

# DEVELOPING ASIA'S FINANCIAL NORMS AND STANDARDS

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The purpose of this paper is to examine the role of financial “infrastructure” institutions and discuss regional norm / standard setting by these institutions and their relations with global financial institutions. The central question is whether these financial “infrastructure” institutions strengthen regionalism in Asia. In the first section, the paper analyses how and why the Asian (especially East Asian) financial norms, standards and institutions have evolved over time, focusing on the role of the Asian financial crisis of 1997-1998 and the global financial crisis of 2007-2009. The second section discusses the limited development of regional financial norms and standards at the traditional international level, in the context of ASEAN, APEC and the Asian Development Bank (ADB). As a separate paper addresses the Chiang Mai Initiative (CMI), Asian Bond Markets Initiative (ABMI) and monetary integration proposals, these are not addressed in detail in this paper. The fourth and fifth sections discuss central bank organisations and regulatory organisations, respectively, addressing their origin, context and factors promoting or hampering their institutionalisation, describing main attributes as well as how they have promoted regional cooperation and integration. The paper concludes a preliminary assessment of the role of financial norms and standards in broader Asian integration, focusing on the way in which initiatives developed at the network level are being incorporated into regional arrangements, including their relationship to the Multilateralised CMI (CMIM) and proposals for an Asian Monetary Fund.

## I. Background and Evolutionary Context

Asian regionalism in the development of financial norms and standards has a limited albeit expanding history. In the initial post-war period, focus was very much on domestic development, with a range of competing models adopted, from central planning and financial allocation to economic laissez-faire, with a range of developmental state models (including administrative direction of financial allocation) gradually emerging as the most successful.<sup>1</sup> In this period, in the context of the Bretton Woods system restrictions on capital movements and domestically oriented financial systems, there was in fact very limited attention paid to these sorts of issues at the international level or even in the context of Europe. We do see however initial developments in Asia, first with the development of the SEANZA forum from the late 1950s, focusing on central bank communication and cooperation in shared training needs. In addition, with the success of post-war Japanese development, Japan begins to increase its profile in international economic and financial organisations, joining the OECD in 1964.<sup>2</sup> At the same time, from the late 1960s, we see initial movements toward increasing Asian voice in international institutions, with SEACEN and the development of the South East Asia voting group in the IMF and World Bank, and the creation of the ADB (1966).

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<sup>1</sup> See Q. Liu, D. Arner & P. Lejot, *Finance in Asia: Institutions, Markets and Regulation* (Routledge, forthcoming 2010)

<sup>2</sup> The only other Asian members are Australia (1971) and Korea (1996).

Following these initial steps, focus across the 1970s continued to be domestic financial development in the region, increasingly modelled on Japanese experience and developmental model (including administrative direction of financial allocation). International cooperation in development of financial norms and standards also remained limited, albeit expanding across the 1970s on a largely informal basis. As a result, there was little need or demand for Asian regionalism in this respect. In the wake of the collapse of the Bretton Woods international monetary system and the return of cross-border finance and currency instability, the 1970s witnessed the initial beginnings of a range of transnational regulatory networks, such as the Basel Committee on Banking Supervision based at the Bank for International Settlements (BIS) in the early 1970s, and the establishment of the Library Group (1974), Group of 6 (G-6, 1975) and Group of 7 (G-7, 1976), all including Japan.

Across the 1980s and 1990s, as capital movements were increasingly liberalised and global finance began to return, international cooperation in development of financial norms and standards increased, largely on the basis of transnational networks.<sup>3</sup> During this period, Asian countries increased participation in related international institutions, largely taking on the consensus supporting financial liberalisation and seeking to learn from Western experience, without any desire or move towards leadership but also recognising increasing value in communication in relation to regional issues with the establishment of EMEAP in 1991. With the Asian financial crisis in 1997-1998 came the first major impetus for Asian regionalism in supporting regional financial stability and regionalising international cooperation and coordination.<sup>4</sup>

Following the Asian financial crisis, in the area of finance, East Asian countries felt the need for alternatives to international mechanisms such as the IMF. In the wake of the Asian financial crisis, cooperation in relation to financial norms and standards through EMEAP, ASEAN/ASEAN+3 and ADB has increased dramatically. At the same time, the regional consensus shifted away from financial liberalisation and towards export led growth and reserve accumulation in the context of monetary and financial stability domestically, regionally and internationally. Efforts during this period focused on bond market development through the ABMI, alternative liquidity arrangements through CMI and initial steps towards regionalisation of international financial norms and standards.

At the international level, following the Asian financial crisis, transnational networks addressing international financial norms and standards were institutionalised through the Financial Stability Forum (FSF), the Group of 20 (G-20, operating at Finance Minister and Central Bank Governor level until 2008) and the IMF / World Bank Financial Sector Assessment Programme (FSAP).<sup>5</sup> It is during this period as well that international institutions such as the BIS and IOSCO began to court Asian participation, in some cases in direct competition with regional institutions such as EMEAP, with the BIS establishing its first regional office (in Hong Kong) in 1998. At the same

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<sup>3</sup> For discussion, see D. Arner, *Financial Stability, Economic Growth and the Role of Law* (Cambridge University Press, 2007).

<sup>4</sup> See D. Arner, P. Lejot & W. Wang, "Assessing East Asian Financial Cooperation and Integration", 12 *Singapore Yearbook of International Law* 1 (2009).

<sup>5</sup> See R. Weber & D. Arner, "Toward a New Design for International Financial Regulation", 29 *University of Pennsylvania Journal of International Law* 391 (2007).

time, East Asia's participation in the FSAP has been more limited than that of other regions,<sup>6</sup> reflecting to some extent a continuing distrust of the IMF and also increasing support for more regionally tailored approaches. Finally, it is during this period that Asia's first international financial norm and standard setting organisation is established, the Islamic Financial Services Board (IFSB) in 2002 (in Kuala Lumpur) and that ASEAN agreed to regional limited liberalisation of financial services (with the development of the financial provisions of the AFAS) and developed the first regional versions of international financial standards (with the ASEAN and Plus Standards Scheme in 2008).

In the wake of the global financial crisis of 2007-2009, new impetus has developed for Asian regionalism in the development of financial norms and standards. At the international level, Asian participation is being courted with the expansion of the G-20 to heads of government meetings (with Korea to host in 2010) and the restructuring of the FSF into the Financial Services Board (FSB), including expansion of membership and governance to parallel the G-20 not only in the FSB but also across the major international financial regulatory organisations (Basel Committee, IOSCO, IAIS, IASB).<sup>7</sup> Within the region, countries are working to establish an Asian FSB equivalent and also looking toward regional arrangements to support monetary and financial stability, such as an Asian currency and/or Asian Monetary Fund.

Today, international financial norm and standard development takes place mainly through the G-20 (agreeing overall policy), the FSB / BIS (coordinating international standard-setting organisations such as the Basel Committee etc), with domestic implementation (supported by the MDBs) and regional implementation in the European Union (and increasingly ASEAN) and monitoring through the FSB and IMF. At the same time, trade in financial services operates in parallel through the WTO as well regionally in the EU and to a more limited extent in ASEAN/APT/APS.

In Asia, the ASEAN/APT/APS Finance Ministers process to some extent plays a policy setting role, with CMI and most recently with ASEAN's adoption of a capital market integration plan in 2009. Regional financial and monetary policy cooperation also takes place through EMEAP and the BIS ACC, with support from the BIS. Standards have largely been taken from the international process, but with increasing moves to develop regionally tailored equivalents both through regional groups of international organisations such as IOSCO and increasingly through ASEAN. At the same time, there are now initial moves to develop an Asian FSB equivalent to coordinate regional cooperation, coordination and standard development. Implementation of international standards is widespread in the region but willingness to participate in international monitoring through the IMF is limited (though likely to increase as a result of G-20 commitments to FSAP participation). Likewise, regional trade in financial services liberalisation is largely WTO-equivalent to date. As a result of the current global financial crisis, there is the potential for regionalism at all levels of financial norm and standard development to increase, not only in the context of ASEAN/APT/APS but also more widely, in order to support financial stability and development.

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<sup>6</sup> Asian FSAPs at present address: Australia (2006), Hong Kong (2003), Japan (2003), Kazakhstan (2004), Korea (2003), Kyrgyz Republic (2003), Mongolia (2008), Pakistan (2004), Singapore (2004), Sri Lanka (2007), Tajikistan (2008), Thailand (2009).

