.* ¶ 8.

109. *Id.* ¶¶ 9-10.

110. Criteria will be developed to identify jurisdictions of concern, evaluation process procedures will be developed to complement FSAP assessments, and a toolbox of measures will be developed to promote adherence and co-operation among jurisdictions. *Id.* ¶¶ 12-51. This included strengthening the global capital framework, making global liquidity more robust, reducing the moral hazard created by systemically important institutions, strengthening accounting standards, sound compensation practices, expanding oversight of the financial system, strengthening the robustness of the OTC derivatives markets, re-launching securitization on a sound basis, and securing adherence to international standards. *Id.* ¶¶ 14-51. Regarding "too big to fail" (referred to as "too big and too complex to fail") issues, measures considered included additional capital, liquidity, prudential requirements, the use of stand-alone subsidiaries, and contingency planning (including promoting the resiliency of key functions and allowing rapid resolution and wind-down where necessary). *Id.* ¶¶ 24-26. During implementation, the FSB will develop a global compliance "snapshot" of standards, building on the IMF Financial Sector Assessment Program (FSAP). *Id.* ¶ 50.

111. *Id.* ¶¶ 53-55.

112. Fin. Stability Bd., *Overview of Progress in Implementing the London Summit Recommendations for Strengthening Financial Stability: Report of the Financial Stability Board to G20 Leaders*, (Sept. 25, 2009), *available at* www.financialstabilityboard.org/publications/r_090925a.pdf [hereinafter *Overview of Progress in Implementing the London Summit*].

113. The London Summit had called on accounting standards setters to work urgently to improve standards, valuation, and provisioning and to produce a single set of high-quality, global accounting standards. The Financial Services Authority (FSA) recommendations were also supported on limiting procyclicality in accounting issues. Almost all FSB member jurisdictions were committed to implement IASB standards by 2012. The IASB had published an exposure draft in May on fair value measurement to identify inactive markets and determine whether transactions were orderly. This followed U.S. Financial Accounting Standards Board (FASB) staff guidance. A further consultation document was issued on the effects of fair value gains arising from deterioration in a company's own credit risk. The IASB was working on separate proposals to enhance the accounting and disclosure treatment of off-balance sheet entities in December 2008 and March 2009. This included proposals on both accounting consolidation and de-recognition following financial asset transfers. The FASB published its final standards on the accounting treatment of financial assets in

On macro-prudential risks, quantitative tools were being developed to monitor and assess relevant exposures, including on aggregate risk and tools to measure systemic liquidity risk, margins, haircuts, and other system wide indicators, including leverage.[114] The work of other bodies on macro-prudential oversight was reviewed.[115] The IMF, BIS, and FSB were developing guidelines to identify systemically important institutions, markets, and instruments. The Basel Committee had set up a working group on macro-prudential supervision, which was considering how to deal with the externalities created by systemically important banks, macro and micro stress tests, systemic impact, information exchange, and possible capital surcharges.[116] The IMF and FSB were separately working on their treatment of data gaps. Two 'Early Warning Exercises' (EWEs) had been carried out on financial market conditions and expected future developments. Priority vulnerabilities had been identified by the FSB's Standard Committee on Assessment of Vulnerabilities (SCAV). EWE methodologies would be further refined over time.[117] The paper reviewed work in other areas such as the scope of regulation, including hedge funds and OTC derivatives, compensation, adherence, accounting standards, and credit rating agencies.[118]

B. Sound Compensation Practices

The FSB has taken forward a number of initiatives in the area of compensation practices within large financial institutions following the criticism during the recent financial turbulence and perceived distorting effects of excessive bonus entitlement. A separate report had been prepared by a Senior Supervisors Group on the Risk Management Lessons from the Global Banking Crisis in October 2009.[119] The FSF issued nine Principles for

June 2009 (FAS 166 and FAS 167) on the treatment of securitization and special purpose entities. Further work was being carried out to converge IASB and FASB standards. Three new exposure drafts had been issued in 2009 on reducing complexity. The FASB would attempt to develop a single comprehensive model for accounting for financial instruments to replace IAS 39. The Basel Committee had proposed a set of high level principles to the IASB in April 2009 dealing with complexity, provisioning, fair value, and disclosure. The IASB was separately working with the Basel Committee on provisions to replace IAS 39. The IASB had consulted on an impairment standard based on expected loss (expected cash flow). Guidance was also issued by the IASB and FASB on valuation to improve fair value measurement. Neither the IASB nor the FASB had yet included any valuation adjustments where significant valuation uncertainties arose. The IASB and FASB were working with other prudential supervisors, regulators, and stakeholders on various issues. A Financial Crisis Advisory Group had specifically been set up with a report being issued in July 2009. This work continues. *See id.* at 14-20.

114. This would cover the measurement of systemic liquidity risk, margins, and haircuts and other system-wide indicators, such as leverage. *Id.* at 8.

115. The IAIS had prepared a progress report on the development of macro-prudential tools in connection with insurance companies. The Basel Committee and CGFS were working systemic liquidity risk with identification of early warning signals and policy options. The BIS and IMF were looking at data collection on systemic liquidity risk. The CGFS was reviewing margining practices in securities financing and OTC derivatives transactions to develop options to reduce procyclicality in margining. The BIS and CGFS were working on a data framework and common vocabulary to facilitate co-operation and discussion on market conditions and relevant exposures. *Id.* at 7-8.

116. *Id.* at 9.

117. *Id.* at 5.

118. *Overview of Progress in Implementing the London Summit*, *supra* note *112*, at 8-20.

119. *See generally* Senior Supervisors Group, *Risk Management Lessons from the Global Banking Crisis of 2008* (Oct. 21, 2009), *available at* www.sec.gov/news/press/2009/report102109.pdf. The group was made up of representatives from the Canadian Office of the Superintendent of Financial Institutions, French Banking

Sound Compensation Practices in April 2009[120] structured in terms of effective governance of compensation, effective alignment of compensation with prudent risk-taking, and effective supervisory oversight and engagement by stakeholders.[121]

The FSB produced a series of follow-up implementation standards in September 2009 dealing with governance, compensation and capital, pay structure and risk alignment, disclosure, and supervisory oversight.[122] A review template for member jurisdictions reporting on principles implementation was issued in December 2009[123] with two thematic reviews on compensation in 2010 and 2011.[124] The FSB had commissioned a separate report on Banking Compensation Reform from Oliver Wyman, which reported in March 2010.[125]

C. Systemically Important Institutions

The FSF had set up an initial Working Group on Highly Leveraged Institutions (HLIs) at its inaugural meeting in April 1999; the Working Group produced its first report in

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Commission, German Federal Financial Supervisory Authority, Japanese Financial Services Agency, Swiss Financial Market Supervisory Authority, U.K. FSA, and U.S. Federal Reserve Board, Federal Reserve Bank of New York, Office of the Comptroller of the Currency, and Securities and Exchange Commission. The report identifies the specific funding and liquidity issues which led to the crisis and other deficiencies in governance, firm management, risk management and internal control programs. *Id.*.

120. Fin. Stability Forum, *FSF Principles for Sound Compensation Practices* (Apr. 2, 2009), *available at* www.financialstabilityboard.org/publications/r_0904b.pdf [hereinafter *FSF Principles for Sound Compensation Practices*].

121. *Id.* at 2-3. The FSF principles for effective governance of compensation are: (1) "the firm's board of directors must actively oversee the compensation system's design and operation"; (2) "the firm's board of directors must monitor and review the compensation system to ensure the system operates as intended"; and (3) "staff engaged in financial and risk control must be independent, have appropriate authority and be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the firm." The FSF principles on effective alignment of compensation with risk taking are: (4) "compensation must be adjusted for all types of risks"; (5) "compensation outcomes must be symmetric with risk outcomes"; (6) "compensation payout schedules must be sensitive to the time horizon on risk"; and (7) "the mix of cash, equity and other forms of compensation must be consistent with risk alignment." The FSF principles for effective supervisory oversight and engagement by stakeholders are: (8) "supervisory review of compensation practices must be rigorous and sustained and deficiencies must be addressed promptly with supervisory action"; and (9) "firms must disclose clear, comprehensive and timely information about their compensation practices to facilitate constructive engagement by all stakeholders." *Id.*

122. *See generally* Fin. Stability Bd., *FSB Principles for Sound Compensation Practices: Implementation Standards* (Sept. 25, 2009), *available at* www.financialstabilityboard.org/publications/r_090925c.pdf.

123. *See generally* Fin. Stability Bd., *Thematic Review on Compensation: Review Template* (Dec. 22, 2009), *available at* www.financialstabilityboard.org/publications/r_100109b.pdf.

124. *See generally* Fin. Stability Bd., *Thematic Review on Compensation: Peer Review Report* (Mar. 30, 2010), *available at* www.financialstabilityboard.org/publications/r_100330a.pdf; Fin. Stability Bd., *2011 Thematic Review on Compensation: Peer Review Report* (Oct. 7, 2011), *available at* www.financialstabilityboard.org/publications/r_111011a.pdf.

125. The report provides an independent assessment of the implementation issues that arise following a review of twenty systemically-relevant global firms with material business operations in the Americas, Europe, and Asia. Considerable progress had been achieved, although further work was required. Residual challenges were summarized in terms of regulatory, competitive, financial, operation and technical, and organizational challenges. Some further recommendations were made in terms of revising the principles and considering some further extensions. Oliver Wyman, *Banking Compensation Reform: Summary Report of Progress and Challenges Commissioned by the Financial Stability Board*, Fin. Stability Bd. (Mar. 2010), www.financialstabilityboard.org/publications/r_100330b.pdf.

April 2000.[126] This followed the specific concerns raised with regard to HLIs following the Asian financial crisis, including hedge funds and with regard to the forced support of Long Term Capital Management (LTCM).[127] A Progress Report was issued in March 2001 with an Update Assessment in March 2002 that identified specific further concerns with regard to leverage levels, possible disorderly collapse of an unregulated HLI, and market integrity effects in small and medium sized economies.[128] A further Update was issued in May 2007 and Progress Report in October 2007.[129]

The FSB switched its attention following the global financial crisis to Systemically Important Financial Institutions (SIFIs) at the direction of the G20 rather than HLIs specifically. Six interim principles were issued on the moral hazard risks created by SIFIs in June 2010 with a full report on reducing moral hazard being issued in November 2010.[130] Fifty-one recommendations were produced, structured in terms of higher loss absorbency, SIFI resolution, strengthening SIFI supervision, strengthening core financial infrastructures, and ensuring effective and consistent implementation of national policies for global SIFIs (G-SIFIs or GSIFIs). A separate report was issued on Intensity and Effectiveness of SIFI supervision that outlined ten findings on SIFI supervision and contained thirty-two recommendations for supervisory improvement.[131]

Eight further sets of recommendations were made with regard to SIFI resolution in July 2011, which covered resolution powers and tools, cross-border arrangements, planning,

126. This included a definition of HLIs and identification of potential problems for financial stability and available policy options. The Group concluded that market discipline was the most effective means for dealing with systemic risks and market dynamic concerns supported by additional measures to improve supervision and regulation of HLI credit providers, a stronger market infrastructure, increased HLI disclosure, enhanced national market surveillance, and good practice guidelines for foreign exchange trading. The Group rejected creating a credit register and direct regulation of HLIs at that stage. Financial Stability Forum, *Report of the Working Group on Highly Leveraged Institutions*, 138-141 (Apr. 5, 2000), *available at* www.financialstabilityboard.org/publications/r_0004a.pdf.

127. *Id.* at 5.

128. Developments in the market were reviewed, including with regard to counter-party risk management and regulatory oversight, hedge fund risk management practices, hedge fund disclosures, public sector initiatives to enhance hedge fund disclosures, infrastructure improvements, and documentations and national surveillance of financial market activity and functioning. New concerns arose with regard to the marketing of hedge funds to retail investors, capital guaranteed hedge fund products, in-house hedge funds, and terrorism financing and money laundering. Nine further recommendations were made in response to the issues identified. Fin. Stability Forum, *The FSF Recommendations and Concerns Raised by Highly Leveraged Institutions (HLIs): An Assessment*, 3 (Mar. 11, 2002), www.financialstabilityboard.org/publications/r_0203b.pdf.

129. *See Update of the FSF Report on Highly Leveraged Institutions*, FIN. STABILITY FORUM (May 19, 2007), http://www.financialstabilityboard.org/publications/r_0705.htm; *see also Progress in Implementing the Recommendations of the FSF: Update Report on Highly Leveraged Institutions*, FIN. STABILITY FORUM (Oct. 15, 2007), http://www.financialstabilityboard.org/publications/r_0710.htm.

