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Abay Yimer, S.

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## Chapter 5

### The Design of Means of Enforcement of Regulation

#### 5.1 The Enforcing Organs

##### 5.1.1 Identity of the Organs

###### i. The International Experience

The regulation of financial markets and institutions is central government function in most cases because of its connection with the national monetary policy. There are instances of decentralization only in few countries where there is strong federalism or decentralization such as the United States, Canada, Germany, Australia, Spain and Switzerland.<sup>2087</sup>

This being so, most countries have separated the financial market regulators functionally until the late 1980s. The majority of them have entrusted the banking and securities market regulations to their central banks and specialized agencies, respectively.<sup>2088</sup> They have entrusted the insurance and pension regulations to their ministries of trade, industry, economy, health or social affairs or to ministerial committees that might have to work with the central banks.<sup>2089</sup> The few others have entrusted the banking and securities regulations to their ministries of finance, specialized agencies or inter-ministerial committees and the insurance and pension regulations to specialized agencies.<sup>2090</sup> The US has followed the most disintegrated approach. It has regulated:

- the banking market through the Board of Governors of the Federal Reserve System, the Comptroller of Currency, the Federal Deposit Insurance Corporation, the Federal Trade Commission (for consumer protection matters), state regulators (for small commercial banks) and several federal regulators (for the specialized savings and credit institutions);<sup>2091</sup>

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2087 Möschel, 1991, at pp. 26-30; Pfennigstorf, 1996, at p. 59; Carmichael and Pomerleano, 2002, at pp. 40; Meier, 1988, at pp. 33-48; Wellons, 1999 at pp. 27-32; Davis, 1995, at pp. 123-124; and Busch, 2009. The banking regulatory regime of the US has allowed the banks to follow state or federal regulation and the large banks have often followed federal regulation while the small community banks have followed state regulations (Möschel, 1991, at pp. 26-30; and AP, 2009d). Whether the insurance market should be regulated by the federal government or the states has, however, been contentious issue in the country (NAIC, 2008; NAIC, 2008a; NAIC, 2008b; NAIC, 2007; NAIC, 2007a; Klein, 2009; Coope, 2009; Zimmerman, 2008; Cooper, 2008; Powell, 2008; AP, 2010a; and Bloomberg, 2010).

2088 Möschel, 1991, at pp. 25-35; Pfennigstorf, 1996, at pp. 58-59; Wellons, 1999, at pp. 27-36; Carmichael and Pomerleano, 2002, at p. 37; Carmichael, Fleming and Llewellyn, 2004, at pp. 2-6 & 17-92; and Table 1(Chap. 5).

2089 Pfennigstorf, 1996, at pp. 58-59; Davis, 1995, at pp. 123-124; Carmichael and Pomerleano, 2002, at p. 37; Carmichael, Fleming and Llewellyn, 2004, at pp. 2-6 & 17-92; and Table 1(Chap. 5).

2090 Möschel, 1991, at pp. 25-26; Pfennigstorf, 1996, at p. 58; Wellons, 1999, at pp. 27-28; Davis, 1995, at pp. 123-124; Carmichael and Pomerleano, 2002, at p. 37; Carmichael, Fleming and Llewellyn, 2004, at pp. 2-6 & 17-92; and Table 1(Chap. 5). The pension funds in the Latin American countries were subject to independent regulators while those in most of the transition and the other emerging market countries were often subject to regulatory units under ministries (Rocha, Hinz and Gutierrez, 2001, at p. 194).

2091 Möschel, 1991, at pp. 29-31.

- the insurance market through state commissions, the Federal Department of Defence (for the sale of insurance to military installations), and the Securities Exchange Commission (for the securities aspect of the insurers' investments);<sup>2092</sup>
- the securities markets through the Securities and Exchange Commission, the Securities Investor Protection Corporation, the Commodities Future Trading Commission, the Federal Reserve Board, the Department of Treasury, the Department of Labor, the Office of the Comptroller of Currency, the Federal Deposit Insurance Corporation and the Pension Benefit Guaranty Corporation;<sup>2093</sup> and
- the pensions through the Department of Labor (for the minimum funding rules, investment standards and cases of fraud), the Internal Revenue Service (for the maximum funding rules to prevent tax abuse), the Pension Benefit Guarantee Corporation (for collection of contributions and payment of benefits), and several fund trustees and a master custodian (for the adequacy of funding, the prudent management of funds and the fulfilment of pension law requirements).<sup>2094</sup>

Some like UK, the Netherlands, New Zealand and USA have also entrusted the regulations of their insurance and securities markets to Self Regulatory Organizations (SROs).<sup>2095</sup> Germany, Canada, France, Italy, the Netherlands, Sweden and Switzerland have also allowed the self-regulation of some of the banking matters (such as market conduct, competition or deposit protection) by associations of the banks.<sup>2096</sup>

Most of the countries have, however, integrated their financial market regulators fully or partly after the late 1980s.<sup>2097</sup> Few of them have made this within their central banks while the majority of them have made it outside the central banks.<sup>2098</sup> The countries which relied on SROs have also increased the governmental regulation of their markets by the integrated regulator without eliminating the self-regulation approach completely.<sup>2099</sup> The International Association of Insurance Supervisors (IAIS) and International Association of Securities Commissions (IOSCO) have also recognized the use of SROs to regulate aspects of the insurance and securities markets subject to regulation by the governmental regulators<sup>2100</sup>.

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2092 Caddy, 1986, at p. 1; Meier, 1988, at pp. 35-36; and Carmichael and Pomerleano, 2002, at p. 40.

2093 Wellons, 1999, at p. 32; and Vagts, 2006, at pp. 11-14.

2094 Davis, 1995, at p. 123.

2095 Pfennigstorf, 1996, at pp. 32, 35-38 & 52-53; and Wellons, 1999, at pp. 27-28, 32 & 35-36.

2096 Möschel, at pp. 31-34.

2097 Singapore has been the first to do this between 1971 and 1984. UK, Canada, Norway, Egypt and Malawi have started to do it in the late 1980s. The rest have done it in the 1990s and thereafter. Table 2(Chap. 5); Carmichael and Pomerleano, 2002, at pp. 39-44 & 47; Carmichael, Fleming and Llewellyn, 2004, at pp. 40-80; IAIS, 2005b, at p. 10; Masciandaro, 2006, at pp. 30-32; Vagts, 2006, at pp. 11-14; and Busch, 2009.

2098 Table 2(Chap. 5).

2099 Möschel, 1991, at pp. 25-36; Wellons, 1999, at pp. 37-38; Carmichael and Pomerleano, 2002, at p. 40; and Vagts, 2006, at pp. 11-14.

2100 IAIS, 2003; and IOSCO, 2003.

The countries that have not integrated their regulators have continued to entrust the banking regulations to their central banks and the insurance, securities and pension market regulations to independent agencies and commissions.<sup>2101</sup> Some also consider the regulation of their securities markets through central banks as logical either because they take the central banks to be the most experienced, staffed and responsible institutions for this purpose or because they feel that the central banks have to act as securities regulators by default due to lack of another institution that can regulate the securities markets.<sup>2102</sup> The US has continued with the disintegration approach and established additional regulators (i.e. a specialized bureau for consumer protection - to be seated at the Federal Reserve, a Financial Stability Oversight Council for oversight of large firms and systemic risk - to be led by the Treasury Department, and a Federal Insurance Office for overall monitoring of insurers on top of state regulations - to be seated in the Treasury) by the 2010 financial regulatory overhauling bill.<sup>2103</sup>

The EU has introduced a European System of Financial Supervision consisting of a European Systemic Risk Board (ESRB), a European Banking Authority (EBA), a European Insurance and Occupational Pensions Authority (EIOPA), a European Securities and Markets Authority (ESMA), a Joint Committee of these Authorities, and the supervisory authorities of the member countries in the aftermath of the 2008 financial and economic crises.<sup>2104</sup> The ESRB is responsible for macro-prudential oversight of the financial system and assurance of systemic stability.<sup>2105</sup> It is established as independent body and entrusted to the European Central Bank for support.<sup>2106</sup> The Authorities are not also meant to replace the national regulators of the member countries, but responsible for further harmonization of the national and international regulations.<sup>2107</sup>

The ability of central banks to deal with large crisis and ensure monetary and financial stability is, however, also questioned in the aftermath of the 2008 financial and economic crisis and this has made the location of the integrated financial market regulator a continually debated issue.<sup>2108</sup>

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2101 Table 1(Chap. 5); Busch, 2009; and Vagts, 2006, at pp. 11-14.

2102 Wellons, 1999, at p. 27; and Vagts, 2006, at pp. 11-14.

2103 AP, 2010a; Bloomberg, 2010; and Busch, 2009, at pp. 33-74. China has also continued with the disintegration approach for the markets other than pension and insurance (Tables 1(Chap. 5); 2(Chap. 5); and Brück, 2009).

2104 It used to rely on national regulators of the member countries and three European committees, namely the Committee of European Banking Supervisors (CEBS) (established on 05 November 2003), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) (established on 05 November 2003), and the Committee of European Securities Regulators (CESR) (established on 06 June 2001). The new system (established in November 2010) has become operational in January 2011 and the authorities, i.e. the EBA, EIOPA and ESMA, have replaced the CEBS, CEIOPS and CESR, respectively. EU, 2010; EU, 2010a; EU, 2010b; EU, 2010c; EU, 2010d; ESRB, 2011; ESMA, 2011; EIOPA, 2011; and EBA, 2011.

2105 EU, 2010; and ESRB, 2011.

2106 EU, 2010d; and ESRB, 2011.

2107 EU, 2010a; EU, 2010b; EU, 2010c; EBA, 2011; EIOPA, 2011; and ESMA, 2011.

2108 Walker, 2007; Harris, 2008; Quaglia, 2008; Hall, 2008; Haubrich and Thomson, 2008; Michael and Harold, 2009; Gerlach, et al., 2009; Goodhart, 2009, at pp. 34-41; Chorafas, 2009, at pp. 34-60 & 183ff; Chapman, 2010, at pp. 96-127; and Howard and David, 2010.

Many of the countries also enforce their competition policies and laws through independent competition authorities despite variation in their nomenclature of the authorities.<sup>2109</sup> Some like the US, Australia, New Zealand and the EU follow hybrid approaches. The US enforces them through the Bureau of Competition at the Federal Trade Commission, the Antitrust Division of the Department of Justice, the Courts, and the special administrative forums in which the Federal Trade Commission may file competition cases.<sup>2110</sup> Australia and New Zealand enforce them through competition authorities and the courts.<sup>2111</sup> The EU enforces them through the European Parliament, the Economic and Social Committee (ECOSOC), the Council of Ministers, the European Commission, the European Court of First Instance, the European Court of Justice (assisted by Advocate General), the Advisory Committees on restrictive practices, monopolies and concentrations, and the national competition authorities and courts.<sup>2112</sup> It has increased the responsibilities of the national competition authorities and courts through the modernization reforms of 01 May 2004.<sup>2113</sup>

The issue in competition law enforcement has generally been on whether to follow a judicial or administrative enforcement approach. The use of independent competition authorities with strong powers is administrative approach. The use of more powerful courts than independent competition authorities is judicial approach. The continental competition regimes have grown from a system where the administrative approach used to be dominant to a system that recognizes the importance of the judicial approach while the Anglo-American regimes have relied more on the judicial than the administrative approach.<sup>2114</sup> The recent move in both groups of countries is towards increasing the use of the judicial enforcement machinery without diminishing the use of independent competition authorities.<sup>2115</sup>

## ii. The Case of Ethiopia

Ethiopia makes the regulation of financial markets and institutions and the design of competition policy and law central government function as in most other countries. It used to subject the banks and insurers to direct government decision and concession in the period before 1963 in the absence of independent financial market regulator.<sup>2116</sup> It introduced separate banking, insurance and competition regulators when it enacted the Monetary and Banking Proclamation, the National Bank Charter Order and the Unfair Trade Practices Decree in 1963 and the Insurance Proclamation in 1970.<sup>2117</sup> It, by these laws, authorized:

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2109 World Bank, 2002, at p. 142; and members list of the International Competition Network (ICN, 2010b).

2110 FTC, 2005.

2111 Brunt, 2003, at pp. 1-50.

2112 Richard Whish, 2001, at pp. 48-52; Céline Gauer, et al., 2004; EC, 2003; EC, 2004; and EC, 2005.

2113 Ibid.

2114 World Bank and OECD, 1999, at pp. 1-4; World Bank, 2002, at p. 142; Brunt, 2003, at pp. 1-50; Richard Whish, 2001, at pp. 48-52; Gerber, 2001, at pp. 8, 10, 12-13 & 421-422; and Cseres, et al., 2006.

