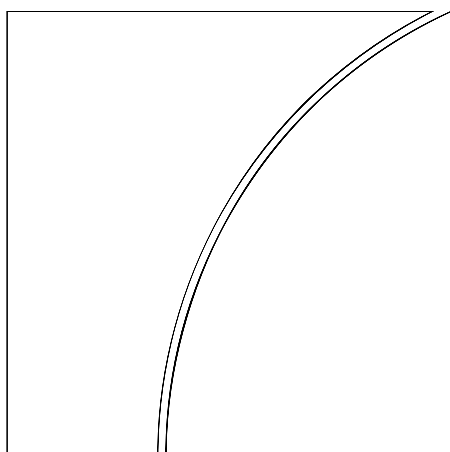
Basel Committee
on Banking Supervision

The Joint Forum



CORE PRINCIPLES

CROSS-SECTORAL COMPARISON

November 2001

BANK FOR INTERNATIONAL SETTLEMENTS

THE JOINT FORUM

BASEL COMMITTEE ON BANKING SUPERVISION
INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS
INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS
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Table of Contents

1. Executive Summary 1
2. Introduction 4
   (a) Mandate 4
   (b) Approach 4
3. Background to the Core Principles 5
4. Subsequent Evolution 6
5. Basis of the Comparison 7
6. Relevant Characteristics of the Three Sectors 8
   (a) Banking 9
   (b) Insurance 10
   (c) Securities 11
7. Analysis of Common Principles and Differences based on the Matrix 13
   (a) Pre-conditions 13
   (b) The Supervisory System 13
      (1) Objectives of supervision 13
      (2) Attributes of supervisory systems 14
         Operational independence and adequate resources 14
         Enforcement powers and capabilities 14
      (3) Clarity and transparency of supervisory process 14
      (4) External participants in the supervisory process 15
   (c) The Supervised Entity 15
      (1) Licensing, qualifications, ownership transfer and corporate control 15
      (2) Corporate governance 15
   (d) Ongoing Supervision 16
      (1) Group-wide supervision 16
      (2) Monitoring and on-site inspection 16
      (3) Reporting to supervisors 17
      (4) Cooperation and information sharing 17
      (5) Confidentiality 17
   (e) Prudential Standards 17
      (1) Risk management 17
      (2) Internal controls 19
      (3) Risk concentration 19
      (4) Capital requirements 19
      (5) Accounting policies and practices 20

(f) Markets and Customers ... 20
(1) Markets ... 20
Market integrity ... 20
Financial crime ... 20
(2) Customer protection ... 21
(3) Information, disclosure and transparency ... 21
(4) Issuers ... 21
8. Observations and Conclusions ... 22
9. Options for Further Work ... 25
A. Content of existing core principles. ... 25
B. Cross-sector interface ... 26
C. Presentation ... 26
10. Future Evolution ... 26
Appendix A: Membership of the Working Group
Appendix B: Comparison Chart

Comparison of Core Principles

1. Executive Summary

1. In March 2000, the Joint Forum set up a Working Group to compare the core principles issued by the Basel Committee on Banking Supervision (Basel Committee), the International Association of Insurance Supervisors (IAIS), and the International Organization of Securities Commissions (IOSCO), identifying common principles and understanding differences where they arise. This report is based on the findings of the Group. The report was completed in Tendo, Japan, in July 2001 and has been updated after consultation with the parent Committees in August 2001.

2. Section 2 explains the origin of this task and describes the approach taken. The Joint Forum hopes that this analysis will help those assessing jurisdictions against the core principles gain a familiarity with, and understanding for, the core principles of all sectors and thus become more effective in their work.

3. Section 3 outlines the background to the core principles. While each sector worked independently in drafting its core principles, there was a great deal of similarity in the approaches taken; in all cases, the process involved extensive and broad consultations within the sector. The subsequent evolution of the core principles – such as the development of methodologies and self-assessment programmes – is discussed in section 4.

4. In both structure and content the core principles reflect characteristics of the respective sector and the nature of the supervised financial institutions, intermediaries and markets. Some of the sector specific attributes thus made a direct comparison across core principles a difficult task. The Joint Forum therefore adopted an issues-based approach described in Section 5. The resulting matrix mapping the core principles is contained in Appendix B.

5. Some of the similarities and differences among the core principles reflect intrinsic characteristics of the banking, insurance and securities sectors. Section 6 highlights sector specific factors necessary in understanding the core principles. Briefly,

- **Banking.** Linkages between the banking sector with the macro economy are perceived to be particularly strong, giving rise to potential concerns about systemic risk and financial stability. The Basel core principles encourage authorities to put in place supervisory frameworks that address significant risks – in particular, credit, concentration, market, liquidity, and operational risks. Unique among the three sectors, banking has an international capital standard. This standard was created to safeguard financial stability and counteract a deterioration of bank capital levels. Moreover, the standard was intended to reduce competitive inequalities across countries. Banks are supervised on a consolidated basis, reflecting the way the institutions themselves manage risk and, in particular, recognising the possibility of contagion risk within a banking group. Market discipline, enabled by good disclosure, is seen as an important adjunct to supervision.
- **Insurance.** Insurance offers protection against uncertain future events. Although this task is of considerable importance to the economy, usually the insurance sector is not a source of financial instability. In addition, despite the fact that most large insurance companies operate in many jurisdictions, supervisors have traditionally been able to “ring-fence” operations, thus containing problems. Much supervisory effort is directed towards the valuation of technical provisions, as they are estimations of the cost of future liabilities. Misestimation can affect pricing decisions

and the overall solvency of a company. Further, meaningful disclosure of information is more difficult to achieve in the insurance sector because of the many underlying assumptions supporting the valuation of liabilities. Because insurance products are often complex, generally insurance companies and intermediaries (i.e., insurance brokers) are subject to market conduct, in addition to prudential, regulation.

- **Securities.** Securities supervisors have very broad responsibilities. They encompass securities firms, markets, exchanges, collective investment schemes, and disclosure by issuers. There are many unique aspects to securities supervision reflecting, in part, this broader scope. For example, in some jurisdictions, self-regulatory organisations can be a valuable complement to the supervisor in achieving the objectives of securities supervision. In addition, securities supervisors place great importance on ensuring that investors are provided with the information necessary to make informed investment decisions on an ongoing basis. Consequently, full, timely and accurate disclosure of current and reliable information material to investment decisions is critical. There is also an emphasis on disclosure by intermediaries to clients of matters including investment risk and conflicts of interest. The broad scope of supervisors' enforcement powers is another aspect unique to securities supervision. This is because the complex character of securities transactions and the sophistication of fraudulent schemes require strong and rigorous enforcement of securities laws. This feature reinforces the need for close cooperation between securities supervisors at the domestic and international levels.

6. Section 7 contains the analysis of the core principles based on the matrix. In its analysis, the Joint Forum has sought to be comprehensive and balanced, drawing on intrinsic characteristics where necessary to explain differences. It emphatically avoided making any judgements as to whether the core principles are right or wrong, recognising that each is designed to meet sector specific needs.

7. Some of the highlights of Section 7 are:

- ***Pre-conditions***. All sectors see sound and sustainable macro-economic policies and well-developed public infrastructure (legal, accounting, etc.) as preconditions to effective supervision.
- ***The supervisory system***. All three sectors consider customer protection and systemic stability as objectives of the supervisory system. However, Basel places greatest emphasis on systemic stability and the IAIS on customer (in this case, policyholder) protection. IOSCO emphasises equally its three objectives of investor protection, fair, transparent and efficient markets and reduction of systemic risk. All sectors recognise the need for operational independence and adequate resources for supervisors, while acknowledging the importance of consulting with their respective industry groups and using outside participants for assisting the supervisory process. All sectors have the ability to apply supervisory sanctions but the IOSCO core principles are more detailed in describing the role of enforcement as a tool in the supervisory process.
- ***The supervised entity.*** All sectors require supervisors to have a regime for licensing entities and vetting of key individuals. Since there are different types of supervised entities in the securities sector, there are different types of licensing requirements. In the banking sector, there are restrictions on the use of the term “bank”. All sectors encourage sound corporate governance within licensed entities.
- ***Ongoing supervision.*** All sectors require an effective framework for monitoring, on-site inspection and cooperation with other supervisors. Basel however regards consolidated supervision as mandatory, but the other sectors have the ability to require consolidated reporting or use other techniques to obtain a group-wide view.

Only the securities sector has enforcement powers that are comprehensive enough enabling supervisors to investigate and prosecute, extending beyond supervised entities. It also views cooperation with other supervisors as vital to fulfilling this role. IOSCO's core principles, unlike those of Basel and IAIS, do not distinguish the responsibilities of home versus host in guiding the flow of information between supervisors.

- ***Prudential standards.*** The sectors have taken different approaches to identifying the risks faced by the entities that they supervise. However, all describe the tools supervisors should possess to effectively manage risks. These include:
  - Setting capital requirements;
  - Ensuring that good accounting and valuation practices are followed;
  - Establishing limits on particular assets or exposures; and
  - Requiring that the necessary policies, procedures and reporting systems be put in place.
- ***Markets and customers.*** All core principles take some supervisory responsibility for the prevention of financial crime. IOSCO places additional responsibility on supervisors to detect and deter market abuses and fraud. IOSCO and IAIS make clear that supervisors have a role in protecting investors and customers; in particular, investors, intermediaries and policyholders should receive relevant material information to make buying and selling decisions.

8. Section 8 summarises conclusions and observations, notably

- Each set of core principles provides an overview of the key elements of the supervisory regime in that sector as at the time they were written. However the pace of developments in the financial sector since then would require consideration of the need for keeping the core principles updated. The impact of this varies between the sectors according to the structure of the relevant documents.
- There is no evidence of underlying conflict or contradiction between the three sets of core principles at the highest levels.
- There are numerous areas of common ground (e.g., authorisation, organisation of supervision, intervention). However it was established that in some cases, there are significant differences in the application of similar principles (e.g., different capital treatment of similar risks in different sectors).
- There are numerous differences between the core principles – some arising from intrinsic differences between the three sectors; others not readily explained in this way. Differences are found in the pre-conditions, group-wide supervision, cooperation and information sharing, safeguarding of client assets and application of uniform prudential standards.

9. In addition, the Joint Forum noted a number of significant developments since the core principles were originally drafted, all of which are considered to be in some degree relevant to a comparison of the core principles as they presently stand. These developments include:

- the use of the core principles as benchmarks for financial sector assessments, in some cases, going beyond the purpose for which they were originally designed;
- the increased provision of similar products and services in different sectors;
- the continuing emergence in a number of jurisdictions of financial conglomerates; and

- the establishment of integrated financial supervisors in a growing number of jurisdictions.

10. The report concludes by presenting some options for further work. These range from issues on the content of the core principles to cross-sector interface and presentation of the principles. Decision to pursue further work should be made by the parent organisations (Basel Committee, IAIS and IOSCO), which can best judge the needs of their members.

2. Introduction

(a) Mandate

11. Recently and independently, the Basel Committee, IAIS and IOSCO identified principles for effective supervision in their respective sectors. Implementation of these principles is being monitored, in some cases, through self-assessments and peer reviews, and by independent bodies such as the International Monetary Fund (IMF) and the World Bank.

12. The mandate of the Joint Forum to compare the core principles originated from a request made by the IMF and the World Bank. In assessing jurisdictions' compliance with the core principles, assessors and supervisory agencies being assessed had indicated the need for a better understanding of why the core principles differed in structure and format between sectors. A comparative analysis of the core principles from all three sectors was deemed beneficial in the implementation and assessment of the principles. Accordingly, at the April 1999 Financial Stability Forum meeting, the IMF and the World Bank suggested "that the Forum encourage a review of the consistency of the core principles developed by the various international supervisory groupings with a view to facilitating their implementation". It was felt that such an exercise would help assessors improve their understanding of the principles and thereby make the implementation and assessment process more effective.

13. This request was passed to the Joint Forum through its parent organisations and incorporated in an updated mandate released in December 1999. The Joint Forum recognised that this was a unique opportunity to gain an in-depth understanding of the three sectors' core principles. The mandate to the Joint Forum is "to compare the core principles issued by the banking, insurance and securities sectors, identifying common principles and understanding differences where they arise." It is not within the mandate to determine changes to the core principles. However, taking this report into account, the parent organisations may wish to consider where revisions to their core principles are desirable or necessary.

(b) Approach

14. The Joint Forum established a working group, consisting of members from each sector and also from the IMF and the World Bank (Appendix A), The work was divided into two phases. The first phase dealt with analysing the structure of each set of core principles and establishing where differences arise, while the second phase focused on looking at the reasons why these differences arise. The documents that formed the basis for this review included:

- The Core Principles for Effective Banking Supervision (September 1997) and accompanying methodology (October 1999);

- The Insurance Core Principles (October 2000) and accompanying methodology (October 2000); and
- The Objectives and Principles of Securities Regulation (September 1998)

The work did not however include a detailed review of the methodologies for the bank and insurance core principles. The methodologies were referred to as needed to add clarification to the comparison of the core principles themselves. In addition, analysis of the various guidance issued by the three standard setters fell outside of the mandate, although in some instances reference is made to these documents in the respective core principles or related methodologies.

15. From the outset, an objective approach to the comparison of the core principles was taken, avoiding any implicit judgements of whether any particular core principle was right or wrong. It was recognised that it is important to have a clear understanding of the objectives of each of the core principles.

16. In this report, observations and findings are presented in the following order: banking, insurance, securities. This order is adopted for the sake of consistency and has no other significance. Also, the term "supervision" is generally understood to apply to oversight of the banking and insurance industries, while the similar term for the securities industry is "regulation", which includes the supervisory function associated with bodies charged with the supervision of securities firms and markets. For ease of reference, the terms "supervisory" and "supervision" are understood to include "regulatory" and "regulation".

3. Background to the Core Principles

17. The need to strengthen financial systems attracted international attention, culminating in a call for action by the G7 at the Lyon Summit in June 1996. In particular, leaders recognised that financial systems, especially banking, and macroeconomic development are closely linked. The following year the Basel Committee reacted to this call for action by issuing the Core Principles for Effective Banking Supervision, with the aim of providing guidance for jurisdictions wishing to strengthen their supervisory regimes.

18. Around the same time the newly formed IAIS adopted a standard-setting role. The Insurance Supervisory Principles were drafted to provide a framework for this purpose and were adopted in 1997. By 2000, it became clear that the principles were also being used for another purpose. Specifically, the IMF and the World Bank assess compliance with financial sector standards mostly in the context of the Financial Sector Assessment Program (FSAP). The IAIS also introduced a systematic program of self-assessment for its members. These developments led to the IAIS updating and extending the document and renaming it as Insurance Core Principles.