130. *See* Fin. Stability Bd., *Reducing the Moral Hazard Posed by Systemically Important Financial Institutions: Interim Report to G20 Leaders* (June 18, 2010), *available at* www.financialstabilityboard.org/publications/r_100627b.pdf [hereinafter *Reducing the Moral Hazard (June)*]; Fin. Stability Bd., *Reducing the Moral Hazard Posed by Systemically Important Financial Institutions: FSB Recommendations and Time Lines* (Oct. 20, 2010), *available at* www.financialstabilityboard.org/publications/r_101111a.pdf [hereinafter *Reducing the Moral Hazard (Oct.)*.

131. *See generally* Fin. Stability Bd., *Intensity and Effectiveness of SIFI Supervision: Recommendations for Enhanced Supervision*, (Nov. 2. 2010), *available at* www.imf.org/external/np/mcm/financialstability/papers/sifisup.pdf [hereinafter *Intensity and Effectiveness of SIFI Supervision (2010)*].

obstacles to resolvability with some further discussion points.[132] G-SIFI Recovery and Resolution Plans (RRPs) would specifically consist of a separate pre-resolution Recovery Plans (RCPs) and follow-up Resolution Plans (RSPs).[133] Twelve sets of *Key Attributes* for effective resolution regimes would later be produced in November 2011 with specific provisions on RRPs, resolvability, bail-in and cross-border cooperation.[134] A Progress Report on SIFI resolution would be issued in November 2012 with additional "Guidance for Recovery and Resolution Planning."[135]

A common data template for Global Systemically Important Banks (GSIBs) was produced in October 2011 to correct key information gaps identified during the crisis and to assist authorities in constructing more effective frameworks for assessing potential systemic risks.[136] The Basel Committee on Banking Supervision issued an assessment methodology with additional loss absorbency conditions for GSIBs in July 2011, which proposed an additional range of 1 to 2.5 percent, with an additional 3.5 percent Common Equity Tier 1 (CET1) for GSIBs.[137] The Macroeconomic Assessment Group (MAG) set up by the FSB and Basel Committee produced an assessment of the macroeconomic impact of the higher absorbency conditions in October 2011.[138]

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132. Fin. Stability Bd., *Consultative Document: Effective Resolution of Systemically Important Financial Institutions- Recommendations and Timelines*, 8-22 (Jul. 19, 2011), *available at* www.financialstabilityboard.org/publications/r_110719.pdf [hereinafter *Effective Resolution*]. The recommendations were concerned with: (1) "key attributes of effective resolution regimes"; (2) "bail-in within resolution"; (3) "institution specific cross-border co-operation agreement"; (4) "resolvability assessment"; (5) "recovery and resolution plans (RRPs)"; (6) "measures to improve resolvability"; (7) "creditor hierarchy, depositor preference and depositor protection in resolution"; and (8) "conditions for imposing temporary stays on contractual early termination rights." *Id.* at 3-4.

133. *Id.* at 53-60. Specific recommendations were made with regard to underlying assumptions and responsibility for the RCP and RSP, review, and national and cross-border co-ordination. On assumption, RRPs should reflect the specific characteristics of the individual firm and tools available under national resolution regimes with no assumptions being made with regard to taxpayer funding of losses. RRPs should contain an executive summary, strategic analysis, intervention conditions (prerequisites for triggering the implementation of recovery or resolution actions), practical recovery and resolution options, implementation actions, and responsibilities. Additional essential elements for RCPs and RSPs and on information requirements and planning. *Id.*

134. *See generally* Fin. Stability Bd., *Key Attributes of Effective Resolution Regimes for Financial Institutions*, (Oct. 2011), *available at* www.financialstabilityboard.org/publications/r_111104cc.pdf [hereinafter *Key Attributes*].

135. *See generally* Fin. Stability Bd., *Resolution of Systemically Important Financial Institutions: Progress Report* (Nov. 2012), *available at* www.financialstabilityboard.org/publications/r_121031aa.pdf; *see also* Fin. Stability Bd., *Recovery and Resolution Planning: Making the Key Attributes Requirements Operations- Consultative Document* (Nov. 20120), *available at* https://www.financialstabilityboard.org/publications/r_121102.pdf.

136. Fin. Stability Bd., *Understanding Financial Linkages: A Common Data Template for Global Systemically Important Banks- Consultation Paper*, 3 (Oct. 6, 2011), *available at* www.financialstabilityboard.org/publications/r_111006.pdf.

137. Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *Global Systemically Important Banks: Assessment Methodology and the Additional Loss Absorbency Requirement- Cover Note*, 2 (Nov. 2011), *available at* www.bis.org/publ/bcbs207cn.pdf.

138. *See generally* Press Release, Basel Comm. on Banking Supervision, Bank for Int'l Settlements, Assessment of the Macroeconomic Impact of Higher Loss Absorbency for Global Systemically Important Banks (Oct. 10, 2011), *available at* http://www.bis.org/publ/bcbs202.htm.

D. Crisis Management and Resolution

The initial work of the FSF on crisis management had focused on deposit protection. A Study Group on Deposit Insurance had been set up in November 1999, which was subsequently converted into a more formal Working Group. A Background Paper was issued in June 2000[139] with a full report on developing effective deposit insurance systems in September 2001.[140]

While the Basel Committee had issued *Supervisory Guidance on Dealing with Weak Banks* in March 2002,[141] the FSF would not issue its formal paper on *Cross-Border Co-operation on Crisis Management* until April 2009.[142] This consisted of fifteen short principles on preparing for and managing a financial crisis and was partly based on a Joint Task Force Report on Winding Down a Large Complex Financial Institution (LCFI) and relevant EU Principles for Financial Crisis Management.[143] The FSB issued a later specific paper on the effective resolution of SIFIs in July 2011.[144] Its initial attention had focused on reducing or withdrawing the various financial sector support measures that had been adopted to contain markets immediately following the crisis, with specific guidance having been issued on temporary deposit insurance arrangements.[145] It would issue its key attributes for the effective resolution of financial institutions in November 2011.[146] The FSB has also been monitoring the G20 recommendations on carrying out OTC derivatives contracts on exchanges or electronic trading platforms as part of its crisis resolution function.[147]

E. Macro-Prudential Policy

Neither the FSF nor FSB considered the development of macro-prudential policy or oversight mechanisms specifically immediately following the crisis, although work in this area was taken forward subsequently. The FSF April 2008 report on "Enhancing Market

139. *See generally* Fin. Stability Forum Working Group on Deposit Ins., *A Consultation Process and Background Paper* (June 2000), *available at* www.iadi.org/docs/Consultation_Paper_English.pdf.

140. *See generally* Fin. Stability Forum, *Guidance for Developing Effective Deposit Insurance Systems*, (Sept. 7, 2001), *available at* http://www.fdic.gov/deposit/deposits/international/guidance/guidance/finalreport.pdf; *see also* Fin. Stability Forum, *Working Group on Deposit Insurance Progress Report* (Mar. 5, 2001), *available at* www.financialstabilityboard.org/publications/r_0103.pdf (an earlier progress report had been issued in March 2001).

141. Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *Supervisory Guidance on Dealing with Weak Banks: Report of the Task Force on Dealing with Weak Banks* (Mar. 2002).

142. Fin. Stability Forum, *FSF Principles for Cross-Border Cooperation on Crisis Management*, at 1, (Apr. 2, 2009), *available at* http://www.financialstabilityboard.org/publications/r_0904c.pdf [hereinafter *FSF Principles for Cross-Border Cooperation on Crisis Management*].

143. *See generally id.*

144. *Effective Resolution*, *supra* note 80.

145. *Exit from Extraordinary Financial Sector Support Measures: Note for G20 Ministers and Governors Meeting 6-7 November 2009* (Nov. 7, 2009), *available at* http://www.financialstabilityboard.org/publications/r_091107b.pdf; Staff of the Int'l Assoc. of Deposit Insurers and Int'l Monetary Fund, *Report to the Financial Stability Board* (June 2010), *available at* http://www.financialstabilityboard.org/publications/r_1006.pdf.

146. *Key Attributes*, *supra* note 134.

147. Fin. Stability Bd., *OTC Derivatives Market Reforms: Progress Report on Implementation* (Oct. 11, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111011b.pdf [hereinafter *Oct. 2011 Progress Report*].

and Institutional Resilience" only referred to strengthening the authority's responsiveness to risk with robust arrangements being put in place to deal with stress in the financial system.[148] The FSF highlighted the importance of procyclicality in the financial system in April 2009, although this was more concerned with capital, provisioning and valuation, and leverage.[149] The FSB September 2009 paper on improving financial regulation only referred to expanding oversight of the financial system, especially with regard to hedge funds, credit rating agencies, the regulatory perimeter, and regulatory arbitrage.[150]

The FSB Secretariat had been directed by the G20 to work with IMF in April 2009 to explore information gaps and provide appropriate proposals for strengthening data collection. An initial joint report titled *The Financial Crisis and Information Gaps* was produced by the IMF and FSB in October 2009, with the IMF and FSB holding a conference in Basel in April 2010 and a Progress Report being published in May 2010.[151] A further *Implementation Progress Report* was published in June 2011.[152] Twenty recommendations were made in the initial 2009 Report on better capturing the build-up of risk in the financial sector, improving data on international financial network connections, monitoring the vulnerability of domestic economies to shocks, and on the communication of official statistics. The June 2011 Report outlined progress to date with the implementation schedule and residual challenges in terms of resources, priorities and inter-linkages, data access, and international co-ordination.[153]

The issue of developing a coordinated macro-prudential policy framework was referred to in the G20 Seoul Communiqué following the Summit in November 2010, which called on further work to be carried out by the FSB, IMF, and BIS in this area.[154] An Update paper was produced by the FSB, IMF, and BIS in February 2011[155] with a further *Progress Report* being produced in October 2011.[156] The February 2011 Report reviews the work undertaken at the national and international levels to develop effective macro-prudential policies and frameworks, including the survey initiatives taken forward by the Committee on the Global Financial System (CGFS) and IMF.[157] Specific difficulties are identified in

148. *Enhancing Market and Institutional Resilience*, *supra* note 50, §§ V, VI.

149. *Report on Procyclicality*, supra note 66.

150. *Improving Financial Regulation*, *supra* note 67, ¶¶ 42-43.

151. Fin. Stability Bd. & Int'l Monetary Fund, *The Financial Crisis and Information Gaps* (Oct. 29, 2009), *available at* http://www.imf.org/external/np/g20/pdf/102909.pdf; Fin. Stability Bd. & Int'l Monetary Fund, *The Financial Crisis and Information Gaps* (May, 2010), *available at* http://www.financialstabilityboard.org/publications/r_100510.pdf.

152. Fin. Stability Bd. & Int'l Monetary Fund, *The Financial Crisis and Information Gaps* (June 2011), *available at* http://www.imf.org/external/np/g20/pdf/063011.pdf.

153. *Id.*

154. Seoul Summit, Seoul, S. Kor., Nov. 11-12, 2010, *The Seoul Summit Document*, ¶ 41 (Nov. 12, 2010).

155. Fin. Stability Bd., International Monetary Fund & Bank for Int'l Settlements, *Macroprudential Policy Tools and Frameworks: Update to G20 Finance Ministers and Central Bank Governors* (Feb. 14, 2011), *available at* http://www.imf.org/external/np/g20/pdf/021411.pdf [hereinafter *Macroprudential Policy Tools Update*].

156. Fin. Stability Bd., International Monetary Fund & Bank for Int'l Settlements, *Macroprudential Policy Tools and Frameworks: Progress Report to G20* (Oct. 27, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111027b.pdf [hereinafter *Macroprudential Policy Tools Progress Report*].