2115 Ibid.

2116 Bahru Zewde, 2002, at pp. 101-102; and NBE, 2001.

2117 IGE, 1963d; IGE, 1963e, at art. 7; IGE, 1970b, at arts. 4 & 5; and IGE, 1963g, at arts. 3(h) & 5.

- the NBE to control and regulate the monetary, credit and banking regimes;
- the Insurance Council and the Insurance Controller's Office (both of which were created outside of the NBE by including it as member) to regulate insurance; and
- the Ministry of Commerce and Industry to enforce the competition law.<sup>2118</sup>

It unified the regulation of all the financial institutions under the NBE in 1976 and required it to exercise its regulatory functions under the national plan of the time.<sup>2119</sup>

It currently makes the NBE regulator of all the financial institutions under the monetary, banking, insurance and microfinance supervision laws.<sup>2120</sup> It enforces the competition policy and law through a Secretariat established in the Ministry of Trade and Industry, a Federal Trade Practice Commission established under the Ministry, and regional legislative councils and trade bureaus.<sup>2121</sup> It does not have special competition authority that is in charge of competition enforcement in the financial markets. It only looks from the competition, monetary, banking, insurance, and microfinance supervision laws that the country opts for the separate enforcement of the competition and the financial market supervision laws through the general competition enforcement organs and the NBE, respectively, although the NBE may not be free from enforcing the competition objective in the financial markets.<sup>2122</sup>

The authorization of the NBE to regulate the future securities market of the country was discussed only when proposals were made in 2001 and thereafter for creation of the market.<sup>2123</sup> The Justice and Legal System Research Institute has proposed, through the draft laws of 2001 and 2003, that the NBE has to be empowered to be regulator of the securities market.<sup>2124</sup> It has also proposed that the NBE needs to be conferred with the powers of:

- registering and licensing the securities market and its actors;
- registering the securities issuers;
- supervising, inspecting, investigating and sanctioning the securities market actors and issuers;

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2118 Ibid. It subjected the securities market that emerged in the 1960s to self-regulation and made the NBE intervene only when the market needed some government assistance (Von Pischke, 1968, at pp. 10-14).

2119 PMGE, 1976i, at arts. 3, 6, 43, 44-50 & 61-67.

2120 TGE, 1994, at art. 7(4); FDRE, 2008a, at art. 5(7); TGE, 1994a; FDRE, 2008b; TGE, 1994b; FDRE, 1996g; and FDRE, 2009.

2121 TGE, 1994, at art. 7(4) & 41; FDRE, 2008a, at art. 5(7) & 14; FDRE, 2003c, at arts. 2(2), 2(3), 12-19 & 25-29.

2122 TGE, 1994; FDRE, 2008a; TGE, 1994a; FDRE, 2008b; TGE, 1994b; FDRE, 1996g; FDRE, 2009; and FDRE, 2003c.

2123 The monetary and financial supervision laws of the country have purported to make the NBE securities market regulator in the absence of such discussion. They state that the NBE is to be the regulator of all financial institutions. The NBE has also issued a directive which signalled its role as securities market regulator. TGE, 1994, at art. 7(4); FDRE, 2008a, at art. 5(7); and Directive No. SBB/12/1996, at art. 8.

2124 JLSRI, 2001, at pp. 33-35 & 41; and JLSRI, 2003, at arts. 33-36 & 39(2).

- suspending and cancelling listings and trades;
- following up, controlling and approving mergers, acquisitions and other forms of business combinations between listed companies; and
- acquiring information and controlling abuses.<sup>2125</sup>

The NBE has not opposed the proposals of the Institute when it commented on the draft law.<sup>2126</sup> It has only suggested that its powers and the powers of the other institutions including the Ministry of Trade and Industry need to be demarcated clearly.<sup>2127</sup> The Awash International Bank S. C. has favoured the setting up of a securities market regulator outside the NBE for fear that the latter is already overwhelmed by many responsibilities while lacking sufficient regulatory capacity.<sup>2128</sup> The Bank of Abyssinia has been silent on the question.<sup>2129</sup> None of the four institutions have, however, proposed comprehensive solution on the modalities of coordinating between the NBE, the competition enforcement organs and the future securities market regulator. The creation of pension regulator has not also been discussed so far even if the expansion of the occupational pension system for the private sector has been discussed for some time.<sup>2130</sup> Hence, fixing the identity of regulator of the future financial markets of the country is pending question and the country needs to resolve it as it creates the securities market and private pensions.

## 5.1.2 The Powers and Functions of the Organs

### 5.1.2.1 The Traditional Powers and Functions

#### i. The International Experience

Many of the countries entrust their financial regulators with differing degrees of rule making, monitoring, investigating, sanctioning and dispute settling powers and operational and financial autonomy from the government.<sup>2131</sup> They do these by general clauses, enumeration (of the powers and measures), or a mixture of the two.<sup>2132</sup> They usually define the powers to include:

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2125 JLSRI, 2003, at arts. 33-36 & 39(2).

2126 NBE, 2002 and the annex, at pp. 40, 43, 46 & 50.

2127 Ibid.

2128 AIB, 2002.

2129 BA, 2002.

2130 Note the discussion under the pension chapter above. The monetary and insurance supervision laws of the country have, however, also purported to make the NBE a pension market regulator. The monetary law has defined the NBE to be the regulator of all the financial institutions while the insurance supervision law has included the undertaking of private pension businesses in the definition of long-term insurance and implied that the NBE can be regulator of such businesses. TGE, 1994, at art. 7(4)); FDRE, 2008a, at art. 5(7); and TGE, 1994b, at art. 2(16).

2131 Möschel, 1991, at pp. 111-118; Pfennigstorf, 1996, at pp. 60 & 138-141; IAIS, 2005b, at p. 11; and Wellons, 1999, at pp. 40-46, 54-58 & 72. The specification of powers and functions and determination of degree of autonomy of the regulators are influenced by the balance between professionalism and political responsibility and the bureaucratic tradition and government structure of the countries. These factors also influence the selection of the heads of the regulatory agencies. Pfennigstorf, 1996, at pp. 58-59; and Wellons, 1999, at pp. 27-35 & 40-46.

2132 Ibid.

- the granting, denying or revoking of licenses;
- the making of market entry, operational and exit rules;
- the conduct of off-site surveillance and on-site inspection and examination;
- the issuance of enforcement orders;
- the take-over of management of the financial institutions; and
- the enforcement of sanctions and liquidation orders.<sup>2133</sup>

They authorize their banking and insurance regulators to make the off-site surveillance through regular and special reporting requirements and to exercise the on-site inspection and examination powers at regular intervals, at any time they may feel to do so, and at any time shareholders of the financial institutions request.<sup>2134</sup> They allow them to carry out the on-site inspection (and examination) by themselves or through independent inspectors, examiners and auditors who should work under their strict control and often impose the cost of inspection and examination on the inspected institutions.<sup>2135</sup> They allow them to sanction the regulated institutions during non-crisis situation when the information obtained through the surveillance and inspection processes show failure of the institutions to meet the regulatory requirements and aims.<sup>2136</sup> They authorize them to:

- implement informal procedures (such as discussion, warning and pressure through public announcement);
- impose interim orders and correction measures (short of prohibition of conduct);
- impose cease and desist orders;
- remove chief executives;
- revoke licenses;
- order cancellation of the actors from membership in associations and fund protection schemes; and
- impose financial sanctions.<sup>2137</sup>

They also authorize them to take four types of measures in crisis situation:

- measures intended to aid the financial institutions (including the takeover of management or placement of personnel in the governing organs of the institutions as step to reorganization, the use of deposit insurance and other guarantee funds, and the use of lender of last resort);
- measures intended to rehabilitate or reorganize the financial institutions (including the ordering of temporary closure, imposition of merger, and prohibition of activities that might impede rehabilitation);

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2133 Ibid.

2134 They allow them to base on the latter when *prima facie* need for inspection or examination is established by request of one third of the shareholders of the institutions. Möschel, 1991, at pp. 110-112; Pfennigstorf, 1996, at pp. 60 & 101-103; and IAIS, 2005b, at p. 11.

2135 The use of external inspectors and examiners is praised for having the advantage of avoiding bureaucratic regulators. Möschel, 1991, at p. 112; and IAIS, 2005b, at p. 11.

2136 Möschel, 1991, at pp. 113-114; Pfennigstorf, 1996, at pp. 60 & 138-141; and IAIS, 2005b, at p. 11.

2137 The instrument of public announcement is rarely used to avoid panic and additional damages to the financial institutions. Ibid.

- measures intended to wind-up the financial institutions; and
- measures intended to rectify a crisis situation that transcends an individual financial institution to affect the economy.<sup>2138</sup>

Many of the countries have also seen the usefulness of broad formulation of the legal bases for official intervention of their regulators, the use of graduated catalogue of administrative measures in non-crisis situation, and the implementation of rehabilitation and reorganization measures in crisis situation as opposed to winding-up.<sup>2139</sup>

The powers of the securities market regulators often range between two extremes.<sup>2140</sup> Some of the countries, at one of the extremes, entrust them with negligible enforcement powers while others, at the other extreme, entrust them with the full powers of rule making, investigating and sanctioning.<sup>2141</sup> Several others fall in between the two by entrusting them with the powers of inspecting and publishing the inspection results without power to sanction.<sup>2142</sup> Each approach has, however, advantages and limits.<sup>2143</sup> The negligible enforcement approach allows the market to develop best practices flexibly, decentres power from the government, reduces the cost of regulatory enforcement, and increases enforcement efficiency. It, however, fails to work in markets where there are no substantial private financial institutions, the business community does not share common values, the market leaders tend to protect their own interests, insider trading is common, and reputation is not vital to do business.<sup>2144</sup> The inspection without sanction approach assumes that the government agencies actively inspect and publicize the outcome and that publicity can sanction the inspected institutions.<sup>2145</sup> It fails to work when the government agencies lack adequate resource (and inclination to inspect) and publicity does not create serious problem to the inspected institutions.<sup>2146</sup> The regulator with extensive powers approach is useful when the other two approaches do not hold.<sup>2147</sup> It is, however, also prone to regulatory abuse unless controlled through strong judicial review and other mechanisms.<sup>2148</sup> The making of choice between the approaches also depends on the stage of development of the securities market, the kind of securities market a country wants to have and the structure of a country's legal system.<sup>2149</sup> The global trend seems to be towards greater empowerment of the securities market

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2138 Möschel, 1991, at pp. 115-118; Pfennigstorf, 1996, at pp. 60 & 138-144; and IAIS, 2005b, at p. 11.

2139 Ibid.

2140 Wellons, 1999, at pp. 40-46, 54-56 & 72; and Vagts, 2006, at pp. 11-14.

2141 The former has been true with the countries that used to rely on self regulation such as UK, the Netherlands, New Zealand and others like Hong Kong. Ibid.

2142 Ibid.

2143 Ibid.

2144 These problems are common in many developing countries. Ibid.

2145 Ibid.

2146 These problems are also common in many developing countries. Ibid.

2147 Ibid.

2148 Note the discussion under the 'legal protection' subtitle below.

2149 Ibid.

regulators.<sup>2150</sup> The IOSCO also favours the conferment of full powers (including the investigating and sanctioning powers) on securities regulators.<sup>2151</sup>

Most of the OECD countries empower their pension regulators to check the annual accounts and audit and actuarial reports of the regulated pension institutions.<sup>2152</sup> Few of them require the use of direct inspection and investigation at intervals.<sup>2153</sup> The International Organization of Pension Supervisors (IOPS) recommends that both the OECD and other countries should entrust their pension market regulators with all the necessary investigating and enforcing powers so that they can fulfil their functions and achieve the objectives of their regulations effectively.<sup>2154</sup>

A number of the countries also entrust their competition enforcement organs with differing degrees of decision and rule making, monitoring, investigating, sanctioning and dispute settling powers and operational and financial autonomy from the government.<sup>2155</sup> Many also feel that the decision making, investigating, dispute settling, and law enforcing powers and the leadership and budgetary independence of the organs from government need to be strengthened in the transition and emerging market countries.<sup>2156</sup>

## ii. The Case of Ethiopia

Ethiopia authorized the NBE to do the following during the pre-revolution (1974) period:

- regulate the supply of money;
- license and supervise the commercial banking operations;
- regulate the reserve and liquidity positions of the banks and insurers;
- control the direction, duration, purpose and amount of credit of the financial institutions;
- provide credit to the banks and other financial institutions;
- issue the conditions for its credit and the credit of the banks and other financial institutions; and

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2150 A number of the transition and emerging market countries in Asia and Africa have entrusted their regulators with extensive regulatory enforcement powers. The countries that historically followed the self regulation approach including UK, the Netherlands and New Zealand have also increased the powers of their securities market regulators as they conducted their big bangs and their regulators were integrated after the late 1980s. *Ibid.*

2151 IOSCO, 2003.

2152 Davis, 1995, at p. 124.

2153 Some like the Netherlands require the conduct of on-the-spot inspection in every ten years while others like the US require regular computer checks to identify pension plans that need investigation. Investigations may also be triggered in the US by complaints of the pension members. *Id.*, at pp. 124-125.