19. IOSCO adopted the Objectives and Principles of Securities Regulation in 1998, recognising that sound and effective regulation brings confidence to the securities markets and strength to the economy, domestically and globally. The document provides securities supervisors with a common set of guiding principles and objectives.

20. While the backgrounds to the creation of the three documents were different, the processes followed were similar in many respects. In all cases the principles are supported by other supervisory guidance. In fact, the Basel Committee and IOSCO's core principles are based largely on previously issued guidance, and since 1997 the IAIS has elaborated on many of its core principles.

21. In addition, each sector consulted broadly and extensively while developing its core principles. Members in both the IAIS and IOSCO come from developed and developing countries representing all regions of the globe. Membership in the Basel Committee is limited to the G10 (plus Switzerland and Luxembourg). However, in developing the Core Principles for Effective Banking Supervision, the Basel Committee established a Liaison Group that included non-G10 countries. All sectors invited IMF and World Bank participation, recognising the important role these organisations play in encouraging adherence and implementation.

4. Subsequent Evolution

22. To help with IMF and World Bank assessment programmes, the Basel Committee in 1999 and subsequently the IAIS in 2000 developed methodologies that include criteria for evaluating compliance with the principles. The criteria are divided into "essential" and "additional". Essential criteria indicate the minimum level that all jurisdictions should fulfil, while additional criteria are best international practices that jurisdictions should strive towards.

23. IOSCO's Objectives and Principles of Securities Regulation are supplemented by narrative discussion intended to illustrate how the principles might be achieved. IOSCO has developed self-assessment methodologies aimed at implementation. As a first step it has developed a high-level self-assessment methodology for the implementation of the principles by having members complete a self-assessment. More detailed self-assessment methodologies on specific sections of the principles are currently being undertaken.

24. Self-assessments have also been used by the Basel Committee and IAIS. The Basel Committee encouraged countries to complete a self-assessment when the Core Principles for Effective Banking Supervision were originally promulgated. Members of the IAIS completed a simple self-assessment of the Insurance Supervisory Principles in 1998 and have now been asked to complete a more detailed self-assessment based on the Core Principles Methodology. Now all three sectors' self-assessments are used as part of, or in preparation for, IMF and World Bank assessments under the FSAP.

25. These self-assessments are intended to provide encouragement and direction to jurisdictions to strengthen their supervisory systems. At the present time, none of the international supervisory bodies uses compliance with the core principles as a condition of membership or to sanction jurisdictions.

26. The Basel Committee and IAIS intend to update and revise their core principles periodically, primarily as a result of developments in the industry, findings from the self or independent assessments, or the issuance of new supervisory standards. Currently, both are targeting revised principles and methodology for the year 2002.

27. IOSCO also plans to update the Objectives and Principles of Securities Regulation, as necessary. This document was crafted with the view that markets change significantly over time and that the supervisor must have flexibility to respond to changes, consistent with the core principles. The IOSCO core principles note that there is often no single correct approach to a supervisory issue. Minor amendments are presently being made to reflect work undertaken by IOSCO since the Objectives and Principles were adopted.

5. Basis of the Comparison

28. The structure of each sectors' core principles reflects the types of entities or markets that are supervised. The table below provides an overview of the structure of the three sectors' core principles grouped according to the sub-headings used in each sectors' documents.

CP	Basel Committee	CP	IAIS	CP	IOSCO
1	Preconditions	1	Organisation of an insurance supervisor	1-5	Principles relating to the regulator
2-5	Licensing and structure	2-3	Licensing and Changes in Control	6-7	Principles for self-regulation
6-15	Prudential regulations and requirements	4	Corporate governance	8-10	Principles for the enforcement of securities regulation
16-20	Methods of ongoing banking supervision	5	Internal controls	11-13	Principles for cooperation in regulation
21	Information requirements	6-10	Prudential rules	14-16	Principles for issuers
22	Formal powers of supervisors	11	Market conduct	17-20	Principles for collective investment schemes
23-25	Cross-border banking	12-13	Monitoring and on-site inspection	21-24	Principles for market intermediaries
		14	Sanctions	25-30	Principles for the secondary market
		15	Cross-border business operations		
		16-17	Coordination, cooperation and confidentiality		

29. Bank supervisors focus on the solvency of supervised institutions. Similarly, insurance supervisors focus on companies on the principle that policyholders will be protected if insurance companies comply with regulations and manage risk in a sound and prudent manner. Therefore principles in both these sectors describe the framework needed to supervise entities.

30. In contrast, as explained in section 6 below, securities supervisors not only supervise securities firms (or market intermediaries) but also collective investment schemes (both the products and the intermediaries who offer them) and secondary markets, (including exchanges and clearing houses) and disclosure by issuers. The principles address both prudential supervision and conduct of business issues. As a result, the structure of the Objectives and Principles of Securities Regulation is very different from those of the banking and insurance core principles. One part of the IOSCO document describes the desirable attributes of a supervisor and the role of SROs. It also considers the enforcement and market oversight work of the supervisor and the need for close cooperation between supervisors. Other parts make particular reference to collective investment schemes, market

intermediaries, secondary trading, the clearance and settlement of transactions, and disclosure by issuers.

31. Since the differing structures did not naturally lend themselves to a comparison of the core principles, the Joint Forum decided to take an issues-based approach and produced the matrix found in Appendix B. There are instances where the mapping of the core principles resulted in some "blank spaces" in the matrix. That is, categories that were not addressed in at least one sector's core principles. These "blank spaces" are a natural and inevitable part of the comparison and help in identifying some of the key intrinsic differences among sectors.

32. A successful comparison of the core principles depends crucially on the choice of issues considered in the detailed work. In designing this framework, it was attempted to use "neutral" terminology, which meant that while all essential elements of the individual core principles were captured, these were not necessarily found under familiar headings. It was also sought to ensure that the comparison is rigorous and comprehensive without being unnecessarily specific, and, as noted earlier, avoid any implicit value judgements. It was important to have a clear understanding of the objective of each principle, not just using literal interpretations.

33. Perhaps the most difficult issue to compare across the three sectors proved to be that of risk. The treatment of risk is a fundamental aspect of the core principles and the understanding what the core principles have to say about risk and why is crucial to the value of the exercise. The approach was to make a comparison of how the core principles reflect what each sector regards as the key risks (risk identification), and what the respective core principles expect of management and/or supervisors in addressing these risks (risk management). It should be noted that the key risks for each sector, and the risk management techniques applied to them, are discussed in detail in the report of the Joint Forum on capital and risk assessment.

34. The Joint Forum has undertaken a comparison of the core principles, not of the actual supervisory practices in the three sectors. Nevertheless this report makes reference in certain places – notably in Section 6 below – to the way in which supervision is conducted. It is important to emphasise that, where it does so, the report sets out generalities to which there will inevitably be local exceptions that it is not practicable to catalogue in a report of this nature.

6. Relevant Characteristics of the Three Sectors

35. Some of the similarities and differences among the core principles reflect, at least in part, intrinsic characteristics of the banking, insurance, and securities sectors. Consequently, an analysis was undertaken of the similarities and differences of these intrinsic characteristics, restricting it self primarily to those areas that are most relevant to understanding the differences in core principles. Not all differences between the sectors are apparent from a comparison of the core principles, nor are all differences between the sectors relevant to such a comparison. In this report the Joint Forum makes no claim to have undertaken a comprehensive comparison of the three sectors more generally. This section of the report summarises the results of the analysis as an aid to explaining the differences between the core principles set out in section 7 below.

36. In general, the banking, insurance, and securities sectors offer a variety of financial products and services that facilitate the efficient transfer of economic resources or risk. In many jurisdictions the lines between the sectors have grown increasingly blurred; banks

engaging in securities activities, securities firms selling and exchanges trading financial instruments designed to hedge risk, and insurance companies offering savings vehicles, for example. Thus the traditional demarcation between the three sectors is subject to a process of erosion, in which the growth of financial conglomerates is a contributory factor.

37. This does not mean that products have become identical or that all financial services activities are generally provided by one type of business. There exist areas where the sectors differ, such as in the form of financial intermediation and risk transfer. The analyses were focused on intrinsic differences among the three sectors, recognising that the work may mask some areas where the sectors overlap. In addition, the high level approach to analysing sector differences may not fully illustrate the complexities within each of the sectors.

(a) Banking

38. Problems arising in any of the three sectors can have an impact on overall financial stability and, of course, vice versa. Traditionally, distress in the banking sector and instability in the macroeconomic environment have been perceived as reciprocally linked. Interaction between financial services and the economy is clearly not unique to the banking sector. Nevertheless, concerns about the importance of banks to the overall economy, including their use as a tool in the implementation of monetary policy, are reflected in the historic tendency of many governments to support their banking sectors during times of crisis, as well as the widespread existence of depositor protection schemes. Because of the strong linkage between the banking sector and the macro economy, banking supervisors - many of which are (or were) also central bankers - have placed a great deal of emphasis on systemic stability and preconditions for effective supervision.

39. A number of defined risks of banking activities are identified in the Basel core principles. The most significant risk for banks has historically been credit risk - which can be amplified by concentration risk - on the asset side of the balance sheet. Risk arises on the liability side as well, in the form of liquidity risk posed by maturity mismatches between short-term deposits and long-term loans. Other banking risks include market risk (including volatility in the trading book), interest rate risk in the banking book, foreign exchange risk, funding risk, operational risk, country and transfer risk, legal risk, and reputation risk. Banks are expected to have policies in place to identify, control, and manage these risks, and specific requirements in this regard (e.g., credit granting and monitoring procedures to manage credit risk) are described for individual risk categories.

40. Proper asset valuation is an important issue in the banking sector, particularly as it relates to loan valuation and provisioning. Failure to take adequate provisions against troubled loans can mask the true financial condition of a bank. Supervisors and bank counterparties consequently have an interest in ensuring that a bank values its assets properly and that the financial statements present a fair and accurate picture of the bank's financial condition. Supervisors also promote disclosure of information by banks, believing that market discipline can serve as an adjunct to regulation and reinforce the need for banks to behave in a safe and sound manner.

41. Supervisors in all three sectors must take into account the balance of advantage in making public any supervisory action that has been taken to prevent or remedy problems in supervised firms. This leads banking supervisors in many jurisdictions to avoid or postpone public disclosure of banks' problems because of the importance of maintaining confidence in the banking system. Public confidence is essential to ensure stable funding. Loss of confidence in the banking sector can create financial instability by resulting in a run on banks by depositors, with a subsequent systemic drain on liquidity.

42. Unique among the three sectors, a uniform risk-based capital standard (the Basel Accord) applies to all internationally active banks. In practice a large number of countries also apply the standard to domestic banks. The Basel Accord was created to safeguard financial stability and counteract a deterioration of bank capital levels. Moreover, this international standard was intended to reduce competitive inequalities across countries. It was first adopted in 1988, with several amendments and revisions in the years following. In January 2001, the Basel Committee issued for a second round of public consultation a major proposed revision to the Accord. This revision is intended to greatly enhance the risk sensitivity of the international capital framework.

43. In the banking sector, international business is conducted to a large extent through foreign branches and subsidiaries. Recent years have seen an increasing number of cross-border mergers as well. There is significant interdependence between internationally active banks in different countries through the interbank market and the payment systems. To supervise internationally active banks most effectively, supervisors have relied on a pragmatic home/host division of supervisory responsibilities supported by information sharing. In particular, host country supervisors are expected to share relevant information with the appropriate home country supervisor.

44. Within banking groups - both international and domestic - there is a risk of contagion from one part of the group to another. Banking supervisors are concerned that problems may spread to deposit-taking institutions within a banking group. The Basel Committee therefore requires that all banks be supervised on a consolidated basis, which should minimise double gearing of bank capital, ensure that risks are managed on a group-wide basis, and mitigate the risk of contagion within a banking group.

(b) Insurance

45. Insurance provides a safety net when underlying adverse events occur. Insurance firms themselves are directly affected by economic events such as interest rate movements, which can impact asset valuation, and inflation, which can result in policyholders cashing out policies. Moreover, economic distress leading to deteriorating social or economic conditions, or obligations to pay damages as a result of judicial rulings, can result in new liabilities and potentially catastrophic losses.

46. Insurers intermediate risks directly. They manage these risks through diversification and the law of large numbers. For example, diversification of policy liabilities can be achieved through reinsurance. Aside from these direct business risks, the most significant risks to insurers are generated on the liability side of the balance sheet. These risks are referred to as technical risks and relate to the actuarial or statistical calculations used in estimating liabilities. If these calculations are incorrect (for example, if one or more of the assumptions on which they are based prove to be inaccurate), the consequences for the insurer can be significant. In particular, premiums charged could be inadequate to cover the risk and costs, insurers may pursue lines of business that are not profitable, and liabilities may be under- or over-stated, masking the true financial state of a company. On the asset side of the balance sheet, insurers incur credit, market and interest rate risk from their investments, as well as risks arising from asset-liability mismatches.

47. Accounting plays an important part in the insurance sector. Of particular importance to insurers is the valuation of liabilities, which affects pricing decisions and the ability of the insurer to operate as a going concern. In order to assess a company's long-term solvency, supervisors need to obtain extensive information about the actuarial and statistical assumptions used to establish prices and technical provisions. However, similar disclosure is not normally provided to the marketplace. As a result market discipline has played a lesser

role in insurance supervision, largely because of the opaqueness of liability valuations. Nonetheless, the need for insurers and intermediaries to provide accurate and appropriate advice and treat customers fairly is recognised in many jurisdictions where the responsibility of insurance supervisors includes the conduct of business.

48. Insurance supervisors are concerned that disclosure to the public of regulatory actions being taken could cause policyholders or others to take actions that could worsen the situation the supervisor was trying to remedy. Furthermore, the public awareness of difficulties of individual companies might affect public confidence in the insurance sector as a whole. However, in at least some jurisdictions, a distinction is made between supervisory actions related to prudential issues, which tend not to be made public, and those related to conduct of business issues, where disclosure is more common.

49. While much reinsurance business is international in nature, the cross-border size of the overall insurance market is relatively small. Like banks, insurance companies establish subsidiaries and branches in foreign jurisdictions. However, in the case of branch operations, companies are generally required to "vest" assets (i.e., hold sufficient assets in the jurisdiction to cover the related policy liabilities). Because of the limited amount of cross-border business and ability to "ring-fence" operations by jurisdiction, the need for world-wide consolidated supervision has been less apparent for insurance supervisors, although this is changing, and cross-border cooperation is increasing.

(c) Securities

50. Supervision in the securities sector addresses more than just securities intermediaries (broker-dealers and investment advisors). It also includes securities markets, exchanges, collective investment schemes, and disclosure by issuers. Consequently, whereas banking and insurance supervisors deal almost entirely with the supervision of firms, securities supervisors have a much broader scope of jurisdiction.

