

## Remarks for IOSCO Board Meeting

Sydney, 14<sup>th</sup> May 2019

FMSB 2016-21

Good morning ladies and gentlemen.

I'm not sure whether it will be my role as a part-time prudential regulator, or my role as a standard bearer for the private sector that will make me the most suspect person in the room today; but I am honoured to be here and thank you for the opportunity to address you all this morning.

I know we are not here for a philosophical discussion – and I wouldn't normally do this - but I thought I would start by addressing two “existential” questions: first, the reasons why FMSB was created in the first place; and second, some arguments why FMSB might not work as intended. Of course I don't accept any of these “non-believer” arguments, but I think it is important to acknowledge them head-on.

Then I will talk briefly about what we have done these past two and a half years and what we hope to do in the next three.

This should take about 10 minutes and then I would be delighted to take questions.

### **Why was FMSB created?**

I don't need to rehearse for this audience the massive costs of misconduct – both direct and in terms of the loss of trust and social licence for financial services and particularly wholesale market participants.

Nor do I need to dwell on the difficulty of regulating business practices in a global, mobile and highly innovative industry that is in the middle of massive structural upheaval.

These are both powerful reasons for creating a private sector body to overhaul global markets business practices, and either would have justified setting up FMSB.

But there are two other crucial reasons why FMSB exists that need to be called out:

- first, the vision and support of the UK public authorities – particularly the FCA and the Bank of England – who recognised that dramatic change in private sector's sense of responsibility would not be achieved by more, prescriptive,

regulation; and that the pool of markets expertise concentrated in London was a global good that needed to be harnessed; and

- second, the enthusiastic support of the most senior executives of 50 of the largest wholesale markets firms who recognised that they and their firms had to take responsibility for changing the way markets operate, and needed to do so in a co-operative fashion with all other participants.

### **Why might FMSB fail?**

I am a passionate proponent of the private sector standards approach, but I accept that not everyone is yet a convert.

We come across a number of sceptics in our travels. Their reservations, which I am sure are sincerely held, fall into two categories.

Some have *philosophical* objections to what we are attempting.

- they believe that powerful, commercially motivated financial services firms need to be reined in by “black letter” laws and regulation; and that voluntary standards are much less effective – or just ineffective – when compared to formal, legally-supported rules and regulations; or
- they believe that standards need to be created by public sector, as opposed to private sector, bodies to be credible.

Others have *practical* objections to what FMSB is attempting.

- they think that it will be impossible for multiple competing private sector actors to reach consensus, or to create standards that reach across jurisdictional boundaries; or
- they think that it will be impossible to get voluntary standards adopted or to use them for robust enforcement.

I know that in this room that are many supporters of FMSB – and I am very grateful for that - so I don’t want to tilt at windmills; but I genuinely don’t accept either premise.

The philosophical arguments for and against private sector standards, as opposed to regulation, are ultimately a matter of belief and well-intentioned people can disagree with each other. I would just observe that prescribing every acceptable action in legal

terms can risk perverse cultural and business outcomes as much as it can create a sense of control for legislators and regulators.

As to the practical objections, I would add that there is now a growing body of evidence of the successful creation of international and global standards, and of the adoption of these internationally. Enforcement is a matter for others, not FMSB; but in several jurisdictions there are emerging regulatory mechanisms to use FMSB standards; and I hope more appear in due course.

### **What have we done?**

This slide really speaks for itself, but I am pleased that we have:

- Lifted membership from 20 to 50 firms;
- Engaged a very large number of executives across the industry in our work;
- Published in two years 13 standards and statements of good practice on a wide variety of topics; and we have another 6 in progress for publication this year;
- Created an adherence mechanism for standards that seems to be working in its - admittedly early - days;
- Started the necessary outreach to the global regulatory community.

So we now have 50 major firms, representing all interests and up to 80% of activity in the wholesale FICC markets, not only creating high quality standards, but also using them globally in their day to day businesses, and stating publicly each year that they do so. Many of those firms have also used the FMSB BCA work on the historic causes of misconduct to restructure their staff training programmes and compliance surveillance efforts.

In truth, this is rather more than we had expected to get done when we started out. But there is much more to do to make FMSB an institution rather than an initiative.

### **What do we hope to do?**

There is much more to do to complete the current work on uncertainties in specific trading practices, and moving towards an authoritative, integrated and coherent set of standards covering all activities and markets, distributed widely on-line and in whatever social media format best suits our audience.

But I also want to draw your attention to three other priorities that FMSB has agreed for the next 3 years. We will also develop:

- responses to the challenges created by the FICC market structure reforms championed since 2009: in particular screen-based, electronic trading; high frequency trading and centralized market infrastructures (e.g. central clearing counterparties). These changes bring many benefits, but they also create difficulties, some of which have not yet been fully analysed or mitigated: for example the role played by “anonymized” liquidity on trading platforms or the potential frailty of the risk waterfalls used by CCPs. The first part of our work in this area will be on the impact of Artificial Intelligence and data science in wholesale markets. It is known for example that, absent appropriate controls, AI-driven trading engines will invariably tend to optimize their activity in unethical ways and the institutional, as well as systemic, consequences of having markets with mechanical agents that are incentivized to optimize their activity in unethical or highly risky strategies has not - so far - been sufficiently considered;
- ways to measure the impact of new Standards developed by FMSB. How are business practices actually changing in response to new Standards? In what ways are market participants changing their governance, surveillance, control and training programmes; and how do market users experience different outcomes when they are accessing markets to borrow, invest and hedge;
- a series of individual, personal FICC market practice qualifications that could be recognized across institutions and locations (as distinct from today’s firm-based conduct and other training which is only recognized by the firm that delivers it, and then typically only in one location). Developing such a regime is in our view a vital step towards professionalizing the FICC industry and binding individuals, as well as firms, closely into the Standards that FMSB develops.

In each of these three areas we could – as in our core standards setting business – work more closely with IOSCO. I would be interested to hear your views on whether that is an attractive idea.

In due course, if we are successful over the next few years, I hope that FMSB will come to be regarded as a critical, core component of global wholesale FICC market infrastructure, just as trade repositories, payment systems and clearing houses are today: a global asset for markets and their users. But a great deal remains to be completed before this vision can be realized.

Ladies and Gentlemen, thank you very much for your attention. I am very happy to take any questions if we have time and there is the interest.