General Assembly
Ad Hoc Open-ended Working Group to follow up on the issues contained in the Outcome of the Conference on the World Financial and Economic Crisis and Its Impact on Development

Fifth meeting on
"Improved financial regulation and supervision"
(New York, 3 May 2010)

Informal summary by the Secretariat

Overview. The meeting was co-chaired by H.E. Mr. Lazarous Kapambwe (Zambia) and H.E. Mr. Morten Wetland (Norway). The meeting was based in particular on paragraphs 37-41 of the Outcome Document. The presentations and discussion focused on several questions suggested by the Co-Chairs on the current working relationship between members and non-members of key international standard-setting bodies in financial regulation and supervision, the relevance of new standards in these areas for developing countries and the role of the UN in facilitating information exchange among Member States in these matters.

Summary of the presentations by the panelists

Mr. William Coen, Deputy Secretary General, Basel Committee on Banking Supervision (BCBS), presented on the global role and current initiatives of the BCBS. The committee was created in 1974 by G10 central bank governors after serious disruptions in international banking markets highlighted the need for cross-border cooperation and improved global banking supervision. Membership had been expanded in 2009 from 13 to 27 governments. Outreach to non-members took place through the Basel Consultative Group, the International Conference of Banking Supervisors, the Financial Stability Institute, as well as regular interaction with regional supervisory groups. The Committee secretariat was hosted and fully funded by the Bank for International Settlements. Its governing body met twice a year and included central bank governors and heads of supervisory authorities. The BCBS met four times per year and was supported by a Secretariat staff. Agreements were reached by consensus and had no formal authority but over time, BCSC standards had become global standards

He explained that the work of the BCBS included the development of the Concordat on cross-border supervision, Basel I, Basel II, core principles for effective banking supervision, as well as the creation of sound principles and guidance on risk management and supervisory topics. Mr. Coen highlighted that the BCBS needed to address the root causes of the crisis through policies that ensured that regulatory capital covered all material risks and that high quality capital, forward-looking provisioning and capital buffers could absorb losses. Preparations were underway to introduce new sets of global capital and liquidity standards by year end. Moreover, efforts should focus on improved supervision of systemically important banks, more effective risk governance and management, improved market discipline through better disclosure and practical approaches for better management of cross-border bank resolutions. These initiatives should be carefully calibrated and open to extensive public consultations.

The speaker further emphasized that impact assessments and macroeconomic evaluations during the transition period were crucial components of the reform effort. Ideally these measures would be forward-looking, foster greater banking resilience, enhance sustainable economic growth and increase the ability of banks and financial systems to withstand future crises. The implementation of these standards by all jurisdictions was essential to promote a global level playing field. These measures were critical for laying the groundwork to mitigate and minimize the impact of the next crisis. He emphasized that as financial markets were global and diverse, it was critical that all countries strengthened their banking sector resilience.

Mr. Caleb M. Fundanga, Governor and Chairman of the Board of the Bank of Zambia, elaborated on measures undertaken to improve the financial regulation and supervision of the financial system in Zambia. The speaker emphasized that Zambia had weathered the crisis relatively well, with growth largely driven by increased output in the mining and quarrying, construction, agriculture, and energy sectors. However, the collapse in commodity prices led to losses in output and employment that fed back into the deterioration in the loan book of commercial banks.

Comprehensive financial sector reforms that had been undertaken within a Financial Sector Development Plan (FSDP) after the banking sector collapse in the second half of the 1990s helped create a resilient financial sector in Zambia. Reforms included the increase in capital requirements for banks and the consolidation of the supervision of bank and non-bank financial institutions under the Bank of Zambia. The FSDP further introduced legislative reform that gave the Bank of Zambia powers to deal with failing institutions and corporate governance guidelines, including the conduct of outreach programmes on good corporate governance practices for the financial sector and the introduction of credit reference services. The fallout from the crisis highlighted the need to further enhance the regulatory framework by adopting and enhancing supervisory and regulatory practices which ensured prompt and effective policy responses to developments in the financial system.

Key regulatory and supervisory issues that the Bank of Zambia was addressing in this regard included the adoption of a risk based supervision (RBS), enhancing the legislative framework, the determination of capital adequacy, the introduction of a deposit insurance scheme, the enhancement of the lender of last resort regime and more effective cross-border cooperation through consolidated supervision of financial institutions. Moreover, there was a need to improve macro- and micro-prudential regulation of systemic risk. The Bank of Zambia was also developing a financial sector contingency plan to address problems of a systemic nature and enhance practical tools for effectively managing financial distress and potential systemic crisis.