157. Comm. on the Global Fin. System, Bank for Int'l Settlements, *Macro-Prudential Instruments and Frameworks: A Stocktaking of Issues and Experiences*, CGFS Paper No. 38 (May 2010), *available at* http://www.bis.org/publ/cgfs38.pdf; Monetary and Capital Mkts. Dep't, Int'l Monetary Fund, *Central Banking Lessons from the Crisis* (May 27, 2010), *available at* http://www.imf.org/external/np/pp/eng/2010/052710.pdf. *See also Macroprudential Policy Tools Update*, *supra* note 101, Box 1, 9-10; Int'l Monetary Fund, *Macro-Prudential Policy:*

terms of design and collection of necessary information and data, techniques to identify and measure systemic risk, effective tools, and governance arrangements.[158]

In the October 2011 Report, the core characteristics of macro-prudential policy are defined in terms of its objective of being to limit systemic risk, its scope focusing on the financial system as a whole, and its primary use of prudential tools re-calibrated to deal with sources of systemic risk and subject to effective governance arrangements.[159] A number of key measurement approaches are identified in terms of monitoring aggregate indicators of imbalances, market condition indicators, metrics of concentration risk, macro stress testing, and integrated monitoring systems.[160] These have to be used to capture both the time and cross-sectional elements of systemic risk.[161] The need to assess the build-up of systemic risk across the financial system, including within the shadow banking area, was highlighted.[162] Initiatives in the area of enhancing data infrastructure and material gaps in data collection were referred to. The most commonly used macro-prudential tools or instruments were summarized in terms of dealing with excessive credit expansion,[163] amplification mechanisms,[164] and limiting structural vulnerabilities and stress spill-over.[165]

Empirical studies have confirmed that pro-cyclicality tools, including loan to value (LTV) and debt to income (DTI) caps, can limit property booms with credit or credit growth caps, reserve requirements, and dynamic provisioning.[166] International policy tools included the procyclical elements within the new Basel III framework with its maximum leverage ratio, capital conservation buffer, and counter-cyclical capital buffer and proposed additional SIFI and GSIB measures. The CGFS had also recommended the possible imposition of additional haircuts and margining practices to limit the build-up of leverage and system-wide effects of rapid de-leveraging.[167] Other work was being taken forward on improving market operations and market infrastructure and on OTC derivatives.[168]

An Organizing Framework-Background Paper (Mar. 2011). The FSB, IMF, and BIS also held two workshops on "High-Level Conference in Macro-Prudential Policy Frameworks" (Washington, April 17, 2011) and "Roundtable on Macro-Prudential Frameworks and Policies" (Basel, June 21-22, 2011).

158. *Id.*

159. *See generally Macroprudential Policy Tools Progress Report*, *supra* note 156.

160. *Id.* ¶ 2.1.

161. *Id.*

162. Fin. Stability Bd., *Shadow Banking: Strengthening Oversight and Regulation* (Oct. 27, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111027a.pdf [hereinafter *Shadow Banking*].

163. Tools to deal with excessive credit expansion include: (1) time varying capital requirements; (2) dynamic provision; (3) credit or credit growth ceilings; (4) loan-to-value (LTV) ration limits on a static or time varying basis; (6) minimum margin requirements on a fixed or time varying basis; and (7) reserve requirements. *See generally Macroprudential Instruments and Frameworks*, supra note 157; *see also id.* at 11.

164. Tools to limit the amplification of systemic risk include: (1) maturity mismatch limits; (2) limit of foreign currency lending; (3) limits on net open currency positions or mismatches; (4) non-core funding levies. *Shadow Banking*, *supra* note 162.

165. Tools to limit structural vulnerabilities and spill-over effects include: (1) additional loss absorbency tied to systemic importance; (2) market and institution disclosure policies targeting systemic risk; and (3) SIFI resolution requirements. *Id.*

166. *Id.* at 12.

167. *Shadow Banking*, *supra* note 162, at 13.

168. Comm. on Payment and Settlement Sys. & Technical Comm. of the Int'l Org. of Secs. Comm'ns, Bank for Int'l Settlements, *Principles for Financial Market Infrastructures: Consultative Report* (Mar. 2011), *available at*

The October 2011 Report considered governance arrangements in terms of mandate, powers and instruments, accountability, composition and domestic policy consistency, and coordination.[169] It was essential that macro-prudential policy was appropriately coordinated at the international level with a number of separate initiatives being referenced.[170] Policy arbitrage in the macro-prudential area would be partly limited through "embedded reciprocity" provisions within new standards, including the Basel Committee counter-cyclical capital buffers and FSB G-SIFIs recommendations. Countries had still to retain sufficient flexibility in assessing local needs and to be able to act quickly to avoid damaging spill-over effects.[171]

F. Shadow Banking

The G20 Seoul Summit Communiqué in November 2010 had referred to the need to strengthen regulation and supervision of the shadow banking sector.[172] Shadow banking had increased from $27 trillion in 2002 to $60 trillion by 2007 and remained generally the same until 2010.[173] Important background papers had been issued by the Federal Reserve,[174] with the European Commission issuing separate reports subsequently.[175] The FSB held a workshop in London with relevant experts on December 6, 2010, to consider relevant definitions, monitoring approaches, and regulatory measures. A Task Force was set up and issued the *Background Note on Shadow Banking: Scoping the Issues* in April 2011.[176] Shadow banking was generally defined as credit intermediation involving entities and activities outside the regular banking system that either raised systemic risk concerns (through maturity/liquidity transformation, leverage, and imperfect (flawed) credit risk transfer) or regulatory arbitrage.[177]

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http://www.bis.org/publ/cpss94.pdf. The FSB had issued recommendations to promote international consistency on standardization, central clearing, organized platform trading, and use of trade repositories in connection with OTC derivatives contracts. Other initiatives were being considered regarding central bank liquidity access for CCPs, the macro-financial effects of different CCP access options, and margining requirements for non-centrally cleared OTC derivatives. Securitization practices were also being reviewed with possible recommendations on sound securitization markets. *See id.* at 14-15.

169. *Id.* at 15-19.

170. These included the FSB Standing Committee on Assessment of Vulnerabilities work, the IMF bilateral and multilateral surveillance work, the IMF/FSB "Early Warning Exercise," the G20 "Mutual Assessment Process," and BIS and CGFS survey work. *Id.* at 19.

171. *Id.* at 19-20.

172. *See* Seoul Summit, *supra* note 154, ¶ 41.

173. *Commission Green Paper: Shadow Banking*, COM (2012) 102 final (Mar. 19, 2012).

174. *See* Zoltan Pozsar, Tobias Adrian, Adam Ashcraft & Hayley Boesky, Shadow Banking, (Federal Reserve Bank of New York Staff Report No. 458, 2010) (revised Feb. 2012).

175. *See Commission Green Paper: Shadow Banking*, supra note 173.

176. Monitoring was considered in terms of macro and micro oversight, with regulatory measures including indirect regulation of banks' interactions with shadow banks, direct shadow bank activity regulation, instrument or risk regulation, and macro-prudential measures, including pro-cyclicality or reducing contagion in market infrastructure. *See* Fin. Stability Bd., *Shadow Banking: Scoping the Issues- A Background Note of the Financial Stability Board* (Apr. 12, 2011), *available at* http://www.financialstabilityboard.org/publications/r_110412a.pdf.

177. *Supra* § I; *id.* § 1.2.

The Task Force on Shadow Banking produced initial recommendations that were approved by the FSB at its Plenary Meeting in July 2011.[178] Five separate work streams would be set up on indirect regulation and bank interaction, money market funds (MMFs), other shadow banking entity regulation, securitization and securities lending, and repos.[179] Information would be collected through Flow of Funds and Sector Balance Sheet data to assess the scale and development of non-bank credit intermediation, with further preparation being carried out on future data collection and assessment. A series of monitoring exercises were conducted over summer 2011 with more substantial recommendations being formulated. The Task Force was chaired by the United Kingdom Financial Services Authority (FSA) Chairman Lord Adair Turner and BIS General Manager, Jaime Caruana.[180]

A formal report on shadow banking was produced in October 2011.[181] This generally deals with overall approach (Section 1), monitoring (Section 2), and enhancing regulation (Section 3). Seven high-level principles are identified for monitoring the shadow banking system based on scope, process, data/information, innovation/mutation, regulatory arbitrage, justification, and information exchange.[182] A stylized three-step approach is constructed to strengthen monitoring based on scanning and mapping, systemic risk identification, and assessment.[183] A further series of five general principles are adopted in designing and implementing regulatory measures for shadow banking based on focus, proportionality, forward-looking and adaptability, effectiveness and assessment, and review.[184] Eleven more specific recommendations are then produced in applying these principles to the areas of concern identified in the Background Note and July Plenary Meeting.[185] The FSB issued a Progress Report in April 2012 with a separate *Report on Securities Lending and Repos*.[186]

178. *See* Press Release, Fin. Stability Bd., The Financial Stability Board's Work on Shadow Banking: Progress and Next Steps, 37/2011 (Sept. 1, 2011), *available at* http://www.financialstabilityboard.org/press/pr_110901.pdf.

179. *Id.*

180. *Id.*

181. *See Shadow Banking*, *supra* note 162.

182. The High-level principles are: (a) authorities should maintain an appropriate system-wide oversight framework of shadow banking and its risks; (b) the monitoring framework should identify and assess risks on a regular and continuing basis; (c) authorities should have power to collect all necessary data and information and define the regulatory perimeter for reporting; (d) monitoring should be flexible and adaptable to cover innovations and mutations producing emerging risks; (e) authorities should recognize incentives to expand shadow banking in response to regulation; (f) the structure of financial markets and regulatory framework should be considered at the domestic level and international connections; and (g) there should be appropriate exchange of information within and across jurisdictions on a regular basis. *See id.* at 6.

183. The three steps consist of: (a) scanning and mapping the overall shadow banking system; (b) identification of specific aspects creating systemic risk or regulatory arbitrage concern; and (c) detailed assessment of relevant concerns. *See id.* at 7.

184. *Id.* at 15.

185. These were generally based on consolidation, quantitative limits, risk-based assessment, implicit support, MMF reform, other activity review, securitization incentives, securities lending and repo assessment, transparency and reporting, improved underwriting, and reduced CRAs' role. *Id.* at 16-26.

186. *See* Fin. Stability Bd., *Strengthening the Oversight and Regulation of Shadow Banking: Progress Report to G20 Ministers and Governors* (Apr. 16, 2012), *available at* http://www.financialstabilityboard.org/publications/r_120420c.pdf; Fin. Stability Bd., *Securities Lending and Repos: Market Overview and Financial Stability Issues-Interim Report of the FSB Workstream on Securities Lending and Repos* (Apr. 27, 2012), *available at* http://www.

The FSB issued a more general consultative document titled *Strengthening Oversight and Regulation of Shadow Banking* in November 2012, which contained an integrated overview of policy recommendations, with two specific papers on other shadow banking activity oversight and on securities lending and repos.[187] The FSB published the results of its second annual monitoring exercise of global shadow banking activity on the same day, which contained data on total financial intermediary assets, share of total financial assets, and non-bank intermediary assets.[188] The *Integrated Overview* document explains the FSB's concerns, approach, and outline recommendations on monitoring and regulation. Authorities had to adopt a targeted approach to shadow banking with the objective of ensuring that it was subject to appropriate oversight and regulation to cover "bank-like" risks to financial stability arising outside the regular banking system without inhibiting sustainable non-bank financing models without equivalent risk. The FSB supported the development of a resilient system of non-bank credit intermediation with a proportionate approach adopted toward financial stability risks.[189] A two-stage approach was generally adopted with all forms of non-bank credit intermediation being monitored to ensure that data gathering and surveillance was sufficiently wide, with authorities then focusing on specific sub-sets of activity creating systemic or arbitrage concerns.

A number of proposals have been developed in each of the five work streams identified to limit shadow banking runs, procyclicality, and systemic risk. A comprehensive approach had also been adopted in response to the interconnectedness of markets and adaptive capacity of the shadow banking system.[190] The second monitoring exercise, conducted in summer 2012, confirmed the interconnectedness between banks and non-bank financial entities, specifically including finance companies, with further improvements being required in data collection and granularity (sub-divisions).[191] The rest of the report focuses on the progress achieved by the FSB or its member organizations in each of the five work streams identified (WS1-5).[192]

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financialstabilityboard.org/publications/r_120427.pdf. The comments received on the April 2012 Securities Lending and Repo report were published in May 2012 on the FSB website.

187. *See* Fin. Stability Bd., *Strengthening Oversight and Regulation of Shadow Banking: An Integrated Overview of Policy Recommendations* (Nov. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121118.pdf; Fin. Stability Bd., *A Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities* (Nov. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121118a.pdf; Fin. Stability Bd., *Strengthening Oversight and Regulation of Shadow Banking: A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos* (Nov. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121118b.pdf.

188. *See* Fin. Stability Bd., *Global Shadow Banking Monitoring Report 2012* (Nov. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121118c.pdf [hereinafter *Global Shadow Banking Monitoring Report*]; Fin. Stability Bd., *Global Shadow Banking Monitoring Report 2012, Exhibits 2-1, 2-2, 2-3* (Nov. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121128.pdf.

189. *See Global Shadow Banking Monitoring Report*, *supra* note 188, at 1.