2154 IOPS, 2006.

2155 World Bank, 2002, at pp. 141-142.

2156 Pradeep S. Mehta, 2002, at pp. 81 & 82; World Bank, 2002, at pp. 141-142; and OECD, 2004, at pp. 5 & 25.

- fix the interest rates with which it, the banks and other financial institutions extend credit.<sup>2157</sup>

It authorized and required it to do the following during the post-revolution period:

- control the money supply;
- plan, coordinate and direct all the banking and non-banking financial activities;
- guide the allocation of credit and foreign exchange;
- set the interest rates of the financial institutions and its own credits; and
- execute the central plan of the country.<sup>2158</sup>

It authorizes it to do the following under the current monetary and banking law:

- license, supervise and regulate the banks, insurers and other financial institutions;
- create favourable conditions for the expansion of the banking, insurance and other financial services;
- regulate the supply and availability of money and credit;
- issue debt and payment instruments;
- fix the standard and discount rates of interest and charges with which it will accept commercial instruments;
- regulate the supply and availability of money and credit and the interest rates and charges of the banks, insurers and other financial institutions;
- govern its credit transactions with the banks and other financial institutions;
- administer the international reserves of the country;
- formulate and implement the exchange rate policy of the country;
- authorize the banks, other financial institutions and dealers to engage in gold and foreign exchange transactions;
- set limits on the gold and foreign exchange assets of the banks, other financial institutions and dealers;
- regulate the gold and foreign exchange transactions of the banks, other financial institutions and dealers;
- set the net foreign exchange positions and the terms and amounts of external indebtedness of the banks and other financial institutions;
- establish and manage a deposit insurance fund;
- provide payment and clearing services to the banks and other financial institutions;
- establish, modernize and regulate the payment, clearing and settlement systems of the country;
- act as banker, fiscal agent and financial advisor of the government;
- conduct periodic economic studies useful for formulation of monetary, saving and foreign exchange policies of the country; and
- exercise the powers and functions that are common to central banks.<sup>2159</sup>

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2157 IGE, 1963e, at arts. 3, 5 & 7.

2158 PMGE, 1976i, at arts. 3, 6, 30-43, 44(1), 44(2), 45-50 & 61-67.

2159 TGE, 1994, at art. 7; and FDRE, 2008a, at arts. 5, 14 & 16(1)(c).

It authorizes it to inspect and examine the financial institutions periodically, at any time it may wish to do so, and when examination is requested by one fifth of the total number of depositors of the financial institutions or by any number of depositors or creditors who hold not less than one-third of the deposits or liabilities of the institutions.<sup>2160</sup> It authorizes it to carryout the inspection and investigation processes through its own officers or external inspectors under its control.<sup>2161</sup> It, by the inspection and examination powers, authorizes it to check the soundness of the financial institutions and the observance of substantive and procedural requirements of regulation by them.<sup>2162</sup> It authorizes it to examine all facts that may come to notice of the inspectors and investigators as possible jeopardy to the position of creditors and to do the following:

- discuss with the boards of directors and officers of the inspected institutions;
- call, and participate in, meetings of the shareholders, boards of directors and management committees of the institutions;
- order the taking of corrective actions by the institutions;
- order dismissal or suspension of the directors and officers of the institutions;
- prohibit acceptance of new deposits and service orders by the institutions;
- suspend the whole or part of the business of the institutions;
- restrict, suspend or prohibit the payment of dividends by the institutions;
- prohibit the opening of new branches by the institutions;
- put the institutions (which it may find to be unsound, imprudent, unlawful or detrimental to the interests of creditors) under receivership or temporary takeover; and
- impose other sanctions as appropriate.<sup>2163</sup>

It authorizes it to implement the measure of receivership against the banks and microfinance institutions when any of the following happens:

- i) their licenses are revoked for reason of issuance based on false or wrong information;
- ii) they
  - become insolvent;
  - engaged in unsafe and unsound practices that constitute significant danger to their depositors;
  - violate applicable laws, regulations and limitations of the NBE;
  - refuse to be inspected by the NBE;

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2160 TGE, 1994a, at art. 20(1); FDRE, 2008b, at art. 29(1)-(2); TGE, 1994b, at arts. 26 & 44; FDRE, 1996g, at art. 24; and FDRE, 2009, at arts. 18 & 28(1).

2161 TGE, 1994a, at art. 20(2)(a); FDRE, 2008b, at art. 29(3); TGE, 1994b, at art. 26; FDRE, 1996g, at art. 24; and FDRE, 2009, at art. 18(3) & 28(1).

2162 TGE, 1994a, at arts. 20(2)(b) & 20(3); FDRE, 2008b, at art. 29(2); TGE, 1994b, at arts. 26, 30 & 44; FDRE, 1996g, at art. 24; and FDRE, 2009, at art. 18(2).

2163 TGE, 1994a, at arts. 20(2)(b), 20(3) & 22-25; FDRE, 2008b, at arts. 31, 33-48 & 58; TGE, 1994b, at arts. 26, 27-28, 30-31, 42 & 44; FDRE, 1996g, at art. 24; and FDRE, 2009, at arts. 18(5-7). Note also the discussion under the 'sanctions' subtitle below.

- become undercapitalized (i.e. have capital below the requirements of the NBE), dissipate their assets substantially, or incur losses that are to deplete their capitals substantially;
  - are unlikely to fulfil their obligations in the normal course of business;
  - pursue policies that endanger the general economic interest of the country or the public;
  - merge with another financial institution without prior authorization of the NBE;
  - fail to appoint directors and executives who fulfil the requirements of the NBE; or
  - cease to operate as legally independent entity; or
- iii) their owners decide to put them under receivership or liquidate them.<sup>2164</sup>

It authorizes it to takeover the long-term insurers when they are on the brink of failure or have violated applicable laws, regulations and limitations.<sup>2165</sup>

It, by the receivership and takeover powers, also authorizes it to:

- take measures that may aid the failing institution;
- order reorganization, merger or acquisition of the institution by another financial institution; or
- liquidate and wind up the institution.<sup>2166</sup>

It also authorizes it to require the inspected and examined financial institutions to bear the costs of inspection, receivership and other measures.<sup>2167</sup>

The country, therefore, confers the NBE with rule making, inspecting, sanctioning and rehabilitating powers. It also confers it with some operational and financial autonomy from the government in exercising the aforementioned powers and functions.<sup>2168</sup>

It also authorizes the competition enforcement organs to investigate and decide on competition cases, issue rules and directives that facilitate the enforcement of the competition law, and enforce sanctions (with assistance of the police).<sup>2169</sup>

It does not, however, confer the NBE with regulatory dispute-adjudication powers although the NBE sometimes tries to exercise this.<sup>2170</sup> It does not also indicate the measures the NBE may have to take during crisis situation which may

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2164 FDRE, 2008b, at art. 33; and FDRE, 2009, at art. 18.

2165 TGE, 1994a, at arts. 20(2)(b), 20(3) & 22-25; and TGE, 1994b, at arts. 26, 27-28 & 44.

2166 TGE, 1994a, at arts. 22-26; FDRE, 2008b, at arts. 33-48; TGE, 1994b, at arts. 27, 28, 39 & 44; and FDRE, 2009, at art. 19.

2167 TGE, 1994a, at art. 20(4); FDRE, 2008b, at arts. 35 & 51; TGE, 1994b, at art. 26(5); and FDRE, 2009, at art. 19(3).

2168 TGE, 1994, at arts. 3 & 9; and FDRE, 2008a, at art. 3(1).

2169 FDRE, 2003c, at arts. 15-19.

2170 It, for instance, plays as arbitrator to settle disputes between the banks that participate in the inter-bank foreign exchange market (Directives No. IBM/01/1998, at art. 12; and IBFEM/02/2001, at art. 10).

transcend an individual financial institution to affect the financial sector or the economy as a whole. It also makes the autonomy of the NBE fragile by authorizing the Prime Minister and the Council of Ministers to administer it directly.<sup>2171</sup> It also puts the competition enforcement organs under direct control of the executive (i.e. the Minister of Trade and Industry) and makes the Trade Practice Commission not anything more than a dispute investigation office.<sup>2172</sup>

The NBE also fails to use the tools of off-site surveillance and on-site examination properly in practice.<sup>2173</sup> Its supervision departments, of course, recognize the importance of developing system for macro-prudential analysis that will allow evaluation of the financial institutions based on macro prudential and macro economic indicators.<sup>2174</sup> They do not, however, do this in practice.<sup>2175</sup> They hardly evaluate the assets, liabilities, balance sheets, off-balance sheet items, accounting, governance, internal control, customer treatment and other performances of the banks, insurers and microfinance institutions against the macro-prudential criteria.<sup>2176</sup> They often focus their examinations on verification of transactions and regulatory compliance of the inspected institutions instead of assessing their risk management functions and future risk exposures.<sup>2177</sup> They do not also collect and make use of public information about the financial institutions in making their examinations. They also carry out their examinations very slowly.<sup>2178</sup> The absence of nationally defined accounting and auditing standards in

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2171 TGE, 1994, at arts. 16(1), 19 & 20(1); FDRE, 1995, at art. 77(4); and FDRE, 2008a, at art. 3(4-5). The NBE sometimes gives up its regulatory functions when the government wants to enforce measures on the government owned banks and insurer that are not compatible with its existing regulations. It does not also enforce some of its regulations on the government banks and insurer as seriously as on the private banks and insurers (Note the annual reports of some of the private banks and insurers regarding the complaint).

2172 FDRE, 2003c, at arts. 16 & 12ff. Most of the activities of the commission have, in practice, been dispute resolution (Note annual reports of the commission).

2173 NBE BSD, 2005, at p. 51; and NBE ISD, 2005, at p. 67 as revised.

2174 They have intended to assess the overall health and vulnerability of the financial institutions and their counter parties according to IMF recommendations. The IMF has recommended the use of macro-prudential and macro economic indicators, including aggregate banking data (i.e. aggregate capital adequacy, liquidity, asset quality, earning and profitability), aggregate borrower data (i.e. average debt-equity ratio, indebtedness, profitability, and market risk sensitivity of the borrowing sector), and macroeconomic data (i.e. overall economic growth, inflation, interest, exchange rate and external sector development) in making macro-prudential analysis of the financial institutions. NBE BSD, 2005, at pp. 3-4; and NBE ISD, 2005, at pp. 96 & 103-104 as revised.

2175 NBE BSD, 2005, at pp. 3-4, 35, 38-40, 42-44 & 61; and NBE ISD, 2005, at pp. 96 & 103-104.

2176 They don't also conduct on-site examinations regularly. NBE BSD, 2005, at p. 63; and NBE ISD, 2005, at pp. 57-58, 67-95 & 115-119 as revised.

2177 Their examiners often focus on assessment of the historical performance of the financial institutions. They examine samples of the reports of the institutions to the NBE and check the assets (as reported in the balance sheets), policies, procedures and management minutes of the institutions for regulatory compliance. The examiners of the banks attempt at evaluating the financial statements, capital adequacy, earning performance, fund management, internal control mechanism and risk exposure of the banks. Much of their focus has, however, been on the loan recovery performance of the banks. NBE BSD, 2005, at pp. 53-54, 57, 60 & 63; and NBE ISD, 2005, at p. 115 as revised.

2178 The banking supervision department, for instance, used to complete a single examination in about three months and a half while the insurance supervision department used to make it in about eight months. This was largely due to limited experience, skill and motivation of the staff of the departments, non-standardization of the processes, poor management and leadership of the departments, poor teaming culture in the departments, poor supply of facilities, and information

the country has also limited the adequacy of the accounting, internal control and external auditing of the financial institutions and disabled the supervision departments of the NBE from enhancing their off-site surveillance and on-site examination functions.<sup>2179</sup>

The NBE does not also enforce its penalties and corrective measures strictly although it, in practice, issues directives that subject the financial institutions to financial and non-financial penalties.<sup>2180</sup> Its supervision departments do not also discuss their off-site surveillance and on-site examination findings with the management of the financial institutions.<sup>2181</sup> It does not also regulate the saving institutions and cooperatives although it is authorized by law to promote the development and regulation of these institutions along with the formal financial institutions.<sup>2182</sup>

The competition enforcement organs have also limited their functions to adjudication of disputes in practice. They do not act proactively to promote competition as independent competition authorities.<sup>2183</sup>

The country, therefore, needs to refine the powers of both the NBE and the competition enforcement organs and that both the NBE and the competition enforcement organs need to eliminate their weaknesses. It needs to entrust the NBE with dispute adjudicating powers without, of course, ruling out the possibility of making recourse to the judiciary. It needs to indicate the measures the NBE should take during crisis situation and pay due attention to the international experience on reorganization and rehabilitation of a financial institution in crisis. It needs to establish the competition enforcement organs as independent competition authorities and entrust them with the complete powers of rule making, inspecting, examining, intervening, adjudicating and sanctioning. It needs to increase the leadership, operational and financial autonomy of both the NBE (as the financial market regulator) and the competition enforcement organs (as the general competition authorities) from the government.