The speaker concluded by stating that the global financial crisis posed a significant opportunity for the international community to address some of the structural weaknesses in domestic economies and the global financial system. These reform measures must not jeopardize the foundations for economic growth that had been laid over the past decade in developing countries, particularly in Sub-Saharan Africa.

Summary of the discussion

The representative of Yemen (on behalf of G77 and China) noted that the crisis had negatively affected most developing countries. He also underscored that any solution to the crisis would be only partial and inadequate unless policy makers from both developed and developing countries promoted an adequate level of policy coordination on fiscal, monetary and exchange rate issue as well as enforceability in the application of agreed policies.

The speaker stressed that the outcome of the UN Conference on the World Financial and Economic Crisis highlighted “major failures in regulation, supervision and monitoring of the financial sector” that resulted in excessive risk taking, unsustainably high asset prices, irresponsible leverage and over consumption fuelled by easy credit. There was a failure to appreciate the full measure of risks in the financial system. Developing countries should actively participate in the reform efforts through full and fair representation in international regulatory bodies including the FSB and BCBS.

Along with more stringent regulation and supervision of financial institutions, the G77 and China favored a less volatile exchange rate system, limits on excessive short-term capital flows and steps to curb illicit financial transactions. Also, the regulatory reform should address the pro-cyclicality in international bank lending to developing countries.

According to the speaker, the current crisis demonstrated the urgent need for introducing internationally harmonized norms and standards for financial regulation and supervision. At the same time, regulatory protectionism by developed countries must be resisted.

There was a critical need for expanding the scope of regulation and supervision with respect to all major financial centers and instruments including derivatives as well as to all financial institutions including rating agencies and hedge funds. This would entail additional mechanisms to allow for the assessment of and the response to systemic risk posed by unregulated or less regulated financial sector segments, centers, instruments and actors. G77 and China also called for the examination of an international insolvency regime governing the resolution of large cross-border financial firms.

The speaker also emphasized the need to build an effective framework for enhanced multilateral surveillance and policy coordination. He stressed a need for even-handed and effective IMF surveillance of systemically important countries, major financial centers, international capital flows and financial markets.

All tax jurisdictions and financial centers should comply with adequate standards of transparency and regulation. International cooperation in tax matters must be encouraged, including within the United Nations and other organizations at the regional and international level. In this regard, the G77 and China called for the conversion of the UN Committee of Experts on International Cooperation in Tax Matters into an International Subsidiary body of the ECOSOC.

The representative of the European Union stressed that it was essential to maintain the strong momentum in regulatory reforms. In this regard, the EU strongly supported the work of the G20, the Financial Stability Board (FSB) and other international forums, in particular on: stronger capital and liquidity buffers; improving supervisory process; convergent and less pro-cyclical international accounting standards; systemic institutions; cross-border crisis resolution; increasing resilience and transparency of derivative markets; corporate governance; the implementation of the FSB standards on remuneration; and non-cooperative jurisdictions.

The speaker noted that mobilizing domestic revenues and fighting tax evasion were key elements in efforts to eradicate poverty. Effective, fair and sustainable tax systems were also critical for state building as well as promoting democracy and improved economic governance. He also stressed that tax evasion constituted a large part of illegal flows and plugging these tax "leaks" required international tax cooperation. The EU was committed to support developing countries in tackling the issue of tax governance and was working on initiatives in order to introduce a more comprehensive and consistent policy approach to all aspects of taxation. The G20 leaders agreed in Pittsburgh on measures against illicit capital outflows from developing countries. The EU would welcome a substantive follow-up on this commitment.

According to the speaker, the rebalancing of global growth remains a challenge for global macroeconomic and financial stability. The G20 Framework for Strong, Sustainable and Balanced Growth was an important tool to build a stronger economy as the world exited the crisis and address challenges, including global imbalances.

Current efforts by the IMF to improve surveillance were important. Collaboration and a division of labor with other relevant bodies, in particular the FSB, needed to be improved, with the IMF being responsible for macro-prudential but not micro-financial issues. A better cross-country understanding, with more thematic multi-country reports, should be promoted.

The speaker also highlighted the importance of Corporate Social Responsibility (CSR) for sustainable development and underlined the complementarity of voluntary and regulatory approaches to CSR. CSR practices and public intervention should be mutually supportive. It was important to integrate existing internationally agreed standards and principles into voluntary CSR initiatives and apply independent monitoring and verification.

G77 and China underscored that the eradication of extreme poverty and hunger required stronger and more equitable and sustainable economic growth. Given limited official resources for external assistance, it is important to leverage private funding and other resources and to fully involve private actors in the achievement of the MDGs. New types of partnership through which business and official sector might contribute to achieving the MDGs should be explored.

