FINANCIAL MARKET COMMISSION OF CHILE

Institutional Arrangements for Financial Sector Authorities: The Case of Chile

COMISIÓN PARA EL MERCADO FINANCIERO

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CMF Chair

October 2019

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Background

- The Chilean financial market previously had a silo supervisory structure:
  - Superintendence of Banks and Financial Institutions (SBIF)
  - Superintendence of Securities and Insurance (SVS)
  - Superintendence of Pension Funds (SP)
- In January 2018 the SVS changed its corporate governance from a "Superintendent" to a "Board" of 5 commissioners (the CMF).
- As of June 1st, 2019; the new General Banking Act provided for the merger of the banks' supervisor with the CMF.
- Currently, 72% of all financial assets are under CMF's supervision.

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The new institutionality: CMF origin

In 2011, the **Desormeaux Commission** commented on the model of financial supervision in Chile:

DIAGNOSIS

- Inability to monitor consolidated risk of financial conglomerates.
- Corporate governance of a single-member authority of the Superintendencies, together with broad powers of supervision and sanction, gives limited guarantees of due process to those affected.
- Reduced capacity to adapt regulation to the challenges imposed by the development of financial markets.
- Limited independence and restrictions to attract and retain qualified personnel.
- By combining different objectives in the same body, some of them are sacrificed.

PROPOSAL

- Adopt a Twin Peaks model or regulation by objectives, grouping supervision and financial regulation tasks into two large areas:
  - ***market conduct supervision***
  - ***prudential supervision***
- This model allows an adequate treatment of financial conglomerates, presents a lower risk of regulatory duplication and arbitration and separates the objectives among which there is a greater risk of conflict.

Risks of the integrated model

- Risk of conflict between the objective of market conduct and the prudential objective. In Chile, under normal conditions, market behavior receives greater attention (reputational risk) from the political world.
- Turner Report to the House of Lords concluded that the British integrated regulator, the FSA, privileged the objective of market conduct at the expense of prudential regulation.
- On the other hand, the focus of certain regulators on solvency leads them to avoid worrying about sectorial competition or the protection of consumers of financial services.

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Principles for designing the organizational structure of the new CMF

- Accountability and clear separation of prudential supervision and the conduct of market participants.
- Integration of common activities: policy proposals and regulations, authorizations, research, statistics and financial analysis.
- Centralization of back office functions (HR, Finance, IT) to pursue cost efficiencies.

Source: IMF

CMF-SBIF Integration

- As of June 1st, 2019; the new General Banking Act provided for the merger of the banks' and the securities and insurance supervisor.
- Objective: To advance in a coordinated, planned and efficient process of legal integration and progressive functional integration.
    - To ensure continuity in the regulatory and supervisory functions, in order to achieve the expected benefits of integration in the medium term..
    - To limit market and the supervisor's personnel uncertainty on the integration process and practical implications.
- Prior integration activities:
    - Request to IMF experts advice for institutional design of the integrated CMF (October 2018)
    - Coordination with SBIF and Integration Governance Structure Steering Committee and Task Force integration (1st Semester 2019)
- Resources for specialized consulting were allocated by the Budget Law.
- It is up to the CMF's Board to define the long-term institutional model and structure.

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CMF-SBIF Integration: Expected benefits

- To extend the advantages of autonomous and collegiate corporate governance to bank supervision and other financial institutions supervised by ex-SBIF.
- To improve on accountability processes towards the market; with a clear legal mandate and assignment of functions within the entity.
- To strengthen the monitoring and supervision of financial conglomerates.
- To generate synergies of specialised knowledge among supervisors.
- To leverage on available resources in order to strengthen supervision.
- To ensure consistency on risk regulation between different supervised entities.
- To extend the benefits of an independent sanctioning process, with reinforced standards on due diligence.

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The new institutionality: CMF mandate and scope of action

Its legal mandate is to ensure the proper functioning, development and stability of the financial market, facilitating the participation of market agents and promoting the care of the public faith

It maintains a general and systemic vision of the market, considering the interests of investors, depositors and insured, as well as the protection of the public interest.