It also needs to re-define the grounds for receivership of the banks and microfinance institutions. First, the 'pursuit of policy by a bank or microfinance institution that will endanger the general economic interest of the country or the public' is too general to be a cause for receivership. Its enforcement requires defining the general economic interest of the country or the public and testing whether the policy and practice of the concerned financial institution violates this interest. This is prone to interpretation and abuse. It needs to be made specific by

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delay by the inspected institutions. NBE BSD, 2005, at pp. 58, 59, 62 & 65; and NBE ISD, 2005, at p. 94.

2179 NBE BSD, 2005, at pp. 53-54 as revised.

2180 Directives No. SBB/20/96; SBB/14/96; SBB/24/99; SIB/14/96; SIB/19/98; SIB/27/2004; and MFI/14/2002. Also Degefe Duessa Obo, 2009, at pp. 207-208 for a general finding that the enforcement of the microfinance regulations is lenient even if the rule making is strict.

2181 NBE BSD, 2005, at pp. 56, 61-62 & 64; and NBE ISD, 2005 as revised.

2182 TGE, 1994, at art. 7(9); FDRE, 2008a, at art. 5(8); FDRE, 1996g, at art. 12(3); FDRE, 2009, at the preamble & art. 28(1); and annual reports of the NBE up to 2009.

2183 Note the discussion above and the unpublished annual reports of the organs.

defining the policies and practices that constitute danger to the country's economic interest or the public in the law itself. Secondly, the "pattern of unsafe and unsound practices that constitute significant danger to ... depositors" is too vague to be cause for receivership. It is also interpretable and prone to abuse. It needs to be narrowed by listing the practices that can constitute danger to the depositors. Thirdly, the cause of 'non-compliance with applicable laws, regulations and limitations imposed by the NBE' is too general to be ground for receivership. The country needs to refer only to the most serious violations that will lead to license revocation as it is only these that will matter. Fourthly, the causes of 'substantial dissipation of assets and incurring of losses that will deplete capital' are qualitative and difficult for enforcement. They need to be defined with quantitative indicators so that the level that will constitute substantial dissipation of asset or depletion of capital for purpose of the receivership measure can be known. Fifthly, the 'cessation of operation as a legally independent entity' is not clear to be ground for receivership. Either the features that lead to this conclusion need to be defined in the law or the ground has to be deleted.

The country does not also define the powers and functions of the securities and pension market regulators.<sup>2184</sup> It needs to institutionalise them as independent regulators and confer them with the following powers and functions among others by taking the international experience into account:

- rule making and adjudicating cases;
- inspecting, investigating and sanctioning abuse and violations;
- evaluating, preventing and correcting institutional failures;
- enforcing disclosure requirements;
- encouraging the making of ratings;
- keeping and publishing data about the market institutions and operations;
- conducting research;
- building their own capacities and the capacities of the market actors;
- advising the government on policy matters; and
- working with domestic and foreign regulators.<sup>2185</sup>

### 5.1.2.2 The New Roles

#### i. The International Experience

The financial market regulators and competition authorities around the world have been more reactive than proactive and were taken to be law enforcement bodies rather than contributors in the formulation of economic policy.<sup>2186</sup> Many of both the developed and the transition and emerging market countries have, however, developed interest in proactive approach and altered the roles of their financial regulators and competition authorities as crises, anti-competitiveness and

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2184 Note the discussion under the 'identity of regulators' subtitle above.

2185 Note also the discussion under the 'coordination between the organs' subtitle below.

2186 World Bank and OECD, 1999, at p. 8.

illegal actions recurred and market based systems grew.<sup>2187</sup> They have felt that the regulators and competition authorities need to be authorized to participate in the formulation of economic policies and to influence governments so that the latter will eliminate (or minimize) policies and interventions that adversely affect competition and the soundness of markets.<sup>2188</sup> They have also felt that the proper implementation of regulatory and competition objectives and laws requires the building of capacity and education of the government officials, the regulated market actors, the business people and the general public.<sup>2189</sup>

Many of them have, accordingly, made the financial market regulators and competition authorities responsible for the following functions on top of their traditional powers and functions:

- building their own capacities and the capacities of the financial markets and actors;
- advocating competition;
- attacking the adoption of institutional arrangements, government policies, public attitudes and private actions that interfere with the free market principle;
- fighting illicit behaviour and financing; and
- participating in the general formulation of economic policies.<sup>2190</sup>

Hence, many of the developed market countries have either expressly conferred the aforementioned powers and functions on their regulators and competition authorities or implied them from the existing powers and functions of the authorities.<sup>2191</sup> Many of the transition and emerging market countries have also found the importance of entrusting their regulators and competition authorities with the advocacy, market enhancing and crime fighting functions in their efforts to:

- promote privatisation;
- eliminate market concentration;
- reduce barriers to market entry and exit;
- discourage anticompetitive business practices;
- encourage pro-competitive government policies and interventions;
- control illicit activities;

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2187 World Bank and OECD, 1999, at pp. 8 & 93; OECD, 2004, at pp. 5 & 14-28; and Wellons, 1999, at p. 39.

2188 Ibid.

2189 World Bank and OECD, 1999, at pp. v & 99-100; and Pradeep S. Mehta, 2002, at pp. 80 & 84. The OECD has also often shown that the level of financial understanding and awareness of consumers has been low due to the increased sophistication of the financial markets and services and hence that the financial regulators and competition authorities need to make the building of public awareness among their priorities (OECD, 2005b; and OECD, 2008h).

2190 World Bank and OECD, 1999, at pp. v, 8 & 93; Wellons, 1999, at p. 39; Pradeep S. Mehta, 2002, at pp. 80 & 84; OECD, 2004, at pp. 5 & 14-28; and IAIS, 2005b, at p. 11.

2191 Pradeep S. Mehta, 2002, at p. 84; World Bank and OECD, 1999, at pp. 93-94; OECD, 2004, at pp. 5-6, 10-13 & 25; and Gerber, 2001, at pp. 10-11.

- educate consumers, the business community and policy makers on the uses of free market and competition;
- build public support for their reforms; and
- develop free markets.<sup>2192</sup>

Many have also found the usefulness of the aforementioned functions of the regulators and competition authorities to assist the carrying out of functions in non-financial policy.<sup>2193</sup> They have found their uses:

- in the area of trade policy formulation, to ensure that both policy makers and the public are fully informed of the benefits of liberalized trade, competition and consumer welfare;
- in the area of economic regulation, to ensure that competition rules are properly and consistently included in new legislation and regulation, that competition is promoted in industries that were considered to be monopolies such as the infrastructure industry, and that industry standards by government (such as safety and environmental standards and license requirements) are transparent, non-discriminatory and non-restrictive of competition;
- in the area of state aid, to eliminate government discrimination between domestic and foreign companies, state owned and private firms, and large and small enterprises so that there will be equal condition for all market operators;
- in the area of local governance, to eliminate conflict between government and citizen interests that may arise due to ownership of services by local government authorities as the competition authority may advocate privatisation; and
- in the area of privatisation, to ensure that the privatisation is not simply transfer of the position of market dominance from the public to private hands.<sup>2194</sup>

Hence, it is often felt that the regulators and competition authorities in the transition and emerging market countries need to be conferred with extensive proactive powers and functions so that they will have the legal base and firm responsibility to promote the development of free market and regulate both the governments and other groups that tend to restrain competition.<sup>2195</sup>

There is, however, also fear that the combination of the regulatory, advocacy and market enhancing functions may lead to conflict of interest in the regulators and competition authorities since the regulators and competition authorities may lose the neutrality they need to enforce regulation.<sup>2196</sup> Hence, it is also advised that the countries need to develop mechanisms for balancing between the different roles of the regulators and competition authorities.<sup>2197</sup>

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2192 Pradeep S. Mehta, 2002, at p. 84; World Bank and OECD, 1999, at pp. 93-94; Wellons, 1999, at p. 39; and IAIS, 2005b, at p. 11.

2193 World Bank and OECD, 1999, at pp. 94-99.

2194 *Id.*, at pp. 94-97.

2195 *Ibid.*

2196 This problem was observed in some countries like Indonesia in the 1980s (Wellons, 1999, at p. 39).

2197 *Ibid.*

The regulators and competition authorities are also advised to get public support for their regulatory and competition enforcement functions and to cooperate with other domestic and foreign regulators once they are entrusted with the functions of advocating competition, enhancing market and fighting illicit behaviour.<sup>2198</sup> They are also advised to cooperate with the international institutions including the G-7 Financial Action Task Force on Money Laundering (FATF) in their function of fighting illicit financing.<sup>2199</sup>

The 2008 financial and economic crisis has also shown that the risk prevention, stress testing and failure resolution functions and proactive roles of the financial market regulators need to be strengthened in order to ensure that there are sound, stable and efficient financial systems.<sup>2200</sup>

## ii. The Case of Ethiopia

Ethiopia authorizes the competition investigation commission to conduct professional studies and the department of the Ministry of Trade and Industry to exercise competition advocacy roles.<sup>2201</sup> It also makes the approach of its competition law enforcement both proactive and reactive.<sup>2202</sup> It, however, fails to make it clear if, on the one hand, the competition enforcement organs can participate in the formulation of general economic policy in order to control anti-competitive government decisions and, on the other, the NBE has to enforce its rules proactively, engage in the function of competition and regulatory advocacy, and stimulate the creation and development of the future securities market and private pensions.<sup>2203</sup> It does not also define the roles of the NBE fully in the fight against illicit financing.<sup>2204</sup> It needs to bridge these deficiencies.

2198 World Bank and OECD, 1999, at pp. 99-100.

2199 Yilmaz Akyüz, 2002, at pp. 53-55. Note also the discussion under the 'use of international cooperation' subtitle below.

2200 McIlroy, 2008; Marcelo, et al., 2008; Gert Wehinger, 2008; Gert Wehinger, 2009; Gert Wehinger, 2009a; Adrian Blundell-Wignall, et al., 2009; Christoph Ohler, 2009; J. Balvin Hannibalsson, 2009; García, 2010; OECD, 2009f; World Bank, 2009b; IMF, 2009; WTO, 2009; G-20, 2009; AP, 2009; AP, 2009a; AP, 2009b; AP, 2009c; and Bloomberg, 2010.

2201 FDRE, 2003c, at arts. 15(1)(f), 18(1)(d), 2(9) & 2(2).

2202 Id., at arts. 3, 15 & 16.

2203 The monetary and banking law expressly authorizes the NBE to disseminate the banking and insurance services in the country. It is, however, not clear if the law authorizes the NBE to promote the creation and development of the future securities market and private pensions. One can only rely on the authorization of the NBE to promote sound financial system and the inclusion of pension in the definition of long-term insurance to imply a role to the NBE that it should promote the development of formal securities market and private pensions. The involvement of the NBE in the formulation of economic policies is already made clear under the monetary and banking law. The Bank is expressly authorized to conduct economic studies and to participate in the formulation of financial, monetary, saving and exchange policies of the country although the government has the final say on these. The NBE and its supervision departments also intend to make their regulatory enforcement functions proactive. FDRE, 2003c, at arts. 15(1)(f) & 15(2); TGE, 1994, at arts. 6, 7(9) & 7(10); FDRE, 2008a, at arts. 4, 5(8) & (13); FDRE, 1995, at arts. 51(4), 55(10), 77(4) & 77(6); NBE BSD, 2005, at pp. 48, 50, 61 & 63-64; and NBE ISD, 2005, at pp. 106 & 115-119 as revised.

2204 It has introduced special enforcement machinery to enhance implementation of the criminal code provisions on money laundering and terrorist financing and recognized some roles to the NBE (regarding the issuance of directives on identification of customers and indication of the cautionary measures to be taken by the financial institutions) (FDRE, 2009d, at art. 3 - the NBE has also issued directive on identification of customer and due diligence of the banks: SBB/46/2010). It does not

It needs to require and fully empower the NBE to design and enforce its regulation proactively, promote and encourage financial market diversification (including the creation of the securities markets and private pensions), build its own capacity and the capacities of the financial institutions, raise regulatory awareness, advocate the importance of competition in the financial market (in cooperation with the competition organs), and work with national and international networks of cooperation in both systemic crisis prevention and the fight against illicit financing.<sup>2205</sup> It also needs to enhance the proactive and competition advocacy roles of the competition enforcement organs (in order to enhance enforcement of the competition policy) and authorize them to participate in the formulation of economic policies by the government (in order to check the consistency between the competition and other policies).

