

MEGAREGULATOR IN THE RUSSIAN FINANCIAL MARKET: PROBLEMS OF FORMATION AND WAYS OF IMPROVEMENT

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ABSTRACT

Actualization of the consolidation of the State Regulatory Authority for Financial Markets is caused by the fact that on 1 September 2013 the Federal Financial Markets Service was abolished in Russia, it was previously responsible for development of the national stock market, and its powers are given to the Central Bank. Thus, a megaregulator of financial markets is based on this institution. The article deals with the specifics of concentration, within one authority, of the powers to regulate the whole domestic financial market against the background of clearly expressed orientation towards the strengthening of the country's vertical of power.

Based on the analytical, monographic, statistical, graphical and logical-comparative methods, the neoclassical state methods of influence on the financial markets were investigated; this resulted in the conclusion that at present they are not able to respond effectively to the contemporary challenges. Thus, the conceptual basis of the high-priority state policy for developing financial markets that can effectively and timely respond to the existing and potential threats in conditions of globalization was formulated.

The objective necessity of rethinking the liberal regulation methods toward centralization is conditioned by the fact that imbalances in one of the financial markets are able to destabilize the condition in all markets, and it can lead to a systemic crisis both in the financial markets and in the real economy.

Keywords: *megaregulator, financial regulation, financial market, integration, financial institution.*

INTRODUCTION

The dominant trend in evolution of the financial regulation is transition to the integrated systems, i.e. megaregulation, in the last 15-20 years. Embodiment of the reform concept for the financial services market infrastructure, in particular, formation of a megaregulator, solves the Russian problems of rapid development of the financial industry, technologies, and increased risk, as far as financial instruments, disintegration and intermediary functions of credit institutions are complicated, and banking products and services are universalized as part of their intersectoral combination.

We have noted that the most domestic studies on improvement of the supervisory process taking into account the financial instruments' multipolarization and tasks of control functions' adaptation to the best practices of the industrially developed countries, have general theoretical character; it was also found there is a deficit of applied tools disclosing some methods of

practical reforming of domestic surveillance based on the existing risks concentrated at the level of the whole financial sector.

Let us try to determine the content of the "megaregulator" definition. In the opinion of A.V. Romashkin, this is a single authority for regulation of financial and credit relations in the markets of securities, bank services and insurance. According to the point of view of V.V. Mandron, a megaregulator means a model of combined or integrated supervision over the financial sector, main type of institutional structure of the financial regulation, which competence includes the market of securities and banking sector and insurance. Zh.G. Golodova complements the above definitions and notes that the concept of an integrated megaregulator includes not only a megaregulator responsible for all aspects of regulation and supervision throughout the financial system, but also agencies that supervise more than one segment of the financial sector.

In our opinion, megaregulator represents institution acting within the cross-sectoral model of the financial markets regulation and supervision, which is designed to regulate the market participants' activities through the preliminary, current and subsequent oversight of financial operations and transactions.

In most cases, a specially formed autonomous authority, in some states - a state bank serves as a megaregulator. Moreover, in recent years a twin peaks model - concept of integral regulation and supervision becomes prevalent; it is based on the functional principle and covers two independent institutes. One of the peaks is responsible for protecting the rights of financial services consumers, while the second one takes over the prudential supervision mission.

Initially, Singapore took the course towards a new institutional paradigm of the financial regulation, when in 1977, along with its functions of prudential regulation in the banking sector, an analogue of the Central Bank - Money and Credit Department was delegated with the supervisory competence in the insurance market and since 1984 - in the stock market as well. After some time, a number of small European states took this experiment on board: Norway (1986), Iceland and Denmark (1988), followed by Sweden (1991). Such large countries like the UK and Germany moved towards the creation of a megaregulator in 1998 and 2002, respectively, afterwards a victorious period of the integrated model began in the financial industry.

A great many note a potential productivity of the megaregulator's model, at the same time, there are opposing points of view supported by the facts. For example, in the United Kingdom, whose experience is most often cited as a good example, in 2012 the process began to separate the megaregulator into two independent regulators that allows to be skeptical of the megaregulation idea.

METHODOLOGY

Contemporary economic scientists and practitioners consider three main approaches to the megaregulator's creation:

1. The evolutionary approach provides a gradual transformation into megaregulation allowing to avoid some imprudent fundamental reforms, and it corresponds to the degree of development of financial relations.
2. The administrative approach requires a "regulator for the regulator", thus, taking into account only the state policy in this area and the needs of financial and credit institutions.
3. The alternative, or service, approach is a modern way of refocusing the state authorities on the interests of certain financial services consumers.