190. *Id.* at 2.

191. Macro-mapping confirmed that non-bank financial intermediation grew substantially before the crisis and continued subsequently at a much slower pace. There was considerable diversity in the relative size and composition of non-bank financial intermediaries across jurisdictions. Data granularity improved, with the share of unidentified non-bank financial intermediation reduced from 36 percent to 18 percent. More detailed breakdowns of activity categories were nevertheless required across countries to increase granular analysis. *See id.*

192. *Id.* at 5-14.

G. Enhanced Disclosure

The FSF issued an initial report, *Improved Disclosure Practices for Financial Intermediaries*, in April 2001 at the same time as a Multidisciplinary Working Group report on enhanced disclosure.[193] A Senior Supervisor's group published a separate report entitled *Leading-Practice Disclosures for Selected Exposures* in April 2008.[194]

The FSB produced a request for comments on "Risk Disclosure Practices" in July 2010 as part of a peer review of the implementation of the recommendations contained in the FSF April 2008 Report, with a thematic review being conducted on risk disclosure in March 2011.[195] The FSB established an Enhanced Disclosure Task Force (EDTF) in May 2012 after a roundtable meeting of senior officials and experts in December 2011, which considered means of improving the quality, compatibility, and transparency of risk disclosures, while at the same time reducing the use of redundant information so as to streamline the bringing of disclosures to the market in a timely manner.[196]

The EDTF produced a report, *Enhancing the Risk Disclosures of Banks*, in October 2012.[197] This established seven fundamental principles to enhanced disclosure practices to produce high quality, transparent disclosures that could clearly communicate business models and key risks.[198] The EDTF had established six work streams on governance, capital, liquidity, funding, market, and credit, amongst other risks.[199] A number of private sector press statements were subsequently produced from major banking institutions, banking associations, investors, end users, SSBs, and audit firms confirming support.[200]

H. Supervision

The FSB issued a specific report on the intensity and effectiveness of SIFI supervision in November 2010, with second and third progress reports issued in November 2011 and

193. Press Release, Fin. Stability Forum, Report Recommends Improved Disclosure Practices for Financial Intermediaries (Apr. 26, 2001), http://www.bis.org/press/p010426.htm; Basel Committee on Banking Supervision et. al, *Multidisciplinary Group on Enhanced Disclosure: Final Report* (Apr. 26, 2001), *available at* http://www.financialstabilityboard.org/publications/r_010426.pdf.

194. Senior Supervisor's Group, *Leading-Practice Disclosures for Selected Exposures* (Apr. 11, 2008), *available at* http://www.newyorkfed.org/newsevents/news/banking/2008/SSG_Leading_Practice_Disclosures.pdf; Fin. Stability Bd., *Thematic Review on Risk Disclosure Practices* (Mar. 18, 2011), *available at* http://www.financialstabilityboard.org/publications/r_110318.pdf [hereinafter *Thematic Review*].

195. Press Release, Fin. Stability Bd., FSB invites Feedback on Risk Disclosure Practices (July 21, 2010), *available* at http://www.financialstabilityboard.org/press/pr_100721.pdf; *Thematic Review*, *supra* note 194.

196. Press Release, Fin. Stability Bd., Formation of the Enhanced Disclosure Task Force (May 10, 2012), *available at* http://www.financialstabilityboard.org/press/pr_120510.pdf.

197. Enhanced Disclosure Task Force, Fin. Stability Bd., Enhanced Disclosure Task Force, *Enhancing the Risk Disclosures of Banks* (Oct. 29, 2012), *available at* https://www.financialstabilityboard.org/publications/r_121029.pdf.

198. The seven fundamental principles on enhanced disclosure consisted of: (a) disclosures being clear, balanced, and understandable; (b) disclosures being comprehensive and including all key activities and risks; (c) present relevant information; (d) disclosures reflecting the manner in which the bank manages the risks; (e) disclosures being consistent over time; (f) disclosures being compatible with other banks; and (g) disclosures being provided on a timely basis. *Id.* at 6.

199. *Id.* at 2.

200. Fin. Stability Bd., *Private Sector Press Statements and Informative Releases in Response to the EDTF Report* (Dec. 18, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121218.pdf.

2012.[201] The November 2010 paper contains a number of recommendations, under ten headings, intended to make the supervision of financial institutions more intense, effective, and reliable, while also following a coordinated assessment of the principal lessons from the global financial crisis.[202] The report contains thirty-two specific recommendations intended to improve the supervision of SIFIs, as well as supervisory practices more generally.

A Supervisory Intensity and Effectiveness (SIE) group was set up within the FSB, which produced the 2011 and 2012 progress reports. A number of difficulties and supervisory challenges were referred to in the November 2011 report.[203] Work was also reviewed in other areas, including acquisitions, Supervisory Colleges, stress testing, corporate governance, and macro-prudential surveillance or oversight, with FSB members submitting self-assessments against the Basel *Core Principles for Effective Banking Supervision*.[204] Five follow-up recommendations were made on supervisory expectations, resource adequacy, progress assessment, thematic review, and audit quality.[205] The report contains detailed examples of recommended disclosures on capital, liquidity, funding, and credit risk, as well as examples of leading or best-practice disclosures in current bank reporting.[206]

I. Financial Derivatives

The G20 Leaders agreed at their Pittsburgh meeting that all standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where possible, and cleared through central counterparties by the end of 2012, with all OTC derivative contracts being reported through trade repositories. A Working Group was set up in April 2010 at the initiative of the FSB, with the Committee on Payment and Settlement Systems (CPSS), the International Organization of Securities Commissions (IOSCO), and the European Commission to bring forward recommendations to implement the G20 commitments.

The FSB set up a separate internal OTC Derivatives Working Group (ODWG), with an initial report being produced on "Implementing OTC Derivatives Market Reforms" in October 2010 and implementation reports published in April 2011, October 2011, and

201. *See Intensity and Effectiveness of SIFI Supervision (2010)*, *supra* note 131; Fin. Stability Bd., *Intensity and Effectiveness of SIFI Supervision: Progress Report on Implementing the Recommendations for Enhanced Supervision* (Oct. 27, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111104ee.pdf [hereinafter *Intensity and Effectiveness of SIFI Supervision (2011)*]; Fin. Stability Bd., *Increasing the Intensity and Effectiveness of SIFI Supervision: Progress Report to the G20 Ministers and Governors* (Nov. 1, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121031ab.pdf.

202. The recommendations are based on mandates, independence, resources, supervisory powers, improved techniques, group-wide and consolidated supervision, continuous and comprehensive supervision, supervisory colleges and home/host information sharing, macro-prudential surveillance (including multi-disciplinary approach), and the use of third parties. *See Intensity and Effectiveness of SIFI Supervision (2010)*, *supra* note 131, § II, Appendix A. The senior line supervisors that contributed to the report are listed in Appendix B.

203. These included data aggregation, resources, business models and financial analysis, risk appetite frameworks (RAF), model risk, and external auditor. *See Intensity and Effectiveness of SIFI Supervision* (2011), *supra* note 201. § II.

204. *Id.* at 1.

205. *Id.* at 20-23.

206. *Id.* at 24-26.

June 2012, along with a final report in October 2012.[207] The ODWG had conducted a survey of Central Counterparty (CCP) and Trade Repository (TR) practices in July 2012, with FSB members also being asked to set out their approaches to central clearing in August 2012.[208]

The Group's recommendations have principally been concerned with increasing standardization, promoting central clearing and trading on exchanges or electronic trading platforms, trade repository reporting, assessing progress, and cooperating on market reforms. Market infrastructure was in place and could be scaled up by the time of the final report in October 2012 and cover all of the five major asset classes identified, including commodity, credit, equity, foreign exchange, and interest rate products. Policy work on safeguards for global clearing had been substantially completed, while national implementation work is continuing. Regulatory uncertainty remained the most significant obstacle, with authorities having been encouraged to identify and resolve any residual conflicts, inconsistencies, and gaps.[209]

J. Legal Identifiers

The FSB has been the key coordinating body in the development of a Global Legal Entity Identifier (LEI) system that would provide unique numeric and alphabetic identifications for parties to financial transactions. This was agreed at the Cannes G20 Summit with the FSB producing an initial report before the Los Cabos Summit.[210] This outlined the proposed Global LEI System with development and implementation recommendations, high-level principles, and outline provisions for inclusion within the Charter of the new Global LEI Regulatory Oversight Committee (ROC).[211] The objective was to establish an independent, open, fair, and transparent system. The FSB had earlier set up an internal LEI Expert Group with an outside LEI Industry Advisory Panel and separate LEI Implementation Group. A substantial amount of work has subsequently been carried out in bringing the legal identifier initiative forward.[212]

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207. Fin. Stability Bd., *Implementing OTC Derivatives Market Reforms* (Oct. 25, 2010), *available at* http://www.financialstabilityboard.org/publications/r_101025.pdf; Fin. Stability Bd., *OTC Derivatives Market Reforms: Progress Report on Implementation* (Apr. 15, 2011), *available at* https://www.financialstabilityboard.org/publications/r_110415b.pdf; *Oct. 2011 Progress Report*, *supra* note 147; Fin. Stability Bd., *OTC Derivatives Market Reforms: Third Progress Report on Implementation* (June 15, 2012), *available at* https://www.financialstabilityboard.org/publications/r_120615.pdf; Fin. Stability Bd., *OTC Derivatives Market Reforms: Fourth Progress Report on Implementation* (Oct. 31, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121031a.pdf [hereinafter FSB, *Fourth Progress Report*].

208. Fin. Stability Bd., *Jurisdictions' Declared Approaches to Central Clearing of OTC Derivatives: Secretariat Information Note* (Nov. 5, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121105a.pdf.

209. Nineteen CCPs had been set up in nine jurisdictions and Fourteen TRs. Summary information was provided in Appendices A and B. A summary of national implementation progresses, cataloged by country, was provided. FSB, *Fourth Progress Report*, *supra* note 207, at 13 n.42.

210. Fin. Stability Bd., *A Global Legal Entity Identifier for Financial Markets* (June 8, 2012), http://www.financialstabilityboard.org/publications/r_120608.pdf.

211. *Id.* at 8.

212. *See generally Legal Entity Identifier*, Fin. Stability Board, http://www.financialstabilityboard.org/list/fsb_publications/tid_156/index.htm (last visited July 31, 2013).

K. Credit Risk Transfer and Service Regulation

The FSF and FSB have been involved in other areas of reform activity. In addition to its work on capital flows, OTCs, HLIs, and Deposit Protection, the FSF had cooperated with the Joint Forum on Financial Conglomerates on Credit Risk Transfer (CRT), with three reports being produced in October 2004, March 2005, and April 2008.[213] The FSB has also subsequently issued separate papers on such other issues as emerging markets and developing economies, residential mortgage underwriting, consumer finance protection, and the availability of long-term finance.[214]

L. Standards Implementation

The issue of standards implementation was initially considered by the FSF. The FSF produced a working group report on Offshore Financial Centres (OFC) in April 2000 with two reports by a Follow-Up Group on *Incentives to Foster Implementation of Standards* in September 2000 and 2001.[215] The FSB issued a statement on a framework for strengthening adherence to international standards in January 2010,[216] with a separate initiative to promote global adherence to cooperation and information exchange standards in March 2010, and with follow-up papers being produced in April and October 2011 and November 2012.[217] The FSB confirmed its commitment to strengthening adherence to

213. Fin. Stability Forum, *Credit Risk Transfer Activity*, Fin. Stability Board (Sept. 21, 2003), http://www.financialstabilityboard.org/publications/r_0309.htm; Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *The Joint Forum: Credit Risk Transfer* (Oct. 2004); Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *The Joint Forum: Credit Risk Transfer* (Mar. 2005); Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *The Joint Forum: Credit Risk Transfer- Developments from 2005 to 2007* (Apr. 2008).

214. Fin. Stability Bd., Int'l Monetary Fund & Bank for Int'l Settlements, *Financial Stability Issues in Emerging Market and Developing Economies: Report to the G-20 Finance Ministers and Central Bank Governors* (Oct. 20, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111019.pdf; Fin. Stability Bd., *Identifying the Effects of Regulatory Reforms on Emerging Market and Developing Economies: A Review of Potential Unintended Consequences* (June 19, 2012), *available at* http://www.financialstabilityboard.org/publications/r_120619e.pdf; Fin. Stability Bd., *Consultation Paper: FSB Principles for Sound Residential Mortgage Underwriting Principles* (Oct. 26, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111026b.pdf; Fin. Stability Bd., *FSB Principles for Sound Residential Mortgage Underwriting Practices* (Apr. 2012), *available at* http://www.financialstabilityboard.org/publications/r_120418.pdf; Fin. Stability Bd., *Financial Regulatory Factors Affecting the Availability of Long-Term Finance: Report to G20 Finance Ministers and Central Bank Governors* (Feb. 8, 2013), *available at* http://www.financialstabilityboard.org/publications/r_130216a.pdf.