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empower and require it to act proactively and regulate the market by issuing directives that are consistent with recommendations of the international organizations. The monetary and banking and NBE establishment laws do not also authorize and require the NBE expressly to act proactively and regulate the financing of illicit activities (TGE, 1994, at art. 7; and FDRE, 2008a, at art. 5). The NBE has not also established mechanisms for controlling illicit financing. The country has, accordingly, relied more on the criminal law and prosecution system (which is usually reactive) than on the regulatory actions of the financial market regulator (which can be proactive and preventive).

2205 The NBE has in fact started to exercise some of these functions by implication from its existing powers. It has developed a Financial Sector Capacity Building Project in cooperation with the International Development Association (IDA) of the World Bank which focuses on building capacity of the NBE, strengthening the financial sector infrastructure of the country, developing new financial products, and enhancing the professional skills in the financial market of the country. The project is approved by the Board of Executive Directors of the World Bank on 22 June 2006 to be effective on 19 December 2006 and run for a period of three years as of 01 January 2007. The NBE capacity building component of the project focuses on development of the banking and insurance supervision; economic research, policy formulation and implementation; and other capacities of the NBE. The financial sector infrastructure component focuses on modernization of the payments, credit information and asset registration systems of the country and on development of capital market including government and corporate bond and stock exchange markets. It aspires to develop a national payments system framework (legal and institutional); to upgrade and automate the Addis Ababa clearing house; to introduce electronic payments system and credit cards; to strengthen the credit information centre at the NBE; to develop the regulatory and infrastructure framework for bond and equity markets; to develop depository, clearance and electronic settlement mechanisms for the bond and equity markets; and to improve the lending services and collateral system of the country. The financial products component focuses on the development of housing finance, leasing finance, small and medium enterprises finance, agriculture risk insurance, and venture capital fund for the country. The professional skills component focuses on introduction of continuing education, training and certification programs for professionals of the financial sector of the country; development of the research capacities of the professional associations in the financial sector of the country; and provision of training in banking, insurance and microfinance. (Note the information from website of the NBE accessed in September 2007 and August 2010). The country needs to strengthen these works of the NBE. It also needs to fully define the powers, functions and preventive roles of the NBE in the fight against illicit financing and require it to work on its own initiative (as the regulator of financing) as well as in collaboration with the domestic criminal law enforcement machinery and the international organizations. The special law of the country on money laundering and terrorist financing also recognizes the need for cooperation with the international community on the matter and this needs to be strengthened (FDRE, 2009d, at arts. 4 & 12-13).

### 5.1.3 The Coordination between the Organs

#### i. The International Experience

The traditional approach in most countries was to have financial market regulators separated by function.<sup>2206</sup> The internationalization and cross-sectoral integration of the financial markets have, however, called for regulatory neutrality and challenged the traditional approach in the 1990s and thereafter.<sup>2207</sup> Hence, three major models have been adopted to meet the need:

1. The majority of the countries have adopted integrated regulator model where the regulator combines jurisdiction over a range of institutions.<sup>2208</sup> The integration has ranged from one where any two of the banking, insurance, securities and pension market regulators are combined to one where all the regulators are combined to form a 'super regulator'.<sup>2209</sup>
2. Others have adopted a lead regulator model where one of the traditional institutional regulators takes the responsibility to coordinate the group of regulators and becomes a de facto conglomerate regulator. UK has followed this before the full integration of its regulators in 2001.<sup>2210</sup>
3. The third group of countries have followed a functional model where separate institutions regulate the competition, market conduct, asymmetric information and systemic stability functions across the banking, insurance, securities, pension and other markets. Australia is the most cited example for this. It has adopted the functional model since July 1998 by introducing the Australian Competition and Consumer Commission to be responsible for competition and consumer protection matters throughout the economy; the Australian Securities and Investments Commission to be responsible for the market integrity and consumer protection in the financial system; the Australian Prudential Regulation Authority to be responsible for the prudential soundness of all the deposit-taking, insurance and private pension institutions; and the Reserve Bank of Australia to be responsible for the stability of the financial system, the control of monetary policy and the payments system.<sup>2211</sup>

The Netherlands has followed a mixture of the integrated and functional models in its twin-peaks model by integrating the prudential regulation of all the financial institutions in the Central Bank and putting the regulation of quality of businesses (market conduct) of the financial institutions in the Authority for Financial

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2206 Note the discussion under the 'identity of regulators' subtitle above.

2207 Carmichael and Pomerleano, 2002, at pp. 37-41; and Carmichael, Fleming and Llewellyn, 2004, at pp. 2-6 & 30-32.

2208 Note the discussion under the 'identity of regulators' subtitle above; and Table 2(Chap. 5).

2209 Ibid.

2210 Table 2(Chap. 5); Carmichael and Pomerleano, 2002, at p. 42; Laboul, 1992, at pp. 34-38; and Wellons, 1999, at p. 34.

2211 Carmichael and Pomerleano, 2002, at pp. 44-47; Carmichael, Fleming and Llewellyn, 2004, at pp. 40-80 & 93-113; and Möschel, 1991, at pp. 29-31.

Markets for the reason that the two regulatory functions will conflict if assigned to a single regulator.<sup>2212</sup> The US has also included elements of the functional regulator model in the disintegrated regulatory structure.<sup>2213</sup> The super-regulators in the integrated model have also replicated the functional model when they establish their functional units.<sup>2214</sup>

Some of the countries have also adopted other mechanisms to meet the need. France has, for instance, recognized a right of pursuit to the banking and insurance regulators to enable them to examine the activities of the institutions affiliated to a bank or insurer under consideration.<sup>2215</sup> Others have used coordinating committees staffed with members of the concerned regulators or imposed requirements of harmonization, specialization and networking.<sup>2216</sup> Others have also tried to handle the matter by restricting the linkage in the market, by empowering the sectoral regulators to regulate aspects of the activities of the institutions that traditionally belonged to another sector according to rules of that other sector, or by requiring the exchange of information between the regulators.<sup>2217</sup>

The international experience has also shown the following lessons:<sup>2218</sup>

1. All the three models have advantages and disadvantages. The integrated regulator model has the advantage of addressing the problems of conglomeration and regulatory arbitrage. It, however, creates misconception among consumers that all financial services and products are regulated and supported alike. It does not also eliminate conflict between the objectives of

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2212 See Tables 1(Chap. 5); 2(Chap. 5); and the information from websites of the Central Bank of the Netherlands (De Nederlandsche Bank) and the Netherlands Authority for Financial Markets (DNB, 2010; and AFM, 2010, respectively).

2213 The Board of Governors of the Federal Reserve System, the Comptroller of Currency, the Federal Deposit Insurance Corporation, the Federal Trade Commission (for consumer protection matters), the state commercial banking regulators and the specialized regulators for the federal savings and credit institution, for instance, share the task of regulating banks. The State Commissions and Commissioners regulate the insurance industry and the Department of Defence regulates the sale of insurance to military installations. The Securities Exchange Commission regulates the securities market and the securities aspect of bankers' and insurers' investments. It also regulates the separation and unification of insurance, banking and securities businesses through Federal Acts. The Bureau of Competition of the Federal Trade Commission, the Antitrust Division of the Department of Justice, the Courts, and the special administrative forums to which the Federal Trade Commission may file competition cases also share the responsibility of enforcing the competition policies and laws. Carmichael and Pomerleano, 2002, at pp. 44-47; Carmichael, Fleming and Llewellyn, 2004, at pp. 40-80 & 93-113; Möschel, 1991, at pp. 29-31; Meier, 1988, at pp. 35-36; Caddy, 1986, at p. 1; and FTC, 2005.

2214 Many of the countries have retained the functional separations as departments while integrating them in one super-regulator (Carmichael and Pomerleano, 2002, at p. 46; Hall, 2003, at pp. 45-51 & 55; and Carmichael, Fleming and Llewellyn, 2004, at pp. 40-80).

2215 Laboul, 1992, at pp. 34-38. Germany and the Netherlands have also done this for the insurance regulator and UK and Denmark for the banking and insurance regulators during the time before the integration of their regulators (ibid.).

2216 France and Canada are examples. France has done the former and Canada the latter for the securities markets (Wellons, 1999, at p. 34).

2217 Laboul, 1992, at pp. 34-38.

2218 Carmichael and Pomerleano, 2002, at pp. 42-46; Carmichael, Fleming and Llewellyn, 2004, at pp. 2-15 & 17-263; Granlund, 2009; and OECD, 2009f.

sectoral regulatory functions and departments. The lead regulator model has the advantage of eliminating conflict of regulatory interest between the different regulators. It is, however, inadequate to address the problems of conglomeration and regulatory arbitrage since it does not achieve regulatory uniformity across institutions. The functional regulator model has the advantages of bringing same functions under one roof; allowing regulatory neutrality, specialization and efficiency; and minimizing regulatory arbitrage. It, however, also lets the financial actors to multiple functional regulators whose objectives and regulations are not entirely free from conflict. The integrated regulator model is, however, most favoured in practice for the reason that it is easier to handle inter-departmental conflicts within a regulator than conflicts between separate regulators. The integration outside the central bank is also most favoured for the reason that the central bank will be overwhelmed by the regulatory functions if the full integration is made in it.

2. The choice of appropriate regulatory structure is a function of the financial market development and specific context in a country despite the general trend towards the integrated regulator model.
3. The choice should not be between full integration and total fragmentation but from a spectrum of forms of integration.
4. The transition from the fragmented to the integrated regulatory structure requires time and careful planning.
5. The choice of particular regulatory structure should be based on the best way of achieving the objectives of regulation.
6. The new regulatory structure should be backed by change of legal framework, creation of strong governance structures, careful management of the working habits, skills and insecurities of staffs of the regulators, and enhancement of the communication mechanisms with stakeholders.

#### ii. The Case of Ethiopia

Ethiopia has followed the traditional institutional regulator model with an element of the functional model when, in the 1960s and 70s, it authorized:

- the NBE to control and regulate the monetary, credit and banking regimes and institutions;
- the Insurance Council and the Insurance Controller's Offices to regulate its insurers; and
- the Ministry of Commerce and Industry to enforce the competition law.<sup>2219</sup>

It followed the integration approach when it nationalized the financial institutions and authorized the NBE to supervise, control and direct the 'banks and other

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2219 IGE, 1963d; IGE, 1963e, at art. 7; IGE, 1970b, at arts. 4 & 5; and IGE, 1963g, at arts. 3(h) & 5.

financial institutions' under a national plan in 1976.<sup>2220</sup> It currently integrates the banking, insurance, and microfinance regulations in the NBE.<sup>2221</sup> It does not, however, integrate the competition law enforcement organs as it entrusts the responsibility of enforcing the competition policy and laws to the Secretariat in the Ministry of Trade and Industry, the Trade Practice Commission, and the regional legislative councils and trade bureaus.<sup>2222</sup> It does not also define the work relationship between the NBE as the financial market regulator and the competition enforcement organs.<sup>2223</sup> Its future securities market and pension regulators are not also institutionalised and located yet.<sup>2224</sup>

The integration of the financial regulators in the country is commendable in view of the limited regulatory capacity of the country and the international experience towards this. It will enable the country to unify the regulatory capacity building efforts without, of course, excluding the possibility of building specialized regulatory functions in the integrated regulator. It will also enable the country to deal with the less serious problem of inter-departmental regulatory conflict instead of the more challenging inter-regulatory-agency conflict. It will also ease the future effort of the country to deal with financial conglomeration and regulatory arbitrage.<sup>2225</sup>

Whether the integration has to be done within or outside the NBE is, however, pending issue. The integration within the NBE is justified by:

- the responsibility of the NBE to manage the monetary policy objectives of the country and the role of financial regulation to transmit these policy objectives,
- the need to coordinate between the objectives of monetary policy and the other objectives of financial regulation,
- the infancy of the current financial market of the country, and
- the facilitation the NBE can make in the institutionalisation and growth of the different segments of the financial market as regulator and central bank.

The integration of the regulatory functions in the NBE can also be more beneficial than the other models if the financial system of the country continues to be bank-dominated.

The country, however, needs to consider the case for integrated financial market regulator outside the NBE as housing all the financial regulatory objectives and functions in the NBE is likely to burden it with more functions than its functions as central bank. The integration of the functions outside the NBE will also be

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2220 PMGE, 1974d; and PMGE, 1976i, at arts. 3, 6, 43, 44-50 & 61-67.