51. The securities sector is sensitive to macroeconomic factors in that there is typically a predictable correlation between macroeconomic indicators and market sentiment. Extreme macroeconomic conditions can lead to rapid changes in confidence, resulting in, for example, runs on assets by fund managers or rapid unwinding of futures positions with leverage on equity values. A catastrophic loss of confidence, for whatever reason, on the part of the markets can lead to massive and rapid withdrawal of short-term funds, producing a collapse in asset prices. Securities firms are also potentially vulnerable to problems in the banking sector to the extent that payment and settlement systems are compromised; large-scale market default could bring gridlock to the payment and settlement systems. Consequently, securities supervisors place an emphasis on pre-conditions for effective supervision, sound market processes, observance of detailed operating processes, and trading and settlement issues.

52. Securities supervisors generally disclose enforcement actions. This is because in the securities sector, supervisory transparency and accountability are linked to the maintenance of confidence in the markets, which is vital for the maintenance of orderly markets. In the view of securities supervisors such transparency strengthens perceptions of regulatory predictability, which in turn facilitates normal market functions and improves the credibility of the enforcement process. In addition, transparency contributes to supervisory accountability.

53. Securities markets have a strong international component. An increasing number of securities trading platforms and clearing and settlement systems operate on a multi-jurisdictional basis, and a number of large, international firms operate in the securities

markets. Technology-based trading of securities and ease of remote access to the market by investors and securities firms also facilitates cross-border operations, including the cross-border raising of capital by issuers. Given the international nature of the securities markets, supervisory cross-border cooperation serves several purposes. As with supervision in the banking and insurance sectors, it allows for effective supervision of an institution where related companies trade in several jurisdictions. It also allows for the effective monitoring of risk across markets.

54. In addition to the characteristics discussed above, there are features unique to the securities sector that are reflected in the IOSCO Objectives and Principles of Securities Regulation. These need to be highlighted:

- ***Self-Regulatory Organisations.*** One of the unique features of securities supervision is that it may rely on market participants through self-regulatory organisations (SROs) to regulate some of their own activities under supervisory oversight. In some jurisdictions much of the inspection and supervision of entities engaged in the securities business is done by SROs, which also are primarily responsible for market surveillance and for rule enforcement with respect to their members. SROs must obtain supervisory approval for the rules by which they govern their members and activities, and a securities supervisor can directly enforce the rules if it finds that the SRO is unable or unwilling to take appropriate action. Supervisors can also bring an enforcement action against the SRO itself.
- ***Issuers/Disclosure.*** Investors are best able to make informed investment decisions when they have access to transparent financial reporting and full and fair disclosure regarding an issuer, its securities and the respective transactions. Securities trading depends on a continuous stream of current information. Adequate disclosure of financial information is essential to accurate price formation, informed investor choice, and efficient allocation of capital. Most jurisdictions take a disclosure approach whereby individual customers, rather than supervisors, have responsibility for evaluating the merits of an investment in the issuer's securities. While not all supervisors are responsible for issuers directly, there are detailed disclosure requirements as well as a general requirement that the materials used in connection with an offering not contain any material misstatements or omissions. A disclosure system relies on adequate accounting, auditing and financial reporting, in order to assist customers in determining the true position and profitability of enterprises and make informed decisions. High quality accounting and auditing standards are therefore a critical element of securities supervision.
- ***Enforcement.*** In many jurisdictions, securities supervisors have comprehensive enforcement powers. Securities supervisors generally have broader authority than their banking and insurance counterparts to investigate possible violations involving both supervised and non-supervised entities and individuals. Furthermore, many securities supervisors have the authority to compel production of information and to initiate legal proceedings themselves either administratively or in court for violations of securities laws. In addition, securities supervisors can recommend that the relevant domestic criminal prosecutors take enforcement actions. Securities supervisors require such comprehensive enforcement powers because individuals and entities other than supervised regulated firms can perpetrate securities violations. Investors are vulnerable to misconduct by intermediaries. Securities violations also can occur both on and off the securities markets.

  Because of the internationalisation of the world's securities markets, the emphasis that securities supervisors place on investigation and enforcement and the fact that securities violations can be conducted from or involve activity or proceeds located in other jurisdictions, securities supervisors have developed an extensive network of

cooperative arrangements that facilitates their investigating and taking action on behalf of a foreign counterpart. In some jurisdictions, a securities supervisor may share information with and assist its foreign counterparts even where the supervisor has no interest in the enforcement matter itself. The IOSCO core principles address the importance of cooperation without regard to whether the conduct at issue would be a violation of the laws of the jurisdiction from which information is requested.

- ***Market Surveillance.*** Monitoring also involves market surveillance, which is unique to the securities sector. Securities supervisors and, where applicable, SROs are responsible for monitoring trading in listed securities to determine whether there is evidence of securities law violations.

7. Analysis of Common Principles and Differences based on the Matrix

(a) Pre-conditions

55. All sectors agree that effective supervision cannot take place in a vacuum and that it is dependent upon the existence of other factors, or "pre-conditions" outside the supervisory framework itself. Thus, all three sectors include in their respective core principles a list of pre-conditions necessary for effective supervision.

56. While all three sectors focus on pre-conditions, the core principles of each sector emphasise different areas. The Basel core principles state expressly that jurisdictions should have sound and sustainable macroeconomic policies and a well-developed public infrastructure. This reflects the role that banks traditionally have played in the financial system as discussed in Section 6(a). The IAIS core principles also mention preconditions; however, like the IOSCO core principles, these focus on the infrastructure needed for effective supervision (i.e., effective legal, accounting and, for IOSCO, tax frameworks) and not on macroeconomic policies.

(b) The Supervisory System

(1) Objectives of supervision

57. Each sector sets out key objectives for banking, insurance or securities supervision in its respective documents. In striving to meet these objectives, supervisors should be guided by the core principles.

58. All three sets of core principles mention both customer (i.e., depositor, policyholder, investor) protection and systemic stability as key objectives. In addition, IOSCO has a third objective: ensuring that markets are fair, efficient and transparent. This third objective reflects the role of supervisors in overseeing securities markets. As explained in section 6, banking and insurance supervisors oversee financial institutions, not markets.

59. Although all sectors regard systemic stability as an objective, the Basel core principles place greater emphasis on systemic stability and consider customer protection as a by-product of stability. The importance of banks to the macro economy and financial system generally is discussed in Section 6(a). According to the IAIS core principles, the key objective of insurance supervision is policyholder protection. IOSCO places equal weight on its three objectives: investor protection, fair, transparent and efficient markets and the reduction of systemic risk.

(2) Attributes of supervisory systems

Operational independence and adequate resources

60. All three sets of core principles mention the need for supervisors to have operational independence. Such independence is seen as the ability of supervisors to act without interference from the political process and supervised industries in day to day operational decision making. Independence does not mean that supervisors should not consult with the industry they supervise in the formulation of supervisory regulations. This consultation occurs in all three sectors, and its value is expressly recognised in the IOSCO core principles.

61. All three sets of core principles also contain detailed requirements for adequate minimum resources, legal protection for supervisory staff acting within their responsibilities, and staff observance of high professional standards (e.g., expertise and ethics).

62. Finally, the core principles in all three sectors mention the need for supervisors to be accountable to the public for their supervisory actions. This is achieved in part by issuing annual reports to the public.

Enforcement powers and capabilities

63. The core principles in all three sectors acknowledge that supervisors need powers to take remedial action on a timely basis to deal with impending and actual problems.

64. As noted in Section 6(c), the IOSCO core principles place the most emphasis on the significance of, and need for, comprehensive enforcement powers. This is a major difference among the three sets of core principles. While supervisors in all three sectors have the authority to investigate possible violations and take legal action against supervised institutions and associated individuals, securities supervisors also have wider authority to take action against non-supervised entities and individuals for violations of securities laws.

65. Another difference is the transparency of the enforcement process, which was discussed for each sector in Section 6. While investigations conducted by securities supervisors are not public, enforcement proceedings are generally public proceedings. Securities supervisors generally publish the results of proceedings and sanctions imposed to warn customers of particular entities, individuals or schemes. In the banking sector supervisory remedial actions of a prudential nature are not always publicly announced for fear that in so doing problems could be compounded, thus reducing the chance of the action being effective. Similar considerations apply to prudential issues in the insurance sector, although insurance supervisors in some jurisdictions favour disclosure of remedial action in respect of conduct of business issues.

(3) Clarity and transparency of supervisory process

66. All three sets of core principles require supervisors to adopt clear supervisory processes. Practices must be transparent to the public and comprehensible. Such clarity allows supervised entities to be certain of the rules to which they must adhere when undertaking their business activities. It also facilitates supervisors' accountability to the public.

67. All three sectors require that supervisory rules be applied in a consistent manner to all supervised entities.

(4) External participants in the supervisory process

68. External participants are parties outside the supervisory authority. Supervisors in all sectors may use external participants to assist in supervisory functions.

69. Each set of core principles cites the use of external participants (e.g., external auditors) in the supervisory process. Some external participants are specific to the sector. For example, the IAIS core principles explicitly refer to actuaries. Similarly, the IOSCO core principles discuss the role of SROs in complementing the work of supervisors. The potential role of SROs to the securities sector is described in Section 6(c).

(c) The Supervised Entity

(1) Licensing, qualifications, ownership transfer and corporate control

70. In most cases, entities must be licensed and the appropriate supervisor must vet key individuals before they can conduct banking, insurance or securities business. All three sets of core principles require that supervisors have a regime for licensing entities and regulating the appointment of key individuals. Supervisors should determine how entities and individuals qualify to do business in their jurisdictions. For example, qualification requirements may stress the competence, skill and ethics of individuals. Also, supervisors should have authority to set minimum standards for licensing entities and reject applications that do not meet the standards set.

71. In the securities sector, there may exist a broader array of licensing requirements because there are different types of supervised entities. Supervised entities include intermediaries (both broker-dealers and investment advisors), collective investment schemes, trading systems and markets. The IOSCO core principles address the licensing requirements for each of these entities. For example, when licensing new trading systems, the IOSCO core principles mention “operator competence” as being relevant.

72. All sets of core principles require that permissible activities of licensed entities be clearly set forth and allow each supervisor to define the list of permissible activities. Moreover, legal and regulatory restrictions on the types of business exist in each sector.

73. The Basel core principles protect the word “bank.” This is done to prevent the public from being misled by an entity that inappropriately represents itself as a bank. Customers can thus be assured that institutions using the work “bank” are supervised institutions and allowed to provide banking services.

74. All sectors have rules enabling the supervisory authority to be notified of ownership transfers of supervised entities. However, banking and insurance core principles specifically state that supervisors may accept or reject significant ownership transfers of supervised entities. Banking supervisors are required to have criteria in place for determining which acquisitions require prenotification and approval. Basel deems that a major investment in a subsidiary or affiliate could pose risks to the parent bank and wants to ensure that there is no obstacle to receiving all relevant information on the acquisition (for supervisory purposes).

(2) Corporate governance

75. All three sectors encourage sound corporate governance within licensed entities. Supervisors, if so authorised by domestic financial sector legislation, may establish corporate governance requirements, such as defining the roles and responsibilities of management.

76. While similar corporate governance requirements apply to supervised entities in all three sectors, these requirements also apply to issuers in the securities sector. For issuers, good corporate governance means accountability to shareholders by boards of directors in selecting, monitoring, compensating and, when necessary, replacing, the managers who direct corporate operations on a daily basis. Good corporate governance for issuers also means transparency and certainty in the system of corporate accountability and responsibility, on which access to capital markets depends.

(d) Ongoing Supervision

(1) Group-wide supervision

77. All sets of core principles require group-wide supervision. Treatment of group-wide supervision differs, however, among the three sets of core principles.

78. As noted in Section 6(a), the Basel core principles emphasise the importance of consolidated supervision[1]. As a result, banking supervisors have access to information on banking and non-banking activities undertaken by the bank and its affiliated entities. Consolidated supervision allows banking supervisors to assess whether these banking and non-banking activities pose risks to the bank and, in turn, to the overall financial stability of the banking system.

79. Consolidated supervision is not generally required in the insurance sector. However, according to the IAIS core principles, supervisors should have the ability to impose reporting requirements on a consolidated basis. Furthermore, insurance supervisors take a group-wide approach by requiring that capital requirements be structured so as to prevent multiple gearing. The need for taking this group-wide view is also recognised in the core principles dealing with cross-border establishments.

80. The IOSCO core principles do not prescribe consolidated supervision. Securities supervisors have diverse ways to obtain information about the activities of a broker-dealer and its affiliates. The IOSCO core principles expressly state that supervisors need to obtain information about unlicensed and off-balance sheet affiliates of supervised entities. The IOSCO core principles also state the importance of enhancing cooperation with authorities responsible for supervising other parts of the group and establishing measures to safeguard regulatory capital within the individual firms.

(2) Monitoring and on-site inspection

81. All sectors require an effective framework for monitoring and on-site inspection of supervised entities to assess compliance with relevant laws and supervisory requirements. As discussed in Section 6(c), monitoring in the securities sector also includes market surveillance.

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[1] Supervision of the banking group on a consolidated basis goes beyond accounting consolidation. It implies that there is a group-wide approach to supervision whereby all risks run by a banking group are taken into account, wherever they are booked. It is important to note that both accounting consolidation and consolidated supervision are key aspects of the supervision of banking groups.

(3) Reporting to supervisors

82. Supervisors in all three sectors can require from supervised entities information necessary to verify compliance with laws and supervisory requirements. All sectors expect supervisors to have the power to require the provision of information and the right to inspect relevant records. The Basel and IAIS core principles provide examples of the types of information that would be required (e.g., statistical returns and other prudential requirements) and identify other requirements, such as the frequency of reporting.

(4) Cooperation and information sharing

83. All three sets of core principles require supervisors to have arrangements for information sharing and cooperation both domestically and with foreign supervisors. However, the objectives of such arrangements differ among the sectors.

84. For the reasons set out in Section 6(a), in the banking sector, supervisors establish information-sharing arrangements between home and host country supervisors. Banking supervisors must have power to share with home country supervisors information relating to the local operations of foreign banks, and vice versa. These arrangements are necessary for consolidated supervision.

85. The IAIS core principles identify the need for adequate and effective communication in order for insurance supervisors to share relevant information with each other. In particular, consultation between home and host supervisors is necessary in the creation of cross-border insurance establishments (branches and subsidiaries). Insurance supervisors may rely on home country supervision "if prudential rules in the two countries are broadly equivalent".

86. The IOSCO core principles address the need for information sharing mechanisms for both supervisory and enforcement purposes. The IOSCO document provides greater detail as to the scope of cooperation and the content of information sharing arrangements than the other sets of core principles. This includes cooperation between securities regulators and criminal and judicial authorities in cases of suspected fraud or market abuse.