215. *See* Fin. Stability Forum, *Report of the Working Group on Offshore Centres* (Apr. 5, 2000), *available at* http://www.financialstabilityboard.org/publications/r_0004b.pdf; Fin. Stability Forum, *Report of the Follow-Up Group on Incentives to Foster Implementation of Standards* (Aug. 31, 2000), *available at* http://www.financialstabilityboard.org/publications/r_0009.pdf [hereinafter *Report of the Follow-Up Group (2000)*]; Fin. Stability Forum, *Final Report of the Follow-Up Group on Incentives to Foster Implementation of Standards* (Aug. 21, 2001).

216. *See* Fin. Stability Bd., *FSB Framework for Strengthening Adherence to International Standards* (Jan. 9, 2010), *available at* http://www.financialstabilityboard.org/publications/r_100109a.pdf.

217. *See* Fin. Stability Bd., *Promoting Global Adherence to International Cooperation and Information Exchange Standards* (Mar. 10, 2010), *available at* http://www.financialstabilityboard.org/publications/r_100310.pdf; Fin. Stability Bd., *Promoting Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange* (Apr. 29, 2011), *available at* http://www.financialstabilityboard.org/publications/r_110429.pdf; Fin. Stability Bd., *Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange: Public Statement* (Nov. 2, 2011); Fin. Stability Bd., *Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange: Status update* (Nov. 2, 2012), *available at* http://www.financialstabilityboard.org/publications/r_121102a.pdf.

international financial standards in January 2010 through "leading by example," with FSB member jurisdictions being committed to implement relevant standards and disclose their adherence, participate in periodic peer reviews, and comply with the measures set out in the toolbox to encourage adherence to standards on international cooperation and information exchange.[218] This toolbox was developed in the subsequent documents in 2011 and 2012.

The FSF had issued a number of papers on implementation. Work in this area dates from the establishment of a Study Group on Implementation of Standards by the FSF in November 1999 with an Issue Paper being produced in March 2000, as well as other follow-up group reports.[219] The FSF had identified 12 policy areas for priority implementation selected in accordance with specified criteria, including: relevant and critical, universal, flexible, broadly endorsed, and assessable. These would form the key measures within the FSF and the FSB Compendium of Standards, which still effectively constitutes the international rulebook for financial regulatory provisions.

This work would subsequently be taken forward by the FSB following the global financial crisis. A general framework was issued in January 2010, with two specific initiatives on co-operation and information exchange, as well as regulatory and supervisory standards.[220] These aimed to achieve a "race to the top" by encouraging all countries and jurisdictions to adhere properly to all relevant international financial standards. Three specific mechanisms were developed based on leading by example,[221] periodic thematic and single country peer reviews,[222] and the introduction of adherence procedures, including those by non-co-operative jurisdictions.[223]

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218. *See FSB Principles for Sound Residential Mortgage Underwriting Practices*, *supra* note 214, at 9.

219. Fin. Stability Forum, *Issues Paper of the Task Force on Implementation of Standards* (Mar. 25-26, 2000), *available at* https://www.financialstabilityboard.org/publications/r_0003.pdf; Fin. Stability Forum, *Report of the Follow-Up Group on Incentives to Foster Implementation of Standards* (Sept. 6-7, 2000), *available at* http://www.financialstabilityboard.org/publications/r_0009.pdf; Fin. Stability Forum, *Final Report of the Follow-Up Group on Incentives to Foster Implementation of Standards* (Sept. 6-7, 2001), *available at* http://www.financialstabilityboard.org/publications/r_0109a.pdf.

220. *FSB Framework for Strengthening Adherence to International Standards*, *supra* note 216; *Promoting Global Adherence to International Cooperation and Information Exchange Standards*, *supra* note 217; *available at* http://www.financialstabilityboard.org/publications/r_100310.pdf; *Promoting Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange*, *supra* note 217.

221. FSB members had committed to implementing relevant international standards, assessed under the IMF World Bank FSAP program every five years, as well as disclosure of adherence levels. *See FSB Framework for Strengthening Adherence to International Standards*, *supra* note 216, Annex A. FSB members also committed to undergoing periodic peer reviews.

222. The peer reviews would complement, but not duplicate, the existing IMF (WB FSAPs) and ROSCs. Thematic reviews would compare policy and standards implementation across countries with country peer reviews focusing on individual country adherence. Reports would be produced by experts from FSB member countries and international institutions under the Standard Committee on Standards Implementation. The FSB prepared a *Handbook for FSB Peer Reviews*.

223. The FSB was developing procedures to secure adherence by all countries, including non-cooperative jurisdictions. This work would specifically focus on securing international cooperation and information exchange in the regulatory and supervisory areas. A pool of countries would be examined to attempt to assess and improve adherence. Countries would be ranked according to domestic financial assets, external financial assets and liabilities, gross capital flows, and market share of selected global market segments (including cross-border inter-bank assets, pension fund assets, hedge fund assets, OTC derivatives, and insurance premiums). *See Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange: Status Update*, *supra* note 217.

A number of specific papers and press releases have been produced subsequently on implementation of the FSB recommendations on *Enhancing Market and Institutional Resilience* and related G20 measures.[224] The G20 and FSB agreed a Co-ordination Framework for Implementation Monitoring (CFIM) in October 2011.[225] This would build on existing mechanisms but create a coordinated new mechanism for monitoring G20/FSB recommendations specifically. Other facilities included the IMF/World Bank Financial Sector Assessment Programmes (FSAPs) and Reports on the Observance of Standards and Codes (ROSCs) with the FSB having a simpler Implementation Monitoring Network (IMN) and with other standard setting bodies (SSBs) operating their own processes.[226] Monitoring was also carried out by the FSB through its Standing Committee on Standards Implementation (SCSI), which would be incorporated within the new CFIM under the FSB, IMN, and SSB mechanisms. The FSB also published separate substantial *Ongoing and Recent Work* reports every six months on work being carried out in strengthening financial systems by the FSB and other financial institutions, groups, and committees.[227]

V. Financial Stability Comment and Conclusions

A substantial work program has been brought forward and a large number of informed papers have been issued by the FSB since its establishment in 2009. While this has extended some of the earlier work of the FSF following the Asian financial crisis, much of this is original and in response to the new challenges generated by the global financial crisis. The FSB has emerged as the most senior institution in the hierarchy of international technical agencies and new international financial architecture constructed. While substantial progress has been made, a significant amount of further reform work remains to be carried out.

The following provisional comments and conclusions may be drawn with regard to the significance and contribution of the FSB to date.

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224. Fin. Stability Forum, *Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience: Follow-up on Implementation*, (Oct. 10, 2008), *available at* http://www.financialstabilityboard.org/press/pr_081009f.pdf; Fin. Stability Forum, *Report on Enhancing Market and Institutional Resilience: Update on Implementation* (Apr. 2, 2009), http://www.financialstabilityboard.org/publications/r_0904d.pdf; *Overview of Progress in Implementing the London Summit, supra* note *112*; Fin. Stability Bd., *Overview of Progress Since the Pitisburgh Summit in the Implementation of the G20 Recommendations for Strengthening Financial Stability* (June 18, 2010), *available at* http://www.fsa.go.jp/inter/fsf/20100702/03.pdf; Fin. Stability Bd., *Progress since the Washington Summit in the Implementation of the G20 Recommendations for Strengthening Financial Stability* (Nov. 8, 2010), *available at* http://www.financialstabilityboard.org/publications/r_101111b.pdf; Fin. Stability Bd., *Progress in the Implementation of the G20 Recommendations for Strengthening Financial Stability* (Feb. 2011), *available at* http://www.financialstabilityboard.org/publications/r_110415a.pdf; Fin. Stability Bd., *Progress in the Implementation of the G20 Recommendations for Strengthening Financial Stability* (Apr. 10, 2011), *available at* http://www.financialstabilityboard.org/publications/r_110415a.pdf. *See also* Mario Draghi, Chairman, Fin. Stability Bd., *To G20 Leaders: Progress and Issues on the Global Regulatory Reform Agenda* (June 24, 2010), *available at* http://www.financialstabilityboard.org/publications/r_100627a.pdf. .

225. Fin. Stability Bd., *A Coordination Framework for Monitoring the Implementation of Agreed G20/FSB Financial Reforms* (Oct. 2011), *available at* http://www.financialstabilityboard.org/publications/r_111017.pdf.

226. *Id.* at Annex A.

227. Fin. Stability Forum, *Ongoing and Recent Work Relevant to Sound Financial Systems* (Mar. 6, 2009), *available at* http://www.financialstabilityboard.org/publications/on_0903.pdf; *Ongoing and Recent Work Relevant to Sound Financial Systems*, FIN. STABILITY BD. (June 11, 2010), http://www.financialstabilityboard.org/publications/on_1006.htm.

A. FSF AND FSB TRANSITION

The FSB has enjoyed a successful transition from its earlier FSF origins with a number of important actions being taken to strengthen its capacity, resources, and governance, especially following the Cannes, November 2011 Summit. While Steering Committee meetings are of a similar size to the earlier full FSF meetings, Plenary Representation has almost doubled. It is interesting that the revised June 2012 Charter does not place any limits on the nature or size of its composition and only refers to member authorities from jurisdictions responsible for financial stability, IFIs and international SSBs, including central bank bodies on an unlimited basis (Article 5).

The internal organizational structure and governance arrangements are clearly set out in Article 7 of the Charter, while the specific responsibilities of each of the internal parts of the FSB are detailed in Articles 9-22, and the express consultation, accountability, and transparency requirements in Articles 3 and 4. Key membership provisions and further organizational directions are set out in Articles 3-6 of its new Articles of Association, which were adopted in January 2013.[228] Funding is also expressly provided for under the BIS, by way of a Multi-Year Funding Agreement and through voluntary member contribution under Article 7 of its Articles. Its accounts and annual financial statements are to be audited by external auditors under Article 8. All of this substantially improves the funding stability and accountability of the FSB.

The functions of the Secretariat are expanded in Article 22 of the Charter. The Secretariat is to be directed by a Secretary General appointed by the Plenary for a five-year term and then responsible to the Chair. Secretariat staff are to be appointed on a balanced-composition basis, having regard for geographic and institutional function and retention of 'institutional memory' through the use of open-ended contracts. The Secretary General and Secretariat are stated to owe their duties entirely to the FSB and to no other authorities' institutions, although they are to be located in Basel at the BIS. The principal responsibilities of the Secretariat are also specified in the Charter. All of this strengthens its operational integrity and independence.

The liability of the Association is limited under Article 9 of the Articles with members not being responsible for its liabilities. Despite these strengthened arrangements and the conferment of legal status under the Articles on the FSB as an Association under Article 60 of the Swiss Civil Code, the activities and any decisions of the FSB are expressly stated not to be binding or to give rise to any legal rights or obligations under Article 10 of the Articles, with the Charter not intended to create any legal rights or obligations under its Article 23. Membership does not constitute any waiver of sovereign immunity or IFI privilege or immunity unless otherwise provided for.

The effect of this is to confirm the status of the FSB as a leading international institution despite its still relatively limited size. It has clear organizational, governance, and funding arrangements with a dedicated Secretariat independent from the BIS and member institutions. This will apply even where Secretariat staff are appointed on recommendation from other organizations. Limited liability is confirmed with legal effect excluded. While the legal effectiveness of any of the FSB's work is expressly excluded, this can be considered necessary in light of the highly sensitive nature of its activities and the need for

228. *See FSB Articles of Association*, *supra* note 96.

these to be conducted on an informal and extralegal basis, with implementation being dealt with through member commitment, adherence, and national adoption. Much of this continues the earlier consensus based nature of the Basel Committee model. The only significant anomaly is that no other non-formal, IFI technical committee has been given similar status.[229] This was presumably considered necessary in light of the immediate and potentially longer term importance of the FSB as the central standard setting body at the international level and its position at the apex of the new international financial architecture at the political G20.

