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## MEGA-REGULATION PROSPECTS ON RUSSIA'S FINANCIAL SERVICES MARKET



**Kotlyarov Maxim Alexandrovich** - Prof., Doctor of Economics, State University of Management, the Deputy Chairman of the Expert Council of the «International markets, trade and economic cooperation» with the Committee on economic policy, innovation and entrepreneurship of the State Duma of the Federal Assembly of the Russian Federation.

In recent months in Russia, the issue of consolidation in a single structure of supervision of financial market participants has been raised again. We remember that the mega-regulator idea was proposed occasionally in the business and research community, but in the mid-2000s a different view on this issue existed. It was about the formation of a separate structure with supervisory functions on the financial market, including those of the Central Bank of Russia. Now the situation has changed radically. Government is elaborating on the consolidation of supervision using the Central Bank of Russia's structure.

In this report, we would like to draw attention to some aspects, which are still important in the light of the formation in Russia of an international financial center.

### *1. Need for a systemic approach in government regulation of the financial market*

Unfortunately, the systemic approach is still lacking in the regulation of the Russian financial market. For example, the previous 2006-2008 Strategy for the Development of the Financial Market in the Russian Federation admitted that in Russia the principle of integrated regulation of the financial market failed, therefore the plan was to switch to a collegial body. Moreover, the action plan included "the transfer to the Federal Service for Financial Markets of the regulation, control, and supervision authority in all sectors of the financial market, including insurance and banking."

As we know, in late 2008 the 2020 Strategy for the Development of the Financial Market was adopted. The very first sentence in the 2020 Strategy is puzzling: "This Strategy identifies priorities for the government in the regulation of the financial market till 2020. But this Strategy does not address the development of the banking and insurance sectors, as well as their regulation, monitoring and supervision." First, this wording is an almost obvious statement of commitment to the principles of the so-called sectoral, and in Russia rather departmental, oversight. The red thread of the Strategy are the thoughts on the increasing complexity of the financial market tools, on the harmonization of regulation, on the cross-border nature of transactions and institutions. Second, discussing the development of the financial market and its regulation while leaving out such sectors as banking and insurance seems strange. Third, the 2020 Strategy reads: "... to standardize approaches to risk management in the financial market based on the basic principles of efficient banking supervision as



formulated by the Basel Committee on Banking Supervision." In other words, the banking supervision methodology is desirable to use (especially to the extent of the application of prudential regulation), but banks are not considered by the Strategy as financial market participants. Third, Chapter 6 of the Strategy 2020 explicitly states: "[...] in the context of formation and development of diversified financial holding, the peculiar problem of their integrated management arises. In these circumstances, tasks of [...] consolidating the related government functions become relevant." There is no expressly stated commitment to mega-regulation ("consolidation of the related government functions") in the 2020 Strategy, and on the whole the problem of a single supervisory and regulatory authority is politely ignored.

In March 2011, the Presidential Decree "On the measures to improve the state regulation of the financial market of the Russian Federation" [3] was issued, according to which the Federal Insurance Supervision Service was consolidated with the Federal Service for Financial Markets. In fact, it was long overdue, though the current 2020 Strategy does not apply to the insurance sector. As noted above, neither does it apply to the banking industry, however, in October 2012, the idea was put forward on the top level of government to consolidate the financial supervision at the Central Bank of Russia or on its platform.

Turning to the Action Plan for building an international financial center in Russia (approved by decree no. 911-r of the Government of the Russian Federation of July 11, 2009), the Regulation of Financial Markets section does not mention the consolidated supervisory authority. Hopefully, efforts of regulatory agencies will gain greater consistency in such a fundamental issue as the regulation of the financial market.

## *2. Central Bank's status and mega-regulator's function*

It is well known that the Central Bank of Russia possesses a special status. More precisely, by its legal nature it is a body of state power. Thus, the transfer of supervision of all financial market participants is the transfer of the function to a body that is formally independent of the other branches of government, which has established specific supervisory procedures that so far apply only to commercial banks. A study should be undertaken of interagency cooperation and coordination, especially in the conceptual development of the financial market and its regulation.

## *3. Introduction of prudential standards in the regulation of the financial market participants*

This is an issue partly arising from the second direction, though it has its own relevance. As a mega-regulator, the Central Bank will naturally begin to apply its traditional approaches to other financial market participants. Systematizing all existing prudential standards, at least five areas can be distinguished:

1. Licensing and granting market access
2. Remote supervision
3. Inspection
4. Working with troubled institutions
5. Liquidation procedures.

We emphasize that the priority is not just expedited transfer of functions to another body; rather it is the formation of clear regulation methodology, especially of a system of prudential standards in the selected areas of activity. In the context of building an international financial center, this problem is even more relevant as the international participants we will bring to our market will definitely want a transparent and uniform system of regulation and clarity in terms of strategic development of a regulatory framework for the financial market.