CMF's scope of action

Supervisory Role

- Monitoring and Controling Regulatory Compliance
- Risk-based supervision: Solvency and Market Conduct
- Power to implement preventive measures

Regulatory Role

- Regulatory and interpretive faculty
- Public consultation of new regulations
- Regulatory Impact Reports
- Power to propose legal reforms to the Ministry of Finance

Sanctioning Role

- Independent Research Unit (UI)
- Intrusive powers to investigate. Compensated Collaboration
- CMF Council resolves sanctions after due diligence process

Final remarks

- The financial industry constantly develops and grows, the regulator and supervisor must be up to the challenge by adapting its internal processes to best capture the risks that arises from its supervised entities.

- This is not an easy task, but optimal and efficient financial supervision requires that the regulator and the industry are always in tune.

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ANEXOS

- Assests under CMF's supervisión
- CMF's priorities and main challenges
- Countries with a Single Supervisor, Semi-integrated Supervisory Agencies and Multiples Supervisor in 2002

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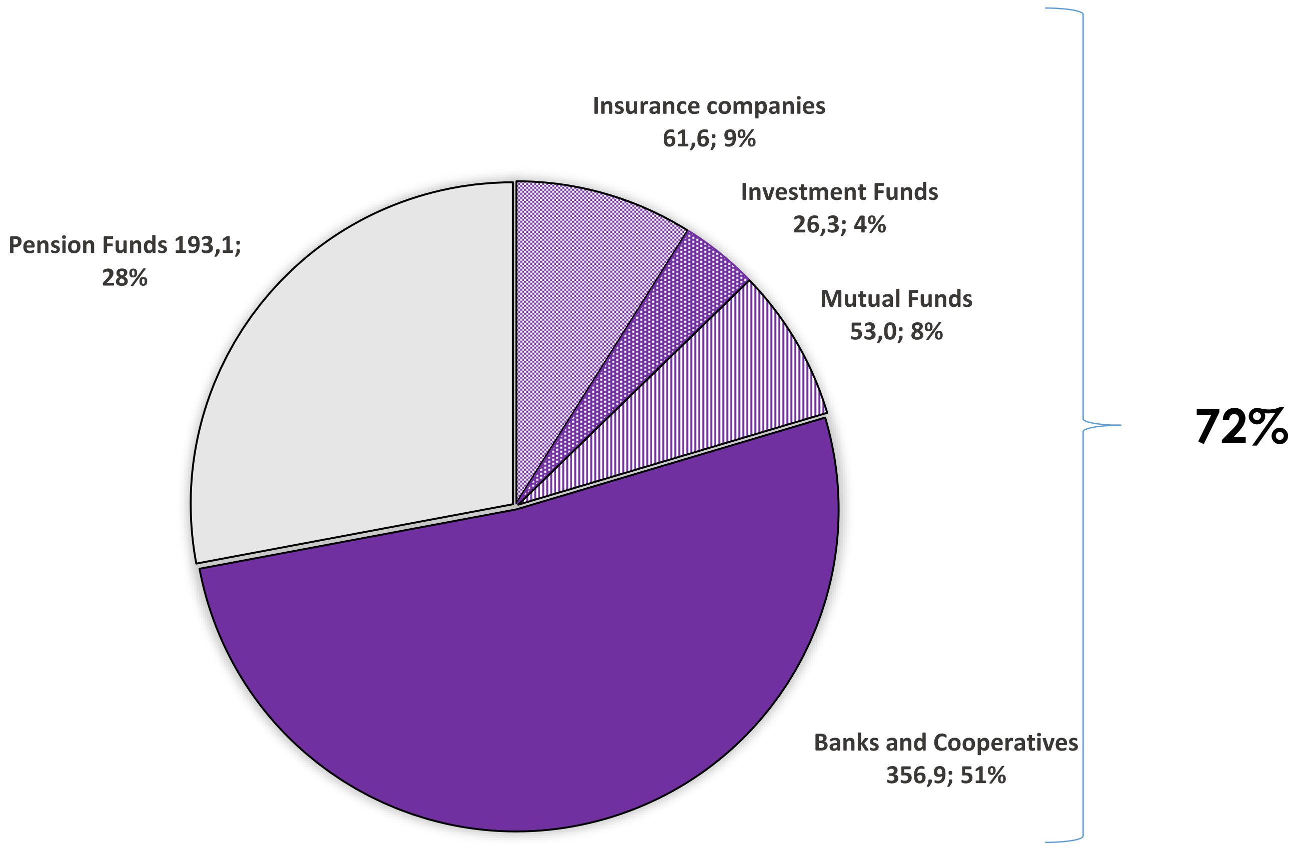
CMF's mandate and scope of action