B. FSB Function and Financial Stability

The FSB objectives are defined in terms of agency coordination and policy development with SSBs, as well as to address vulnerabilities with IFIs under Article 1 of its Charter with specific tasks being set out in Article 2. Article 2 of its Articles further specifies that its purpose is to promote international financial stability, including the furthering of the objectives as set out in the Charter. While financial stability has been expressly incorporated into the FSB's purposes from 2013, financial stability is not separately defined. While stability was referenced in the original G7, October 1998 Declaration, which set the mandate for the February 1999 Tietmeyer Report that was principally concerned with organizational arrangements and vulnerabilities. The main FSF post-crisis report examined *Enhancing Market and Institutional Resilience*, although this does not consider the nature of financial stability directly with the first FSB report in September 2009, focusing on *Improving Financial Regulation* without further express comment.[230]

The issue of promoting financial stability has been raised in a number of more recent research papers following the global financial crisis, as well as in speeches and presentations by senior officials. A number of different approaches have been adopted, with some attempting to define financial stability positively and others negatively in terms of its obverse or opposite of financial instability.[231] Some papers have attempted to develop quantitative measures.[232] The most appropriate definition is arguably in terms of financial function with the need to ensure that financial markets can carry out their normal functions on a continuing basis.

It is possible that the FSF and FSB have avoided attempting to define financial stability expressly in light of these difficulties. Attempting to do so would nevertheless substantially clarify the FSB's purpose and objectives, especially as financial stability is now expressly referred to in its Articles of Association. The FSB has a range of express separate purposes, objectives, and mandates and tasks to secure. Its role and vision could be substantially improved if this was clarified and made consistent.

229. The Basel Committee was given a Charter in January 2013. *See* Basel Comm. on Banking Supervision, Bank for Int'l Settlements Charter (Jan. 2013).

230. *See Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience*, *supra* note 224; *see also Improving Financial Regulation*, *supra* note 67; *see also* TIETMEYER, *supra* note 25.

231. *See, e.g.*, Andrew Crockett, *The Theory and Practice of Financial Stability*, GEI NEWSL., No. 6 (Global Economic Institutions, Centre for Economic Policy Research, Washington D.C.), Jul. 14 1997; Roger Ferguson, Vice Chairman, Bd. of Governors of the Fed. Reserve Sys., Conference at the IMF in Washington, D.C.: Should Financial Stability be an Explicit Central Bank Objective? (Sept. 16-17, 2002).

232. *See, e.g.*, CARMEN M. REINHART & KENNETH S. ROGOFF, THIS TIME IS DIFFERENT: A PANORAMIC VIEW OF EIGHT CENTURIES OF FINANCIAL CRISES, 76-79 (NBER Working Paper No. 13882, 2008).

C. Regulatory Access and Clarity

While the FSB has issued a substantial number of papers since the global financial crisis, one of the difficulties that has arisen is that its continuing work streams and publication archive are not always clear from its website. The FSB has retained a number of "Publications by category" listings rather than clearly demarcated work areas, with a number of these categories retaining earlier FSF work areas, such as on Highly Leveraged Institutions (HLIs) and Credit Risk Transfer (CRT). Some of these separate areas may then overlap or conflict over time. The issue of financial stability, referred to above, can be considered to be dealt with separately under "Market and Institutional Resilience" and "Ongoing Work on Sound Financial Systems," as well as under the new category of "Macro-prudential Policy tools and Frameworks." Adoption is also still separately included under "Adherence to Standards" and "Implementation of financial reforms."

In terms of Standing Committees, the FSB also retains three principal committees on Assessment of Vulnerabilities, Standards Implementation, and Supervisory and Regulatory Cooperation, with a separate, new committee on Budget and Resources. The FSB could substantially clarify its ongoing operations and publications output if it established a new Standing Committee on Financial Stability with a new publications category being included at the top of its current "publications by category" list on Financial Stability. While it is arguable that all of the activities of the FSB are concerned with financial stability, a more general sub-set of publications focusing on wider financial stability issues would be of value. This would incorporate all of the existing Market and Institutional Resilience publications, although some of these could be moved elsewhere, with the highly valuable biannual update reports on *Sound Financial Systems* being incorporated as a sub-set within Financial Stability. The FSB could also consider producing, for example, a separate Background Note on its understanding of Financial Stability and explaining the organizational structure of its work and publications.

D. Compensation and Incentives

The FSB has made a substantial contribution in the development of effective *Principles for Sound Compensation Practices*, which date from its original April 2009 report and September 2009 *Implementation Standards*.[233] Nine basic Principles were issued and organized in terms of effective governance, alignment to risk taking, and oversight and engagement. This has been followed up by thematic reviews and an implementation report and separate workshop.

This is highly valuable with the FSB having taken a significant lead in this area in the early post-crisis period. A number of more substantial programs have subsequently been constructed, such as by the Basel Committee in the banking area,[234] and at the domestic

233. *See* Senior Supervisors Group, *supra* note 119; *see also FSF Principles for Sound Compensation Practices*, *supra* note 120.

234. Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *Compensation Principles and Standards Assessment Methodology* (Jan. 2010), *available at* http://www.bis.org/publ/bcbs166.pdf; Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *Range of Methodologies for Risk and Performance Alignment of Remuneration* (May 2011), *available at* http://www.bis.org/publ/bcbs194.pdf; Basel Comm. on Banking Supervision, Bank for Int'l Settlements, *Pillar 3 Disclosure Requirements for Remuneration* (July 2011), *available at* http://www.bis.org/publ/bcbs197.pdf.

level with the provisions incorporated within Section 19A of the UK FSA Senior Management Arrangements, Systems and Controls (SYSC) within its Handbook of Rules and Guidance.[235] The FSB should consider these separate remuneration Codes and incorporate possible revisions to its basic Principles as necessary.

The issue of compensation is also intimately connected with the wider issue of management incentives and governance. Executive and non-executive board members as well as senior management and all other personnel within financial institutions must be properly incentivized and rewarded. Using variable reward entitlements within a payment package is legitimate, provided it does not distort risk management or conflict with customer interests. This should also be tied into other larger incentive structures within firms, including retraining and promotion entitlements. The FSB could reconsider the wider issue of incentives within financial firms and produce appropriate formal principles as necessary. The FSB could also consider issuing further governance requirements outside the remuneration area, following its more recent review work on risk governance.[236] A number of difficult issues also arise with regard to financial ethics, which are generally left to be dealt with at the national level. The FSB could consider issuing some guidance in this area, so that a common, minimum best practice can be identified.

E. Systemically Important Financial Institutions

The FSB has highlighted the importance of SIFIs, GSIFIs, and DSIFIs. A number of papers have been issued on SIFI supervision, moral hazard, and resolution. Thirty two specific recommendations were included within the November 2010 report on *Intensity and Effectiveness of SIFI Supervision*, with 12 sets of *Key Attributes of Effective Resolution Regimes*, as well as additional provisions on RRPs, resolvability, bail-in, and cross-border cooperation.[237]

The November 2010 recommendations on *Intensity and Effectiveness* were principally concerned with adjusting the application of the Basel Committee Core Principles for *Effective Banking Supervision* and are consequently bank centric. The initial FSB list of 29 GSIFIs, published in November 2011, only contained banking groups.[238] Many SIFIs derive their systemic status as complex groups involved in more than one core financial area with this work having to be extended to include Global Systemically Important Financial Groups (GSIGs) in addition to single institution SIFIs. The development of a more complete set of SIFI recommendations should also be considered, while incorporating equivalent provisions within the IAIS *Insurance Core Principles*[239] and IOSCO *Securities Standards and Objectives*. These provisions should also be more clearly integrated into the

235. U.K. Fin. Servs. Auth., Senior Management Arrangements, Systems and Controls Handbook, Chapter 19A, (2013) *available at* http://media.fshandbook.info/content/full/SYSC/19A.pdf.

236. *See* Fin. Stability Bd., *Thematic Review on Risk Governance: Peer Review Report* (Feb. 12, 2013), *available at* http://www.financialstabilityboard.org/publications/r_130212.pdf.

237. *See supra* § IV(D); *see also Reducing the Moral Hazard (June)*, *supra* note 130; *see also Reducing the Moral Hazard (Oct.)*, *supra* note 130; *see also Intensity and Effectiveness of SIFI Supervision (2010)*, *supra* note 131; *see also Key Attributes*, *supra* note 82.

238. Fin. Stability Bd., *Policy Measures to Address Systemically Important Financial Institutions* (Nov. 4, 2011), *available at* http://www.financialstabilityboard.org/publications/r_111104bb.pdf.

239. *See* Int'l Ass'n of Ins. Supervisors, *Global Systemically Important Insurers: Proposed Assessment Methodology* (May 31, 2012), *available at* www.iaisweb.org/view/element_href.cfm?src=1/15384.pdf.

earlier papers issued by the FSF on HLIs and the Joint Forum on Financial Conglomerates and Complex Groups.[240]

It must also be stressed that the stability of financial markets may not only be threatened by the systemically important status of specific institutions. A series of "Systemically Important Principles" (SIPs) should be developed for all "Systemically Important Risks" (SIRs) including specifically, as noted, Systemically Important Financial Groups (SIFGs), as well as "Systemically Important Financial Markets" (SIFMs), "Systemically Important Financial Systems" (SIFSs), and "Systemically Important Financial Activities" (SIFAs). All of this should then be integrated into a larger more coherent program on SIFs and SIRs. This should be considered by the FSB in due course.

F. Resolution

The FSB has constructed an impressive program on resolution, especially with its extended consultation package in July 2011, then *Key Attributes* in November 2011, and *Guidance for Recovery and Resolution Planning for SIFIs* in November 2012.[241] The FSB originally consulted on its *Key Attributes* with additional provisions on bail-in powers, cross-border cooperation, resolvability, RRPs and creditor hierarchy, and temporary suspension of proceedings. The October 2011 *Key Attributes* were extended to apply to financial institutions more generally (including holding companies, non-regulated operational entities, and foreign firm branches), with 12 essential features being specified, including the establishment of Crisis Management Groups (CMGs) and additional guidance on specific issues in the Annexes, including institution-specific Cross-Border Cooperation Agreements (COAGS), resolvability assessments, RRPs, and temporary suspensions. The FSB subsequently consulted in November 2012 on the issuance of guidance on recovery triggers and stress scenarios, resolution strategies and operational resolution plans, and critical functions and critical shared services.

While the initial consultation in July 2011 was directed at SIFIs, this was slightly extended in the *Key Attributes* in November 2011 to all financial institutions, with the November 2012 guidance again focused on SIFIs. The FSB accepts that these were also principally concerned with banking groups, although the parallel work being undertaken by IOSCO, IAIS, and the CPSS was referred to in the November 2012 document. As noted, the most significant dangers will arise with regard to larger complex groups, with each of these separate sets of resolution provisions having to be incorporated into a larger integrated set of "Key Attributes for DSIFGs and GSIFGs," which incorporate effective "Group Resolution Plans or Procedures" (or GRPs).[242] CMGs will also have to work with group Supervisory Colleges in practice.

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240. *See* Walker, *supra* note 4, ch. 3. Joint Forum publications are *available at* http://www.bis.org/list/jforum/index.htm.

241. *See* Fin. Stability Bd. Charter, *supra* note XX, Annex B; *Standing Committee on Supervisory and Regulatory Cooperation*, *supra* note 80; *Members of Standing Committee on Supervisory and Regulatory Cooperation*, *supra* note 80; *Standing Committee on Supervisory and Regulatory Cooperation (FSB Watch)*, *supra* note 80; *Members of the Financial Stability Board*, *supra* note 83; *Links to FSB Members*, *supra* note 83; *FSB Steering Committee*, *supra* note 83.

242. The FSB does refer to "group resolution plans" in *Key Attributes of Effective Resolution Regimes for Financial Institutions*, *supra* note 82, ¶¶ 1.3, 11.8, Annex III ¶ 1.24.

While the emphasis in many of the FSB papers is on post-crisis Resolution Planning (RP), the stability of DSIFIs and GSIFIs will be principally dependent on the effectiveness of their initial pre-crisis recovery planning and reconstruction strategies. Firms and supervisory agencies have a common interest in ensuring that the designs of these recovery or reconstruction programs are effective. Some difficulty may arise with regard to the use of the term "recovery" in a pre-crisis situation, as this may suggest an element of asset recovery or liquidation. A more appropriate term may have been "restructuring" or "reconstruction," although it is presumably too late to change this in light of the number of official documents issued in this area.

Further work will also have to be undertaken to integrate the post-crisis Resolution Plans effectively into domestic post-crisis resolution procedures, such as with the Special Resolution Regime (SSR) set up in the United Kingdom under the Banking Act 2009, with possible work on the design of integrated effective "Global Resolution Regimes" (GRRs) being considered over time.

