

**NEW GUIDELINES FOR FINANCIAL MARKET REGULATION:
FROM THEORY TO PRACTICE**

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I would like to speak to you about the problem of regulation in the banking and financial sector. This is a subject that regularly comes back up for discussion, and perhaps too frequently for some. Nevertheless, it should never be forgotten that the regulatory framework conditions heavily influence the development of our business in Switzerland, especially as their repercussions affect the Swiss financial centre's competitiveness in relation to competitors like London, Luxembourg, Singapore and Hong Kong.

With regard to regulation, one of the major events to have marked the year 2005 is indisputably the publication, in September, of a document entitled "Guidelines for Financial Market Regulation". It was drawn up jointly by the Federal Department of Finance, the Swiss Federal Banking Commission and the Federal Office of Private Insurance.

Surprisingly, this publication has gone more or less unnoticed. However, these Guidelines list the Ten Commandments that are to rule the regulatory activities of the above-mentioned authorities. I will not, at this point, enter into the details of the text but will limit myself to summing up its main points.

The first five principles relate to the effects of regulation. Namely,

- safeguarding the competitiveness of the financial centre;
- weighing up the costs and benefits and applying differentiated regulation;
- appraising the impact of regulation on the national economy;
- striving for competitive neutrality in framework conditions and, finally,
- identifying sources of uncertainty, risks and other undesirable effects that could arise.

The last five precepts relate to how the regulation is worked out and recommend:

- examining the need for any new regulation as well as the regulatory framework already in place;
- evaluating available room for manoeuvre from a legal, economic and international point of view as well as any possible regulatory alternatives;
- developing a coherent and transparent regulation in collaboration with the sectors concerned;
- co-ordinating the implementation of regulations in terms of content and timing and
- planning and tracking the measures introduced.

We can but welcome this initiative of our Federal Councillor, Hans-Rudolf Merz, which should help fight the phenomenon of over-regulation which has struck the Swiss banking sector (and which is also a subject of general concern to the profession across the world).

The private bankers particularly welcome the interest in more frequent recourse to cost-benefit analyses which were desperately lacking in the past, as well as the demand for differentiated regulation according to the size and activities of the various players in the financial centre. A stop must be put to the assumption that one size fits all!

We hope that these Guidelines herald a revolution in Switzerland, in the field of regulation. Indeed, if certain past bills were to be analysed according to their criteria, we have to admit that very few would pass the ultimate test.

The draft legislation regarding the implementation of the 40 revised FATF Recommendations on money laundering is a classic example. In view of the general outcry that this text caused in the consultation procedure, the Federal Councillor, Hans-Rudolf Merz had the wisdom to order a pause for reflection for the script to be reviewed in depth.

As a reminder, this bill planned to include insider trading and share price manipulation in the list of predicate offences for money laundering. Furthermore, according to these provisions, several professions and non-financial activities should be subject to the anti-money laundering regulations.

The bill submitted for debate in 2005 could well have compromised the competitiveness of the Swiss financial centre by obliging banks in Switzerland to strengthen further - and before any of their competitors - an already highly developed anti-money laundering set of measures. Moreover, the bill incorporated no serious cost-benefit analysis: only one paragraph out of a 67-page report was devoted to this issue. In addition, there was the fact that the existing arsenal of anti-money laundering measures had not been subjected to any assessment worthy of that name. Finally, the bill was drafted without taking into account the comments made on several occasions by the sectors concerned.

The anti-money laundering dossier will perhaps be the first to which the precepts listed in the Guidelines will be applied in a concrete fashion. It is high time theory be put into practice! Meanwhile, we are waiting to see the contents of the revised and updated bill on the FATF's 40 Recommendations.

At the risk of appearing iconoclastic, I shall not stop my reasoning in midstream. I am convinced that the field of application of the ten principles laid down in the Guidelines must not be limited to state regulation only. It should also be extended to the field of self-regulation. Let me explain.

Within the financial centre, we all too often see self-regulation as a panacea. I'm not sure it is.

Certainly, in fields where one knows the ground, more effective regulation is obtained through self-regulation. For example, in the case of the Swiss Bankers Association's (SBA) Portfolio Management Guidelines.

On the other hand, by wanting to pre-empt state regulation, a profession may set standards that are too restrictive, in fear of being accused of minimalism. The Guidelines aimed at guaranteeing

the independence of financial analysis, published by the SBA in January 2003, are the product of such over-zealousness. The numerous wiles imposed on the banks make this document difficult to implement for small or medium-sized businesses. I am not so sure that these measures would survive should an analysis be undertaken according to the principles of the Guidelines.

Internal surveillance and control also merit our attention. As a reminder, in 2002 the SBA enacted Guidelines for Internal Control. In spring 2005, the Swiss Federal Banking Commission (SFBC) submitted for consultation a draft Circular aimed at regulating this same area. So, one of the principles of the Guidelines should be applied. According to this, the different regulations need to be harmonized and then the decision taken as to which of the aforementioned authorities should be responsible for the regulation.

The same attention to harmonization must prevail regarding stock market supervision, where high-level discussions are currently taking place between the SBA and the SFBC. Once it has been decided who regulates what in this field, the decisions must be adhered to and the necessary done to see that the rules are not scattered among several disparate documents. In reality, how can you expect to work things out if "front running" (advance trading for one's own account based on confidential information from clients' transactions) continues to be admonished by the SBA's Code of Conduct for Securities Traders while, hypothetically, "churning" (another form of reprehensible behaviour consisting of frequent and excessive trading of a client's account) could be targeted by a forthcoming SFBC Circular on market abuse?

In my opinion, the harmonization advocated by the Guidelines must offer a way around the duplication between state regulation and self-regulation. Several measures on the same subject, overlapping at different prescriptive levels, are what sometimes make Swiss banking and securities legislation unworkable. Once it has been decided at which level the regulation is to be enacted, the necessary courage must be found to eliminate all the other texts that, in one way or another, deal with the same subject, be they state products or self-regulatory measures. It is just not reasonable to think that two sets of rules can co-exist without being the subject of conflicting interpretation, causing legal insecurity that is harmful to the smooth running of business.

To conclude, knowing who produces a regulation is less important than making sure that the principles laid down in the Guidelines are scrupulously followed.

The private bankers therefore place a lot of hope in these ten precepts and will follow very attentively their implementation by all those who have a role of regulator, be they from the state or private sectors.

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