2221 TGE, 1994, at art. 7(4); FDRE, 2008a, at art. 5(7); TGE, 1994a; FDRE, 2008b; TGE, 1994b; FDRE, 1996g; and FDRE, 2009.

2222 FDRE, 2003c; and note the discussion under the 'identity of the organs' subtitle above.

2223 FDRE, 2008a; and FDRE, 2003c.

2224 Note the discussion under the 'identity of the organs' subtitle above.

2225 These are likely to be regulatory issues when the country recognizes cross-sectoral market integration and international liberalization of the financial markets in the future. Note also the discussions under the 'market entry and exit' and 'functional and ownership separation' requirements subtitles of the banking, insurance and microfinance chapter above.

beneficial approach if the country chooses to foster competing markets including the securities market and private pensions in the future. The decision has, however, to be made as a matter of value and experiential judgment based on the future financial development, legislative environment and range of regulatory responsibilities and skills.<sup>2226</sup>

The country also needs to form its competition enforcement organs as independent federal and regional competition authorities that will cooperate and work together and with the integrated financial market regulator. It need not integrate the financial market regulator and the competition enforcement authorities as the roles of the latter surpass the financial market to address the competition situation in the other sectors. It only needs to make the integrated financial market regulator responsible for the enforcement of the competition objective in the financial market and define the work relationship and coordination between the financial market regulator and the competition enforcement organs.

## 5.2 The Sanctions

### 5.2.1 Administrative Sanctions

#### i. The International Experience

Both regulatory and competition enforcement are followed by administrative (regulatory), civil and criminal sanctions.<sup>2227</sup>

The administrative (regulatory) sanctions often include a range of measures indicated by law and enforced by the regulator or the competition authority.<sup>2228</sup> Most of the countries use the following measures:

- formal warning,
- pressure on the management of the affected financial institution through public disclosure of intended measures,
- interim orders (short of prohibition of certain conduct),
- cease and desist orders,
- administrative fine,
- removal of chief executives,
- takeover of management,
- cancellation of membership of the concerned financial institution from associations and fund guarantee schemes, and
- cancellation of licenses.<sup>2229</sup>

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2226 This is also the internationally recommended approach (Carmichael and Pomerleano, 2002, at pp. 47-48).

2227 Möschel, 1991, at pp. 113-114; Pfennigstorf, 1996, at pp. 60 & 138-141; Wellons, 1999, at pp. 54-58; World Bank and OECD, 1999, at pp. 53-56; and IAIS, 2005b.

2228 Most of the countries leave substantial discretion on the choice of the particular measure to the regulator or the competition authority. Ibid.

2229 Ibid.

They also recognize the enforcement of regulation through mediation and arbitration (when the problem is between regulated parties).<sup>2230</sup> The use of these powers, however, depends on the balance adopted between the administrative, civil and criminal enforcement approaches and the overall legal structure and culture in a country's legal system.<sup>2231</sup>

A number of the countries also subject anti-competitive mergers and abuse of dominant positions to structural and behavioural measures of the competition authority.<sup>2232</sup> The structural measures include:

- prevention of the merger, and
- dissolution or break up of the merged entity or partial divestiture of its assets and operations to the extent that will eliminate the anti-competitive effect when the merger has already occurred.

The behavioural measures include orders that regulate or modify the conduct of the merged firm to prevent the feared anti-competitive effect such as the following:

- order to supply a product or to serve a certain class of customers for a period of time,
- order to refrain from entering into certain types of contracts,
- order not to raise prices by more than a specified amount for a period of time, and
- order that the merged enterprise licenses a relevant portion of its technology to other firms as a means of introducing new competition.

The countries usually prefer the structural measures to the behavioural in their regulations of mergers. They recognize the difficulty to undo a merger once it has occurred and follow a “fix-it-first” policy – i.e. *a policy that the care should be implemented before consummation of the proposed merger*. Hence, their merger laws and competition authorities usually require pre-merger notification to the competition authority so that the latter can investigate and make decision before rise of the complication.<sup>2233</sup> The notification requirement, however, also differs from country to country depending on the economic and political objectives the countries want to address.<sup>2234</sup> Many of the countries usually consider large mergers above a certain threshold (as defined by the law or their regulators) to be dangerous and,

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2230 Ibid.

2231 Hence, some like Japan used to rely on mediation, arbitration and administrative guidance more than others while some like USA and UK used to provide wide opportunity for regulators to obtain court orders for the regulatory enforcement purposes. Others like Malaysia also used to empower the regulators to investigate and prosecute market related crimes without going to court provided that they obtain consent of the public prosecutors office. The other transition and emerging market countries have increasingly relied on the use of administrative sanctions. Ibid.

2232 They often subject anti-competitive agreements to criminal sanctions. World Bank and OECD, 1999, at pp. 53-56 & 70.

2233 Id., at p. 56.

2234 Ibid.

hence, to be notified to the competition authority.<sup>2235</sup> Their merger control laws also often determine the scope of application of the notification requirement, specify the content of the notice, and allow further investigation by the competition authority when the latter feels necessary.<sup>2236</sup>

## ii. The Case of Ethiopia

Ethiopia authorizes the NBE to take the following measures against the banks, insurers and microfinance institutions when it finds that they have violated regulation:

- propose corrective actions to be implemented by them;
- order the dismissal of their directors and officers;
- prohibit them from accepting new deposits and policy subscriptions;
- prohibit them from opening new branches;
- suspend the whole or part of their businesses temporarily;
- put them under receivership or takeover process; and
- impose financial sanctions on them.<sup>2237</sup>

It subjects the anticompetitive agreements, practices and abuse of market dominance to administrative measures of the Ministry of Trade and Industry and the Trade Practice Commission and authorizes the Ministry and the Commission to:

- impose financial penalties;
- suspend, correct or eliminate the anticompetitive practice in question;
- suspend or cancel the business license of the violator; and
- take measures that will reinstate the competitive position of the victims.<sup>2238</sup>

It leaves the choice of particular sanction to the NBE and the competition organs.

It also prohibits the making of merger between the financial institutions without prior approval of the NBE and authorizes the NBE to sanction violators of this

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2235 Ibid.

2236 The matters they require to be notified often include the names and address of the parties, the description and timing of the merger transactions, the financial situations of the firms, the organizational and ownership structures of the firms, the descriptions of the products and services of the firms, the descriptions of the relevant markets served by the firms, the description of the market share of the firms, the reasons and expected benefits of the merger, and the documents prepared for the corporate decision makers. *Id.*, at pp. 56-57.

2237 TGE, 1994a, at arts. 20(3) & 22-25; FDRE, 2008b, at arts. 31, 33ff & 58; TGE, 1994b, at arts. 26(4) & 27-28; FDRE, 1996g, at art. 24; and FDRE, 2009, at arts. 18(7), 19 & 25. The NBE has also subjected the banks, insurers, microfinance institutions and insurance intermediaries to financial penalty for failure to comply with its directives (Directives No. SBB/14/96; SBB/20/96; SBB/24/99; SIB/14/96; SIB/19/98; SIB/21/2001; SIB/27/2004; SIB/29/2007; and MFI/14/2002).

2238 FDRE, 2003c, at arts. 15(2), 25, 26 & 27.

by the measure of receivership or takeover and its general regulatory enforcement and sanctioning powers.<sup>2239</sup>

The aforementioned measures of the country are commendable since they enable the NBE and the competition enforcement organs to be flexible in their enforcement of the sanctions. Both the NBE and the competition enforcement organs are, however, reluctant in their use of the sanctions to enforce regulation. They need to improve on this.

The country also needs to define the measures the future securities and pension market regulators can take against the securities market and pension operators during regulatory violation and crisis. It also needs to scale the measures and leave discretion to the regulators on the choice of particular measure as these are done in respect of the banking, insurance and microfinance markets.

## 5.2.2 Civil Sanctions

### i. The International Experience

Many of the countries subject the regulated institutions that violate regulatory and competition laws to civil liabilities within the general regime of extra-contractual liability. They, in principle, impose extra-contractual liability on ground of fault and include violation of any law, hence violation of any regulatory or competition rule, in the definition of fault as long as that is done intentionally or with negligence.<sup>2240</sup> Accordingly, they entitle all third parties whose interest is damaged due to regulatory or competition law violation to claim compensation from the regulated institutions through individual or class action suits.<sup>2241</sup> They take this as means of both sanctioning the regulated institutions and consumer protection.<sup>2242</sup>

The use of private civil suits is useful in regulatory enforcement when regulators lack the resource and market information necessary to enforce regulation and when countries want to limit the hands of their governments and encourage powerful players in the market to be active in the enforcement of regulation.<sup>2243</sup> Most of the transition and emerging market countries, however, rely little on it and the lack of data to meet burden of proof requirements, the weakness of the institutions to make it work (including the courts) and the underdevelopment of

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2239 TGE, 1994a, at art. 27(2)(a); FDRE, 2008b, at arts. 3(3)(c), 31, 33(1)(n) & 58; TGE, 1994b, at art. 40; FDRE, 1996g, at arts. 13 & 17(1); and FDRE, 2009, at arts. 17(1) & 19(1)(j). Note also the discussions under the 'market entry and exit requirements' and 'competition regulation' subtitles of the banking, insurance and microfinance chapter above.

2240 Tunc, 1974; Widmer, (ed.), 2005; Gordley, 2006; and Boom, et al., (eds.), 2007.

2241 Some like the US recognize class action law suits. David Smith and Su Sun, 2001, at p. 3.

2242 Ibid.

2243 David Smith and Su Sun, 2001, at p. 3; and Wellons, 1999, at pp. 50-52. Some like the US use it for the second reason (Möschel, 1991, at pp. 113-115 & 118-120; Pfennigstorf, 1996, at pp. 62-63; and Wellons, 1999, at pp. 50-52).

the corporate governance, extra-contractual liability and consumer protection regimes that can protect individuals are said to have contributed to this.<sup>2244</sup>

The countries that use private civil suit for regulatory enforcement allow it to be exercised against the regulated institutions.<sup>2245</sup> They do not allow it against the regulators and competition authorities since they believe that the main concern of regulation and competition law is protection of consumers as a group and, hence, that the decisions of the regulators and competition authorities are in the realm of public interest which should be controlled through judicial review and other control mechanisms instead of through individual civil suit.<sup>2246</sup>

## ii. The Case of Ethiopia

Ethiopia makes violation of any law, including the regulatory and competition law rules, civil fault when it is done intentionally or as a result of negligence.<sup>2247</sup> Hence, it makes all the regulated financial institutions liable for compensating the losses that may arise from violation of regulatory and competition law rules and individuals can lay claims against these institutions in the courts.<sup>2248</sup>

The country does not, however, make it clear if individuals can claim compensation from the financial regulator and competition enforcement organs. One can argue on the basis of the existing extra-contractual liability law, which makes any violation of law a civil fault, that such claim is possible as long as the regulator and competition enforcement organs have violated law. An opponent can also argue, based on the regulatory discretion left to the regulator and the competition enforcement organs and the international experience, that such claim should not be recognized against them as long as they are making their decisions for the public interest. The position on the issue needs to be taken based on the nature of the extra-contractual liability law of the country and the scope of authorization and discretion left to the financial regulator and competition enforcement organs. The extra-contractual liability law does not exclude institutional violators in defining the concept of fault.<sup>2249</sup> The laws establishing the financial regulator and the competition enforcement organs do not also let them to act outside the bound of the law under guise of public interest.<sup>2250</sup> Hence, the financial regulator and the competition enforcement organs are likely to be subject to individual suit for extra-contractual liability. The establishment of mental responsibility is, however, also difficult to make the institutions liable.<sup>2251</sup> The

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2244 Some like Korea, Taiwan, Bulgaria, Kazakhstan, China, Kenya and Zambia have, however, used private civil suits to enforce regulation. *Ibid.*

2245 Möschel, 1991, at pp. 113-115 & 118-120; Pfennigstorf, 1996, at pp. 62-63; and IAIS, 2005b, at pp. 48-49.

2246 *Ibid.*

2247 IGE, 1960a, at arts. 2035 & 2029.

2248 *Ibid.*

2249 *Ibid.*

2250 They define the scope of powers and functions of the institutions and limit their discretions up to the defined powers and functions. They do not allow them to make their mandates limitless although they recognize discretion. TGE, 1994; FDRE, 2008a; and FDRE, 2003c.