The megaregulator's creation in the Russian Federation is based on a declarative approach, since regulatory documents and statements of V.V. Putin and D.A. Medvedev initiated the beginning of this process in 2012, although since 1999 the process had an evolutionary character and generated the inevitable prerequisites.

By the end of the 20th - beginning of the 21st century, the features of formation and development of the domestic regulatory authorities led to a clearly expressed institutional regulatory model. The financial market was divided between dissimilar regulators virtually unrelated to each other. So, the Central Bank regulated the credit institutions activities; the Federal Commission for the Securities Market (FCSM) - professional securities market participants; the Insurance Supervision Department of the Ministry of Finance - activities of insurance companies; the Inspection of Non-State Pension Funds at the Ministry of Labour and Social Development - non-state pension funds (NPF); the Federal Antimonopoly Service regulated commodity exchanges, etc. Naturally, these agencies were not communicating effectively.

The administrative reform of 2004 reformatted some government departments and divided between them the functions of rights establishment, law enforcement and provision of public services. Accordingly, the federal ministries, services and agencies had to fulfil these functions. The FCSM was transformed into the Federal Service for Financial Markets (FSFM) subordinated to the Government of Russia; the FSFM obtained much of the powers to oversee the NPF, and the Federal Service for Insurance Supervision (FSIS) was established under the Ministry of Finance .

The majority of experts and scientists were convinced that the prolonged debate on formation of a megaregulator stopped when on March 4, 2011 the Decree of the President of the Russian Federation No. 270 was signed, according to which the Federal Service for Insurance Supervision (FSIS) was attached to the FSFM. However, on July 26, 2013 the President endorsed a law, according to which the FSFM powers on control and supervision in the financial markets, legal regulation, including microfinance and insurance activities, activities of rating agencies and investment of pension savings and credit cooperation were devolved to the Bank of Russia. To this end, the Bank of Russia Financial Markets Service (BRFMS) was created, which was subsequently abolished, and since March 3, 2014 its powers were distributed between structural units of the bank.

Modification of the financial markets regulation in Russia became imminent indeed due to several circumstances, the main of which was the need to control some systemic risks.

ANALYSES AND RESULTS

In order to further improve the supervisory process, we have proposed conceptual principles, on which a modern megaregulation model should operate:

- amount of risk that the regulatory authority can allow to any financial market participants to accept should be proportionate to the ability of such participants to resist the accepted risks;
- the regulatory authority must impose more stringent supervisory requirements for "systemic" institutions of the financial market infrastructure;

- legal regulation of all financial market participants should be more flexible, and it should be of "countercyclical" nature. It is necessary to develop a unified approach to various types of financial institutions, thereby reducing the regulatory arbitrage possibilities;

- in conditions of the financial markets globalization, the Bank of Russia should fix the stringent requirements for the imported and exported capital.

Identify three groups of the advantages of integration processes in the financial regulation system:

1) Better distribution of regulatory resources, in particular, through the use of economies of scale.

2) Regulation equality.

3) Compliance with the prudential logic of regulation and elimination of inconsistencies between different regulators .

In order to solve the above problems, each country select the institutional regulation model that would best meet the financial market's development level and structure, as well as the current needs and opportunities in the supervisory area.

Initially, several conceptual options for institutional reorganizations were discussed in Russia: 1) concentration of the supervisory and regulatory powers (except for credit institutions) in the FSFM with increment of budget financing; 2) creation of a specialized Agency for Financial Markets at the Central Bank; 3) delegation of all supervisory and regulatory powers to the Central Bank with joining the FSFM to it.

As a result, the government chose the latter option to implement. It is worth mentioning that the central bank based megaregulation model is not generally accepted. In this connection we identified several reasons:

- the existing central bank's mission, goals and objectives may differ from the reference purpose of the financial regulation. Adequate preventive mechanisms do not respond to any specific and comprehensive management, and immediate resolution of these contradictions can cause non-compliance with the principle of the central bank's independence;

- various political systems oppose to the excessive concentration of powers in a non-elected professional institution as it is extremely difficult to ensure the appropriate level of responsibility and accountability of such institution across the entire spectrum of its functions;

- switch of non-bank financial institutions to the central bank's supervision is able to produce "effects of indulging" (moral hazard): the market may form an opinion that the main bank of the country will, at the same time, play a role of the creditor of last instance for the whole financial sector, rather than only for commercial banks. If the authorities clearly postulate that it is not the case, in fact, commercial banks are in a privileged position, and non-bank financial institutions have an incentive to re-register to gain access to the centralized financing;

- simultaneous performance, within a single authority, of the financial regulation functions of different nature and orientation will inevitably place it before the need to to set priorities. It is believed that this type of problem prevented the UK megaregulator (FSA) to find the optimal balance between the regulation purposes in a case with actual bankruptcy of the bank Northern Rock in 2007;

- in some jurisdictions the transfer of the rights establishment functions to the central bank is impossible or significantly limited, which prevents the key concentration, for effective anti-crisis policy, of all regulatory functions in the financial market in a single authority .