Asset under CMF's supervisión (USD bn, %)



Priorities and Main Challenges

FINANCIAL STABILITY & SOLVENCY

- Implement Basel III regulation for banks.
- Strength capital and risk management requirements for insurance companies.
- Strength risk management requirements for intermediary securities.
- Strength supervision and regulation on operational risk and cybersecurity.
- Financial conglomerate monitoring.
- Other relevant initiatives: to create a consolidated debtor registry and to review the resolution framework of financial institutions.

MARKET CONDUCT

- Strength market abuse detection and sanctioning tools.
- Strength the efficiency and liquidity of domestic stock markets.
- Strength companies' corporate governance standards.
- Promote transparency in financial products and services’ fees.

MARKET DEVELOPMENT

- Develop mechanisms to facilitate access to financing in the capital market.
- Promote financial inclusion and access to financial products and services.
- Facilitate financial innovation and new business models.
- Promote financial integration and export of financial services (Regional Financial Center).

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Countries with a Single Supervisor, Semi-integrated Supervisory Agencies and Multiples Supervisor in 2002

Single Supervisor for the Financial System		Agency Supervising 2 Types of Fin. Intermediaries			Multiple Supervisors (at least one for Banks, one for securities and one for insurers)	
		Banks and securities firms	Banks and insurers	Securities firms and insurers		
1. Austria	12. Japan	23. Dominican Republic	29. Australia	40. Bolivia	47. Argentina	62. Italy
2. Bahrain	13. Latvia	24.Finland	30. Belgium	41. Chile	48. Bahamas	63. Jordan
3. Bermuda	14. Maldives	25. Luxembourg	31. 29. Australia	42. Egypt	49. Barbados	64. Lithuania
4. Cayman Islands	15. Malta	26. Mexico	30. Belgium	43. Mauritius	50. Botswana	65. Netherlands
5. Denmark	16. Nicaragua	27. Switzerland	31. Canada	44. Slovakia	51. Brazil	66. New Zealand
6. Estonia	17. Norway	28. Uruguay	32. Colombia	45. South Africa	52. Bulgaria	67. Panama
7. Germany	18. Singapore		33. Ecuador	46. Ukraine	53. China	68. Philippines
8. Gilbraltar	19. South Korea		34. El Salvador		54. Cyprus	69. Poland
9. Hungary	20. Sweden		35. Guatemala		55. Egypt	70. Portugal
10. Iceland	21. UAE		36. Kazakhstan		56. France	71. Russia
11. Ireland	22.UK		37. Malaysia		57. Greece	72. Slovenia
			38. Peru		58. Hong Kong	73. Sri Lanka
			39. Venezuela		59. India	74. Spain
					60. Indonesia	75. Thailand
					61. Israel	76. Turkey
						77. USA
As percent of all countries in the sample						
29%		8%	13%	9%	38%	

Source: Quoted in "International Survey of Integrated Financial Sector Supervision"; World Bank Working Paper 3096.
Original source: How Countries Supervise Their Banks, Insurers, and Securities Markets. 2003. London, Freshfields.