

'Large fines on banks not working'

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Making senior managers accountable can help check benchmark rigging

The credit crisis of 2008 brought about a sea-change in the manner in which regulators function. In an interview with *BusinessLine*, Tajinder Singh, Deputy Secretary-General, International Organisation of Securities Commissions (IOSCO), provides insights into the manner in which regulations have evolved following the global meltdown and the issues that regulators worldwide are concerned about.

The IOSCO is an international policy forum for securities regulators. The organisation's membership regulates more than 95 per cent of the world's securities markets in over 115 jurisdictions. It works with the G20 and the Financial Stability Board (FSB) on the global regulatory reform agenda.

Edited excerpts from the interview:

You have called for reduction on the reliance on credit rating agencies. Are they being penalised for 2008?

I don't think we are trying to penalise credit rating agencies. We try to avoid mechanical reliance on CRAs. It is not about saying that we should not use CRAs at all but previously there was mechanistic reliance. So, that is already in the rules of either the countries or in the market practices of investors and market participants. If there is a downgrade, there will automatically be a pullout, and so on. So, that is the cliff effect. We try to avoid the cliff effect. CRAs will still have a role, except that the reliance will not be mechanistic.

In your report on credible deterrence, you have stated that potential wrongdoers can be deterred when they know that they cannot hide behind borders because cross-border regulatory counterparts are working together. What are the challenges that you envisage in implementing this?

IOSCO multilateral memorandum of understanding deals with what you are mentioning. If you are a signatory to the MMOU, then any market participant will know that if they commit a cross-border violation, they will not be able to escape. The MMOU is a difficult instrument to sign as the entry requirements are very high. Even bank secrecy cannot come in the way. When there is a genuine case, people know that if a jurisdiction is an MMOU signatory then it will share all the information that is available and will also help in the enforcement. Today, we have 105 MMOU signatories. In effect, you are covering a very large percentage of the capital market — 90 per cent of IOSCO members — and I would say 90-95 per cent of the capital markets know that they are covered.

Should safety nets exist for retail investors directly investing in equities or should they only be allowed to invest in equities through the mutual fund route?

The basic principle about capital markets is that there are risks and there are rewards. At the end of the day, the underlying economic philosophy is that the investor has to do due diligence. The main issue, of course, is suitability and avoiding mis-selling. So, you need suitability and you need an informed investor but safety net is not consistent with this philosophy. Finally, the investor will make the decision, so you need investor education and literacy, fair treatment for investors in terms of what is being sold. There should be assessment of suitability by the market intermediary. But I think safety net goes beyond the overall philosophy of capital markets.

In benchmark rigging, are hefty fines the apt panacea as perpetrators seem to have made themselves mentally prepared for such an eventuality? The attitude is one of 'just pay the fine and one can commit such crime again'...

You are right. In the past there have been very large fines on banks for manipulation of benchmarks/tax evasion, all the other stuff on compliance/money laundering and so on. We get a sense that it might be becoming just another cost of doing business.

Therefore, there is now a new focus on individual accountability and the role of senior managers. We in IOSCO have started a new piece of work on market conduct and there we will be looking at whether we need standards for individual accountability, or whether we need something similar to a senior manager's regime.

How does one justify the trades executed on such rigged benchmarks for trillions of dollars — how should the investors who believed these to be true, traded and lost money be compensated? What should be the approach of supervisors to uphold market integrity?

That is really a matter of national law because different jurisdictions have different laws and the way their jurisprudence behaves is different. Deterrence is the key, along with the emphasis on individual accountability that will probably help. Now, whether individual investors should be compensated or not, is really a matter of local/national law; it is difficult to say globally.

How should this message of choosing the right advisor/right product be spread and what steps should be taken to avoid lip service/re-designating product launches or PR exercises such as investor awareness workshops?

It is about responsibility/ accountability of people selling the products. We have to show that violations will have to be punished. That is why enforcement is the bread and butter of securities regulators worldwide. If people are using investor education campaigns and in the process they are marketing their products, it is not the best thing to do. But the important thing to see is whether there is a violation of suitability requirements. If there is, then punish them very severely.

What is your prescription when there is a conflict between regulators? In India, there was this issue of who will govern Unit-Linked Insurance Plans (ULIPs) — IRDAI or SEBI?

This happened when I was still in SEBI. Regulatory architecture is seeing much more national coordination after the crisis. There are different mechanisms like the FSOC (Financial Stability Oversight Council) in the US or another in the UK where regulators are coming together and consulting each other with participation from Ministries of Finance and Treasuries.

Internationally, we try to coordinate through the joint forum and the FSB. We issued the principles of point of sale (POS) disclosures for securities first and then extended it to banking and insurance entities by working with banking and insurance regulators. So, there is an appetite to harmonise to the extent possible.

Should the level of granularity for margin practices for a central counterparty (CCP) be uniform?

Today the PFMI (Principles for Financial Market Infrastructures) do not talk about specifics in terms of margin practices because they are supposed to be international global principles.

Europe recognises the US in terms of whether you have a one-day gross margin or a two-day net margin because that is the difference.

There is probably a need for PFMI to be more granular. IOSCO is working with the CPMI (Committee on Payments and Market Infrastructures) to look into the practices of different CCPs through surveys on issues, such as stress testing, margin practices, liquidity, collateral, recovery practices and governance.

Based on the study we will conclude whether further granularity is desirable, given that they are global principles.

Tajinder Singh profile

An IAS officer, this IIT Kanpur, IISc Bengaluru alumnus held various leadership positions in the government for close to two decades. Prior to his stint with the IOSCO, Tajinder Singh was Executive Assistant to Chairman, SEBI

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