The mentioned problems can be solved with the megaregulator's formation outside the central bank system. In this regard, serious concerns are expressed about the inevitability of an

integrated megaregulator in conditions where the financial markets integration is far from complete, and significant barriers and differences between the types of financial intermediation still exist.

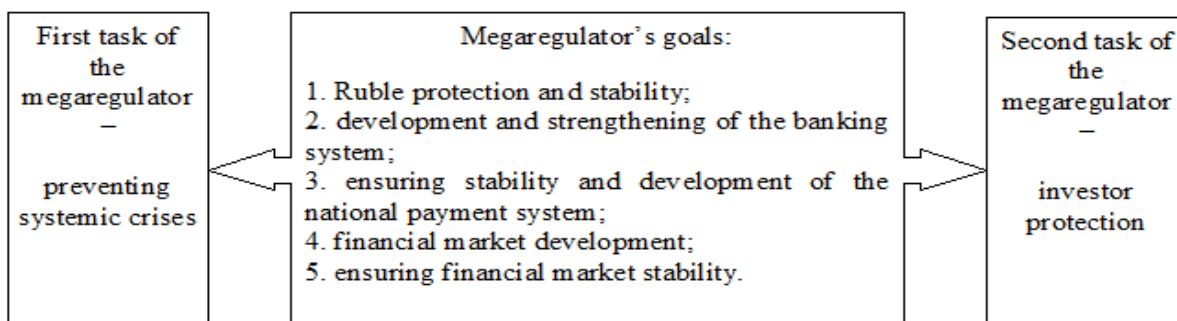
As practice shows, in creating a unified regulator instead of two or more, it is usually difficult to achieve the expected cost savings. In particular, the number of people employed in the supervisory authorities after the reform is not generally reduced. The budget savings, which are formed in the transition to funding of supervision and regulation due to the seigniorage source, are rather illusory.

CONCLUSIONS

Protecting the new institutional regulation paradigm, it should be noted that the concentration of responsibility within the central bank allows to avoid some difficulties of interagency coordination, thief of time and blurring of the separation of powers between the creditor of last instance and supervisory authority, which is critical in the financial instability period.

The theoretical literature describes different sets of megaregulator's goals in the financial market regulation. In this study, we will proceed from the framework of regulation goals and tasks shown in Fig. 1.

Figure 1
MEGAREGULATOR'S GOALS AND TASKS IN RUSSIA



In allotting a task to the central bank to ensure the financial stability, a question arises about the tools to its solution. Application of well-established methods and tools of the monetary and credit policy may lead to contradiction with the chance to achieve other goals (primarily - price stability). In order to articulate the said problem, the macroprudential policy concept was worked out; it is based on the tools of prudential regulation and changes them properly to solve some macroeconomic problems related to the systemic financial risk. The macroprudential policy tools include, for example, requirements to the level of liquidity, restrictions on certain types of financial activities, capital adequacy ratios, taxation of financial transactions, etc. Thus, the relation between different goals of the monetary and credit policy can be established, if the central bank is endowed with the financial regulator's functions, and so, possibilities emerge for adopting the macroprudential policy.

At the same time, however, an open question remains as to whether it is needed to coordinate the macro- and microprudential policy within an institution. The traditional arguments are brought forward against such coordination: moral hazard and excessive bureaucracy. Systemically important financial institutions, to which regulation special attention has been

recently given, can be assumed as an argument in favour of the need for such coordination. Regularity of developments in the post-crisis period leads to the necessity to create a central bank based megaregulator. However, as we have already pointed out, in practice, very few countries have made a transition to this model after 2008. The examples include Ireland, Georgia and Kazakhstan. At the same time, it is noted that the idea of a megaregulator separated from the central bank lost its former popularity.

Thus, transformation of the Central Bank of Russia in a financial megaregulator corresponds generally to the financial regulation logic in the post-crisis conditions and approaches to the monetary and credit policy. The megaregulator should support breathing new life into the project of the Moscow Financial Centre experiencing obvious difficulties despite of its frantic activities.

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