<sup>7</sup> See D. Arner & M. Taylor, "The Global Credit Crisis and the Financial Stability Board: Hardening the Soft Law of International Financial Regulation?", 32 University of New South Wales Law Journal 488 (2009).

## II. Traditional Regional Institutions and Organisations: ASEAN, APEC, ADB

In looking at the main regional international organisations, financial norm and standard development has been limited.

### A. ASEAN

ASEAN finance ministers first met to discuss regional cooperation in 1967.<sup>8</sup> Substantive cooperation was minimal for some years but in 1995 ASEAN's heads of governments declared that it:

shall move towards greater economic integration by building on existing economic cooperation activities, initiating new areas of cooperation, and promoting closer cooperation in international fora.<sup>9</sup>

ASEAN was for long unconcerned with the financial sector but began discussing regional financial matters in the mid-1990s.<sup>10</sup> This was influenced by the 1997-98 financial crisis, a consensual wish to distinguish the region from elsewhere, and a surge in the growth of trade with China and cross-border direct investment to China from ASEAN members.

ASEAN's first venture in financial cooperation was a cooperative framework among national bodies for banking, capital markets, customs, insurance, taxation and related human resources, ironically made immediately prior to the onset of the Asian financial crisis in early 1997.<sup>11</sup> This protocol encourages members to discuss macroeconomic and regulatory policies, improve policy and regulatory transparency, and promote links between the public and private sectors. The agreement was made subject to ASEAN's consensual approach with the proviso that two or more members might engage in the implementation of programmes and projects at their chosen pace rather than be restrained by others.<sup>12</sup> Further, wholly new initiatives must be sanctioned by all members. The intention was rehearsed during the Asian financial crisis in December 1997 when in a forward looking statement ASEAN heads of government undertook to:

promote financial sector liberalization and closer cooperation in money and capital market [sic.], tax, insurance and customs matters as well as closer consultations in macroeconomic and financial policies.<sup>13</sup>

More generally, ASEAN and ASEAN+3 states have been unprepared to relinquish the high degree of national policy control associated with weak or non-existent regional institutions and organizations. Thus the extent of regional integration is consistent with shared norms, whether

<sup>8</sup> Producing the *Ministerial Understanding on ASEAN Cooperation in Finance*, 1 Mar. 1997, online: <<http://www.aseansec.org/1939.htm>>.

<sup>9</sup> *The Bangkok Summit Declaration of 1995*, 15 Dec. 1995, online: <<http://www.aseansec.org/5189.htm>>.

<sup>10</sup> Indeed, no aspect of finance is among ASEAN's 2007 "Priority Sectors for Economic Integration" comprising 12 industrial and service sectors, see ASEAN, *Priority Sectors For Economic Integration* (25 January. 2007), Fact Sheet 2007/AEC/002, online: <[http://www.aseansec.org/Fact Sheet/AEC/2007-AEC-002.pdf](http://www.aseansec.org/Fact%20Sheet/AEC/2007-AEC-002.pdf)>.

<sup>11</sup> *Ministerial Understanding on ASEAN Cooperation in Finance*, 1 Mar. 1997, online: <<http://www.aseansec.org/1939.htm>>.

<sup>12</sup> *Ibid.*, art. 5.

<sup>13</sup> *ASEAN Vision 2020*, 15 Dec. 1997, online: <<http://www.aseansec.org/1814.htm>>.

deliberately adopted as with the consensual ASEAN Way, the making paramount of other aspects of state policy, or indirectly managed as with the participation of commercial and banking interests in governance. The organization of Asian capitalism in the developmental state model has been effective serially in Japan, Korea and China in this respect, characterized by close directional relationships between the state and leading commercial interests.<sup>14</sup> It has been asserted that:

authority structures in the Asia Pacific serve the interests of dominant actors and statebusiness [sic.] coalitions, and that these actors are organized into informal networks of power, that is, particular informal modes of regional governance, serving private as well as public interests.<sup>15</sup>

This institutional involvement of non-state actors in Asian governance is distinct from the more general proposition that international economic activities of all non-state participants may contribute to governance.<sup>16</sup>

The most dramatic result of subsuming regionalism to national policy objectives is seen in the accumulation of international reserves in the region after 2000, partly as a consequence of the primacy of national exchange rate policies over financial integration or regional market development.

## **B. AFTA: Trade in Financial Services**

AFTA began in 1992 as part of a wider ASEAN protocol on economic cooperation,<sup>17</sup> the breadth of language of which makes it doubtful that it constitutes a treaty among its signatories.<sup>18</sup> AFTA's substantive initiating agreement set objectives for removing tariffs and non-tariff barriers,<sup>19</sup> and modifications set the goal of eliminating all import duties by 2015.<sup>20</sup> Similar objectives were adopted within ASEAN+3 so that China-ASEAN and Japan-ASEAN free trade areas are in formation and a Korea-ASEAN free trade area is now largely established.<sup>21</sup>

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<sup>14</sup> See especially G. Redding, *The Spirit of Chinese Capitalism* (W. de Gruyter, 1990).

<sup>15</sup> F. Soderbaum, "Modes of Regional Governance in Africa: Neoliberalism, Sovereignty Boosting, and Shadow Networks", 10 *Global Governance* 419 (2004).

<sup>16</sup> J. Nye & R. Keohane, "Transnational Relations and World Politics: An Introduction", 25:3 *International Organisation* 329 (1971).

<sup>17</sup> AFTA appears in only one of the 15 clauses of the *Framework Agreement on Enhancing ASEAN Economic Cooperation*, 28 Jan. 1992, online: <<http://www.aseansec.org/12374.htm>>.

<sup>18</sup> J. Pelkmans, "ASEAN and APEC, A Triumph of the 'Asian Way'?" in P. Demaret, J. Bellis & G. Jimenez (eds), *Regionalism and Multilateralism after the Uruguay Round: Convergence, Divergence and Interaction* (European Inter-University Press, 1997) at 211.

<sup>19</sup> *Agreement on the Common Effective Preferential Tariff Scheme for the ASEAN Free Trade Area*, 28 January 1992, online: <<http://www.aseansec.org/12375.htm>>.

<sup>20</sup> Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand intend do so by 2010. However, all members may unilaterally retain tariffs on goods they deem sensitive to national interests.

<sup>21</sup> See generally ASEAN Free Trade Areas, online: <http://www.aseansec.org/4920.htm>; see also R. Baldwin, "Multilateralising Regionalism: Spaghetti Bowls as Building Blocs on the Path to Global Free Trade", NBER Working Paper No. 12545 (2006).

ASEAN's 1995 Framework Agreement on Services (AFAS)<sup>22</sup> seeks to reduce barriers to trade in services, requiring members to negotiate to lift restrictions in specific market segments and to some degree expand upon their commitments under the WTO's General Agreement on Trade in Services (GATS). The commitments are not confined to allowing foreign access only to ASEAN members. Overall, ASEAN agreements and AFTA obligations differ little from specific WTO financial sector commitments, from which some are indistinguishable, including those of Brunei, Cambodia and Indonesia,<sup>23</sup> and the additional access granted to foreign interests in most cases is limited. A 2006 assessment of AFAS commissioned by ASEAN and Australia's official Regional Economic Policy Support Facility concluded that its performance was both disappointing and unimpressive.<sup>24</sup>

### C. APEC

Meetings of APEC finance ministers began in 1993, prior to which Japan and the United States resisted its giving attention to economic matters, preferring that economic policy coordination remain the domain of the G-7 industrialized nations and the OECD. APEC involvement in the trade in financial services issues is circumscribed. While APEC was thought an effective forum for economic concerns prior to the 1997-98 crisis, it has been seen since as less successful, and emphasis in governance and resources have shifted to ASEAN+3, the WTO and ASEAN+6.

APEC voiced support for consultations on banking and securities regulation in 1994 and in the same year issued guidelines for regional investment.<sup>25</sup> In 1996 it endorsed regulatory cooperation and prudential regulation of financial markets in accord with international standards. During the 1997-98 crisis, APEC pronounced itself in favour of stable capital flows, domestic financial market development, efforts to promote financial stability, and work to strengthen the regulation of international financial intermediaries and increase cooperation among regulators to lessen global systemic risks.<sup>26</sup> No objection can be made to these pronouncements but APEC's contribution to tangible integration has been negligible due to its lack of institutional authority and political fragmentation. The one exception to this is in the context of the use by the United States of APEC as a means to disseminate U.S. financial and regulatory norms in the region.

