CAU Asia Focus

COUNTRY ANALYSIS UNIT FEDERAL RESERVE BANK OF SAN FRANCISCO MARCH 2010

Regulatory Frameworks for Financial Services in Asia

In the wake of turmoil in global financial markets during the past two years, there has been much discussion about the weaknesses that led to the crisis and how to avoid a similar crisis in the future. Some discussion has focused on financial regulatory architecture, comparing the relative merits of existing structures. Regulatory oversight structures around the world generally employ one of three approaches for supervising financial services industries: 1) a single agency that oversees multiple financial services industries, including banking, insurance and securities; 2) separate agencies for each industry; or 3) a hybrid of these two approaches. The role of a country's central bank varies across these approaches. This *Asia Focus* report serves as a reference for current prudential regulatory regimes overseeing the financial services institutions in several Asian economies, and provides some context for the development of these structures. The scope of this report focuses specifically on prudential supervision and does not include broader issues of ongoing debate such as consumer protection, financial market regulation, and the merits of central banks in supervision.[i]

Asian Models of Financial Regulatory Architecture

Several economies in Asia, including Japan and Singapore, utilize the single-agency approach to supervise financial services industries. Under this approach, a single prudential regulator supervises all banking, insurance and securities institutions. The Japan Financial Services Agency (JFSA) maintains supervision, inspection and monitoring responsibilities for these companies. Likewise, the Monetary Authority of Singapore (MAS) is the sole supervisory agency responsible for Singapore's financial institutions. A key distinction between these two structures is that the MAS also functions as Singapore's central bank, whereas the JFSA is separate from the central bank (Bank of Japan).

Other economies, such as China and India, utilize a separate-agency approach to supervision. Under such a structure, different agencies have authority over companies in different industries – banking, insurance or securities. In China, the China Banking Regulatory Commission (CBRC) supervises banking institutions, while insurance institutions fall under the supervisory purview of the China Insurance Regulatory Commission (CIRC) and securities companies are regulated by the China Securities Regulatory Commission (CSRC). Similarly, India has separate supervisory organizations for financial services industries as follows: the Reserve Bank of India (RBI) oversees banking; the Insurance Regulatory and Development Authority (IRDA) oversees insurance; and the Securities and Exchange Board of India (SEBI) oversees securities. The RBI also functions as India's central bank, but in China, central bank functions are handled by the People's Bank of China (PBOC).

Several hybrid approaches for regulatory oversight in Asia combine different elements of the single-agency and separate-agency formats. For example, Malaysia has a common supervisor for its banking and insurance industries, Bank Negara Malaysia, but a separate agency supervises the securities industry.

Development of Asian Regulatory Structures

<u>Single-Agency Approach</u>

Japan

The JFSA was established in 2000 through the reorganization of the Financial Supervisory Agency. The Financial Supervisory Agency was created in 1998 following a series of large bank failures and growing public dissatisfaction with the Ministry of Finance, which formerly served as Japan's main financial supervisory authority. The JFSA's powers were expanded in 2001 through a merger with the Financial Reconstruction Commission, which held the authority over the disposition of failed financial institutions. On

-site inspections of financial institutions are overseen by the JFSA's Inspection Bureau, while its Supervisory Bureau is responsible for ongoing supervision and for taking administrative action to address the findings of the Inspection Bureau. As previously noted, the JFSA is independent of the Bank of Japan.

South Korea

The Korea Financial Supervisory Service (KFSS) was established in 1999, under the *Act on the Establishment of Financial Supervisory Organizations*, shortly after the 1997-1998 Asian Financial Crisis. The KFSS was created from the combination of four supervisory bodies: 1) Banking Supervisory Authority; 2) Securities Supervisory Board; 3) Insurance Supervisory Board; and, 4) Non-bank Supervisory Authority. Activities of the KFSS are overseen by the Financial Services Commission, which was established during the reorganization of the former Financial Supervisory Commission in 2008. As a result of this reorganization, the Financial Services Commission assumed certain policy responsibilities that were previously held at the former Ministry of Finance and Economy.[ii] The KFSS is outside Korea's central bank, the Bank of Korea.