87. Information sharing for enforcement purposes is not required by banking or insurance supervisors because they refer matters to other authorities in the event that legal action is necessary. The importance of information sharing mechanisms to securities supervisors is explained in Section 6(c).

(5) Confidentiality

88. Maintaining the confidentiality of non-public information is important to all three sectors. In particular, all sectors require that supervisory staff protect confidential information. Additionally, the core principles in all sectors require supervisors to have the ability to safeguard the confidentiality of information received from other authorities and ensure the appropriate confidentiality of information provided to other authorities.

(e) Prudential Standards

(1) Risk management

89. Supervised entities in all sectors are exposed to risks, and all supervisors agree that the entity should have procedures for effectively managing risk. The supervisor's role is to ensure that effective risk management systems are in place and to establish standards of good practice, where necessary.

90. The Basel core principles expressly identify and describe the significant risks faced by banks, including, for example, credit, market, liquidity, and operational risk. Since the primary role of banks is to make loans, these risks largely (but not exclusively) affect the asset side of the balance sheet. Whereas IOSCO and IAIS have mainly a general approach to risk management, the Basel Committee includes specific elements of risk management in its core principles. A more detailed discussion of risks in the banking sector is contained in Section 6(a). Many risks that securities firms face are similar to those of banks. The IOSCO core principles refer to the detailed guidance given to supervisors on risk management in complementary IOSCO standards and papers.

91. As described in Section 6(b), while these risks also apply to insurance companies, the most significant risks for insurers relate to liabilities. An insurer's liabilities are estimations of the future cost of claims. Pricing decisions are made based on these estimates; in addition, asset portfolios are structured to match liabilities in terms of duration, currency, interest rate, etc. Therefore, any inaccuracies or misestimations in valuing liabilities can significantly affect a company's liquidity or financial viability. The IAIS core principles address prudential supervision by balance sheet category, identifying the respective tools supervisors should possess to manage risk effectively. For example, the IAIS core principles require the authority to prescribe standards for establishing technical provisions and check their sufficiency with regard to liabilities.

92. Tools for effective risk management that are described in all three sectors' core principles and related documents include:

- setting capital requirements;
- ensuring that good accounting and valuation practices are followed;
- establishing limits on particular assets or exposures; and
- requiring that the necessary policies, procedures and reporting systems be put in place.

93. Sometimes a particular risk is identified in the core principles of only one sector. This is generally either because the risk is unique to a sector - for instance, reinsurance risk in the insurance sector - or because of the way the document is structured. Off-balance sheet exposures, for example, are addressed separately in the IAIS core principles largely because the document is structured by balance sheet category. The other sectors treat the risks of off-balance sheet exposures no differently than on-balance sheet exposures.

94. Another example is proprietary trading, which is addressed specifically in the IOSCO core principles. Securities firms trade for proprietary purposes as well as on behalf of clients. In order to prevent unauthorised trading of clients' assets, securities supervisors need to be assured that firms' proprietary assets are physically segregated from client assets. In addition, financial responsibility requirements address risks associated with trading on behalf of clients. Proprietary trading is closely linked to prudential requirements since the adequacy of a firm's net capital will be determined relative to the risk associated with its proprietary trading. Trading on behalf of clients is not seen as a traditional activity for banks and insurance companies in many jurisdictions and is therefore not addressed in their core principles.

95. In addition, only the IOSCO core principles deal with the risks relating to secondary markets, collective investment schemes and clearing and settlement systems.

(2) Internal controls

96. Supervisors in all three sectors stress the importance of internal controls within regulated entities, recognising that these need to be tailored to fit specific industry circumstances. The supervised entities are responsible for establishing and maintaining appropriate internal controls; supervisors are responsible for ensuring appropriate controls exist. All three sectors consider that internal controls, as broadly defined, cover both internal procedures and external requirements such as compliance with relevant supervisory requirements.

(3) Risk concentration

97. The core principles of all three sectors provide rules limiting risk concentration. However, the type of risk concentration covered by such rules differs between the various sectors. For the Basel Committee, risk concentration is focused on counter party risk, and to some extent sectoral and geographic risks, in terms of assets. In the IAIS core principles, the main focus for controlling risk concentration is in promoting a suitably diversified investment portfolio. For the securities supervisors, risk concentration refers mainly to the impact on the markets of large positions being taken.

98. The Basel and IAIS core principles state that supervisors should have the authority to establish standards to limit concentrations in assets. Insurance supervisors should require companies to diversify their assets by type, including, where applicable, establishing limits or placing restrictions on particular assets. Banking supervisors must establish large exposure limits. The Basel core principles methodology sets forth very specific limits, reflecting previously established guidance issued by the Basel Committee.

99. The IOSCO core principles require market authorities to monitor large exposures on a market and to share information with one another to permit appropriate assessment of risk. Market authorities must establish trigger levels appropriate to their markets and continuously monitor the size of positions.

100. Reinsurance is a means of diversifying concentrations on the liability side of an insurer’s balance sheet. Consequently, only the IAIS core principles specifically address reinsurance.

(4) Capital requirements

101. The core principles of all three sectors specify that supervisors should set capital requirements for supervised entities. In the case of IOSCO, this applies primarily to market intermediaries (i.e., securities firms). These capital requirements should reflect the risks undertaken by the entities. The Basel and IOSCO core principles expressly state that the capital requirements should be risk-based. IAIS expects insurance supervisors to take into account the size and complexity of insurance companies, in addition to the risks undertaken, in setting capital requirements.

102. As discussed in Section 6(a), the Basel Committee has established an international capital standard (the Basel Accord) which is intended to apply to all internationally active banks. Supervisors are expected to establish capital requirements - including defining eligible capital components - that are at least as strict as the requirements of the Basel Accord. IOSCO and IAIS, by contrast, expect supervisors to promulgate capital requirements but do not have a single international capital framework for their respective sectors.

103. Insurance supervisors have yet to develop an international capital standard, in part because there are still great differences in insurance accounting and actuarial standards

among jurisdictions. Work is underway both within the IAIS to identify principles on which a capital standard can be built and within the professions to harmonise accounting and actuarial standards.

104. Jurisdictional differences also preclude a uniform international capital standard in the securities sector. In contrast to banking and insurance supervisors' emphasis on the supervised entity as a going concern, securities supervisors focus their attention primarily on the liquidity of the entity. Generally, securities firms must have liquid assets in excess of liabilities so that the firm could be wound down in an orderly manner.

(5) Accounting policies and practices

105. Supervisors in all three sectors stress in their core principles that high-quality accounting policies and practices serve both supervisory purposes and the public interest. For IOSCO, this applies not only to market intermediaries, but to disclosure by issuers as well, as discussed in Section 6(c). The Basel and IOSCO core principles also refer to the importance of internationally acceptable auditing standards. The IOSCO principles note that these standards should be of high quality.

106. The Basel and IAIS core principles allow for supervisors to set accounting and valuation standards, recognising that, in some cases, these may be relevant solely for supervisory reporting purposes. Insurance supervisors, in particular, have generally found that commercial general accounting practices are not appropriate for the insurance business in part because of the extent to which an insurer's liability can only be based on estimation. Only the IOSCO core principles describe the characteristics of acceptable accounting and auditing standards. High quality accounting and auditing standards are necessary safeguards of the reliability of financial information in the securities industry.

(f) Markets and Customers

(1) Markets

Market integrity

107. The importance of ensuring market integrity is cited solely in the IOSCO core principles. This is a function of the role of securities supervisors in overseeing securities markets, whereas banking and insurance supervisors generally oversee individual firms but not the markets themselves.

Financial crime

108. All three sectors' core principles discuss the role of supervisors in addressing fraud and money laundering.

109. The Basel core principles indicate that banking supervisors should have appropriate laws or supervisory requirements in place and should expect bank management to establish internal controls to prevent the bank from being used in fraudulent or criminal activities such as money laundering. The Basel core principles state that banks should be required to report suspicious activities and significant incidents of fraud to their supervisors. The IAIS takes a similar view.

110. The IOSCO core principles address money laundering in a like fashion. However, the IOSCO core principles do not impose a requirement for supervised entities to report suspected money laundering activity to the supervisor. The IOSCO as well as the Basel core principles do refer to the recommendations of the Financial Action Task Force on Money

Laundering (FATF) as additional guidance to the principles themselves. In addition, unlike the Basel and IAIS core principles, the IOSCO core principles require supervisors to have enforcement powers to detect and deter market abuses. This is described in Section 6(c).

(2) Customer protection

111. Both the IAIS and IOSCO core principles make clear that supervisors in their respective sectors have a role in protecting customers.

112. Customer protection is not specifically addressed in the Basel core principles, except to the extent that depositor protection is cited as an objective of banking supervision. This may be in part because not all jurisdictions were involved in customer protection when the Basel core principles were drafted. Although this has changed in many jurisdictions in recent years, customer protection is not mandated for bank supervisors in all countries.

113. As described in Section 6(b), the IAIS core principles focus on the importance of insurer and intermediary (i.e., broker) conduct vis-à-vis customers. This is a function of their central role in the sale of insurance products.

114. The IOSCO core principles state that investor protection is one of the three objectives of securities supervision and the core principles work together to achieve the stated objectives. The IOSCO core principles, for example, state that securities supervision should govern the segregation and protection of client assets that are held separate from company funds. This applies not only to firms, but also to specific products such as collective investment funds. The IOSCO core principles also address investor protection through principles on disclosure and enforcement powers.

(3) Information, disclosure and transparency

115. Each of the three sectors' core principles notes the importance of disclosure and transparency, although with different aims.

116. The Basel core principles do not address customer disclosure. However, they do address the importance of market disclosure. In particular, public disclosures are seen as playing an essential role in imposing market discipline on banks to operate in a safe and sound manner. This is discussed in Section 6(a).

117. The IAIS core principles emphasise the importance of requiring disclosure to customers so that they have the information necessary to make appropriate decisions relating to their insurance contracts.

118. The IOSCO core principles address disclosure by intermediaries to investors. In addition, the IOSCO core principles address disclosure by issuers and disclosure about trading on a market. For securities supervisors, public disclosure and transparency are essential to allowing investors to make timely, informed investment decisions, as described in Section 6(c). Furthermore, transparent trading promotes confidence that the pricing and functioning of the market is fair.

(4) Issuers

119. This item is only referred to in the IOSCO core principles and is unique to the securities sector. Discussion of disclosure by issuers is contained in Section 6(c).

8. Observations and Conclusions

120. A side-by-side comparison of the key documents highlights differences in format, style and language. It is also apparent that the three sectors' core principles have different origins. Analysing these differences, and understanding how they arise, is important in distinguishing between issues where the core principles differ in form and those where they differ in substance. This is the reason, as explained in Section 5, why it was decided to undertake a detailed comparison based not just on the text of the core principles but on the underlying issues as well.

121. The Joint Forum found that a thorough comparison of this kind is necessary but not in itself sufficient for identifying common principles and differences. The results of that comparison, as set out in Section 7, are the product of extensive discussion within the group. The comparison actually reveals a good deal more by way of similarity between the three sectors than initial appearances might suggest. On some important issues, the core principles have many common features, in respect of the supervisory system, the supervised entity, ongoing supervision and at least some aspects of prudential requirements (for example, all three sectors stress the importance of internal controls within regulated entities - see paragraph 96). Only in the area of markets and customers does it become difficult to establish such high-level common ground, and that is primarily because of the difference in the traditional scope of supervisory responsibility between the three sectors.

122. Inevitably, the work undertaken has had limitations, and has not necessarily exposed every possible area of conflict or contradiction between the requirements of the three sectors. In particular, while the analysis has drawn on the methodologies to assist the comparison of the core principles (see paragraph 125 below),a comparison of the methodologies themselves has not been undertaken. With that caveat, no evidence of underlying conflict or contradiction between the three sets of core principles has emerged from the comparison. In other words, there is no reason to suppose that adherence to the core principles of one of the three sectors automatically causes supervisors or supervised entities to be in breach of the core principles of either of the other two sectors.

123. There are nevertheless significant differences in both presentation and content which need to be considered in determining the extent to which they may impair the effectiveness of the core principles in practice, particularly in terms of cross-sectoral work on assessment or for integrated supervisors. Differences of form, style and language exist and cannot be ignored. The core principles documents are clearly not based on a common template, and do not have a common structure. They were written at different times, which means that circumstances may have changed and thinking evolved meanwhile. Discussions in the course of the Joint Forum’s work were often indicative that the core principles were written by different people with different backgrounds and consequently reflect different perspectives and philosophies. They were written for different audiences - the three ‘constituencies’ are very different in terms of numbers and diversity of membership and jurisdiction. The IOSCO objectives and principles were written for the use of IOSCO members. Although the international financial institutions, especially the IMF and World Bank, had an interest in these objectives and principles, and were consulted along with IOSCO members on the content, the objectives and principles were not designed primarily for assessment purposes. By contrast, the Basel and IAIS principles were written both for self and external assessment. But it would be wrong to see these differences purely as accidents of independent evolution, when in some cases at least they result from deliberate choices on the part of the standard-setting bodies.

124. Differences in the use of language and terminology can present particular problems. They can create the risk of misunderstanding where the same word or phrase is used by different sectors with a different meaning or nuance: an example is the word ‘intermediary’

which has different meanings for IOSCO and IAIS. Conversely, the use of different words or expressions by different sectors can cause confusion where the underlying meaning is the same - for example ‘solvency margin’ as used by IAIS has essentially the same meaning as 'capital adequacy' for Basel. Other terms to which this applies include ‘corporate governance’ (which is the subject of the detailed study by the Joint Forum on Corporate Governance and the use of the audit functions in the supervisory process) and ‘large exposures’. The issue is widely acknowledged; addressing it is complicated by the fact that the use of language and terminology is not necessarily under the control of the supervisors but often reflects conventional usage in the sector concerned.

125. In each sector a full understanding of the core principles cannot be gained from reading the basic core principles document on its own. In the case of Basel and IAIS, as explained in paragraph 22 above, methodologies have been developed to facilitate understanding for assessment purposes of how the core principles should be applied in practice. These methodologies typically refer to further guidance issued by the IAIS and Basel Committee, to give assessors a better understanding of the intent of each core principle. For IOSCO, by contrast, the text of the core principles itself gives more detailed guidance, but for the purposes of implementation rather than assessment, and in this case the document makes extensive reference to other IOSCO papers, typically by way of footnotes.

126. Each sector's core principles provide an overview of the key elements of the supervisory regime in that sector as at the time they were written. However, the pace of developments in the financial sector means that the core principles documents may periodically need updating. The impact of this varies between the sectors according to the structure of the relevant documents. For example, both the IAIS and IOSCO core principles refer to exchanging information specifically with supervisors from the other sectors, while this reference is not found in the Basel core principles. Sharing information with other sectors has increased in importance as a result of the developments in cross-sector conglomerates.