2251 Note the discussion under the 'critique' subtitle below.

country needs to set clear rule on the question, allow individual tort action against the financial regulator and the competition enforcement organs when the latter violate the scope of their discretion, enhance the protection of consumers, and encourage the participation of individuals in the control of proper enforcement of regulation.<sup>2252</sup>

### 5.2.3 Criminal Sanctions

#### i. The International Experience

A number of the countries subject serious violations of their financial market regulations and cartel agreements to heavy criminal sanction.<sup>2253</sup> They subject non-cartel agreements to criminal sanction when there is good reason, on balance, to believe that they are seriously harmful to competition.<sup>2254</sup> They often exclude the use of criminal sanction from the measures against abuse of market dominance and merger for a reason that firms often engage in these without criminal or anti-competitive intent.<sup>2255</sup>

The criminal sanction, when imposed, normally forms part of the general criminal law and requires the fulfilment of the material, legal and mental requirements of the latter. Criminal law normally requires that:

- there is action or omission by a person capable of bearing criminal responsibility (material element);
- there is law that makes the action or omission crime or petty offence at the time of its happening (legal element); and that
- the actor has intended or was negligent at the time of action (mental element).<sup>2256</sup>

Hence, the civil law countries subject the regulatory criminal sanctions to the general principles of incrimination under their criminal laws while the Anglo-American countries have introduced some strict liability cases that can be prosecuted without the requirement of mental responsibility since the late nineteenth century.<sup>2257</sup> The use of criminal sanctions for regulatory and competition law enforcement is also praised for its more severity and deterrence than the civil sanctions.<sup>2258</sup>

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2252 This will not be against the BCBS and IAIS core principles which expect that regulators need to be given legal protection in order to encourage their enforcement of regulation since the BCBS and IAIS do not also expect that the regulators will be allowed to act beyond the bounds of their legal authorizations. BCBS, 2006, at Principles 1(1) & 1(5); and IAIS, 2003, at Principles 1, 2 & 3.

2253 Möschel, 1991, at pp. 35, 113 & 115; Pfennigstorf, 1996, at pp. 137-138; World Bank and OECD, 1999, at p. 24; David Smith and Su Sun, 2001, at p. 2; World Bank, 2002, at pp. 140-141; OECD, 2004, at pp. 5 & 28; and Wellons, 1999, at p. 47. USA, China and Romania are prominent examples for the use of the criminal law machinery to enforce regulation.

2254 World Bank and OECD, 1999, at pp. 29-31.

2255 *Id.*, at pp. 53-56 & 83-84.

2256 Williams, 1961; Allen, 2005; Fletcher, 2007; Ashworth, 2006; and Ormerod, 2008.

2257 *Ibid.*

2258 Wellons, 1999, at p. 47; and Allen, 2005, at pp. 99-113.

## ii. The Case of Ethiopia

Ethiopia also requires fulfilment of mental, material and legal elements of incrimination to establish all kinds of criminal liability.<sup>2259</sup> It also requires that the sanctions have to take into account the degree of guilt of the criminal.<sup>2260</sup> It applies these principles on all incriminating clauses even if these are not in the Criminal Code itself unless express exception is made in the laws that incorporate the incriminating clauses.<sup>2261</sup> It also makes regulatory contraventions petty offence (except in cases where the criminal law makes them ordinary crime) and applies both the intention and negligence elements on them (except when the particular criminal law expressly excludes the negligence element). It also includes several incrimination clauses relating to the financial market in both the ordinary crimes and petty offences parts of the criminal code and the competition, banking, insurance and microfinance supervision laws and directives without excluding applicability of the general criminal law principles.<sup>2262</sup> Hence, the authorities that sanction the crimes indicated in the banking, insurance, microfinance and competition laws of the country need to establish the mental, material and legal elements of the criminal law.

### 5.2.4 The Problem with the Civil and Criminal Sanctions and the Solution

#### i. The International Experience

The use of civil (extra-contractual liability) and criminal sanctions to enforce regulatory and competition rules faces several problems.<sup>2263</sup>

First, both regulatory and competition laws require only wrongful act and make mental responsibility irrelevant since both are result of *mala prohibita* (specific prescription).

Secondly, both types of laws predominantly apply to business entities and make the proof and location of responsibility within the corporate structure difficult. The use of both tort claim and criminal sanction to enforce regulation also faces the problem of locating the responsible person in the market such as in the case of money laundering.

2259 It allows the establishment of ordinary crimes in principle based on intention (and exceptionally based on negligence when the criminal law expressly makes negligence ground for criminal responsibility). It allows the establishment of petty offences based on both intention and negligence in principle (unless the law expressly excludes the negligence element from being ground for liability). It also backs the rules by the principle of “presumption of innocence until guilt is proved”. IGE, 1957, at arts. 23, 57, 59, 690-692 & 697 (as amended by FDRE, 2005); and FDRE, 1995, at art. 20(3).

2260 IGE, 1957, at art. 86 (as amended by FDRE, 2005).

2261 Id., at arts. 3 & 690 (as amended by FDRE, 2005).

2262 IGE, 1957, at arts. 354-365, 671-673, 689 & 742-743 (as amended by FDRE, 2005); TGE, 1994, at art. 59; FDRE, 2008a, at art. 26; TGE, 1994a, at arts. 7(2), 8, 16(3), 16(4), 21 & 29; FDRE, 2008b, at art. 58; FDRE, 1996g, at art. 24; FDRE, 2009, at arts. 25 & 28(1); FDRE, 2003c, at arts. 26-27; SBB/20/1996; SIB/14/1996; and MFI/14/2002.

2263 Ogus, 1996, at pp. 79-89; and Wellons, 1999, at pp. 48-56.

Thirdly, contraventions of regulatory and competition rules cannot be sanctioned in the way criminal and civil liabilities are normally sanctioned. The criminal sanction of imprisonment is of no use when the violator is a business firm and the civil sanction of compensating losses may not have any punitive effect on the firms and individuals since they may act after working out the cost-benefit of their actions.

Fourthly, the use of criminal law suffers from being:

- heavy-handed when regulatory infractions are modest;
- too simplistic when sophisticated financial scams are involved;
- cumbersome when regulatory speed is necessary;
- inflexible when regulators and competition authorities want it to be implemented in a way that will promote their objectives;
- general when regulators and competition authorities require it to locate and deter specific infractions; and
- reactive when regulators and competition authorities need to implement specific preventive and proactive measures.

Fifthly, the use of both sanctions may be constrained by lack of sufficient knowledge of the sophistication involved in financial regulation and competition matters by the judges and prosecutors.

The solution adopted for the first problem has usually been to use separate terminology and procedure for the ordinary crimes and the regulatory and competition law offences.<sup>2264</sup> The solutions adopted for the second (i.e. the problem of proof and locating responsibility within the corporate structure) have been one of three:

- implicating the brain of the physical person acting on behalf of the business entity into the entity itself;
- excluding the notion of mental responsibility and adopting strict liability; or
- compromise between the two by recognizing prima facie strict liability for a proved action or omission and allowing defences that make the conduct lawful.<sup>2265</sup>

The solution adopted for the third has been using instruments other than those used in the mainstream criminal law, such as fines, court injunctions and orders, for regulatory and competition law enforcement.<sup>2266</sup> The solutions to the fourth and fifth problems have been a matter of effective coordination between the enforcement organs.<sup>2267</sup> The solution for the problem of locating the responsible person in the market such as in the case of money laundering has also been a matter of developing the criminal tracing mechanism.

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2264 Ogus, 1996, at pp. 80-81.

2265 Ogus, 1996, at pp. 81-86; and Allen, 2005, at pp. 112-113.

2266 Ogus, 1996, at pp. 87-89.

2267 Wellons, 1999, at pp. 48-56.

Two additional solutions have also been used sometimes to solve the problems.<sup>2268</sup> One is the injection of redistribution and correctional goals into the policies and processes of the regulatory and competition law systems by imprisoning corporate managers whose corporate strategy resulted in great harm.<sup>2269</sup> Another is the adoption of ‘corporate probation’ instead of individual criminal liability so that the corporate entity is monitored and advised through officials appointed by courts or be subject to duty to issue shares to the government equivalent to the cash fine (that would be imposed on it) under assumption that the shareholders of the entity will hate this measure and activate the managers to ensure regulatory compliance.<sup>2270</sup>

The decision on use of strict criminal and tort liability to enforce regulation has, however, also been a matter of value judgment based on socio-economic and political context. The major concern of the continental legal systems has been legal protection while the common law systems were concerned with the balancing of the interests of ensuring compliance to regulation and legal protection.<sup>2271</sup> The design of sanctions for regulatory violation has also been a function of ideology. The capitalistic ideology that encouraged entrepreneurial spirit and individualism has led to less strict civil and administrative punishment for fear of discouraging those values (as it has been the case in the UK) while the ideology that encouraged collectivism (or looked for severe deterrence) has considered regulatory violations as violations against the state interest which lead to strict criminal sanction (as it has been the case in China, USA and Romania, for instance).<sup>2272</sup>

The problem with the civil sanction has also been less serious than the problem with the criminal law sanction tool. Tort law has historically been more liberal than criminal law in terms of its grounds and strict liability principles are more easily adopted in the notion of tort than in the notion of crime.<sup>2273</sup> The aim of tort law is also making loss good and this aim matches with the consumer protection goal of regulatory and competition law enforcement.

Some have also found that the use of criminal and tort laws to stop white collar crimes in the financial services sector (including money laundering, market manipulation and insider dealing) has been only symbolic due to both the problems in the nature of the two laws and the reluctance of enforcement organs of the countries.<sup>2274</sup> Hence, countries have been advised to:

- refine their national solutions to the incompatibility between the criminal and tort law sanctions and the regulatory and competition law rules;
- reduce the reluctance of their enforcement organs; and

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2268 Ogus, 1996, at p. 97.

2269 *Id.*, at p. 97.

2270 These have been tried in the UK. *Id.*, at pp. 97-98.

2271 Ogus, 1996, at pp. 79-89; and Fletcher, 2007.

2272 ONG and Baxter, 1999, at pp. 102-103; Wellons, 1999, at p. 47; and Fletcher, 2007.

2273 Hall, 1943, at pp. 986-995.

2274 Gilligan, 1999, at pp. 101-161 & 163-209.

- increase their international cooperation for enforcement of regulation.<sup>2275</sup>

The 2008 financial and economic crisis has also shown the need for strengthening regulatory enforcement and avoiding reluctance in the exercise of regulatory discretion by the regulators in order to prevent abuse and crisis.<sup>2276</sup>

## ii. The Case of Ethiopia

Ethiopia also needs to be considerate of the problems criminal and tort sanctions face in connection with regulatory and competition law enforcement. It needs to balance between the need for:

- i) ensuring compliance to its regulatory and competition rules through adoption of strict criminal and tort liability, and
- ii) legal protection of defendants through recognition of basic human rights (such as the presumption of innocence until fault is proved).

It, of course, needs to ensure strict compliance to its regulatory and competition laws in order to meet the demands of its transition to market economy if not for the sake of ideology. This begs for adoption of strict criminal and tort liability regime for the regulatory and competition law contraventions. Strictness may, however, also result in uncertainty and frustration among the business entities and adversely affect their efficiency. Legal protection is also equally important. The regulatory and competition laws can, however, also be defeated if guilt has to be proved beyond doubt to sanction them for sake of ensuring legal protection. Proving the existence of guilt beyond doubt is difficult in Ethiopia partly because of the very difficult nature of proving the mental situation behind contravention of regulatory and competition laws and partly because of the less advancement of the machinery and techniques for collection of evidence in the country.

Hence, it needs to do the balancing by:

- limiting the use of criminal law and its guilt requirement to the most serious contraventions;<sup>2277</sup>
- making the imprisonment of corporate managers, fine and forced closure of business the main forms of criminal sanction for the most serious contraventions (since corporate probation is not feasible in the current legal situation of the country);
- making all the regulatory and competition law contraventions civil fault that will result in strict civil (tort) liability without need to prove mental situation;
- subjecting the majority of the regulatory and competition law contraventions to strict administrative (regulatory) sanction; and
- subjecting the regulatory and administrative sanctions to judicial review for the reason of legal protection.<sup>2278</sup>

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2275 Id., at pp. 183-209.

2276 García, 2010.

2277 Degrees of contravention may be defined by taking into account the impact or importance of the contravention to the regulatory and competition law objectives.