Taiwan

Following many years of discussion, support for the creation of a single regulator gained momentum in Taiwan when banks were allowed in 2001 to establish financial holding companies. In 2003, the Legislative Yuan passed the *Organic Act for Establishment of the Financial Supervisory Commission, Executive Yuan*, which transferred many of the former duties of Taiwan's Ministry of Finance to a new Cabinet-level commission, the Taiwan Financial Supervisory Commission (TFSC). The TFSC opened in 2004, merging nearly all of Taiwan's financial regulators into one organization. It oversees Taiwan's financial services industries through four bureaus: supervisory responsibility resides in the Banking Bureau, the Securities and Futures Bureau, and the Insurance Bureau, and the Financial Examinations Bureau conducts examinations in coordination with the other three bureaus. Taiwan's central bank is not involved in the primary supervision of financial services.

Singapore

As noted above, Singapore's central bank oversees financial services industries in the country. The *Monetary Authority of Singapore Act* was passed in 1970 and led to the creation of the MAS in 1971, at which time the MAS was granted the responsibility for monetary policy and banking supervision. Over the next decade and a half, as Singapore's financial sector and overall economy expanded significantly, the MAS assumed supervisory authority over other financial services industries; oversight of the insurance industry was transferred to the MAS in 1977, while authority for the securities industry was transferred to the MAS in 1984.

	China	Hong Kong	India	Indonesia	Japan
Central Bank	People's Bank of China	Hong Kong Monetary Authority	Reserve Bank of India	Bank Indonesia	Bank of Japan
Primary Prudential Regulator for Financial Services Industries					
Banking	China Banking Regulatory Commission	Hong Kong Monetary Authority	Reserve Bank of India	Bank Indonesia	Japan Financial Services Agency
Insurance	China Insurance Regulatory Commission	Office of the Commissioner of Insurance	Insurance Regulatory and Development Authority	Directorate of Insurance	Japan Financial Services Agency
Securities	China Securities Regulatory Commission	Securities and Futures Commission	Securities and Exchange Board of India	Indonesian Capital Market and Financial Institutions Supervisory Agency	Japan Financial Services Agency

Separate-Agency Approach

China

China's government embarked on a series of bank reforms in the 1980s and 1990s, and as financial markets in China evolved, so did the country's financial market architecture. Shortly after the 1990 openings of the Shanghai Stock Exchange and the Shenzhen Stock Exchange, the CSRC was created in 1992, marking a significant milestone in the development of China's capital markets. In 1995, the National People's Congress adopted the *Law of the People's Republic of China on Commercial Banks*, which outlined a framework for the prudential supervision with regulatory oversight held by the PBOC. The central bank's supervisory responsibilities over insurance activities were subsequently transferred to the CIRC, which was established in 1998 as a separate entity to supervise and regulate the Chinese insurance market. Similarly, banking regulatory powers were held by the PBOC until the CBRC was created in 2003 to assume the role of the primary regulator for banking supervision.

Hong Kong

The Hong Kong Monetary Authority (HKMA) has had responsibility for banking supervision since its creation in 1993 through the merger of the Office of the Exchange Fund and the Office of the Commissioner of Banking. In contrast with the CBRC in China, the HKMA also carries out several central banking functions. The Office of the Commissioner of Insurance was established in 1990 and currently administers the *Insurance Companies Ordinance*. However, the Hong Kong government is reportedly considering a proposal to create a new insurance authority.[iii] The Securities and Futures Commission, established in 1989 by the *Securities and Futures Commission Ordinance*, oversees the securities industry in Hong Kong.

India

In addition to serving as India's central bank, the RBI has responsibility for banking supervision. Supervisory responsibility for the insurance industry rests with the IRDA, which was established in 1999. Since the creation of the IRDA, India's insurance industry has expanded from two to 42 companies.[iv] Responsibility for supervising the securities industry was assumed by the SEBI in 1992 through *The Securities and Exchange Board of India Act*, enacted during a period of increased private investment in the economy.