127. Section 7 of this report shows that the underlying principles of the three sectors are very similar in a number of areas such as authorisation, the organisation of supervision, and the circumstances in which supervisors should intervene. In many cases it is in the application of the principles, rather than in the principles themselves, that the differences occur. As a simple illustration, notification of ownership transfers is a common requirement, but the action to be taken in response to that notification may not be the same. A more complex example is that the core principles of all three sectors require capital to be held against risk but each sector assesses and aggregates risks in a different manner. Only the Basel core principles specifically refer to how the minimum capital standards are applied by making reference to the Basel Capital Accord. (This area is being further explored in the study on Risk Assessment and Capital.)

128. Intrinsic differences between the sectors, discussed in Section 6, are of course one of the main sources of differences between the core principles. It is not surprising to find that differences between the core principles arise from differences in the characteristics of the sectors to which they apply. Some examples include IAIS's emphasis on the valuation of liabilities and IOSCO's focus on markets and issuers.

129. There are, however, some significant differences which emerge from the comparison of the core principles which are not readily explained either as differences of form or as intrinsic differences. These differences were discussed at length without reaching complete agreement on the reasons for the differences, which appear to be attributable to differences of choice of supervisory approach, objectives or underlying philosophy. They include:

- ***Preconditions*** (paragraphs 55-56). The existence of preconditions is a common feature of each sector's core principles, but the expectations set out in these preconditions is different, for example in respect of the emphasis on macro-economic policies and market infrastructure, for no obvious reason. This point is also noted in terms of the objectives of supervision (paragraph 59), where the Basel Committee places greater emphasis on systemic stability.
- ***Group-wide supervision*** (paragraphs 78-80). Again the basic requirement is common, but the main differences as to how that requirement is to be fulfilled appear to follow from differences in perception of risk between the sectors. (This is also an example of a similar principle confused by differences of terminology.)
- ***Cooperation and information sharing***. For IOSCO, the scope of cooperation and information sharing is very wide. IOSCO places significant emphasis on enforcement powers (paragraph 64) and protection of investors in securities supervision. This is further reflected in terms of the importance it attaches to cooperation and information sharing (paragraph 86).
- ***Safeguarding of client assets*** (paragraph 114). This is partly intrinsic in that it is not a core business for insurers. Considering that banks also offer safekeeping of assets as one of their products, it is not clear what accounts for the differences in detail between Basel and IOSCO on this issue.
- ***Application of uniform prudential standards*** (paragraph 102). The Basel core principles alone incorporate the requirement for a uniform risk-based capital standard. This standard was created to safeguard financial stability and counteract a deterioration of bank capital levels. Moreover, the standard was intended to reduce competitive inequalities across countries. However, while not specifically mentioned in the core principles, it is acknowledged that the IAIS is moving towards an international capital standard (paragraph 103).

130. In considering the treatment of risk in the core principles, significant differences were found in the extent to which the core principles documents bring out what each sector regards as its key risks, although in no case should the core principles on their own be regarded as a sufficient guide to risk management in the sector concerned. Each set of core principles refers to the link between financial stability and systemic risk, but without expanding on what is meant by systemic risk. Compliance with the core principles is not to be regarded as guaranteeing financial stability.

131. In the course of the work, a number of significant developments were noted affecting the financial sector generally since the core principles were originally being discussed and drafted. These developments include:

- the use of the core principles by international financial institutions (IFIs), especially the IMF and The World Bank, for purposes of financial sector assessments, going, in some instances, beyond the purposes for which they were originally designed;
- the increased provision of similar products and services in different sectors;
- the continuing emergence in a number of jurisdictions of financial conglomerates; and
- the establishment of integrated financial supervisors in a growing number of jurisdictions.

132. These developments are considered to be relevant partly because of the different extent to which they may have influenced each sector up to now and partly because they should be borne in mind in considering the ongoing evolution of the core principles.

9. Options for Further Work

133. While the Joint Forum's mandate does not extend to making proposals for action in the light of its findings, it is nevertheless putting forward some options for further work. The Joint Forum recommends its parent organisations to study these options and consider whether to pursue further action.

134. The identified differences will potentially affect a number of different parties, and their significance will vary accordingly. The options set forth below should therefore be considered from the perspective of both the implementation of the core principles and the assessment process, and from the point of view of, for example:

- the supervisors in the sector concerned;
- supervisors in the other sectors (this is particularly relevant with regard to the supervision of financial conglomerates);
- governments setting up supervisory systems or contemplating changes in them;
- independent assessors (such as the IFIs);
- supervised entities; and
- others (public, academics, etc).

135. Arguably, differences at the implementation level may not greatly matter to individual sectors in isolation. But they may become more important in the context of cross-sectoral supervision and the emergence of integrated supervision, and may impede fair and effective supervision and assessment of the financial sector in general.

136. The options are grouped under three headings:

A. Content of existing core principles

B. Cross-sector interface

C. Presentation

For each option brief comments are given summarising the perceived benefits and drawbacks involved.

A. Content of existing core principles

137. These options seek to address issues where the Joint Forum has identified the potential for misunderstanding, confusion, or inconsistency in the interpretation or application of the core principles.

138. *Clarify definitions of key terms used in the core principles*. This would help to improve understanding of the core principles and would reduce the possibility of confusion. Each sector might wish to consult its own membership about the terms to be clarified and the definitions to be used. Some useful input may be provided by the work of the Joint Forum undertaken on risk assessment and capital. However, many of the terms used are terms of art or highly technical and simple definitions will not always be possible.

139. *Review core principles relating to group-wide supervision* with regard to their scope, effectiveness and consistency. Work in this area could make an important contribution to reducing the risk of supervisory arbitrage, and could draw on the work already undertaken by

the Joint Forum on this subject. The task is likely to be complicated, however, by different sectoral objectives, structures and local practices.

B. Cross-sector interface

140. These options arise from the observation that no one sector can be viewed in complete isolation from the others, as evidenced by the existence of the Joint Forum. This implies a need for consultation between the sectors in developing and implementing their respective core principles.

141. *Add cross-reference to other sectors' core principles* where appropriate. Cross-referencing would benefit cross-sectoral supervision and help assessors in their evaluation, particularly in cases where two or more sets of core principles give rise to similar but not necessarily identical requirements (for example, reporting to supervisors). Care might be needed to avoid giving the unintended impression of one sector's core principles 'endorsing' those of another. However, the comparison chart (Appendix B) demonstrates that this would not be an easy task.

142. *Provide for consultation between sectors on issues of common interest when changes to core principles are envisaged.* Such consultation would promote cooperation between supervisors of different sectors and would reduce the risk of unnecessary differences or inconsistencies between the core principles. An additional layer of consultation could, however, extend the process of amending the core principles.

C. Presentation

143. The option under this heading is concerned with the ease of use of the core principles documents; how readily they can be consulted, how easy it is to find a particular topic in each case and how different sectors' requirements can be compared. The focus is therefore on the core principles as tools of reference. This option involves little or no change to the core principles themselves.

144. *Develop a matrix-type guide to the core principles*, on the lines already produced (appendix to this report). Such a guide would permit easier navigation through the existing core principles documents and better understanding of their contents, and would facilitate cross sector comparisons. For these purposes it could be particularly useful for integrated supervisors, assessors and other interested parties. While much of the work on this option is accomplished, the matrix would require updating as the core principles evolve.

10. Future Evolution

145. In addition to the options set out above, the three parent Committees need to consider whether the core principles should be revised to take into account contemporary developments such as e-commerce, transparency, corporate governance, and financial conglomerates. The case for doing so is to enhance the topicality and credibility of the core principles, and to maintain their usefulness for supervisors, assessors and others. The difficulty, apart from the need to amend the core principles, is the risk that supervisors might be seen to be "moving the goalposts" for those economies which are in the process of implementing the existing set of principles. That could undermine efforts to achieve higher standards of supervision.

Appendix A

Membership of the Working Group on Comparison of Core Principles

Chairman: Richard Diggory, Financial Services Authority, United Kingdom

			*Sector**
Austria	Peter Braumüller	Ministry of Finance	I
Canada	Jane Lamb	OSFI	I
Finland	Kaija Kilappa	Financial Supervision	B
France	Noël Guibert	Commission de Contrôle des Assurances	I
France	Bénédicte Doumayrou	Commission des Opérations de Bourse	S
Germany	Stefan Niessner	Deutsche Bundesbank	B
Hong Kong	Andrew Procter	Securities and Futures Commission	S
Italy	Carlo Biancheri/ Gianluigi Gugliotta	Commission Nazionale per le Socièta e la Borsa	S
Japan	Tatsuo Sato (effective July 2000)	Financial Services Agency	I
Netherlands	André van Dorssen	De Nederlandsche Bank N.V.	B
Norway	Kirsten Nordbø Steinberg	Kredittilsynet	I
Sweden	Göran Lind	Sveriges Riksbank	B
United Kingdom	Julian Adams	Financial Services Authority	S
United States	Felice Friedman/ Marianne Olson	Securities and Exchange Commission	S
United States	T. Kirk Odegard	Board of Governors of the Federal Reserve System	B
	Udaibir S Das	International Monetary Fund	
	Alain Laurin/ Gabriella Ferencz	The World Bank	
	Luo Ping	Secretariat	
	Johanne C Prévost	Secretariat	

* I = Insurance; B = Banking; S = Securities

Comparison of Core Principles

Appendix B

Comparison Chart

Note: This document should be read in conjunction with the complete report on the Comparison of Core Principles.

JOINT FORUM

COMPARISON OF CORE PRINCIPLES

PHASE I

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Section I **Pre-Conditions**	Section II	Banking supervision is only part of wider arrangements that are needed to promote stability in financial markets. These arrangements include: sound and sustainable macro-economic policies; **a well developed public infrastructure; effective market discipline; procedures for efficient resolution of problems in banks; and mechanisms for providing an appropriate level of systemic protection.** A well developed public infrastructure needs to cover the following facilities: a system of business laws including corporate, bankruptcy, contract, consumer protection and private property laws, that is consistently enforced and provides a mechanism for fair resolution of disputes;	Section 1.3.4 of meth	1.3.4 Preconditions for effective insurance supervision Effective insurance supervision requires a set of preconditions to be in place. While these preconditions are largely beyond the control of the supervisory authority, weaknesses or shortcomings in these areas may significantly impair the ability of the supervisory authority to implement the Core Principles effectively. The preconditions cover a range of areas, including i) **a well-developed public infrastructure; ii) procedures for the efficient resolution of problems in insurance companies; iii) effective market discipline; and iv) sound and sustainable macroeconomic policies**.	The Regulatory Environment Section 5 and Annexure 3	There must be an appropriate and effective **legal, tax and accounting framework** within which the securities markets can operate. Securities law and regulation cannot exist in isolation from the other laws and the accounting requirements of a jurisdiction. Effective securities regulation depends upon an appropriate legal framework. The matters to be addressed in the domestic laws of a jurisdiction include: company law; commercial code/contract law; taxation laws; bankruptcy and insolvency laws; competition law; banking law; **dispute resolution system.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Section I **Pre-Conditions (continued)**	Section II	comprehensive and **well-defined accounting principles and rules** that command wide international acceptance; a system of independent audits for companies of significant size so that users of financial statements, including banks, have independent assurance that the accounts provide a true and fair view of the financial position of the company and are prepared according to established accounting principles, with auditors held accountable for their work; effective banking supervision (as outlined in this document); well-defined rules governing, and adequate supervision of, other financial markets and, where appropriate, their participants; and, a secure and efficient payment and clearing system for the settlement of financial transactions where counterparty risks are controlled.	Section 1.3.4 of meth	The public infrastructure may have a profound effect on a jurisdiction's ability to implement the Insurance Core Principles. The legal system is the foundation of the financial system, which ensures the honouring and enforcement of insurance contracts. An adequate infrastructure also requires that **accounting standards be comprehensive, internally consistent and approach international best practices**, so that investors and supervisors can properly evaluate the financial conditions of the insurance companies, and the insurance companies can assess the health of the institutions that they lend to or invest in. The development of insurance products and sound financial management, in particular the calculation of technical provisions (policy liabilities), requires a strong actuarial profession. Accurate financial data requires qualified experts including accountants, auditors and financial analysts. Other key considerations in evaluating the public infrastructure are **the effectiveness of supervision in other financial sectors and markets, as well as the risks inherent in the payment system**.		