G. Shadow and Wholesale Markets

The FSB examined the nature of the general problems that arise with regard to shadow banking with its *Scoping the Issues* paper in April 2011. This was followed by the *Strengthening Oversight and Regulation* paper in October 2011, which focused on definition, monitoring, and outline regulatory measures. This included seven high level principles and a three-stage approach to monitoring with five general principles on regulatory tools and eleven specific recommendations. The FSB had already decided at the Paris meeting in July 2011 to focus on indirect regulation, MMFs and other entities, securitization and securities lending, and repos, with five work streams being set up. Much of this was confirmed in the *Integrated Overview* document in November 2012, following the further macro-mapping work and with two separate papers (*Securities Lending and Repos* and *Shadow Banking Entities*) based on a five-part functional approach, focusing on cash pools, short-term funded lending, and investment, credit creation, and securitization. The FSB has also continued its data collection work through its Global Shadow Banking Monitoring Reports.

A substantial amount of work has been carried out in this area with important recommendations issued, especially on monitoring and regulatory tools. This is nevertheless a complex area and covers a large number of different activities, which will necessarily change and evolve over time. The early IMF work was of particular value in identifying the nature of extended credit intermediation chains running between separate markets. All of these activities are not necessarily part of larger credit chains, with the credit intermediation definition possibly causing more difficulties than it solves. The principal vulnerabilities before the crisis arose in such new wholesale investment markets, as the ABCP, ABS, CDO, and CDS markets, which are not strictly credit, but also investment or capital markets, and in the use of off-balance sheet investment holding conduits and structured investment vehicles (SIVs). Separate concerns then arose with regard to such other specific markets as MMFs, which have a retail connection, as well as securities and repo markets and re-hypothecation.

It would be simpler and more inclusive to refer to these markets as more generic "wholesale markets" or "wholesale credit and investment markets," which would include

the corporate ends of the MMF and securities and repo market. All of this only strictly constitutes "credit intermediation" if this is extended to include the provision of funding both through lending and investment through the purchase of bonds, notes, commercial paper, financial derivatives, and other corporate stock or other capital market instruments. If the term "shadow banking" is to be retained, it could be limited for use with regard to the use of off-balance sheet conduits or holding vehicles by regulated institutes, which could either be included within FSB WS1 (on Banks' interactions with shadow banking entities) or a separate work stream.

In terms of regulatory control, each of the existing work streams should be continued to identify the extent to which existing direct or indirect regulation is sufficient or whether specific new sets of measures are required. The principal difficulties will arise within WS3, which covers other non-specific functions or activities (including cash pools, short-term funding, and credit creation), although there is overlap with WS4 on securitization. As the FSB has already acknowledged, many of these activities are highly useful and assist liquidity, risk management, collateral cover, investment choice, and overall stability. Five basic regulatory principles were identified in developing control tools in the October 2012 *Strengthening Oversight and Regulation* paper (based on focus, proportionality, adaptability, effectiveness, and review). These could be extended to include market efficiency and advantage, or be made subject to an overall presumption in favor of the preservation of market function. The authorities should generally avoid the temptation of imposing new regulatory controls on shadow banking more generally when it covers such a wide, unspecified, incoherent, separate, and often valuable set of financial activities. Controls should only be imposed where specific areas of risk or regulatory concern arise.

H. Crisis Management and Support

The establishment of effective cross-border crisis management arrangements remains a sensitive and difficult issue. This is closely connected with national interest and sovereign identity, sovereign autonomy, and the territorial exclusivity of the nation state and national jurisdiction. Many crisis management tools will also be discharged at the national level and be dependent on domestic powers and competences. The global financial crisis nevertheless confirmed the dangers of market integration and interdependence with consequent new global contagion. It is essential that effective cross-border crisis management arrangements be put in place to facilitate market support and firm restructuring, or winding down.

The FSB's work on crisis management has been relatively limited. The FSF was involved in the review and production of guidance on effective deposit insurance systems, and later work was being undertaken by the IMF and the International Association of Deposit Insurers (IADI) following the recent crisis.[243] The FSB issued a separate note on planned exit from exceptional financial support in November 2009.[244] All of the other

243. *See* Int'l Ass'n of Deposit Insurers & Int'l Monetary Fund, *Report to the Financial Stability Board on Update on Unwinding Temporary Deposit Insurance Arrangements*, 2, (June 4, 2010), *available at* http://www.financialstabilityboard.org/publications/r_1006.pdf.

244. *See Exit from Extraordinary Financial Sector Support Measures*, *supra* note 145, at 1. This followed an agreement in June 2009 to exchange notes on planned exits from exceptional financial support measures introduced since 2007. A number of institutions had to rely on such support with continuing difficulties with

FSB documents on its website are listed under "Crisis Resolution" and cover financial institution resolutions, GSIBs, OTC derivatives, and higher loss absorbency for GSIBs.[245] This effectively combines crisis management with institutional resolution. The only specific document that deals with crisis management separately is the *FSF Principles for Cross-Border Cooperation on Crisis Management* issued in April 2009 in advance of the London G20 Summit.[246]

The April 2009, *FSF Principles for Cross-Border Cooperation on Crisis Management* was stated to be based on the earlier Joint Task Force Report on "Winding Down an LCFI" in 2001 and EU principles for financial crisis management.[247] These consisted of fifteen outlined principles and were limited in scope, content, and detail with the express recognition that financial crisis management remained a domestic competence at that time.[248] The FSB website does refer to the consultative document on effective resolution of SIFIs in July 2011 and *Key Attributes* in November 2011,[249] which incorporate its work on Crisis Management Groups (CMGs) and RRPs. Firm-specific CMGs and RRPs will be of key importance in managing individual institutions in difficulty, although these may not directly deal with larger systemic threats and systems crisis management.

It is essential that a comprehensive set of global arrangements are at least outlined, if not formally adhered to, by the principal financial jurisdictions. The FSB April 2009 *Principles for Cross-Border Cooperation on Crisis Management* is too short and unspecified for this purpose. E.U. Finance Ministers and Central Bank Governors agreed to a formal Memorandum of Understanding (MoU) on cross-border financial stability in May 2005, which was updated in June 2008.[250] This constitutes one of the most comprehensive and

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weak institutions. This required judgment and flexibility in terms of timing and sequencing in light of the possible spillover effects on other countries. Some measures had either expired or had not been used, with others being temporary but retained, and others permanent. Four general principles were identified for exit strategies in terms of pre-announcement, flexibility, transparency, and credibility.

245. *See Publications - Crisis Resolution*, FIN. STABILITY BOARD, http://www.financialstabilityboard.org/list/fsb_publications/tid_72/index.htm (last visited Aug. 1, 2013).

246. *FSF Principles for Cross-Border Cooperation on Crisis Management*, *supra* note 142, at 1.

247. *Id.* at 4; Comm'n of the Eur. Cmty., *An EU Framework for Cross-Border Crisis Management in the Banking Sector*, 2, COM(2009) 561/4 (Oct. 20, 2009), *available at* http://ec.europa.eu/internal_market/bank/docs/crisis-management/091020_communication_en.pdf. This acknowledges that the crisis had exposed the E.U.'s lack of effective crisis management for cross-border financial institutions, with Member States having to recapitalize and guarantee banks on an ad hoc basis in Autumn 2008. The Commission proposed a fundamental reform of the regulatory and supervisory system with a new supervisory architecture and EU resolution framework. The 2009 Communication included separate sections on Early Intervention (Section 3), Resolution (Section 4), and Insolvency (Section 5). *Id.* at 5-17.

248. *FSF Principles for Cross-Border Cooperation on Crisis Management*, *supra* note 142, at 2-4.

249. *Publications - Crisis Resolution*, *supra* note 245.

250. *See* Eur. Cent. Bank, *Memorandum of Understanding on Cooperation Between the Financial Supervisory Authorities, Central Banks and Finance Ministries of the European Union on Cross-Border Financial Stability*, at 1, ECFIN/CEFCPE(2008)REP/53106 REV (June 1, 2008), *available at* http://www.ecb.int/pub/pdf/other/mou-financialstability2008en.pdf. This consists of eleven articles on (1) objective and scope of the memorandum; (2) common principles for cross-border financial crisis management; (3) cooperation arrangements; (4) activation of procedures and responsibility for coordination in a cross-border crisis; (5) information exchange; (6) public communication; (7) contingency planning; (8) confidentiality; (9) implementation and review; (10) nature; and (11) entry into effect. *Id.* at 4-10. This includes Common Practical Guidelines (Annex 1) and a Template for a Systemic Assessment Framework (Annex 2). *Id.* at 14, 32. This extends the 2005 Memorandum of Understanding based on the council conclusions of October 9, 2007 and ECF Report of September 5, 2007 (ECFIN/CEFCP (2007) REP/53990). *Id.* at 1.

complete MoUs on financial stability available and extends to thirty-six papers. It is possible that non-E.U. governments have entered into other bilateral MoUs or Financial Services MoUs (FSMoU)[251] at the international level. The FSB could nevertheless assume a leading role in this area by producing a draft or outline FSMoU for global use following the revised 2008 E.U. model.

I. Global Rulebook

One of the most significant early successes of the FSF was the construction of the Compendium of Standards. This initially operated on a virtual basis using HTML links to each of the key documents produced by all the member institutions in the financial area. The standards are more generally classified in terms of sector and function and consist of a range of principles, practices, and other methodologies or guidelines. While the number of documents included was relatively limited to begin with, this has expanded substantially to consist of almost 100 documents.[252] The FSF had identified twelve key standards from an early stage based on macroeconomic policy and data transparency, financial regulation and supervision, and institutional and market infrastructure.[253] These were identified on the basis of relevance and critical nature, universality, flexibility, endorsement, and accessibility.

The establishment of the Compendium has been one of the more significant achievements of the FSF and FSB. This forms the basis for a single global financial rulebook. Despite the earlier advances secured, however, the Compendium has since become too large, complex, and opaque, as well as uncertain in scope and content. While the key standards should be retained, the larger Compendium has to be restructured to provide a clear and succinct statement of all relevant principles, practices, and methodologies or guides. The basic division used in the Key Standards of Macroeconomic Transparency, Regulation and Supervision, and Market Infrastructure may be retained, although this could be substantially expanded and include appropriate sub-divisions. Key standards should be listed with their methodologies and other supporting guidelines or link documents that could be archived through the use of columns or sub-links.

251. *See* Walker, *supra* note 4. Relevant Parties are encouraged under Annex 1 of the E.U. Memorandum of Understanding to enter into "Voluntary Specific Cooperation Agreements" (VSCA) with a common "Cross-Border Stability Group" (CBSG). Eur. Cent. Bank, *supra* note 187, at 15. Annex 1 also covers strengthening crisis preparedness in normal times; crisis alert; crisis assessment; establishing a crisis management network (with "Domestic Standing Groups" (DSGs) and the CBSG); crisis management (including supervisory functions, central bank functions, public sector functions, monitoring, and involvement of other bodies or authorities); and external communication. *Id.* at 15-22. A model VSCA is attached to Annex 1. *Id.* at 22-31. Annex 2 contains a template for a systemic assessment framework based on a "systemic assessment heat map" covering relevant financial institutions, financial markets, financial infrastructure, and the real economy with a best outcome, likely outcome, and worst outcome assessment against four systemic impact scores of zero (no impact), one (limited impact), two (serious impact), or three (very severe impact). *Id.* at 33-37.

252. Although this only covered the subject and issuing body listed documents for the last five years, ninety-three standards were listed on the FSB website in early 2013. While earlier standards were included, a number of these will have since been updated. It is nevertheless unclear whether there are other papers still included within the Compendium that either pre-date the initial FSF work in 1999 or were issued between 1999 and 2008. .

253. *See Key Standards for Sound Financial Systems*, *supra* note 41.

Accordingly, the FSB should consider preparing a "Consolidated Statement of Standards" (CSS). This could explain the structure and organization of the Compendium with more specific key standards that could restate the existing selection criteria of relevance and critical nature, universality, flexibility, endorsement, and accessibility. Separate sectoral and functional sub-divisions may then be included and a menu or code used to distinguish principles, practices, assessment methodologies, and supporting guidelines.[254] A separate "Compendium Guide" could also be issued, such as the U.K. FSA User Guide.[255] The CSS should list all of the relevant standard setting bodies as already provided for on the FSB website.