The representative of Japan asked for clarification of several issues pertaining to the activities of the BCBS including the definition of systemic risk, the process of BCBS expansion and the Committee's involvement in public diplomacy. He also asked about the attitude of Zambian authorities towards BCBS recommendations.

In his reply, Mr. Coen noted that the BCBS had always been concerned about the risk of contagion. He informed the participants that, in 2009, 14 new jurisdictions became members of the Committee. The panelist indicated that the BCBS was aware of the need for better communication. In his turn, Mr. Fundanga stressed that financial reforms in Zambia had been a response to results of the Financial Sector Assessment Programme (FSAP).

The representative of Switzerland stressed that developing countries need technical assistance in developing supervisory regimes. According to the speaker, the implementation of standards was a long-term goal. Therefore, the most important standards should be implemented first. He noted that the United Nations could be a useful platform, especially for non-members of international standard-setting bodies, to discuss regulatory issues on a complementary basis.

The representative of the United States noted that, due to a lack of technical expertise, the United Nations was not an appropriate forum to discuss regulatory issues. The speaker was encouraged by the fact that the BCBS cooperated closely with non-members and asked Mr. Coen to elaborate on how to ensure proper interaction of non-members with regulatory bodies.

The representative of Mexico asked about the BCBS interaction with non-members, its relationships with the IMF, the World Bank and the G20 as well as about the standards implementation process.

In his reply, Mr. Coen stressed that first standards had been developed for large, complex organizations. He pointed out that, while working on standards, the BCBS had always been trying to avoid the least common denominator. After agreement on a standard, it was up to each member to implement it, depending on local circumstances and practices; hence, implementation could vary greatly. Mr. Coen also pointed out that the BCBS was paying more attention to communications and outreach, including dissemination of the latest information and promotion of standards globally through the Financial Stability Institute. The Basel Consultative Group provided a forum for deepening the Committee's engagement with supervisors around the world on supervisory issues and facilitated dialogue with non-member countries. Regional supervisory groups also constituted very important channels of communication. Regarding BCBS relations with the Bretton Woods institutions, he noted that IMF was an observer at BCBS meetings. The World Bank did not attend these meetings but participated in the Basel Consultative Group.

Mr. Fundanga noted that non-members of international regulatory bodies had a feeling that their interests were not taken into consideration. Consequently, all countries should contribute to the discussion on financial regulation.

The representative of Venezuela disagreed with the view that this forum lacked the expertise for discussion of financial regulation issues as representatives could rely on the support of their respective central banks and national financial organizations. He posed a question to Mr. Coen on how to promote a more balanced financial and economic system given the existing emphasis of the financial sector on speculation rather than on servicing productive activities.

The representative of Brazil thought that it would be useful to gather all information and data from several panelists, including those in the 30 April meeting, to update the state of play of financial reform since the crisis. He asked the panelists the following questions: 1) How was shadow banking, as well as other non-bank financial institutions and support organizations, such as insurance companies and rating agencies, being addressed in the BCBS? 2) How were reforms in banking standards applied to African countries? 3) Regarding winding down of cross-border financial institutions, how would the different jurisdictions be affected?

Mr. Coen emphasized that BCBS produced standards as best practices that represented minimum requirements. It was up to each jurisdiction to implement them and to enforce them to suit local conditions and frameworks. Thus, this was a local and not global issue. With respect to shadow banking, the issue was addressed in the Joint Forum created in 1996 by the BCBS, where a group of technical experts working under the umbrella of the Committee identified activities in shadow banking and issues involved. In parallel, other groups, such as the International Organization of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors dealt with the securities and insurance institutions. The work of the Joint Forum encompassed issues relating to financial conglomerates as well as issues of common interest.

Mr. Fundanga explained that in implementing financial reforms and banking standards, there was continent-wide cooperation in Africa through the Association of Central Banks as well as on a sub-regional basis. He stressed that African countries should also have cooperation with the rest of the world.

The representative of Portugal asked Mr. Fundaga what was being done in Zambia in broadening and deepening financial inclusion. Mr. Fundanga responded that this was important in all African countries as there were still large numbers of the population without access to financial services. He pointed out that the mobile telephone was a key innovation in increasing access in this regard.

The representative of the Order of Malta supported greater participation of developing countries in norm-setting and standard-setting bodies. He asked whether IMF had focused its surveillance sufficiently on financial centres.

Mr. Coen responded that the work of the Bank of International Settlements (BIS) also did research on global economic trends and policies which was a form of surveillance. Therefore, there was more that one international institutions doing surveillance and there was a close relationship between BIS and IMF. Adoption of BCSC standards tended to be done by countries through FSAPs.