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Section II **The supervisory system** **Basic Characteristics** 1. Objectives of supervision	Section I: Intro Page 8	The key **objective of supervision** is to maintain stability and confidence in the financial system, thereby **reducing the risk of loss to depositors** and other creditors.	Section 3 par. 7 and 8 CP1	An **insurance supervisor is expected** primarily - to **protect policyholders** by ensuring that companies comply with the legislation and regulations governing the business of insurance; - to maintain efficient, fair, safe and stable insurance markets for the benefit and protection of policyholders.	Intro 4.1 Page 6 4.2.3	The three core **objectives of securities regulation** are: The **protection of investors**; ensuring that markets are fair, efficient and transparent; the reduction of systemic risk. Although regulators cannot be expected to prevent the financial failure of market intermediaries, regulation should aim to **reduce the risk of failure.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Attributes of supervisory systems • Operational Independence and adequate resources	Part CP 1 CP(1) AC1 EC2	An effective system of banking supervision will **have clear responsibilities and objectives** for each agency involved in the supervision of banking organisations. Each such agency should possess **operational independence and adequate resources**. A **suitable legal framework** for banking supervision is also necessary, including provisions relating to authorisation of banking organisations and their ongoing supervision**; powers** to address compliance with laws as well as safety and soundness concerns; **and legal protection for supervisors.** The supervisory agency sets out objectives, and is subject to regular review of its performance against its responsibilities and objectives through a transparent reporting and assessment process. The supervisory agency and its **staff have credibility based on their professionalism and integrity.**	CP 1 CP 1 EC2	... In particular, the insurance supervisor should: be **operationally independent** and **accountable** in the exercising of its functions and powers; have **adequate powers, legal protection and financial resources** to perform its functions and exercise its powers; …; clearly **define the responsibility** for decision making; and hire, train and maintain **staff with high professional** standards who also follow the appropriate standards of confidentiality. The insurance supervisor is **operationally independent** from both political authorities and the insurance companies that it supervises in the execution of its supervisory tasks and is **accountable in the exercise of its functions and powers**	CP 2 CP 3 CP 5 6.2	The regulator should be **operationally independent** and **accountable** in the exercise of its functions and powers. The regulator should have adequate powers, **proper resources** and the capacity to perform its functions and exercise its powers. The **staff** of the regulator should observe the **highest professional standards** including appropriate standards of confidentiality. The capacity of the regulator to act responsibly, fairly and effectively will be assisted by: a **clear definition of responsibilities**, preferably set out by law; adequate **legal protection for regulators** and their staff acting in the bona fide discharge of their functions and powers.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
					6.3	The regulator should be **operationally independent** from external political or commercial interference in the exercise of its functions and powers and **accountable in the use of its powers and resources**. Independence will be enhanced by a stable source of funding for the regulator. In some jurisdictions particular matters of regulatory policy require consultation with, or even approval by, a government, minister or other authority. The circumstances in which such consultation or approval is required or permitted should be clear and the process sufficiently transparent or subject to review to safeguard its integrity. Generally, it is not appropriate for these circumstances to include decision making on day to day technical matters. Accountability implies: a regulator that operates independently of sectoral interests; a system of public accountability of the regulator; a system permitting judicial review of decisions of the regulator.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Attributes of supervisory systems • Enforcement powers and capabilities within law and judicial system	CP22 CP 2 EC 2	Banking supervisors must have at their disposal **adequate supervisory measures** to **bring about timely corrective action** when banks fail to meet prudential requirements (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the **ability to revoke the banking license or recommend its revocation**. The permissible activities of institutions that are licensed and subject to supervision as banks are clearly defined either by supervisors, or in laws or regulations.	CP1 EC3 CP14 CP2(2)EC14	The insurance supervisor has **adequate powers**, legal protection and proper resources and staff, and the capacity to perform its functions and its powers Insurance supervisors must have the **power to take remedial action** where problems involving licensed companies are identified. The insurance supervisor has **the right to withdraw the licence** on grounds of substantial irregularities eg. if the company no longer meets the licensing requirements or seriously infringes the law in force.	CP3 Section 12.3	The regulator should have **adequate powers**, **proper resources** and the capacity to perform its functions and exercise its powers. The licensing authority should also have the **power to withdraw or suspend the license** or otherwise sanction the licensee whenever the entry criteria are not fulfilled. The regulator should be empowered to **withdraw a licence or authorisation where a change in control** results in a failure to meet relevant requirements.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
3. Clarity and transparency of regulatory process	Part of CP1 CP1(1) AC1	An effective system of banking supervision will have **clear responsibilities and objectives** for each agency involved in the supervision of banking organisations. The supervisory agency sets out objectives, and is subject to regular review of its performance against its responsibilities and objectives through a **transparent reporting and assessment process.**	Part CP 1 CP 1 EC 1 CP1 EC4	Adopt a clear, **transparent and consistent regulatory and supervisory** process. The responsibilities of the insurance supervisor are **clear and objectively stated.** The insurance supervisor adopts a **clear, transparent and consistent regulatory and supervisory process**. The rules and procedures of the insurance supervisor are published and updated regularly.	CP 1 CP 4 6.3 6.5	The responsibilities of the regulator **should be clear and objectively stated.** The regulator **should adopt clear and consistent regulatory processes.** In some jurisdictions particular matters of regulatory policy require consultation with, or even approval by, a government, minister or other authority. The circumstances in which such consultation or approval is required or permitted should be **clear and the process sufficiently transparent** or subject to review to safeguard its integrity. In exercising its powers and discharging its functions, the regulator should adopt processes which are: **consistently applied**; comprehensible; **transparent to the public**; fair and equitable.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
4. External participants in the supervisory process (Conduct of Supervision) • External Auditors	CP 19	Banking supervisors must have a means of **independent validation of supervisory information** either through on-site examinations or use of **external auditors**. **Auditors** have the legal duty to report to the supervisor matters of material significance, for example, failure to maintain the licensing criteria, or breaches of banking or other laws. The law protects auditors from breach of confidentiality when information is communicated in good faith. **Auditors** also have the legal duty to report matters to the supervisor, in situations where they become aware of matters which, in the context of the available information, they believe is likely to be of material significance to the functions of the supervisor.	CP 12c	A process should be established for ensuring that **external audits** of insurance companies operating in the jurisdiction are acceptable.	CP 21-24 12.3	The financial position of the intermediary should be regularly **audited by independent auditors**.
• Other third parties (**other than supervisors**) for supervisory process.	CP 21 AC 3 and 4		CP 1 EC 10	If its own capacities are not sufficient, the insurance supervisor should be able to **outsource to third parties** (e.g. auditors, actuaries) supervisory tasks such as on-site inspections and monitoring in the solvency position or the sufficiency of technical provisions (policy liabilities).	CP 8-10 8.2	Inspections may be carried out by the regulator itself or **another competent authority**. Alternatively, the regulator might consider delegating such authority to SROs or using third parties, properly supervised, to carry out some of this inspection work on its behalf.
• SROs			CP12 EC9	The insurance supervisor requires that information is verified periodically through on-site examinations conducted by himself, **external auditors or other qualified parties**	CP 6	**SROs** The regulatory regime should make appropriate use of Self-Regulatory Organisations **(SROs**) that exercise some direct oversight responsibility for their respective areas of competence, to the extent appropriate to the size and complexity of the markets.
			CP12 EC11	The insurance supervisor has the authority to require insurers to hire, using their own resorces, **independent auditors or actuaries for auditing or reviewing all or specific items of financial statements** whenever the insurance supervisor has doubts as to their accuracy.	CP 7	**SROs** should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
The Supervised Entity 1. Licensing, ownership transfer and corporate control	CP 2	The permissible activities of institutions that are **licensed** and subject to supervision as banks must be clearly defined, and the use of the word "bank" in names should be controlled as far as possible.	Part CP 2	Companies wishing to underwrite insurance in the domestic insurance market should be **licensed**. Where the insurance supervisor has authority to grant a **license**, the supervisor: in granting a **license**, should assess the suitability of owners, directors, and/or senior management, and the soundness of the business plan, which could include pro forma financial statements, a capital plan and projected solvency margins;.	CP 17	The regulatory system should set standards for the **eligibility** and the regulation of those who wish to market or operate **a *collective investment scheme.***
	CP 2 EC3	The use of the word "**bank" and any derivations such as "banking" i**n a name are **limited to licensed and supervised** institutions in all circumstances where the general public otherwise might be misled.			CP 18	The regulatory system should provide for rules governing the **legal form** and **structure** of ***collective investment schemes*** and the segregation and protection of client assets.
					CP 21	Regulation should provide for **minimum entry standards** for ***market intermediaries.***
	Part CP 3	The **licensing** authority must have the right to set criteria and reject applications for establishments that do not meet the standards set. The **licensing process,** at a minimum, should consist of an assessment of the banking organisation's ownership structure, directors and senior management, its operating plan and internal controls, and its projected financial condition, including its capital base;	CP2(1)EC1 CP2(1)EC2	**Legal provisions on licensing** are in place through the insurance law. These legal provisions define the types of company or entity that are insurance companies or entities, and **the insurers which must be licensed** or define insurance business and **prescribe that all of entities writing insurance business must be licensed**	Section 12.3	The **licensing** and supervision of ***market intermediaries*** should set minimum standards for market participants and provide consistency of treatment for all similarly situated intermediaries. The **licensing process** should require a comprehensive assessment of the applicant and all those who are in a position to control or materially influence the applicant.
	CP 4	Banking supervisors must have the authority to review and reject any proposals to **transfer significant ownership or controlling interests** in existing banks to other parties.	CP2(2)EC13	A company licensed to operate life insurance should not also be licensed to operate non-life insurance and vice versa, unless there are clear provisions, which the insurance supervisor finds satisfactory, requiring that risks be handled separately on both a going concern and a winding-up basis.		Changes of control or material influence should be made known to the competent authority in order to ensure that its assessment on the intermediary remains valid.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Licensing, ownership transfer and corporate control (cont'd)			CP 3 CP3 EC2 CP 14 EC1	The insurance supervisor should review **changes in the control** of companies that are **licensed** in the jurisdiction. The insurance supervisor should establish clear requirements to be met when a change in control occurs. These may be the same as, or similar to, the requirements which apply in granting a license. In particular, the insurance supervisor should: require the purchaser or the licensed insurance company to provide notification of the change in control and/or seek approval of the proposed change; and establish criteria to assess the appropriateness of the change, which could include the assessment of the suitability of the new owners as well as any new directors and senior managers, and the soundness of any new business plan. The law defines such changes and permits the insurance supervisor to take into account the substance as well as the form of the transaction. The insurance supervisor has the **authority to refuse or revoke a licence** if the organisational (or group) structure of the applicant or licensee hinders the effective supervision.	CP 25 Section 13.3 Secondary Markets	The establishment ***of new exchanges or trading systems,* requires proper approval.** When direct regulation is appropriate, relevant matters include: Operator competence and operator oversight.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Qualifications	Part of des. of CP3 CP 3 EC5-7	The licensing process, at a minimum, should consist of an assessment of the banking organisation's ownership structure, **directors and senior management**,… This should include determining that appropriate **corporate governance** will be in place. The licensing authority determines **the suitability of major shareholders,** transparency of ownership structure and source of initial capital. A minimum initial capital amount is stipulated for all banks. The licensing authority evaluates proposed **directors and senior management as to expertise and integrity (fit and proper). The** fit and proper criteria include: (1) skills and experience in relevant financial operations commensurate with the intended activities of the bank and (2) no record of criminal activities or adverse regulatory judgements that make a person unfit to uphold important positions in a bank.	Part CP2 CP2(2) EC2 CP3b5 CP 11 EC 1	... the supervisor in granting a licence, should assess **the suitability of owners, directors and/or senior management** Legal provisions exists on whether **key functionaries** such as owners, directors and/or senior managers **are fit and proper (i.e. possessing the necessary knowledge, skills and integrity of their positions).** The insurance supervisor should establish criteria to assess the appropriateness of the change, which could include the assessment of the **suitability of the new owners** as well as any new directors and senior managers, … The insurance supervisor requires that insurance entities (insurers and intermediaries) have key functionaries who are and remain **fit and proper for their roles (i.e. possessing the necessary knowledge, skills and integrity for their positions)**, and has effective means to enforce this. (Market conduct)	CP 17 CP 21 CP21-24 Footnote 44 12.3 12.8	The regulatory system should set **standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.** Regulation should provide for **minimum entry standards** for **market intermediaries.** Many jurisdictions set out detailed criteria relating to education, training, experience and the so called "**fitness and properness"** of an applicant to be met before a person may be licensed. These criteria are intended to protect the investor. Regulation should determine whether participation in the market by an **intermediary** should be based upon a demonstration of **appropriate knowledge, resources, skills and ethical attitude** (including a consideration of past conduct). If an investment adviser also deals on behalf of customers, the capital and other operational **controls applicable to other market intermediaries also should apply to the adviser.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
3. Corporate Governance	Intro CP14 EC1	**Corporate Governance** Supervisors should encourage and pursue market discipline by encouraging good **corporate governance** (through an appropriate structure and set of responsibilities for a bank's board of directors and senior management) and enhancing market transparency and surveillance. Corporate or banking laws identify the **responsibilities of the board of directors** with respect **to corporate governance** principles to ensure that there is effective control over every aspect of risk management.	Part CP 4 CP4 EC1	**Corporate Governance** It is desirable that standards be established in the jurisdiction which deal with **corporate governance**. Where the insurance supervisor has responsibility for setting requirements for corporate governance, the supervisor should set requirements with respect to: the roles and responsibilities of the board of directors. The insurance supervisor has the authority to require boards of directors to clearly set out their responsibilities towards acceptance of and commitment to the **specific corporate governance principles** for their undertaking.	CP 23 12.5	***Market intermediaries*** should be required to comply with **standards for internal organisation** and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters. The details of the appropriate internal organisation of a firm will vary according to the size of the firm, the nature of its business and the risks it undertakes but generally regulation of ***market intermediaries*** should adhere to the following standards: • Integrity and Diligence • Terms of Engagement • Information about Customers • Customer Assets • Market Practice • Operational Controls • Conflicts of Interests • Proprietary Trading

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Ongoing Supervision 1. Group-wide supervision	CP18 CP20 CP23	Banking supervisors must have a means of collecting, reviewing and analysing prudential reports and statistical returns from banks on a solo and **consolidated basis**. An essential element of banking supervision is the ability of the supervisors to **supervise the banking group on a consolidated basis**. Supervisors need to take into account that non-financial activities of a bank or group may pose risks to the bank. Banking supervisors must practise **global consolidated supervision** over their internationally-active banking organisations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organisations worldwide, primarily at their foreign branches, joint ventures and subsidiaries.	CP 12 EC1 Part CP15	The supervisor has the legal authority to require companies to submit information on both a solo and a **consolidated basis,** on their financial condition and performance. Insurance companies are becoming increasingly international in scope, establishing, branches and subsidiaries outside their home jurisdiction and sometimes conducting cross-border business on a services basis only. The insurance supervisor should ensure that **no foreign insurance establishment escapes supervision**.	CP11-13 9.5 12.4	The growing emergence of **financial conglomerates** that combine the activities of firms in different financial sectors and, in some jurisdictions, of financial and non-financial firms has heightened the **need for cooperative efforts to improve the effectiveness of supervisory methods** and approaches. Without proper cooperation between regulators it may be difficult to be aware of all the activities of a group. Such cooperation is particularly important when, as is commonly the case, the **group is active in several jurisdictions**. Risk may result from the activities of **unlicensed and off balance sheet affiliates and** regulation should consider the need for information about the activities of these affiliates.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Monitoring and on-site inspection	CP 16 CP 17 CP18 EC5	An effective banking supervisory system should consist of some form of both **on-site and off-site supervision**. Banking supervisors must have **regular contact** with bank management and thorough understanding of the institution's operations. The supervisor has the **authority to request and receive any relevant information from banks, as well as any of their related companies, irrespective of their activities**, where the supervisor believes that it is material to the financial situation of the bank or the assessment of the risks of the bank.	CP 13 CP 12 EC8 CP12 EC9	The insurance supervisor should be able to: carry out **on-site inspections** to review the business and affairs of the company, including the inspection of books, records, accounts, and other documents. This may be limited to the operation of the company in the jurisdiction or, subject to the agreement of the respective supervisors, include other jurisdictions in which the company operates: and request and receive any information from companies licensed in its jurisdiction, whether this information be specific to a company or be requested of all companies. The supervisor has a framework for **on-going monitoring** of the condition and performance of the companies The insurance supervisor requires that **information is verified periodically through on-site examinations** conducted by himself, external auditors or other qualified parties.	CP 8 CP 10 8.2	The regulator should have comprehensive **inspection,** investigation and surveillance powers. The regulatory system should ensure an effective and credible use of **inspection**, investigation, surveillance and enforcement powers and implementation of an effective compliance program. …consideration needs to be given to the balance between **on-site** inspection and interview and the requirement to provide information from time to time which can be reviewed **off-site.** Also additional details on supervision of ***intermediaries*** (Section 12.7); on the regulation of those who wish to operate a ***collective investment scheme*** (CP 17 and section 11.4); and on the supervision of ***exchanges and trading systems*** (CP26 and section 13.3) (the conduct of business rules and other prudential requirements. Sec 12.5)