Philippines

The Bangko Sentral ng Philippines (BSP) serves as the country's banking supervisor and central bank. The BSP was established in 1993 to replace the Central Bank of the Philippines after the debt crisis of the 1980s. The *Central Bank Act of 2000* governs the operations of banks, quasi-banks and trust entities, and outlines the BSP's responsibility for supervising bank-

Korea	Malaysia	Philippines	Singapore	Taiwan	Thailand
Bank of Korea	Bank Negara Malaysia	Bangko Sentral ng Pilipinas	Monetary Authority of Singapore	Central Bank of the Republic of China (Taiwan)	Bank of Thailand
Korea Financial Supervisory Service	Bank Negara Malaysia	Bangko Sentral ng Pilipinas	Monetary Authority of Singapore	Financial Supervisory Commission	Bank of Thailand
Korea Financial Supervisory Service	Bank Negara Malaysia	Office of the Insurance Commissioner	Monetary Authority of Singapore	Financial Supervisory Commission	Office of the Insurance Commission
Korea Financial Supervisory Service	Securities Commission Malaysia	Securities and Exchange Commission	Monetary Authority of Singapore	Financial Supervisory Commission	Securities and Exchange Commission

ing institutions. The BSP's Monetary Board has the ultimate authority for bank licensing and regulatory oversight. The Supervision and Examination Sector within the BSP is charged with the day-to-day supervision of all banks operating in the country. The *Republic Act No. 275* took effect in 1949 and created the Office of the Insurance Commissioner, responsible for overseeing the insurance industry. The Securities and Exchange Commission was established by the *Securities Act* in 1936, when the local stock market was experiencing rapid growth.

Thailand

In recent years, the regulatory landscape for the banking and insurance industries changed significantly as part of efforts by the Thai government to modernize, strengthen and improve the efficiency of the financial system. In 2007, the *Office of Insurance Commission Act* granted the Office of Insurance Commission supervisory authority for the insurance sector in Thailand. This authority had formerly been under the Commerce Ministry's Department of Insurance. The *Financial Institutions Business Act* of 2008 consolidated banking supervision and enforcement responsibilities with the Bank of Thailand, the country's central bank, increasing the scope of regulatory oversight for banking activities as well as expanding the range of business activities in which financial institutions may engage. Supervisory authority for the securities industry has remained with the Securities and Exchange Commission since its establishment in 1992.

Indonesia

Bank Indonesia, the central bank of Indonesia, maintains responsibility for banking supervision. According to current banking legislation, banking sector oversight will be transferred from Bank Indonesia to a newly created financial services authority, the *Otoritas Jasa Keuangan*, by year-end 2010. However, there has been recent discussion about revising banking legislation, which may delay or derail this transition.[v] The Directorate of Insurance is responsible for insurance industry supervision, while the Indonesian Capital Market and Financial Institutions Supervisory Agency is responsible for securities industry supervision.

Hybrid Approach

Malaysia

Malaysia employs a hybrid approach to the oversight of its financial services industries; supervisory responsibility for the banking and insurance industries is maintained at a single organization, while supervisory responsibility for the securities industry is held at a separate agency. Bank Negara Malaysia was established in 1959 and, at present, retains responsibility for the banking and insurance industries, in addition to serving as a central bank. The securities industry is regulated by the Securities Commission Malaysia, which was established in 1993 under the *Securities Commission Act*.

Conclusion

In light of the recent global financial crisis, many governments are considering changes to existing regulatory structures to address the complex issues arising from growing and increasingly interconnected financial sectors. But even as regulators work toward converging international prudential standards, Asian economies will likely employ differing financial regulatory regimes based upon the characteristics and needs of their respective markets.

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i In addition, this report does not address other issues of ongoing debate that relate to institutions of systemic importance, capital requirements, macro-prudential supervision, and the independence of supervisory bodies.

ii This reorganization was part of a broader organizational reform in which the former Ministry of Finance and Economy and the former Ministry of Planning and Budget were merged into the new Ministry of Strategy and Finance.

iii "Insurance Authority Scheme Pushed," *South China Morning Post*, Enoch Yiu, February 16, 2010 (www.scmp.com)

iv As per the Insurance Regulatory and Development Authority (http://www.irdaindia.org/hist.htm)

v "BI Calls for Revision of Banking Law," The Jakarta Post, Aditya Suharmoko, February 16, 2010 (www.thejakartapost.com)

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