The CSS should be separately integrated with the FSB's *Ongoing and Recent Work on Sound Financial Systems* (SFS), which provide comprehensive summaries of progress and implementation work. The continuing updated CFS and SFS should adopt the same structure and be provided on an integrated basis on the FSB website. The provision of a clear, coherent, complete, accessible, and updated set of standards would be a significant achievement for the FSB.

J. Effective Supervisory Oversight

Even with effective standards, national and international authorities must ensure that relevant standards are properly applied in practice and that all relevant firms are subject to effective supervision. The need to strengthen the prudential oversight of capital, liquidity, and risk management was referred to in the original FSF recommendations on *Enhancing Market and Institutional Resilience* in April 2008,[256] although the discussion tended to mix the imposition of relevant standards and ensuring effective supervisory monitoring and compliance.

A number of further weaknesses in supervision were identified in the 2012 progress report on, *Intensity and Effectiveness of Supervision*, especially with regard to GSIFI supervision, corporate governance, risk appetite and culture, operational risk, revenue stream and business return supervision ("follow the money"), and stress testing.[257] A number of further specific resource difficulties within national authorities were identified following a Supervisory Intensity Effectiveness (SIE) group member questionnaire and IMF review of recent FSAP assessments.[258] Supervisory Colleges had been set up for all GSIFIs, with separate Crisis Management Groups (CMGs) also having been established for resolution purposes. Thirty-two global and ninety regional colleges had been appointed in the insurance area, with thirty-two countries using the IAIS Multilateral MoU (MMoU) and with a central repository for insurance college information being managed through a Re-

254. Such as with simple references to "Ps," "Pr," "M," and "G," which is similar to the designations used in the U.K. FSA Handbook of Rules and Guidance.

255. *See User guide – Handbook online*, Fin. Conduct Authority, http://fsahandbook.info/FSA/userguide.jsp#part2a (last visited Aug. 1, 2013). The FSA has also issued a short Factsheet. *FSA Factsheet for Handbook Online*, Fin. Services Authority, http://www.fsa.gov.uk/pubs/other/hbonline.pdf (last visited June 5, 2013).

256. *Enhancing Market and Institutional Resilience*, *supra* note 50, at 2; *see supra* § II.

257. *Increasing the Intensity and Effectiveness of SIFI Supervision*, *supra* note 201 at i; *see supra* § II.

258. *Increasing the Intensity and Effectiveness of SIFI Supervision*, *supra* note 201, at 24. Difficulties remained with regard to: (a) supervisory numbers and seniority and skill; (b) attracting and retaining quality staff; (c) high staff turnover; and (d) supervisory culture and "mind-set," including "soft skills." *Id.*; *see supra* § III.

pository of Supervisory Colleges (IROSC) set up in 2011. A separate review of compliance against the *Insurance Core Principles* by FSB member countries was carried out in 2012.[259] Although not referred to in the 2012 FSB Report, IOSCO had also adopted a separate MMoU in the securities area, with all 115 ordinary and associate members expected to become signatories or committed to obtaining legal authority to become signatories.[260]

It is essential that all financial institutions are subject to effective ongoing supervision to ensure compliance on a continuous basis. The FSB reports have revealed a number of significant continuing difficulties in terms of domestic supervisory resources, technical capabilities, experience, involvement, and commitment. Financial firms must ultimately remain responsible for the management of the risks that their activities generate, although supervisory authorities must also ensure that effective monitoring and compliance systems are in place in all cases. All of this will be supported by the enhanced transparency and disclosure standards issued by the FSB with the IMF, which will promote external market discipline in addition to strengthened external official oversight and internal risk management and governance.

K. Standards Implementation and Adherence

It is essential that all key jurisdictions fully adopt and implement relevant international standards in all core financial sector areas. The issue of implementation was initially examined by the FSF in November 1999 under one of its earlier working groups, with an issues paper being produced in March 2000.[261]

The FSF produced a Working Group report on Offshore Financial Centres (OFC) in April 2000 with two reports by a follow-up group (*Incentives to Foster Implementation of Standards*) in August 2000 and 2001.[262] The FSB issued a statement, its *Framework for Strengthening Adherence to International Standards*,[263] in January 2010, with a separate initiative to promote global adherence to cooperation and information exchange standards in March 2010 and with follow-up papers in April and October 2011 and November 2012.[264]

The FSB lists on its website separate initiatives on "Implementation of Financial Reforms." While these initiatives include some of the *Recommendations for Enhanced Supervision* papers, they are generally concerned with the implementation of G20

259. Int'l Ass'n of Ins. Supervisors, *Multilateral Memorandum of Understanding on Cooperation and Information Exchange* (Feb. 15, 2007), *available at* http://www.iaisweb.org/__temp/IAIS_MMoU.pdf. On the IAIS Repository of Supervisory Colleges (IROSC); *see Supervisory Cooperation Subcommittee*, Int'l Ass'n of Ins. Supervisors, http://newsletter.iaisweb.org/newsletterlink-381?newsid=751&call=1 (last visited Aug. 1, 2013).

260. Int'l Org. of Sec. Comm'ns, *Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information* (May 2012).

261. *See* FSF Task Force on Implementation of Standards, Fin. Stability Forum, *Terms of Reference*, at 1, (Nov. 19, 1999); *Issues Paper of the Task Force on Implementation of Standards*, *supra* note 219, at 1; *supra* § IV(L).

262. *See Report of the Working Group on Offshore Centres*, *supra* note 215; *Report of the Follow-Up Group on Incentives* (2000), *supra* note 152; *Final Report of the Follow-Up Group on Incentives* (2001), *supra* note 152.

263. *See FSB Framework for Strengthening Adherence to International Standards*, *supra* note 216.

264. *See Promoting Global Adherence to International Cooperation and Information Exchange Standards*, *supra* note 218; *Promoting Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange*, *supra* note 217; *Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange: Public Statement*, *supra* note 217; *Global Adherence to Regulatory and Supervisory Standards on International Cooperation and Information Exchange: Status Update*, *supra* note 217.

recommendations, more generally and specifically with regard to FSB work on OTC derivatives, SIFIs, and compensation. This includes FSB chair letters to G20 leaders and overview progress reports.[265]

It is essential that the FSB report on implementation of relevant G20 measures, although this does create some confusion with regard to the distinction between implementation and adherence, especially with earlier FSF work on implementation being included within the FSB's "Adherence to Standards" publications. It may be preferable to reserve the term "adherence" for use in connection with measures governing relations between FSB members and member authorities, such as with regard to cooperation and exchange of information. The term "implementation" would then be reserved for domestic application of relevant international standards. The separate term "adoption" may then be used to refer to other continuing initiatives on the negotiation and publication of relevant international standards in specific areas of G20 direction or recommendation. This distinction may then be reflected in the continuing progress reports produced by the FSB that could include separate sections on adoption, adherence, and implementation.[266] Clarifying the meaning and use of these terms could be undertaken as part of a larger restructuring of the FSB Compendium and website more generally, as referred to above.[267]

L. Financial Stability and Financial Function

With the primary purpose of promoting international financial stability under its Articles,[268] the FSB must ensure that a complete and coherent program of measures is adopted in all key regulatory areas at the international level. All relevant G20 recommendations must be given effect. A complete program of relevant global standards must be adopted, and must be presented in a clear, comprehensive, and accessible manner, with the FSB also promoting and reporting on relevant adherence and implementation as appropriate.[269]

The FSB must also ensure that no significant residual gaps are left in the emerging new control framework. While a substantial amount of work has been undertaken in key specific areas to deal with the core lessons identified following the global financial crisis, difficult and sensitive issues remain. The FSB must ensure that all relevant global systemically important risks (GSIRs) are properly managed and contained, including with regard to Global Systemically Important Financial Institutions (GSIFIs) and Global Systemically Important Financial Groups (GSIFGs).[270] This must also include relevant Global Systemically Important Markets (GSIMs), Global Systemically Important Systems (GSISs), and Global Systemically Important Activities (GSIAs).[271]

In so doing, the FSB must attempt to deal with all aspects of too big to fail (TBTF),[272] including "too big to manage, govern, and understand" (TBTM, TBTG or TBTU), "too

265. *See Publications - Crisis Resolution*, *supra* note 245.
266. *See supra* § V(J).
267. *See supra* § V(I).
268. *FSB Articles of Association*, *supra* note 96, art. 2; *see supra* § V(B).
269. *See supra* § V(I), (K).
270. *See supra* § V(E).
271. *Id.*
272. *See supra* § IV(A), (A) n.110.

big to close, restructure or resolve" (TBTC), "too big to support, rescue or bail" (TBTS), and "too big to oversee, direct or correct" (TBTO). All of this results from wider international changes and trends, including the continuous consolidation, concentration, integration, and innovation of financial markets and institutions, and the increased dangers of contamination, contagion, closure, crisis, and collapse.

Specific difficulties also arise with regard to the wider issue of incentives in addition to remuneration, as well as with the even more general problem of financial ethics within modern financial markets.[273] The FSB has also avoided the highly sensitive issue of market support, with the implied intent being that no further major financial crises will arise with strengthened regulation and effective ongoing supervision. This cannot be guaranteed, and during the last crisis a number of new support mechanisms had to be developed on an ad hoc basis to contain specific market crises and wider contagion in a number of countries. Even if this is not discussed expressly or publically, FSB members must cooperate in the design and establishment of appropriate new support facilities that must be in place in the event of a future extreme crisis. These must specifically include necessary individual institution funding of last resort (FLR), market liquidity of last resort (MLR), guarantees of last resort (GLR), capital of last resort (CLR), and asset purchase of insurance of last resort (ALR).

Monitoring all of these risks and exposures must be carried out on a continuous basis through the establishment of effective new macro-prudential oversight and surveillance arrangements. These include the U.S. Financial Stability Oversight Counsel (FSOC), E.U. European Systemic Risk Board (ESRB), and U.K. Financial Policy Committee (FPC). Further guidance could be provided by the FSB on the determination of the most effective institutional and operational structures for macro-prudential oversight following a review of these initiatives in due course. The role of the FSB with regard to the conduct of global macro-prudential oversight could also be clarified with the parallel functions of the IMF and BIS. All of the new initiatives announced at the international, European, and domestic levels will have to be drawn together within these new macro-prudential arrangements, which must also operate in a complimentary and coordinated manner. The FSB could, for example, consider designing appropriate contact mechanisms between these macro-prudential agencies, such as through the production of a new Macro-prudential MoU (MpMoU) model.

The FSB should also assist in promoting the ultimate regulatory objective of continued market function. National and regional economies and the international trading and financial systems will only be able to grow and develop if they are supported by efficient and effective financial markets. The residual or default objective of authorities must be to restore and maintain financial function, rather than impose unnecessary financial control or restriction. Authorities must promote financial growth, expansion, and innovation by only imposing financial restrictions or obligations as necessary to ensure the continued provision of effective financial services. The presumption must be in favor of financial function, rather than financial restriction or contraction. At the international and European levels, there has been an understandable but unfortunate tendency to look to over-regulate and over-react since the global financial crisis. The FSB could discharge a further leadership role by attempting to create an appropriate balance with an intelligent,

273. *See supra* § V(D).

informed, and proportionate package of financial regulatory and supervisory standards and control systems.

VI. Financial Stability Close

The establishment of the FSB has been one of the most significant and successful response initiatives adopted since the global financial crisis. This reflects both an extension of jurisdictional participation following the expansion of the G7/G8 to include the G20 and a further increasing role, function, and operational capability of the FSB beyond the earlier FSF. The FSB must now ensure that it has all necessary funding, personnel, and administrative resources to carry out its key role in as complete and effective manner as possible.

Since its inauguration, the FSB has been able to develop an original and substantial program of regulatory and supervisory reform. It has created an almost overwhelming body of new international financial reference material. The FSB must focus on ensuring that all of its documentation is made available in as clear and accessible a manner as possible, and that all residual areas of regulatory and policy gaps and omissions are corrected.

The FSB has assumed an almost unique role in international relations, particularly in acting as a connector or conduit between the central bank, regulatory, and finance operations of all of the major countries, and SSBs and IFIs at this time. Its operational principles of contact, cooperation, and consensus facilitate negotiation and agreement on necessary measures in difficult and sensitive areas of national interest, and international significance and importance. In so doing, the FSB has, to a significant extent, extended the earlier cooperative culture established by the Basel Committee in the early 1970s to create a new multi-functional, high-level standards production, adherence, and implementation model.

The FSB deserves the full support and commitment from its constituent member countries and organizations to ensure that it can carry out all further necessary reforms and revisions both to its own practices and operations and with regard to the construction of a complete and effective new body of global regulatory, governance, and market oversight standards at this time.