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<sup>22</sup> 15 Dec. 1995, art. IV, online: <<http://www.aseansec.org/6628.htm>>. Certain financial sector requirements commitments were strengthened in 2002-03: *Protocol to Amend the ASEAN Financial Services Agreement*, 2 Sep. 2003, online: <[http://www.aseansec.org/AFAS\\_Amendment\\_Protocol.pdf](http://www.aseansec.org/AFAS_Amendment_Protocol.pdf)>.

<sup>23</sup> See respectively GATS/SC/95, GATS/SC/43/Suppl.3, and WT/ACC/KHM/21/Add.2/.

<sup>24</sup> V. Thanh & P. Bartlett, *Ten Years of ASEAN Framework Agreement on Services (AFAS): An Assessment* (2006) at 6, online <<http://www.aseansec.org/16945.htm>>.

<sup>25</sup> See Sixth APEC Ministerial Meeting, Joint Statement, (11-12 Nov. 1994), online: <[http://www.apec.org/apec/ministerial\\_statements/annual\\_ministerial/1994\\_6th\\_apec\\_ministerial.html](http://www.apec.org/apec/ministerial_statements/annual_ministerial/1994_6th_apec_ministerial.html)>. APEC's Non-binding Investment Principles issued in 1994 are not only non-binding but insubstantive, *ibid*. On capital mobility, the document states only that "Member economies accept that regulatory and institutional barriers to the outflow of investment will be minimized" but at the same time foreign and domestic investors shall be treated alike subject to "exceptions as provided for in domestic laws, regulations and policies." *Ibid*. There is no more recent or specific APEC examination of cross-border investment.

<sup>26</sup> By the Basel Committee on Banking Supervision, the International Organization of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS).

### **III. Central Bank Organisations**

At the international level, the primary international central bank organisations are the IMF, BIS and the various Gs. Prior to the 1990s, these organisations had limited Asian representation and participation. While this changed in the 1990s, so did attitudes within the region to the IMF especially. Although the IMF has been relatively less successful in providing support for regional central bank communication and cooperation, Asia has developed other organisations such as SEANZA, SEACEN and EMEAP. At least partially in response, the BIS has been working to increase its role in supporting its Asian membership, following its increase during the 1990s and increasingly plays a significant supporting role for EMEAP and regional central bank cooperation, as well as in relation to regulatory cooperation and standard-setting – the subject of Section IV below.

#### **A. SEANZA: Central Banks of South East Asia, New Zealand and Australia**

SEANZA grew out of a 1956 meeting of central bank governors from the British Commonwealth countries in the Asia Pacific region, in which the governors agreed they should pool resources to provide training courses for staff. There are now 19 members. The original members were the central banks of Australia, New Zealand, Pakistan and Sri Lanka. In addition to the original four, the central banks of the a range of Asian economies also now participate.<sup>27</sup>

The main functions of SEANZA are: (1) provision of a biennial central bank training course, (2) provision of a forum for central bank governors, and (3) provision of a forum for banking supervisors. The first central banking course was held in Australia in 1956 and was scheduled to take place every two years on a rotating basis. The SEANZA Forum of Banking Supervisors was established in 1984 as a forum for banking supervisors from the region. Today, SEANZA organises events primarily with the Financial Stability Institute (FSI).

SEANZA provides a parallel training forum to SEACEN and EMEAP, coordinating especially with the FSI at the global level, although it largely functions as a mailing list to access the membership (which is not entirely identical to SEACEN).

#### **B. SEACEN: South East Asian Central Banks**

SEACEN was established 1966, with its first meeting in Thailand at the Bank of Thailand, with representatives from the central banks of Laos, Malaysia, Philippines, Singapore, Sri Lanka, Thailand, and Vietnam. The initial meeting was targeted at the establishment of a South East Asian voting group in the IMF, World Bank and ADB.<sup>28</sup> In 1972, following initial discussions at the 2<sup>nd</sup> Governors' Conference in 1967, at the 7<sup>th</sup> SEACEN Governors' Conference, an informal SEACEN Centre was established. In 1982, governors agreed to establish the SEACEN Research and Training Centre in Kuala Lumpur, with an agreement signed in Bangkok and involving Bank

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<sup>27</sup> As of 2009: Bangladesh, China, Hong Kong, Indonesia, Iran, Japan, Korea, Malaysia, Macao, Mongolia, Nepal, Papua New Guinea, Philippines, Singapore, and Thailand.

<sup>28</sup> The relevant IMF Executive Director represents the following: Brunei, Cambodia, Fiji, Indonesia, Laos, Malaysia, Myanmar, Nepal, Philippines, Singapore, Thailand, Tonga, and Vietnam. Japan and China are represented by individual Executive Directors. The majority of other Pacific IMF members are grouped together: Australia, Kiribati, Marshall Islands, Micronesia, New Zealand, Palau, Papua New Guinea, Samoa, Seychelles, Solomon Islands, and Vanuatu. Korea and Mongolia are also included in this group. Bangladesh, Bhutan, India and Sri Lanka are represented by a single Executive Director.

Indonesia, Bank Negara Malaysia, Central Bank of Myanmar, Nepal Rastra Bank, Bangko Sentral ng Pilipinas, Monetary Authority of Singapore, Central Bank of Sri Lanka, and Bank of Thailand.

## **1. Structure and Organisation**

There are now 16 members<sup>29</sup> and 2 observers.<sup>30</sup> In addition, staff from a wide range of central banks in the region are “Invitees for Training”.<sup>31</sup>

The SEACEN Centre was established as a company limited by guarantee without a share capital under the Companies Act of Malaysia in 1982 and today has around 35 staff. Since 2008, governance consists of three bodies: the SEACEN Board of Governors as the highest policy-making body, the SEACEN Executive Committee as a supervisory body, and the SEACEN Board of Directors to ensure compliance with Malaysian law. The Executive Director is appointed by the Board of Governors for a three year term, supported by two Directors appointed by the Executive Committee on three year terms. Staff are either permanent or contract, from SEACEN member countries and in some cases are seconded from member banks.

As the policy-making body, the Board of Governors meets once a year, with member banks hosting on a rotating basis, and is responsible for: (1) appointment of the Executive Director; (2) ratification of the budget and programme of activities; (3) admission of new members and observers; and (4) any other matters of strategic importance. The Executive Council oversees SEACEN Centre operations and is comprised of the deputy governors of all the member banks and meets at least once per year. It is responsible for: (1) advising the Board of Governors on policy matters; (2) approving the funding for the Centre's annual budget; (3) approving the Centre's proposed research and training programme; (4) formulating and approving staff rules and regulations, financial procedures and other management policy matters; (5) recommending to the Board of Governors new members and observers; (6) approving arrangements with other central banks or monetary authorities or specialised regional or international organisations, fora or agencies; (7) recommending to the Board of Governors the appointment of the Executive Director and approving the appointment of the Directors; and (8) exercising all powers for management and administration delegated by the Board of Governors.

## **2. Functions and Activities**

Pursuant to the SEACEN Centre agreement, the objectives of the SEACEN centre are to: (1) promote better understanding of financial, monetary and banking and economic development matters of interest to the central banks and monetary authorities of the countries in South East Asia or of interest to the region as a whole; and (2) stimulate and facilitate cooperation among

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<sup>29</sup> The members are: Bank Indonesia, Bank Negara Malaysia, Central Bank of Myanmar, Nepal Rastra Bank, Bangko Sentral ng Pilipinas, Monetary Authority of Singapore, Central Bank of Sri Lanka, Bank of Thailand, Bank of Korea (1990), Central Bank of the Republic of China (Taiwan) (1992), Bank of Mongolia (1999), Ministry of Finance, Brunei Darussalam (2003), Reserve Bank of Fiji (2004), Bank of Papua New Guinea (2005), National Bank of Cambodia (2006), State Bank of Vietnam (2006).

<sup>30</sup> Bank of the Lao, PDR and the National Reserve Bank of Tonga are currently observers.