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
3. Reporting to supervisors • Periodic information (quantitative and qualitative)) • Powers to require information	CP 18 EC1 EC5	Banking supervisors must have a means of collecting, reviewing and analysing **prudential reports** and statistical returns from banks on a solo and consolidated basis. The supervisor has the legal authority to **require banking organisations to submit information,** on both a solo and consolidated basis, on their financial condition and performance, at regular intervals. These reports provide data on matters such as on- and off-balance sheet assets and liabilities, profit and loss, capital adequacy, liquidity, large exposures, loan loss provisioning, market risk and deposit sources. The supervisor has the authority **to request and receive any relevant information from banks**, as well as any of their related companies, irrespective of their activities, where the supervisor believes that it is material to the financial situation of the bank or the assessment of the risks of the bank.	Part of CP 12 Part of CP13 CP 12 EC1	It is important that insurance supervisors **get the information they need** to properly form an opinion on the financial strength of the operations of each insurance company in their jurisdiction. The information needed to carry out this review and analysis is obtained from financial and statistical reports that are **filed on a regular basis**, supported by information obtained through special information requests, on-site inspections and communication with actuaries and external auditors. A process should be established for setting the **scope and frequency of reports** requested and received from all companies licensed in the jurisdiction, including financial reports, statistical reports, actuarial reports and other information. The insurance supervisor should be able to **request and receive any information from companies** licensed in his jurisdiction, whether this information be specific to a company or be requested of all companies. See On going supervision Par. 1 Group-wide supervision	CP 21-24 12.3 CP 8 and section 8.2 12.7	The capital requirement should be maintained and should be the subject of **periodic reporting** to the regulator or competent SRO. To ensure that continued licensing remains appropriate, there should be a requirement for **periodic updating** of relevant information and a requirement for **reporting** material changes in circumstances affecting the conditions of licensing. The regulator should have the **power to require the provision of information** or to carry out inspections of business operations whenever it believes it necessary to ensure compliance with relevant standards. The suspicion of a breach of law should not be a necessary prerequisite to use of inspection powers in respect of authorised or licensed persons. And additional details in CP 25, 26, 28, 30 and sections 13.3, 13.4,13.9 Powers of Inspection - The right to inspect the books, records and business operations of a market intermediary should be available to a regulator to ensure compliance with all relevant requirements, **even in** the **absence of** a **suspected breach of conduct.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
4. Enforcement • Implementation • Sanctions • Market abuse	CP 22 CP22 EC2	Banking supervisors must have at their disposal adequate supervisory **measures to bring about timely corrective action when banks fail to meet prudential requirements** (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the ability to revoke the banking licence or recommend its revocation. The range of **possible actions** available is broad, including, in addition to the others mentioned, restricting the current activities of the bank, withholding approval of new activities or acquisitions, restricting or suspending payments to shareholders or share repurchases, restricting asset transfers, barring individuals from banking, replacing or restricting the powers of managers, directors, or controlling owners, arranging a take-over by or merger with a healthier institution, and imposing conservatorship.	CP 14 CP 14 EC5	Insurance supervisors must have the **power to take remedial action** where problems involving licensed companies are identified. The supervisor must have a range of actions available in order to **apply appropriate sanctions** to problems encountered. The legislation should set out the **powers available** to the supervisor and may include: the **power to restrict the business activities of a company**, for example, by withholding approval for new activities or acquisitions; the **power to direct a company to stop practices that are unsafe or unsound**, or to take action to remedy an unsafe or unsound business practice; and the **option to invoke other sanctions on a company** or its business operation in the jurisdiction, for example, by revoking the licence of a company or imposing remedial measures where a company violates the insurance laws of the jurisdiction The insurance supervisor ensures that **remedial actions are taken in a timely manner**.	CP8 CP9 CP 10 8.3	The regulator should have comprehensive inspection, **investigation and surveillance powers**. The regulator should have comprehensive **enforcement powers.** The regulatory system should ensure an effective and credible use of inspection, **investigation, surveillance** and **enforcement** powers and **implementation** of an effective compliance program. The regulator or other competent government authority should, therefore, be provided with comprehensive investigatory and **enforcement powers i**ncluding: regulatory and investigative powers to obtain data, information, documents statements and records from persons involved in the relevant conduct or who may have information relevant to the inquiry; power to seek orders and/or to take other action to ensure compliance with these regulatory, administrative and investigation powers; power to impose administrative sanctions and/or to seek orders from courts or tribunals;

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
4. Enforcement (cont'd)			CP1 EC5 (See p 23 Risk management and p 32 Internal Controls)	The decision-making lines of the insurance supervisor are structured so that **action can be taken immediately in the case of an emergency situation**.	CP 28 Related section 12.3 Section 12.7	Regulation should be designed to **detect and deter manipulation** and other unfair ***trading practices.*** The regulation of trading in the ***secondary market*** should **prohibit market manipulation, misleading conduct, insider trading and other fraudulent** or deceptive conduct which may distort the price discovery system, distort prices and unfairly disadvantage investors. (Also see Section IV.1 on Markets.) Regulations should provide for **powers of inspection, powers of investigation and enforcement, discipline and revocation.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
5. Cooperation and information sharing (incl. cross-border supervision) 1. Overall arrangement for information sharing	Part CP1 (6)	Arrangements **for sharing information between supervisors** and protecting the confidentiality of such information should be in place.	CP2	Where the insurance supervisor has authority to grant a license, the supervisor in permitting access to the domestic market, may choose to **rely on the work carried out by an insurance supervisor** in another jurisdiction if the prudential rules of the two jurisdictions are broadly equivalent.	CP 11	The regulator should have authority to **share both public and non-public information with domestic and foreign counterparts**.
	EC 1	There is a system of **cooperation and information sharing between all domestic agencies** with responsibilities for the soundness of the financial system**.**			CP 12	Regulators should establish **information sharing mechanisms** that set out when and how they will share both public and non-public information with their domestic and foreign counterparts.
2. Cooperation in licensing and on-going supervision	EC 2	There is a system of **cooperation and information sharing** with foreign agencies that have supervisory responsibilities for banking operations of material interest to the domestic supervisor**.**	Part CP4	Corporate Governance: **reliance on other supervisors** for companies licensed in another jurisdiction	CP 13	The regulatory system should allow for **assistance to be provided to foreign regulators** who need to make inquiries in the discharge of their functions and exercise of their powers
			CP15	The supervisor should ensure that; **no foreign insurance establishment escapes supervision;** all insurance establishments of international insurance groups and international insurers are subject to effective supervision; the creation of a cross-border insurance establishment is subject to **consultation between host and home supervisors**; and foreign insurers providing insurance cover on a cross-border services basis are subject to effective supervision.		
	Part CP 3	Where the proposed owner or parent organisation is a foreign bank, the prior **consent of its home country** supervisor should be obtained.			Part of 9.5	It is also appropriate to consider the regulator's capacity to **exchange information with other regulators,** for example in the **banking and insurance sectors** at both the domestic and international levels. And additional details in section 9.5, part of CP 27, 28 and sections 13.6 and 13.7.
	CP 24	A key component of consolidated supervision is **establishing contact and information exchange with the various other supervisors involved**, primarily host country supervisory authorities.				
	CP 25	Banking supervisors must require the local operations of foreign banks to be conducted to the same high standards as are required of domestic institutions and must **have powers to share information needed** by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.				

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
5. Cooperation and information sharing (incl. cross-border supervision) (con't)			CP 16	In order to **share relevant information with other insurance supervisors,** adequate and effective communications should be developed and maintained. In developing or implementing a regulatory framework, consideration should be given to whether the insurance supervisor: is able to enter into an **agreement or understanding with any other supervisor both in other jurisdictions and in other sectors of the industry** (i.e. insurance, banking or securities) to share information or otherwise work together; is permitted to share information, or otherwise work together, with an insurance supervisor in another jurisdiction. This may be limited to insurance supervisors who have agreed, and are legally able, to treat the information as confidential; should be informed of findings of investigations where power to investigate fraud, money laundering, and other such activities rests with a body other than the insurance supervisor; and is permitted to set out the types of information and the basis on which information obtained by the supervisor may be shared.		

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
6. Confidentiality 1. In the domestic context 2. In the cross-border context	CP 1 (6) EC 3 CP16 AC 4 CP25 EC 4	Arrangements for sharing information between supervisors and protecting the **confidentiality** of such information should be in place. The supervisor: may **provide confidential information to another financial sector supervisor;** is required to take reasonable steps to ensure that **any confidential information released to another supervisor will be treated as confidential by the receiving party**; is required to take reasonable steps to ensure that any **confidential information released to another supervisor** will be used only for supervisory purposes. The supervisor is legally required to treat as **confidential information received as part of the supervisory process.** However, the supervisor is given powers under the law to disclose information in certain defined circumstances. The law prevents **disclosure of confidential information unless the supervisor is satisfied that it will be held confidential by the recipient,** or unless disclosure is otherwise required by law. **The host country supervisor can share with home country supervisors information about the local operations of foreign banks provided** its **confidentiality is protected**.	CP 17 CP16 EC 2	All insurance supervisors should be subject to professional secrecy constraints in respect of information obtained in the course of their activities, including during the conduct of on-site inspections. The insurance supervisor is required to hold **confidential** any information received from other supervisors, except where constrained by law or in situations where the supervisor who provided the information provides authorisation for its release. Jurisdictions whose confidentiality requirements continue to constrain or prevent the sharing of information for supervisory purposes with insurance supervisors in other jurisdictions, and jurisdictions where information received from another supervisor cannot be kept confidential, are urged to review their requirement. The insurance supervisor is permitted to share confidential information, or otherwise work together, with an insurance supervisor in another jurisdiction. This may be limited to insurance supervisors who have agreed, and are legally able, to treat the information confidential.	CP 7 Part CP12 ref. 9.4 Part CP 12	SROs should be subject to the oversight of the regulator and should observe standards of fairness and **confidentiality** when exercising powers and delegated responsibilities …These arrangements, whether formal or informal, should have several basic characteristics:… safeguards of the **confidentiality** of information transmitted …(and the design of these should also take into account) **confidentiality** and use restrictions under applicable law. Where assistance to another authority is provided through the provision **of confidential information** gathered by the regulator in the exercise of its functions or powers, particular care must be taken to ensure that the information is provided subject to conditions which, to the extent consistent with the purpose of the release, preserve **the confidentiality of that information.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Section III **Prudential Standards** 1. Risk management			Core Principles Par 3.5 Prudential Rules	Insurance companies, by the very nature of their business, are exposed to risk. Insurance companies should meet prudential standards established to limit or **manage the amount of risk that they retain**.	Objectives 4.2.3 CP 21-24 12.4	… **regulation** should aim to **reduce the risk of failure** (including through capital and internal control requirements). Where financial failure nonetheless does occur, **regulation should seek to reduce the impact of that failure,** and, in particular, attempt to **isolate the risk** to the failing institution. Market intermediaries should, therefore, be subject to adequate and ongoing capital and other prudential requirements. Rather, regulators should promote and allow for the **effective management of risk** and ensure that capital and other prudential requirements are sufficient to address appropriate risk taking, allow the absorption of some losses and check excessive risk taking. An efficient and accurate clearing and settlement process that is properly supervised and utilises effective risk management tools is essential. Risk may result from the **activities of unlicensed and off balance sheet affiliates** and **regulation should consider the need for** information about the activities of these affiliates.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Management responsibility	CP13	Banking supervisors must be satisfied that banks have in place a **comprehensive risk management process (including appropriate board and senior management oversight**) to identify, measure and control all other material risks and, when appropriate, to hold capital against these risks.	CP6 EC3 CP4 EC7 CP 5	The insurance supervisor requires **insurers to have in place comprehensive risk management** policies and systems capable of promptly identifying, measuring, reporting and controlling the risks associated with investment activities that might affect the coverage of technical provisions (policy liabilities) and/or solvency margins (capital). The supervisor has the authority to require boards to have in place and monitor **independent risk management functions** related to the type of business undertaken. The insurance supervisor should be able to: … require the board of directors to provide suitable prudential oversight, such as **setting standards for underwriting risks, valuation of technical provisions (policy liabilities) and setting qualitative and quantitative standards for investment and liquidity management** and reinsurance. (EC2)	CP 21-24 Section 12.5 CP 25-30 Section 13.11 clearing and settlement systems	**The management of a *market intermediary*** should bear primary responsibility for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the whole firm. This includes the **proper management of the risks associated with the business of the intermediary**. [fn See Report of IOSCO Technical Committee, July 1994 (35) **Operational and Financial Risk Management Control Mechanisms** for Over-the-Counter Derivatives Activities of Regulated Securities Firms.] There should be **procedures to** identify and **monitor risks on an on-going basis.**

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Management responsibility			Part CP14 EC2	The insurance supervisor has the authority to act **if it determines that the board of directors and senior management of the institution do not understand the underlying risks in their business** or are not committed to, and accountable for, the control environment.	CP 21-24 Section 12.5	**Periodic evaluation** of **risk management processes** within a regulated entity is appropriate. Instances of operational breach can occur despite the existence of internal procedures designed to prevent the relevant misconduct or negligence. It is not practical for the regulator to oversee adherence to those internal procedures on a day to day basis. That is **the responsibility of senior management of the intermediary.** Senior management must ensure that they are able to discharge that responsibility. They must themselves understand the nature of the firm's business, its internal control procedures and its policies on the assumption of risk. They must clearly understand the extent of their own authority and responsibilities.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Assets	CP7	An essential part of any supervisory system is the evaluation of a bank's policies, practices and procedures related to the **granting of loans and making of investments** and the ongoing management of the loan and investment portfolio.	CP 6	Standards should be established with respect to the **assets of companies** licensed to operate in the jurisdiction. Where insurance supervisors have the authority to establish the standards, these should apply at least to an amount of assets equal to the total of the technical provisions, and should address: **Diversification by type; any limits**, or restrictions, on the amount that may be held in financial instruments, property, and receivables; the basis for valuing assets which are included in the financial reports; the safekeeping of assets; appropriate matching of assets and liabilities, and liquidity.		
	CP8	Supervisors must be satisfied that banks establish and adhere to adequate policies, practices and procedures for evaluating the **quality of assets and the adequacy of loan loss provisions and loan loss reserves.**				
	CP10	In order to prevent abuses arising from **connected lending**, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.	CP6 EC3	These **main risks** are: • **market risk** (adverse movements in, for example, stocks, bonds and exchange rates); • **credit risk** (counterparty failure); • **liquidity risk** (inability to unwind a position at any price near fair market value); • **operational risk** (system/ internal control failure); • **legal risk**; and • **safe keeping of assets**		
	CP11	Banking supervisors must be satisfied that banks have adequate policies and procedures for identifying, monitoring and controlling **country risk and transfer risk i**n their international lending and investment activities, and for maintaining appropriate reserves against such risks				
	CP 12	Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor and adequately control **market risks**.	CP5 EC7	The supervisor has the authority to require **controls of safeguarding of assets and investments, including physical control**.		