<sup>31</sup> These are: Central Bank of Afghanistan, Reserve Bank of Australia, Bangladesh Bank, Royal Monetary Authority of Bhutan, People's Bank of China, Hong Kong Monetary Authority, Reserve Bank of India, Central Bank of the Islamic Republic of Iran, Bank of Japan, Monetary Authority of Macao, Maldives Monetary Authority, Reserve Bank of New Zealand, State Bank of Pakistan, Central Bank of Samoa, Central Bank of the Solomon Islands, Banking of Payment Agency Timor-Leste, and Reserve Bank of Vanuatu.



central banks and monetary authorities in the area of research and training. To achieve these objectives, the SEACEN Centre is mandated to: (1) undertake research into the fields of financial, monetary, banking and economic development matters; (2) organise and conduct training courses; (3) collect, publish and distribute results of research and studies and other information related to its objectives; (4) arrange and organise seminars, workshops and conferences; (5) provide advisory and technical services to the South East Asian central banks; (6) cooperate with other institutions to promote its objectives; and (7) undertake other activities in furtherance of its objectives.

Since 2001, training has become the principal activity of the SEACEN Centre, with research playing a supporting function.

### **3. Coordination and Impact**

Overall, SEACEN's role is now focused on the training of mid-level central bank officials from across Asia-Pacific. In this context, it is generally seen as useful and effective. From the standpoint of regionalism, such a role is useful not only in enhancing human capital development and knowledge exchange but, from a longer term perspective, useful in introducing officials from around the region to one another, exposing them to common problems and approaches and building regional networks, which become more valuable as officials rise in seniority in their home institutions.

### **C. EMEAP: Executives' Meeting of East Asia Pacific Central Banks**

EMEAP was established 1991 as a cooperative organisation of central banks and monetary authorities in the East Asia and Pacific Region, with the primary objective of strengthening the cooperative relationship among its members.

#### **1. Structure and Organisation**

There are currently 11 member central banks from the region.<sup>32</sup> EMEAP does not have a secretariat. Instead, the member hosting the next Governors' Meeting is responsible for arrangements. Initially, meetings between central bank executives (typically at deputy governor level) were held twice per year. In 1996, members decided to enhance the structure, with the first EMEAP Governors' Meeting held in Tokyo. At that meeting, the group agreed to hold Governors' Meetings on an annual basis (with a rotating host) and also to create two standing Working Groups (the Financial Market Development Working Group and the Central Banking Operations Working Group) and one standing study group (the Banking Supervision Study Group). In 2007, members established a new Monetary and Financial Stability Committee (MFSC), comprising relevant deputies, and a three level structure: (1) Governors' Meeting; (2) Deputies' Meetings and the MFSC; and (3) the Working Groups (including the Banking Supervision Study Group which has been upgraded to a Working Group), to which has been added the IT Directors' Meeting.

#### **2. Functions and Activities**

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<sup>32</sup> Reserve Bank of Australia, People's Bank of China, Hong Kong Monetary Authority, Bank Indonesia, Bank of Japan, Bank of Korea, Bank Negara Malaysia, Reserve Bank of New Zealand, Bangko Sentral ng Pilipinas, Monetary Authority of Singapore, and Bank of Thailand.

The central function of EMEAP is to strengthen cooperation between its members, focusing on key issues of concern, as expressed in its various meeting structures (monetary and financial stability, financial market development, central bank operations, banking supervision, IT).

Governors' Meetings support exchange among members and provides the highest decision-making level of the organisation. Governors' Meetings are responsible for policy decisions, with working groups reporting to the Governors' Meeting. Deputies' Meetings, held twice per year, are the core forum of the organisation. The MFSC is tasked to enhance the macro-monitoring and crisis management mechanisms of EMEAP, with meetings usually held back-to-back with Deputies' Meetings. The Working Group on Payment Systems addresses the domestic and cross-border payment and settlement systems, including publishing a comprehensive survey.<sup>33</sup> The Working Group on Financial Markets addresses central bank services and the development of foreign exchange, money and bond markets, playing a central role in the ABF Initiative. The Working Group on Banking Supervision addresses banking supervision issues and now includes supervisory agencies to the extent that banking supervision has been separated from the central bank in some EMEAP members, e.g. China). The IT Directors' Meeting discusses IT and its application in member central banks.

EMEAP's highest profile activity has been the Asian Bond Fund (ABF) Initiative, with the first stage launched in 2003, the second stage launched in 2004 and future directions currently under discussion. In addition to EMEAP, the ABF also involves the Reserve Bank of India – thus paralleling the BIS ACC – with support coming from the BIS Asia Office). In addition, it now coorganises meetings with the European Central Bank (EMEAP-Eurosystem High Level Seminars<sup>34</sup>, to increase communication and deepen relations between EMEAP and the Eurosystem), with meetings held annually since 2004, and also coordinates training programmes with the FSI and others.

### **3. Coordination and Impact**

EMEAP plays a significant role in central bank coordination and cooperation amongst its membership and works closely with ASEAN/APT/APS, ADB, BIS (especially the BIS ACC and Asian Office) and international standard setters. As a result of shared crisis experiences, the effectiveness and impact of the group has grown, with regional initiatives such as the ABF and support for CMI.

#### **D. BIS: Bank for International Settlements**

Established 1930 and headquartered in Basel, Switzerland, the BIS is the international organisation of central banks. In 1998, the BIS established its first representative office, the Representative Office for Asia and the Pacific (Asian Office) in Hong Kong.

There are currently 12 Asian members of the BIS.<sup>35</sup> In 2001, the BIS established the BIS Asian Consultative Council (ACC), comprising the 12 Asian BIS member central banks, with the BIS

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<sup>33</sup> EMEAP, Payment Systems in EMEAP Economies (Jul. 2002) ("Red Book").

<sup>34</sup> The Eurosystem comprises the European Central Bank and the national central banks of the euro area.

<sup>35</sup> Namely: the central banks of: Australia, China, Hong Kong, India, Indonesia, Japan, Korea, Malaysia, New Zealand, Philippines, Singapore, and Thailand.

Asian Office providing the Secretariat for the ACC. The BIS ACC is thus EMEAP plus India and parallels the largest and/or most developed members of ASEAN/APT/APS. While EMEAP operates separately, it also works closely with the BIS through the Asian Office and the ACC, with the Asian Office increasingly focusing on the needs of the ACC, including providing support for regional initiatives such as the ABF.

## **E. Other Organisations**

The **Four Markets Group**, established in 1992, brings together senior officials from finance ministries and central banks, usually at the deputy level, from Australia, Hong Kong, Japan and Singapore.

## **IV. Regulatory Agency Organisations**

The main international regulatory organisation is the FSB, formed as the FSF in the wake of the Asian financial crisis and reconstituted in 2009. The FSB brings together G-20 finance ministries, central banks and/or regulatory authorities, along with the main international and regional financial institutions (BIS, IMF, World Bank, OECD, ECB, European Commission) and international standard-setting bodies (Basel Committee, IOSCO, IAIS, IASB, Committee on the Global Financial System (CGFS), Committee on Payment and Settlement Systems (CPSS)).

### **A. Financial Stability Board**

The FSB Secretariat is hosted by the BIS in Basel, Switzerland. As a result of its recent reconstitution, a variety of Asian agencies from 8 Asian economies are now represented: Reserve Bank of Australia and the Treasury (Australia), People's Bank of China, China Banking Regulatory Commission, Ministry of Finance (China), Hong Kong Monetary Authority, Reserve Bank of India, Securities and Exchange Board of India, Ministry of Finance (India), Bank Indonesia, Bank of Japan, Financial Services Agency, Ministry of Finance (Japan), Bank of Korea, Financial Services Commission (Korea), and Monetary Authority of Singapore.

### **B. Basel Committee on Banking Supervision**

The Basel Committee is the primary international standard setting in the area of banking. Until 2009, the Basel Committee comprised G-10 banking supervisors. Following G-20 directions, it has now expanded its membership to encompass the G-20. Asian members thus include the banking regulators of: Australia, China, Hong Kong, India, Indonesia, Japan, Korea, and Singapore.

The Basel Committee and the BIS jointly organised the Financial Stability Institute (FSI) in 1999. The objectives of the FSI are to: (1) promote sound supervisory standards and practices globally, and to support full implementation of these standards in all countries; (2) provide supervisors with the latest information on market products, practices and techniques to help them adapt to rapid innovations in the financial sector; (3) help supervisors develop solutions to their multiple challenges by sharing experiences in seminars, discussion forums and conferences, and (4) assist supervisors in employing the practices and tools that will allow them to meet everyday demands and tackle more ambitious goals.

Today, the FSI coorganises training events frequently with SEANZA, SEACEN and EMEAP.

### **C. Committee on Payment and Settlement Systems and Committee on the Global Financial System**

Unlike other international regulatory organisations, the membership of the CPSS and CGFS have not (yet) been expanded to encompass G-20 representatives. At present, the Asian members of the CPSS are: Hong Kong Monetary Authority, Bank of Japan, and Monetary Authority of Singapore. At present, only Japan is a member of the CGFS.

### **D. IOSCO: International Organisation of Securities Commissions**

IOSCO is the primary international financial standard-setting organisation in the area of securities regulation. Unlike the Basel Committee, its membership prior to the global financial crisis of 2007-2009 was open, with wide Asian participation.

Today, the 23 Asian securities regulators are IOSCO Ordinary members.<sup>36</sup> In addition, 6 Asian agencies are Associate (non-voting) members.<sup>37</sup> Finally, there are two Asian Affiliate members, the Australian Securities Exchange and ADB.

#### **1. Asia-Pacific Regional Committee**

In the wake of the Asian financial crisis, IOSCO was active in organising a variety of regional committees. The Asia-Pacific Regional Committee comprises securities regulators from 21 Asian jurisdictions.<sup>38</sup>

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<sup>36</sup> Australian Securities and Investments Commission, Bangladesh Securities and Exchange Commission, Brunei International Financial Center of the Ministry of Finance, China Securities Regulatory Commission, Hong Kong Securities and Futures Commission, Securities and Exchange Board of India, Indonesian Capital Market and Financial Institutions Supervisory Agency, Financial Services Agency (Japan), Financial Supervision Agency (Kazakhstan), Financial Services Commission / Financial Supervisory Service (Korea), State Agency for Financial Surveillance and Accounting (Kyrgyzstan), Malaysia Securities Commission, Financial Regulatory Commission (Mongolia), New Zealand Securities Commission, Securities and Exchange Commission (Pakistan), Papua New Guinea Securities Commission, Philippines Securities and Exchange Commission, Monetary Authority of Singapore, Sri Lanka Securities and Exchange Commission, Financial Supervisory Commission (Chinese Taipei), Securities and Exchange Commission (Thailand), Center for Coordination and Control over Functioning of Securities Market (Uzbekistan), and Vietnam State Securities Commission.

<sup>37</sup> Forward Markets Commission (India), Ministry of Agriculture, Forestry and Fisheries (Japan), Ministry of Economy, Trade and Industry (Japan), Securities and Exchange Surveillance Commission (Japan), Korea Deposit Insurance Commission, Labuan Offshore Financial Services Authority (Malaysia).

<sup>38</sup> Australian Securities and Investments Commission, Securities and Exchange Commission (Bangladesh), Brunei International Financial Center of the Ministry of Finance, China Securities Regulatory Commission, Hong Kong Securities and Futures Commission, Securities and Exchange Board of India (SEBI), Indonesian Capital Market and Financial Institutions Supervisory Agency, Financial Services Agency (Japan), Financial Services Commission/Financial Supervisory Service (FSC/FSS) (Korea), State Agency for Financial Surveillance and Accounting (Kyrgyz Republic), Securities Commission (Malaysia), Financial Regulatory Commission (Mongolia), Securities Commission (New Zealand), Securities and Exchange Commission (Pakistan), Securities Commission (Papua New Guinea), Securities and Exchange Commission (Philippines), Monetary Authority of Singapore, Securities and Exchange Commission (Sri Lanka), Financial Supervisory Commission (Chinese Taipei), Securities and Exchange Commission (Thailand), and State Securities Commission (Vietnam).

In addition, the following are Associate Members (Non-Voting) of the IOSCO Asia-Pacific Regional Committee: Forward Markets Commission (India), Ministry of Economy, Trade and Industry (Japan), Ministry of Economy, Trade

## **2. IOSCO Multilateral Memorandum of Understanding (MMOU)**

As a deeper expression of cooperation, IOSCO has developed a self-regulatory mechanism to support information exchange and regulatory cooperation, the IOSCO Multilateral Memorandum of Understanding (MMOU). Significantly, there are a large number of Asian signatories, with 10 Asian regulatory agencies currently parties to the agreement.<sup>39</sup> In addition, there are additional 5 pending Asian applicants.<sup>40</sup>

## **3. Regionalisation and the ACMF: ASEAN Capital Markets Forum**

Initially through the IOSCO Asia Pacific Regional Committee, ASEAN members are engaging in discussions (with support from ADB) on use of IOSCO standards as the basis for regional standards. In this context, as a first step, the ASEAN Capital Markets Forum (ACMF) has now agreed regional standards based upon IOSCO standards for equity and debt securities disclosure (the ASEAN and Plus Standards Scheme).<sup>41</sup> The ACMF, established in 2004 and comprising ASEAN capital markets regulators, initially focused on harmonisation of rules and regulations (for example for cross-border offerings of securities through the ASEAN and Plus Standards Scheme). In April 2009, with the endorsement of the ASEAN Capital Markets Integration Plan<sup>42</sup> at the 13<sup>th</sup> ASEAN Finance Ministers Meeting in April 2009, ACMF's focus has become broader and more strategic.

## **E. IAIS: International Association of Insurance Supervisors**

The IAIS is the primary international standard-setting organisation for insurance regulation. Like IOSCO, its membership is universal and it has 27 members from a wide range of Asian jurisdictions.<sup>43</sup> Unlike IOSCO, however, the IAIS has not yet established a formal regional committee.

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and Industry (Japan), Ministry of Agriculture, Forestry and Fisheries (Japan), Securities and Exchange Surveillance Commission (Japan), Korea Deposit Insurance Corporation, and Labuan Offshore Financial Services Authority (Labuan).

<sup>39</sup> Australia Securities and Investments Commission, China Securities Regulatory Commission, Hong Kong Securities and Futures Commission, Securities and Exchange Board of India, Financial Services Agency (Japan), Securities Commission (Malaysia), Securities Commission (New Zealand), Monetary Authority of Singapore, Securities and Exchange Commission (Sri Lanka), and Securities and Exchange Commission of Thailand.

<sup>40</sup> Indonesian Capital Market Supervisory Agency, Financial Services Commission / Financial Supervisory Service (Korea), Financial Regulatory Commission (Mongolia), Securities and Exchange Commission (Philippines), and Financial Supervisory Commission (Chinese Taipei).

<sup>41</sup> ACMF, ASEAN Equity Securities Disclosure Standards (Oct. 2008); ASEAN Debt Securities Disclosure Standards (Oct. 2008), online: <<http://www.aseansec.org/acmf/introduction.htm>>.

<sup>42</sup> ACMF, The Implementation Plan (Apr. 2009).

<sup>43</sup> Australia (Australian Prudential Regulatory Authority, Motor Accidents Authority of New South Wales, Private Health Insurance Administration Council), Bhutan, Cambodia, China (China Insurance Regulatory Commission, Chinese Taipei (Financial Supervisory Commission), Fiji (Reserve Bank of Fiji), Hong Kong (Office of the Commissioner of Insurance), India, Japan (Financial Services Agency), Kazakhstan (National Bank of Kazakhstan), Korea (Financial Supervisory Service), Labuan Malaysia (Labuan Offshore Financial Services Authority), Macau (Monetary Authority of Macao), Malaysia (Bank Negara Malaysia), Mongolia, Nepal, New Zealand, Pakistan (Securities and Exchange Commission), Papua New Guinea (Department of Finance & Treasury, Bank of Papua New Guinea), Philippines, Samoa, Singapore (Monetary Authority of Singapore), Sri Lanka (Insurance Board of Sri Lanka), Thailand, Uzbekistan, Vanuatu (Vanuatu Financial Services Commission), and Vietnam.

## **F. ASEAN Regionalisation and AITRI: ASEAN Insurance Training and Research Institute**

In 2000, ASEAN established an ASEAN Insurance Regulators Meeting and an ASEAN Insurance Training and Research Institute (AITRI). AITRI was officially incorporated in 2004, with the Malaysian Insurance Institute in Kuala Lumpur providing the Secretariat. AITRI provides training for regulators and the private sector, conducts research studies and is supporting the implementation of IAIS standards in ASEAN

## **G. IASB: International Accounting Standards Board**

IASB is the primary international standard-setting organisation for accounting standards (International Financial Reporting Standards (IFRS)). At present, Australia, China / Hong Kong, India, and Japan all have reserved places in the governance framework. Importantly, essentially all of Asia Pacific has or is in the process of adopting IFRS or adjusting domestic standards for equivalence.

## **H. Islamic finance: IFSB and AAOIFI**

Islamic finance is the only area in which international norms and standards have emanated from Asia and Asian-based organisations.