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk Management • Liabilities			Part CP 7 Part CP 12	**Liabilities** Insurance supervisors should establish standards with respect to the **liabilities** of companies licensed to operate in their jurisdiction. In developing the standards, the insurance supervisor should consider: What is to be included as a **liability** of the company, for example, claims incurred but not paid, claims incurred but not reported, amounts owed to others, amounts owed that are in dispute, premiums received in advance, as well as the provision for policy liabilities or technical provisions that may be set by an actuary; A process should be established for setting the standards for the establishment **of technical provisions or policy and other liabilities to** be included in the financial reports in the jurisdiction		

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Liabilities			Part CP 7 Part CP 10	Re-Insurance The insurance supervisor should consider The amount of **credit allowed** to **reduce liabilities** for amounts recoverable under **reinsurance a**rrangements with a given **reinsurer,** making provision for the ultimate **collectability** Insurance companies **use reinsurance as a means of risk containment.** The insurance supervisor must be able to review reinsurance arrangements, to assess the degree of reliance placed on these arrangements and to determine the appropriateness of such reliance. Insurance companies would be expected to assess the financial positions of their reinsurers in determining an appropriate level of exposure to them. The insurance supervisor should set **requirements with respect to reinsurance contracts or reinsurance** companies addressing: the amount of the credit taken for reinsurance ceded. The amount of credit taken should reflect an assessment of the ultimate **collectability of the reinsurance** recoverables and may take into account the supervisory control over the reinsurer.		

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Off-balance sheet items			Part CP 9	Off-balance sheet items The insurance supervisor should be able to set requirements with respect to the **use of financial instruments that may not form a part of the financial report** of a company licensed in the jurisdiction. In setting these requirements, the insurance supervisor should address: Restrictions in the **use of derivatives and other off-balance sheet items.**		
1. Risk management (cont'd) • Proprietary trading					CP 21-24 Section 12.5	There should be clear policies within the firm covering the circumstances in which **proprietary trading** is permitted. The regulator should obtain information about a regulated firm's own proprietary trading and determine that the firm's net capital is adequate in relation to **the risk associated** with its proprietary trading.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
• Secondary markets					CP 25-30 Section 13.3	The operator should be accountable to the regulator and, when assuming principal, settlement, guarantee or performance risk, must comply with prudential and other requirements designed to **reduce the risk of non-completion of transactions**
1. Risk management (cont'd) • Transparency of Trading					CP 25-30 Section 13.5	Ensuring timely access to information is a key to the regulation of secondary trading. Timely access to relevant information about secondary trading allows investors to better look after their own interests and **reduces the risk of manipulative or other unfair trading practices.** See also IV.1 Market integrity • Transparency

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd)					CP 25-30 Section 13.11 Risk issues in clearing and settlement systems: margining, netting, and short selling and securities lending	There should be procedures to identify and **monitor risks on an on-going basis.** Regulators of the securities market should be interested not only in risk reduction but also in the assumption and shifting of risk amongst participants. It is crucial that the stability, financial health and activities of participants in clearing and settlement systems be monitored in order to **minimise the risk of failure of individual** participants **and overall risk to the systems.** Margin requirements may be used in combination with other mechanisms to manage risk to market participants, clearing houses and exchanges. **Other risk controls may include: circuit breakers**, position limits, price limits, trading halts, capital adequacy, risk management systems, operational standards, lending limitations, insurance coverage, back-up systems and guarantee funds.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
1. Risk management (cont'd) • Collective Investment Schemes					CP 17-20 11.5 and 11.7	The legal form and structure chosen for **collective investment schemes** have implications for the **nature of the risk of** default or breach associated with the scheme. It must be disclosed to investors. The **regulatory system must ensure that these risks to investors are addressed either through statute,** conduct rules or mandatory covenants in the constituent documents of a scheme.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Internal controls	CP14 CP14 EC6	Banking supervisors must determine that banks have in place **internal controls** that are adequate for the nature and scale of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes; safeguarding its assets; and appropriate independent internal or external audit and compliance functions to test adherence to these controls as well as applicable laws and regulations**.** The supervisor has access to the reports of the audit function For further details see CP 14.	CP5 Part CP9 Part CP5 EC8	The supervisor should be able to: review the **internal controls** that the board of directors and management approve and apply, and to request strengthening of the controls where necessary; and require the board of directors to provide suitable prudential oversight, such as setting standards for underwriting risks and setting qualitative and quantitative standards for investment and liquidity management. The insurance supervisor should address: the establishment of adequate **internal controls** and monitoring of derivative positions The insurance supervisor has the authority to require that the insurer has an **ongoing audit** function of a nature and scope appropriate to the nature and scale of business.	CP 18 CP 23	The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and **the segregation and protection of client assets.** Market intermediaries should be required to comply with **standards for internal organisation** and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
3. Risk concentration	CP9 CP5	Banking supervisors must be satisfied that banks have management information systems that enable management to identify **concentrations** within the portfolio and supervisors must set prudential limits to restrict bank exposures to single borrowers or groups of related borrowers. Banking supervisors must have the authority to establish criteria for reviewing **major acquisitions or investments** by a bank and ensuring that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.	Part CP 6 CP 10	Where insurance supervisors have the authority to establish the standards, these should apply at least to an amount of assets equal to the total of the technical provisions, and should address: **Diversification by type; any limits**, or restrictions, on the amount that may be held in financial instruments, property, and receivable Insurance companies **use reinsurance as a means of risk containment.**	CP 25-30 Section 13.7 Large Exposures	The expression "large exposure" refers to an open position that is sufficiently large **to pose a risk to the market or to a clearing firm.** Market authorities should closely monitor large exposures and share information with one another so as to permit appropriate assessment of risk. For market intermediaries the monitoring of "large exposures" is implicit.
4. Capital requirements	CP 6	Banking supervisors must set prudent and appropriate **minimum capital adequacy requirement**s for all banks. Such requirements should reflect the risks that the banks undertake, and must define the components of capital, bearing in mind their ability to absorb losses. At least for **internationally active banks, these requirements must not be less than those established in the Basel Capital Accord** and its amendments.	CP 8	The **requirements regarding the capital** to be maintained by companies which are licensed, or seek a licence, in the jurisdiction should be clearly defined and should address the minimum levels of capital or the levels of deposits that should maintained. Capital adequacy requirements should reflect the size, complexity, and business risks of the company in the jurisdiction.	CP 22 12.4	There should be initial and ongoing **capital and other prudential requirements** for market intermediaries that reflect the risks that the intermediaries undertake. **A capital adequacy test should address the risks faced by securities firms** judged by reference to the nature and amount of the business undertaken by the firm.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
5 Accounting policies and practices	CP 21 EC 5 EC 6 EC 9	Banking supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with **consistent accounting policies and practices** that enable the supervisor to obtain a true and fair view of the financial condition of the bank and the profitability of its business, and that the bank publishes on a regular basis financial statements that fairly reflect its condition The supervisor provides report instructions that **clearly establish the accounting standards** to be used in preparing supervisory reports. Such standards are based on accounting principles and rules that command wide international acceptance and are aimed specifically at banking institutions. The supervisor requires banks to **utilise valuation rules** that are consistent, realistic and prudent, taking account of current values where relevant, and that profits are net of appropriate provisions. The supervisor requires banks to produce annual audited financial statements based on **accounting principles and rules** that command wide international acceptance and have been audited in accordance with internationally accepted auditing practices and standards.	Part of CP 12 CP 12 EC3 CP12 EC4	**Accounting**: A process should be established for setting the **accounting requirements** for the preparation of financial reports in the jurisdiction. The insurance supervisor has the authority to stipulate the principles and **norms regarding accounting** and consolidation techniques to be used for the purposes of reports provided to it for supervisory purposes. The insurance supervisor requires insurance companies to utilise **valuation rules** that are consistent, realistic and prudent**.**	CP 16 and section 10.6 CP 21-24 12.3 12.5	**Accounting and auditing standards** should be of a high and internationally acceptable quality The statements should be characterised by comprehensibility, consistency, relevance, reliability and comparability. Financial statements should also show the results of the stewardship of management or the accountability of management for the resources entrusted to it. **High quality accounting** and auditing standards provide a framework for other disclosure obligations. **Accounting standards** should ensure that fundamental information is available. There should be **comprehensive and well-defined accounting** principles that are of a high and internationally acceptable quality, and provide accurate and relevant information on financial performance.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
Section IV **Markets and Customers** 1. Markets • Market Integrity					CP 26	There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the **integrity of trading** is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.
					CP 30	Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are **fair, effective and efficient and that they reduce systemic risk**
					CP 25	The **establishment of trading** systems including securities exchanges should be subject **to regulatory authorisation and oversight**.
• Financial Crime	CP 15	Banking supervisors must determine that banks have adequate policies, practices and procedures in place**, including strict "know-your-customer**" rules, that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, **by criminal elements**.	CP 16	The supervisor is informed about findings of investigations where the power to investigate fraud, **money laundering,** and other such activities rests with a body other than the insurance supervisor.	CP 8-10 Section 8.5	Securities regulators should consider the sufficiency of domestic legislation to address the risks of **money laundering**. The regulator should also require that market intermediaries have in place policies and procedures designed to minimise the risk of the use of an intermediary's business as a vehicle for **money laundering**. See footnote 18 of IOSCO principles for reference to FATF report.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
• Financial Crime	CP15	…supervisors should encourage the adoption of those recommendations of the Financial Action Task Force on **Money Laundering** (FATF) that apply to financial institutions	CP5 EC 9 CP5 EC 10	The insurance supervisor has the authority to require that insurers have formal procedures to recognise **potential suspicious transactions** The insurance supervisor has the authority to require that insurers have established lines of communication both to management, law enforcement authorities and/or the insurance supervisor for the reporting of **irregular and suspicious** activities.	CP 28 CP 25-30 Section 13.6 Prohibition of manipulation and other unfair trading practices	Regulation should be designed to detect and deter **manipulation** and other **unfair trading practices.** The regulation of trading in the secondary market should prohibit market manipulation, **misleading conduct, insider trading and other fraudulent or deceptive conduct** which may distort the price discovery system, distort prices and unfairly disadvantage investors. Such conduct may be addressed by direct surveillance, inspection, reporting, product design requirements, position limits, settlement price rules or market halts complemented by vigorous enforcement of the law and trading rules.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Customer protection	Intro CP Appendix II	The key objective of supervision is to maintain stability and confidence in the financial system, thereby **reducing the risk of loss to depositors and other creditors** Deposit protection	Background CP 11	The insurance supervisors resolve to cooperate together… to maintain efficient, fair, safe and stable insurance markets for the benefit and **protection of policyholders.** Supervisors should ensure that insurers and intermediaries exercise the necessary knowledge, skills and **integrity in dealings with their customers**. Insurers and intermediaries should: at all times **act honestly** and in a straightforward manner; act with due skill, care and diligence in conducting their business activities; conduct their business and organise their affairs with prudence; pay due regard to the information needs of their customers and treat them fairly; seek from their customers information which might reasonably be expected before giving advice or concluding a contract; avoid conflicts of interest; deal with their regulators in an open and co-operative way; support a system of complaints handling where applicable; and organise and control their affairs effectively.	CP 15 CP 18 CP 19 Objective of securities regulation	**Holders of securities** in a company should be treated in a fair and equitable manner. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of **client assets**. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular **investor** and the value of the **investor's interest** in the scheme. **Investor protection** is a fundamental objective of securities regulation. Therefore, all Principles generally are aimed at achieving this objective

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
2. Customer protection (cont'd)					CP 17-20 11.5 Collective Investment Schemes	**The regulatory system should address the legal form and structure of collective investment** schemes to enable investors to assess their interests and rights and to enable the pool of investors' funds to be distinguished and segregated from the assets of other entities.
					Section 11.7 Client Asset Protection	Regulators should recognise the benefits for **investor protection** and confidence in financial markets of effective mechanisms to protect client assets from the **risk of loss** and the insolvency of investment firms.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
3. Information, disclosure and transparency	Part CP 21	Disclosure, therefore, is a complement to supervision. For this reason, **banks should be required to disclose to the public information** regarding their activities and financial position that is comprehensive and not misleading. This information should be timely and sufficient for market participants to assess the risk inherent in any individual banking organisation.	CP 11 EC4 CP5 EC3	The supervisor sets policy and guidelines with regard to **disclosure to the customer** of relevant, meaningful and understandable information in a timely manner. The information to be disclosed covers the insurer, intermediary, product, risks, benefits, obligations, charges and estimated returns as appropriate The insurance supervisor has the authority to require the board of directors to provide suitable oversight of market conduct activities such as setting standards and monitoring controls on fair treatment of customers; **proper disclosure to customers of policy benefits,** risks and responsibilities; conflicts of interest; handling of clients money; and separation of principal and agent activities.	CP 14 CP 19 CP 20 CP 27 Section 13.5	There should be full, timely and accurate **disclosure** of financial results and other information that is material to investors' decisions. Regulation should require **disclosure**, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme. Regulation should ensure that there is a proper and **disclosed** basis for asset valuation and the pricing and the redemption of units in a collective investment scheme. Regulation should promote **transparency** of trading. Ensuring **timely access to information i**s a key to the regulation of secondary trading.

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
4. Issuers					CP 14 10.4	There should be full**, accurate and timely disclosure** of financial results and other information which is material to **investors**' decisions. **Disclosure rules** should extend to, at least: the conditions applicable to an offering of securities for public sale; the content and distribution of prospectuses or other offering documents (and, where relevant, short form profile or introductory documents); supplementary documents prepared in the offering; advertising in connection with the offering of securities; information about those who have a significant interest in a listed company; information about those who seek control of a company (discussed in greater detail below); information material to the price or value of a listed security;

ISSUE	CP#	BANKING	CP#	INSURANCE	CP#	SECURITIES
4. Issuers					CP14 10.5 CP 16	To safeguard the fair and equitable treatment of shareholders, **regulation should require disclosure** of the security holdings of management and of those persons who hold a substantial beneficial ownership interest in a company. This is generally regarded as information necessary to informed investment decisions in the secondary markets. Accounting and auditing standards should be of a high and internationally acceptable quality.