Modern Islamic finance is usually dated to the establishment of the first commercial bank by Barclays in the 1890s. From this initial establishment, there has been a continuing Islamic critique of Western finance and development of Islamic alternatives based on Islamic principles, with the intellectual basis largely formulated by the 1950s. From this basis, during the 1960s and 1970s, initial Islamic finance initiatives emerged in Malaysia (1962) and Dubai (1975). During the oil shocks of the 1970s, although hopes were initially high for rapid development of Islamic finance, in reality oil revenue generally was directed into Western financial institutions, through petrodollar recycling culminating in the developing country debt crisis of the early 1980s. At the same time as the 1980s debt crisis was triggering the development of international arrangements through the Basel Committee, IMF and World Bank, discussions began to be implemented, through legislative support in Pakistan (1980) and extensive research and development relating to equity investment compliant with Shari'a principles across the 1980s.

In the 1990s, as finance increasingly internationalised, Islamic finance likewise developed, supported by the establishment of AAOIFI in 1990 and the launch of the Dow Jones and Financial Times Islamic indices. With increasing interest, a wider range of countries introduced legislative and regulatory support for Islamic financial development and stability. To underpin the development and stability of emerging Islamic finance, the IFSB was established in 2002.

Together, AAOIFI and the IFSB comprise the main elements of the existing international Islamic financial architecture.

### **1. AAOIFI: Accounting and Auditing Organisation for Islamic Financial Institutions**

Formed in 1990 and established in Bahrain in 1991, AAOIFI is the first of the international Islamic financial standard-setting organisations. Its objectives focus on the development and dissemination accounting and auditing standards for Islamic financial institutions.

AAOIFI comprises associate members (financial institutions, organisations and firms operating shari'a compliant businesses), regulatory and supervisory authorities supervising Islamic financial institutions, and observers (institutions with Islamic banking operations, organisations regulating accounting and auditing, and accounting and auditing firms involved in Islamic finance). The General Assembly brings together all members at least once a year. The General Assembly appoints the Board of Trustees, comprising 20 part-time members serving five-year terms. The Trustees are responsible for appointing members of the various AAOIFI boards and committees, appointment of the Secretary General and arrangement of AAOIFI's finances. At present, AAOIFI boards and committees include the Accounting and Auditing Standards Board (responsible for preparing, adopting and interpreting accounting and auditing standards, codes of ethics and educational standards for Islamic financial institutions) and the Shari'a Board (responsible for achieving harmonisation and convergence among Shari'a supervisory boards of Islamic financial institutions and reviewing AAOIFI standards to ensure Shari'a compliance). The Accounting Standards Committee and the Auditing and Governance Standards Committee support the Accounting and Auditing Standards Board, while the Shari'a Board is supported by the Shari'a Standards Review Committee and three Shari'a Standards Committees.

To date, AAOIFI has been most influential in adopting Accounting, Auditing and Governance Standards (for Islamic Financial Institutions), with the most recent comprehensive version dating from 2008 and comprising 26 accounting standards, 5 auditing standards, 7 governance standards and 2 codes of ethics. In addition, AAOIFI has also adopted Shari'a Standards, most recently released in 2008 and addressing 35 areas of Islamic finance. AAOIFI also now provides two professional qualifications, the Certified Islamic Professional Account (CIPA) and the Certified Shari'a Adviser and Auditor (CSAA). Initially in 1999, AAOIFI also addressed capital adequacy<sup>44</sup> but related initiatives have since been centralised with the IFSB.

## **2. IFSB: Islamic Financial Standards Board**

The IFSB was established in 2002 and commenced operations in 2003 in Kuala Lumpur. It serves as the international standard-setting body for the Islamic financial services industry and is Asia's only international financial standard-setting organisation.

### **a. Membership**

The IFSB includes 7 Asian members: Bangladesh Bank, Bank Indonesia, Bank Negara Malaysia, Ministry of Finance, Brunei, Monetary Authority of Singapore, Securities Commission of Malaysia, and State Bank of Pakistan. In addition, there are another 8 Asian associate members, representing an additional 3 countries in the region plus ADB: ADB, Bangko ng Pilipinas, Bursa Malaysia Berhad, Hong Kong Monetary Authority, Labuan Offshore Financial Services Authority, Malaysia Deposit Insurance Corporation, People's Bank of China, and Securities and Exchange Commission of Pakistan.

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<sup>44</sup> AAOIFI, Statement on the Purpose and Calculation of the Capital Adequacy Ratio for Islamic Banks (1999).

Full membership is available to the supervisory body responsible for supervision of Islamic finance and international intergovernmental organisations that have an explicit mandate for promoting Islamic finance. Associate membership is available to any central bank, financial supervisory authority or international organisation involved in setting or promoting standards for international financial and monetary stability which does not qualify or seek to become a full member. Observer membership is available to any firm or association involved in Islamic financial services.

## **b. Structure and Organisation**

The IFSB is structured under the IFSB Articles of Agreement, Malaysia's IFSB Act 2002, the IFSB By-Laws and its Guidelines and Procedures for the Preparation of Standards / Guidelines. Its structure includes the following: (1) General Assembly, (2) Council, (3) Technical Committee, (4) Working Groups; (5) Taskforces; (6) Editing Committee; and (7) Secretariat, which has around 20 staff.

## **c. Activities and operations**

Under the IFSB Articles of Agreement, the objectives of the IFSB are to: (1) promote the development of a prudent and transparent Islamic financial services industry through introducing new, or adapting existing, international standards consistent with Shariah principles, and recommending these for adoption; (2) provide guidance on the effective supervision and regulation of institutions offering Islamic financial products and to develop for the Islamic financial services industry the criteria for identifying, measuring, managing and disclosing risks, taking into account international standards for valuation, income and expense calculation, and disclosure; (3) liaise and cooperate with relevant organisations currently setting standards for the stability and the soundness of the international monetary and financial systems and those of the member countries; (4) enhance and coordinate initiatives to develop instruments and procedures for efficient operations and risk management; (5) encourage cooperation amongst member countries in developing the Islamic financial services industry; (6) facilitate training and personnel development in skills in areas relevant to the effective regulation of the Islamic financial services industry and related markets; (7) undertake research into, and publish studies and surveys on, the Islamic financial services industry; and (8) establish a database of Islamic banks, financial institutions and industry experts.

Current Working Groups address: (1) Special Issues in Capital Adequacy, (2) Governance for Collective Islamic Investment Schemes, (3) Governance of Takaful Operations, (4) Business Conduct, and (5) Shariah Governance. Taskforces have been established to address: (1) Money Market, (2) Human Resource, and (3) Prudential Statistics.

To date, the IFSB has issued 9 sets of standards and is currently working on 3 additional sets of standards relating to Islamic finance.

## **d. Coordination and Impact**

Overall, the IFSB has emerged as the international standard-setting organisation in the area of Islamic finance, thus coordinating international, regional and domestic efforts to support the development of Islamic finance. To date, with the development of a range of standards and a



wide outreach programme, it has had an important impact in standardisation to support market development and stability, especially in Asia and the Middle East. The IFSB has issued eight sets of standards as well as a number of guidance documents and is currently working on 3 additional sets of standards relating to Islamic finance.

Published standards address: risk management (non-insurance); capital adequacy (non-insurance), including recognition of external ratings and requirements for sukuk, securitisation and real estate investment; corporate governance (excluding insurance and mutual funds); transparency and market discipline (excluding insurance and mutual funds); supervisory review (excluding insurance and mutual funds); and governance of Islamic collective investment scheme. In addition to these, IFSB has released reports discussing regulation and supervision of Islamic insurance (with the IAIS), a ten-year strategic development framework for the industry, a compilation addressing prudential and structural indicators for institutions offering Islamic banking services, and development of Islamic money markets and liquidity management frameworks. Currently, three standards are in consultation, addressing Shari'a governance, conduct of Islamic financial services business, and governance of Islamic insurance operations.

### **3. Other Islamic financial norm and standard-setting organisations**

In addition to the IFSB and AOIFI, a range of other Islamic financial standards organisations have emerged, including International Islamic Financial Market (IIFM, 2002), the Council for Islamic Banks and Financial Institutions (CIBAFI, 2001), the International Islamic Rating Agency (IIRA, 2005), and the Liquidity Management Centre (LMC, 2002). In addition, the Loan Market Association has supported transaction development through standardised documentation, with the International Swaps and Derivatives Association (ISDA) seeking to play a similar role in the context of Islamic derivatives development. Finally, domestic regulators, especially in Bahrain, Dubai and Malaysia, have played an important role in both supporting development and stability of Islamic finance. Finally, both the Islamic Development Bank and ADB are active in supporting Islamic financial development and stability initiatives.

#### **I. ACRAA: Association of Credit Rating Agencies in Asia**

Internationally, IOSCO is the primary international standard setting organisation for credit ratings. In Asia, ACRAA was organised in 2001 at ADB by 15 Asian credit rating agencies from 13 countries. ACRAA currently includes 25 rating agencies from 14 countries in Asia.<sup>45</sup>

ACRAA's objectives are to: (1) develop and maintain cooperative efforts that promote interaction and exchange of ideas, experiences, information, knowledge and skills among credit rating agencies in Asia and that would enhance their capabilities and their role of providing reliable market information; (2) undertake activities aimed at promoting the adoption of best practices and common standards that ensure high quality and comparability of credit ratings throughout the region, following the highest norms of ethics and professional conduct; and (3) undertake activities aimed at promoting the development of Asia's bond markets and cross-border investment throughout the region.

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<sup>45</sup> Bahrain, Bangladesh, China, India, Indonesia, Japan, Korea, Malaysia, Pakistan, Philippines, Sri Lanka, Taipei, China, Thailand, and Uzbekistan.

To date, ACRAA has created a Best Practices Committee and established a Code of Ethics and a Best Practices Checklist, as well as a Training Committee and a range of workshops.

## **J. Other Asian Private Sector Organisations Involved in Standard-Setting**

In addition to ACRAA, there are a number of other private sector organisations addressing financial issues such as loan markets and standards (Asia Pacific Loan Market Association – APLMA), securities markets and standards (Asia Securities Industry and Financial Markets Association), banking markets and standards (Asian Bankers Association) and insurance markets and standards (ASEAN Insurance Council).

## **K. Assessing Evolution**

Europe's protracted experience of developing regional financial norms, standards and institutional arrangements to support a single regional financial market indicates the scale of obstacles to Asian financial regionalism, which at best is only at a stage similar to the first European efforts. This in turn suggests that Asia can gain insight from EU experience in certain technical respects:

the principle of minimum harmonization together with mutual recognition principles underlines the potential for leaving integration to market forces once national legal and regulatory frameworks share common minimum standards.<sup>46</sup>

As such, elements of the second stage of European financial regionalization may assist the process of Asian financial cooperation and development, notably in shared commitments to reform, progressive voluntary harmonization to common minimum standards, and eventual liberalization and mutual recognition through more formal regional arrangements, marking the transformation of ASEAN or ASEAN+3 to integrated bodies from mere "regional clubs" of states.<sup>47</sup> Clearly, the recently adopted ASEAN capital markets integration plan reflects this approach in the context of securities. Initiatives adopted within ASEAN+3 and EMEAP may increase accountability, transparency and the extent of participation in reform in ways that become generally beneficial to economic development as well as supporting greater trade and economic integration, which could enhance intra- and extra-regional balance. This is conceptually similar to ASEAN's existing approach and accords with the ADB's identification of accountability, predictability, participation and transparency as principles of essential financial governance.<sup>48</sup>

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<sup>46</sup> C. Jordan & G. Majnoni, "Financial Regulatory Harmonization and the Globalization of Finance", World Bank Policy Research Working Paper No. 2919 (2002), at 9.

<sup>47</sup> V. Cable, *Globalization and Global Governance* (Royal Institute of International Affairs, 1999) at 54-62, noting that the reliance of state clubs upon reciprocity militates against strong governance, *ibid.* at 61. Regional leadership issues are beyond the scope of this paper but several configurations could allow integration to advance even if ASEAN is unwilling to accept leadership by China nor China by Japan, including regional leadership that is formally shared, divided, cooperative, coalitional or goal-centred, see C. Dent, "What Region to Lead? Developments in East Asian Regionalism and Questions of Regional Leadership", in Christopher Dent, ed., *China, Japan and Regional Leadership in East Asia* (Edward Elgar, 2008), at 23-24.

<sup>48</sup> Asian Development Bank, *Improving Governance and Fighting Corruption: Implementing the Governance and Anticorruption Policies of the Asian Development Bank* (Asian Development Bank, 2006).

## **L. Regional norms and standards: A possible basis for regional financial integration?**

Since Asia's prevailing regional organizations and institutions are weak or constrained by state-orientated governance, the outcome for financial integration and development is a function of the nature of the actors involved in their instigation, whether they represent national, commercial or other interests. Despite its contribution to economic integration the commercial sector has been formally included in Asian financial integration only recently, and in contrast with the EU pattern given no transparent role in governance. Financial integration may require "multi-level governance" that involves many actors, rather than Asia's state-centric tradition.<sup>49</sup> Regional efforts in regulatory cooperation and harmonization to common regional standards based upon international standards may be among the most promising roads to greater integration, financial stability and development. This approach could be influenced by EU legal instruments, and reflects experience with international financial standards and technocratic cooperation. In this context, the initial meetings of the Asian Financial Stability Dialogue are a significant development.

In addition, it may become possible through formal commitments and a revised AFAS to liberalize the regional financial service sector gradually without destabilising effects. This would result from state initiatives, and would follow global remedial and re-regulatory responses to the 2007-08 crisis. The process would rely on shared interests and a progressive harmonization to regionally agreed prudential practices and market standards derived from international best practices, as contemplated in the context of ASEAN capital market integration. Any such liberalization would begin with domestic governance requirements and continue through a process of mutual recognition. China's actions may be influential in this respect, especially if its example encourages other states to make liberalization commitments similar to those negotiated in its WTO accession. This approach would be most valuable if China first focused on regional liberalization.<sup>50</sup> Cooperation of this kind might allow ASEAN+3 members to take a more proactive stance in the stalled GATS financial services negotiations and in international standard setting bodies coordinated through the newly reconstituted FSB, especially if China's form of managed capitalism is more widely favoured after the current crisis. At the same time, in the context of cross-border establishment of financial institutions, the EU's experience in the context of the global financial crisis is instructive: in Asia there is little interest in regional regulatory authorities and as a result, while cross-border establishment may be liberalized as domestic regulation becomes increasingly developed to regional standards, the branch-based model should not be pursued but instead should be based on the premise of separately regulated jurisdictional subsidiaries,<sup>51</sup> albeit regulated to harmonized regional norms derived from Asian influenced international standards.

Adjustments of this type would augment mechanisms for convergence in financial activity and regulation. During the 1997-98 crisis, national authorities failed to find collaborative or regional solutions to isolated examples of instability that quickly became contagious, and the problem

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<sup>49</sup> Most of Asia's financial development initiatives to date have been introduced by delegated authorities such as central banks and financial regulatory agencies, but without sustained input from the clients that they respectively regulate.

<sup>50</sup> It should be noted that a state that is open to financial service sector entry may not signify a state willing to permit domestic or foreign participants to engage freely in commercial activities.

<sup>51</sup> For discussion, see D. Arner & J. Norton, "Building a Framework to Address Failure of Complex Global Financial Institutions", 39 Hong Kong Law Journal 95 (2009).

has been avoided recently due only to the global credit crisis being less intense in Asia than elsewhere. Unless Asia devotes resources in governance to improve regional financial integration and support domestic legal and regulatory reform, development will rely on a continuing export orientation, to the detriment of general welfare, financial development and economic stability. Reserve accumulation and risk averse national portfolio management may cease to be acceptable dominant policy options in a less globalized world.

## **M. Implications of the Global Financial Crisis for East Asian Financial Integration**

Asia's post-1998 recovery model differed little from that of Japan in the 1950s, later adopted by South Korea in the 1960s, other newly industrialized economies in the 1970s and China after 1978, namely, an export orientation with financial intermediation considered secondarily.<sup>52</sup> East Asia experienced steep falls in exports and output in 2008, but its financial systems have been less broadly affected than those of many developed countries in Europe or North America. Certain Asian banks and other intermediaries suffered material losses in a similar fashion as their western counterparts but most credit and capital losses in the Asian financial sector arose where financial intermediaries were sold complex instruments by firms domiciled outside the region. Although credit defaults and loan delinquencies are certain to rise in the recovery from recession, non-cyclical losses among Asian banks and dealers have not primarily been Asia's cause.

This propitious outcome may also reflect caution among Asian governments towards financial sector liberalization that followed the loss of confidence in the region in 1997-98, and a general lack of financial innovation among the region's financial intermediaries compared to the intense leveraging of capital, liquidity and structured credit risk by large intermediaries in New York and London.<sup>53</sup> Innovation and financial integration in Asia were impeded after 1999 by supervening state concerns as to national sovereignty and currency policy. This resistance was intensified by reflection on the Asian crisis, with states acutely nervous of capital inflows, sharing the view that IMF policies in 1997-99 were hostile, unnecessarily damaging to output and domestically destabilising. Asian states felt themselves ignored by and represented inadequately within the IMF.

Asia's significant global creditor position and the less severe impact that it suffered compared to other regions in the 2007-09 crisis led to an accrual of strategic influence, especially for China, Japan and Korea, and altered the balance of regional authority between China and Japan. This contributed to certain practical reforms in 2009, both globally and within the region. In the first instance, the G-20 committed itself to:

a shift in [IMF] quota share to dynamic emerging markets and developing countries of at least 5% from over-represented countries to underrepresented countries using the current quota formula as the basis to work from.<sup>54</sup>

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<sup>52</sup> For detailed discussion, see Q. Liu, D. Arner & P. Lejot, *Finance in Asia: Institutions, Markets and Regulation* (Routledge, forthcoming 2010).

<sup>53</sup> See D. Arner, P. Lejot & L. Schou-Zibell, "The Global Credit Crisis and Securitisation in East Asia", 3:3 *Capital Markets Law Journal* 291 (2008).

<sup>54</sup> G-20 Leaders' Statement: The Pittsburgh Summit, 25 Sep. 2009, online: <<http://www.pittsburghsummit.gov/mediacenter/129639.htm>>, Preamble at s. 21.

The G-20 acknowledged that quota changes will ultimately alter IMF decision making, for example in the formulation of subsequent quota adjustments and drawing entitlements, and in the composition of its executive board.<sup>55</sup> Second, China forcefully questioned the US dollar's sole reserve currency status, suggesting that reform might be included in a functional review of the IMF and the global financial architecture.<sup>56</sup> Finally, the same enhanced authority was used in a regional context in two instances in response to the global financial crisis, with the establishment of CMIM and the ADB's increase in capital.

Whether the global crisis continues to spur integration in the region is not straightforward. First, financial sector re-regulation may discourage transnational uses of risk capital and thus obstruct integration at least until confidence is generally restored, even among well-integrated EU financial markets. Second, Asia's greater prominence in a modified global system might lessen its incentive to introduce separate regional measures such as a discrete AMF. Alternatively, pressure for financial integration may increase within ASEAN, a group without the leverage to be afforded by the G-20 to China and Japan and to a lesser extent to Indonesia and Korea.

## **N. An Asian Monetary Fund?**

The attractions of an AMF have returned to discussions among states in the region. This paper concludes by outlining the functions that such an organization might perform and its likelihood of coming into being.

In the long-term, two functions might come to be associated with CMIM, those related to its founding purpose of an interdependently operating liquidity facility and others for which CMIM would be an institutional first step. The latter could include facilities for medium-term infrastructure funding, external budget assistance, and surveillance and operations to assist the formation and management of a currency alignment area comprising all or certain ASEAN+3 members. Currency cooperation is beyond the plans of ASEAN+3 to date, but equally falls well short of a template for a less feasible joint or federal central bank or a single regional currency.<sup>57</sup> Strong advocates of an AMF see CMIM as the first tangible step to its creation, so for example when under CMIM:

an effective regional surveillance mechanism is fully in place, and the surveillance unit exhibits its ability to formulate independent conditionality associated with crisis lending, the multilateral CMI can be delinked from IMF programs, paving the way toward the creation of an Asian Monetary Fund. An AMF is essential to support Asia's rebalancing process, as economies in the region would accept smaller current

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<sup>55</sup> *Ibid.*, at s. 21.

<sup>56</sup> Zhou Xiaochuan, Governor, People's Bank of China, speech "Reform the International Monetary System", 23 Mar. 2009, online: <<http://www.pbc.gov.cn/english/detail.asp?col=6500&ID=178>>, calling for the creation of a "super-sovereign reserve currency" with greater prominence for a reconstituted SDR to include emerging currencies.

<sup>57</sup> A single currency requires user states to share sovereignty, and is arguably blocked by the terms of the current ASEAN Charter, art. 2 s.2(a). However, a formal alignment of currencies among self-selecting states would entail independent tests for admission and ongoing macroeconomic surveillance of the kind projected by ASEAN+3 for CMIM, regardless of the mechanics of alignment (which include a common currency similar to the former European currency unit, or exchange regimes involving fixed or adjusting links to single currencies or indexes).

account surpluses—and less accumulation of foreign exchange reserves—if an AMF would mitigate financial turbulence and act as a regional lender of last resort.<sup>58</sup>

This reflects an official Japanese view of long-standing.<sup>59</sup>

Even without reforms to the regional financial architecture, ASEAN+3 finance ministers and EMEAP would continue to address macroeconomic cooperation and coordination, while regulatory organizations (EMEAP, ABMI, ACMF and regional sub-groups of organizations such as IOSCO) will address standard setting for financial stability concerns but not macroeconomic monitoring. Crisis resolution at sovereign level remains with the IMF with support from ADB and the World Bank, as during the Asian financial crisis. As is the case generally, no transnational arrangements exist to deal with resolution of individual financial intermediaries,<sup>60</sup> nor (outside of the EU) with the contagion impact of rapid losses of confidence that affect several or all states in a region.

In general, global or regional financial cooperation mechanisms have six common elements: (1) macroeconomic policy cooperation and coordination; (2) macroeconomic standard-setting and surveillance; (3) financial stability standard-setting and monitoring; (4) facilitation of liberalization and dispute resolution; (5) liquidity provision; and (6) crisis resolution at the macro (state) or micro (financial intermediary) level.<sup>61</sup> Under this framework, CMIM would embrace macroeconomic policy standard setting and performance surveillance, and operations involving emergency external liquidity.

If CMIM were to evolve into an AMF, it would seem logical to combine liquidity provision and economic policy standard-setting and monitoring with more formal arrangements for developing and monitoring regional financial regulatory standards based on the experiences of the FSB and the EU, using firmer arrangements than those of the former but less extensive than those in Europe. One model is IOSCO's MMoU, with a self-regulatory structure applying to standard-setting and monitoring, together with support from the ADB.

This highlights the important link between macroeconomic and financial stability standard-setting and surveillance in the operation of the liquidity mechanisms of an AMF. The division between liquidity issues and sovereign financial crises is not always clear. Both this issue and the supporting mechanisms merit the greatest design attention. If CMIM is to be introduced according to customary practice, it will require dedicated resources to be effective and generate confidence.

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<sup>58</sup> M. Kawai, "Global Financial Crisis and Japan-ASEAN Economic Cooperation" (speech to Japan-ASEAN Dialogue, 11 Sep. 2009), online: <<http://www.adbi.org/speeches/2009/09/15/3326.kawai.gfc.8th.japan.asean.dialogue/>> at 5.

<sup>59</sup> Former Japan finance vice-minister Eusike Sakikabara, a vocal proponent of AMF in 1997-98, told an ADB conference in May 2009 that earlier proposals were vetoed:

because of a strong opposition from the United States, as well as a lack of consultation by the Japanese government with its Asian neighbours – especially [China]. But now the situation has evolved and Asia is in a stronger position to create an AMF.

Online: <<http://www.adb.org/Media/printer.asp?articleID=12896>>.

<sup>60</sup> National and cross-border arrangements to address financial intermediary failure are current concerns of the G-20 and the subject of ongoing discussions within the Basel Committee on Banking Supervision.

<sup>61</sup> See generally D. Arner & R. Buckley, "Reforming the International Financial Architecture", AIIFL Working Paper No. 7 (forthcoming 2010), online: <<http://www.aiifl.com>>.

The independence of surveillance conducted by CMIM or a future AMF will be critical not only to the organization's reputational standing and whether it becomes a credible force, for the lack of use of CMI lines is believed to stem from the unwillingness of all members to allow drawings. CMIM or an AMF will need to conduct operations reliably and without favour. Institutional developments of this kind provide an opportunity to consider the proper organization of the functions outlined here, whether or not formalized into a new AMF. However, CMIM's operational outcome will not be immediately clear and Asia may well continue with its network-based approach to regional financial norm and standard development.