2278 Most of the transition and emerging market countries have also recognized the use of regulatory and competition enforcement organs with substantial administrative powers since this offers great

### 5.3 The Legal Protection against Regulatory Flaw

#### 5.3.1 The Ground for Protection

##### i. The Theory and International Experience

The enforcement of regulatory and competition rules needs to be governed by statutory goals and principles. It needs to be limited by substantive and procedural laws and principles as public policy and action should pay respect to the law in a legal system and public discretionary power is not absolute freedom but legal commission to serve the public interest after balancing with citizens' interests. Hence, countries often require their regulators and competition authorities to adhere to general principles of administrative law and account financially, substantively and procedurally.<sup>2279</sup> They require them:

- financially, to meet standards of financial management to achieve productive efficiency (i.e. to maximize their outputs relative to the costs of their inputs);
- substantively, to make their rules and decisions within the bounds of the economic and social objectives of regulation and to justify them by public interest goals; and
- procedurally, to make their actions according to principles of administrative law, resist undue influences of market actors, and balance the public interest behind the regulatory and competition systems with the private interests.<sup>2280</sup>

The 2008 financial and economic crisis has also shown the need for strengthening transparency, accountability and liability of the financial market regulators.<sup>2281</sup>

##### ii. The Case of Ethiopia

Ethiopia also subjects the regulators and competition authorities to general principles of administrative law. The current regime of the country is, however, incomplete.<sup>2282</sup>

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flexibility and speed in enforcement, allows to enhance enforcement skills, and increases the chance to protect the fragile infant markets from abuse. They have, however, also seen the undesirability of concentrating too much power in the regulator and the importance of using the judicial review mechanism to mitigate strict sanctions although they also happen to have less powerful courts. Some have also recommended the use of proactive preventive enforcement (instead of reactive criminal and civil enforcement) as alternative to the use of the 'strong regulatory power vis-à-vis judicial review' approach. Note the discussion under the 'powers and functions' subtitle above; and Wellons, 1999, at pp. 57 & 58.

2279 Pierce and Gellhorn, 1994, at p. 10; Pfennigstorf, 1996, at p. 60; Möschel, 1991, at p. 114; and Ogus, 1996, at pp. 22 & 111.

2280 Ibid.

2281 Dempegiotis, 2008; OECD, 2009f; Dijkstra, 2009; and Dijkstra, 2010.

2282 Note the discussions under the following subtitles.

### 5.3.2 The Means of Protection

#### 5.3.2.1 Control by the Legislature and Chief Executive of Government

##### i. The Theory and International Experience

As technical operators in a democratic society, regulators and competition authorities have to account to the public through the legislature and chief executive of government although they should enjoy operational and financial autonomy. Hence, the law makers and chief executives of governments of the many countries define the powers and functions, lay down the policies, frame the organizational structures, and state the standards of actions of the regulators and competition authorities by law and exercise political control over their operations based on the powers delegated to them.<sup>2283</sup> The law makers control them through their legislative, budgeting and hearing powers while the chief executives of government do this through their administration and policing powers based on the constitutional system of delegation of powers and checks and balances.<sup>2284</sup>

##### ii. The Case of Ethiopia

Ethiopia also subjects both the financial regulator (the NBE) and the competition enforcement organs to legislative as well as executive control. It:

- defines their establishment, organization, powers and functions by law of the legislature;
- puts the NBE under control of the Prime Minister and the Council of Ministers;
- puts the competition enforcement organs under control of the Ministry of Trade and Industry; and
- subjects both the NBE and the competition enforcement organs to annual calls of the legislature.<sup>2285</sup>

These are good in terms of control of the regulator and competition enforcement organs. They do not, however, balance between autonomy and accountability. The country needs to redefine them in order to increase independence of both the NBE as the financial market regulator and the competition enforcement organs from the executive in government and indicate the grounds and mechanisms of their accountabilities to the legislature and the chief executive of government.

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2283 Pfennigstorf, 1996, at pp. 58-61 & 136-138; Möschel, 1991, at pp. 25-32; OECD, 2004, at pp. 25-26; David Smith and Su Sun, 2001, at p. 1; and Pradeep S. Mehta, 2002, at p. 82.

2284 Ibid.

2285 TGE, 1994, at arts. 3-23; FDRE, 2008a, at arts. 3(4)-(5) & 24; FDRE, 1995, at arts. 55(17) & 77(4); and FDRE, 2003c, at arts. 12, 15(2) & 16.

### 5.3.2.2 Control by Courts

#### i. The International Experience

Many of the countries that have developed or are developing administrative law tradition also exercise legal control over the operations of their financial market regulators and competition authorities through judicial review despite difference on technicalities.<sup>2286</sup> They often define the concept of administrative act widely to include quasi-legislation, delegated legislation, policy rule and regulatory action, decision or contract and make the general legal remedies behind administrative acts available against the financial market regulators and competition authorities although they vary regarding the review power they entrust to the courts.<sup>2287</sup> They, however, apply the rules of judicial review to the financial market regulators and competition authorities with modifications inspired by the concepts of "public interest in acceleration of proceedings" (which means that the use of the remedies should not suspend the effect of regulatory decisions unnecessarily) and 'legal certainty' (which means that the review of the merits of certain regulatory measures has to be either severely limited or excluded since financial market regulation and competition promotion have quasi-political character).<sup>2288</sup>

The review is often carried out by:

- the ordinary courts of law in the countries that follow unique system;
- specialized administrative courts or tribunals in the countries that follow dual court system; and
- both the ordinary courts and specialized administrative courts (or tribunals) in the countries that follow hybrid system.<sup>2289</sup>

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2286 Several of them (including United Kingdom, Austria, Germany, Switzerland, Portugal, Denmark, Finland, Sweden, France, Italy, Spain, Greece, Cyprus, Turk, Azerbaijan, Belarus, Bulgaria, Chechnya, Croatia, Czech Republic, Estonia, Georgia, Bosnia and Herzegovina, Hungary, Kazakhstan, Poland, Romania, Russia, Slovakia, Slovenia, Serbia and Montenegro, China, Taiwan, Thailand, Vietnam, India, Indonesia, the Philippines, Iran, Bahrain, Qatar, Yemen, Egypt, Tunisia, Angola, Cameroon, Cape Verde, Congo (Brazzaville), Ghana, Equatorial Guinea, Guyana Republic, South Africa, Argentina, Brazil, Chile, Costa Rica, Cuba, Dominican Republic, Antigua and Barbuda, Haiti, Jamaica, Paraguay and Suriname) expressly provide for the judicial review of administrative (and regulatory) actions in their constitutions (See the constitutions of the countries accessed through the Constitution Finder database of the T.C. Williams School of Law of the University of Richmond available at <http://confinder.richmond.edu/>). Many of the others allow the judicial review of actions of the financial market regulators and other authorities without having express provisions for this in their constitutions (Möschel, 1991, at pp. 118-120; Pfennigstorf, 1996, at p. 60; Pradeep S. Mehta, 2002, at p. 82; Wellons, 1999, at pp. 57-58; Weber, 1997, at pp. 237-238; and Solomon Abay, 2001). The European competition regime also allows the review of actions of the European Commission and the national competition and regulatory authorities by the Court of First Instance of the Union and the National courts, respectively, and the making of appeals from the Court of First Instance of the Union and the national courts to the European Court of Justice on questions of law (Whish, 2001, at pp. 50-52).

2287 Möschel, 1991, at pp. 118-120; Pfennigstorf, 1996, at p. 60; Pradeep S. Mehta, 2002, at p. 82; Wellons, 1999, at pp. 57-58; Weber, 1997, at pp. 237-238; and Solomon Abay, 2001.

2288 Ibid.

2289 The unique system is common law tradition while the dual system is common in the continental countries. France is the most cited example for the dual system. The hybrid system is least common. Jacobini, at pp. 25 - 37, 75, 88, 101-103, 113 & 125-132; Gorden, 1996; Brown and Bell, 1993, at pp.

The subject matter of review is often action derived from law or doctrine.<sup>2290</sup> Some of the systems make all the regulatory actions reviewable while others indicate the exceptions to review.<sup>2291</sup> The grounds of review are general principles of good administration consisting of substantive and procedural requirements.<sup>2292</sup> They include the following:

- duty not to exceed the statutory bounds of discretion,
- duty to act in good faith,
- duty not to be influenced by considerations and motives irrelevant to the objectives of regulation,
- duty to hear and treat equally,
- duty to involve public participation,
- duty to give reason,
- duty to be consistent,
- duty to act reasonably and with fairness, and
- duty to compensate.<sup>2293</sup>

The procedure of review varies from country to country depending on whether the system is dual, unique or mixed.<sup>2294</sup> The countries following the dual system have separate civil and administrative law procedures while those following the unique system often adapt their civil law procedures to the administrative litigations.<sup>2295</sup> The countries also require that the solutions available within the regulators and the competition authorities need to be exhausted before the matter is taken to judicial review.<sup>2296</sup>

The remedies also often include:

- annulling, revising and/or modifying the regulatory action retroactively or prospectively;
- awarding compensation;
- ordering new decisions to be taken; and
- granting temporary relief. <sup>2297</sup>

However, the extent of intervention of the courts in the works of the reviewed institutions varies from country to country.<sup>2298</sup> The reviewers either:

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252-270; Fuke, 1997, at pp. 16-20; Kobayakawa., 1997, at pp. 6-9; Zhang, 1997, at p. 94; Zhang, 1997a, at pp. 77-86; Lotulung, 1997, at pp.168-176; Bedner, 1997; Harding, 1997, at pp. 133-162; Drupsteen and Dekker, 1997, at pp. 212-225; Schueler, 1997, at pp. 223 & 231-234; Fuke, 1997, at pp.18-20; Weber, 1997, at pp. 243-251; and Solomon Abay, 2001, at pp. 153-160.

2290 Ibid.

2291 Ibid.

2292 Ibid.

2293 Ibid.

2294 Ibid.

2295 Ibid.

2296 Ibid.

2297 Ibid.

2298 Ibid.

- substitute decisions of the regulator or competition authority by their decisions and order the latter to behave in a certain way, or
- make their decisions and stop there by leaving the compliance decision to discretion of the regulator or competition authority.<sup>2299</sup>

Most of the countries follow the latter approach.<sup>2300</sup>

## ii. The Case of Ethiopia

Ethiopia also subjects all the actions of its governmental organs, including the financial market regulator and the competition enforcement organs, to judicial review as long as there is question of legality that makes them 'justiciable'.<sup>2301</sup> It allows the financial institutions against which the NBE passes a decision of receivership or takeover of management, reconstruction, winding up or dissolution and the parties aggrieved by the administrative measures and penalties of the competition organs to petition to the Federal High Court.<sup>2302</sup> It recognizes a number of substantive and procedural principles of good administration in both its constitution and the various pieces of laws including the commercial registration, investment, labour, civil service and taxation laws.<sup>2303</sup> It also allows the initiation of judicial review after exhaustion of all possible internal remedies and obtaining of final decision of the regulators and administrative organs.<sup>2304</sup> It requires the courts to conduct the review under the civil and criminal procedure laws.<sup>2305</sup> The usual remedies the courts provide also include confirmation, modification or annulment of the regulatory action; award of pecuniary compensation; injunction; publication of pardon; and order for execution.<sup>2306</sup> The country also follows the unique system of judicial review.<sup>2307</sup>

It, however, lacks administrative procedure law and the actions of the NBE and the competition enforcement organs are not reviewed against their legal and public interest grounds in practice. The principles of good administration are also scattered in the various pieces of laws and this makes their enforcement difficult.

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2299 Ibid.

2300 Ibid.

2301 FDRE, 1995, at arts. 9(1), 9(2), 12(2), 72(2) & 78-80. It requires the making of decision by the House of Federation (wing of the parliament) when the issue involves constitutional interpretation (FDRE, 1995, at arts. 50(1), 78(1), 78(4), 79(1), 79(3), 37, 62(1), 62(2), 83, 84 & 89).

2302 TGE, 1994a, at art. 23; FDRE, 2008b, at arts. 38 & 47; TGE, 1994b, at art. 27(2); FDRE, 2003c, at art. 17; FDRE, 1996g, at art. 24; and FDRE, 2009, at art. 19(3).

2303 FDRE, 1995, at arts. 13, 40, 41, 42, 43 & 85-92; FDRE, 1997a; FDRE, 2010a, at arts. 7(3), 33(2), 39(3) & 61; FDRE, 1996c; FDRE, 1998a; FDRE, 2002c; FDRE, 2002d; FDRE, 2002e; FDRE, 2002j; FDRE, 2002k; TGE, 1993a; and FDRE, 2003g.

2304 IGE, 1961a, at arts. 47, 54 & 55; FDRE, 1997a, at art. 53; and FDRE, 2010a, at art. 61.

2305 FDRE, 1996a, at art. 7; and the civil and criminal procedure codes of the country.

2306 IGE, 1960a, at arts. 2090, 2105, 2118, 2126, 2127, 2130, 2035, 2121 & 2033; IGE, 1961a, at art. 56; TGE, 1993a, at art. 17(3); FDRE, 1995, at art. 9; and FDRE, 2003g, at arts. 38, 43(5), 138 & 154(2).

2307 FDRE, 1996a, at arts. 3-5.

The courts also often retreat from reviewing the regulators and administrative institutions for fear that they will interfere in their discretions.<sup>2308</sup>

Hence, the country needs to implement five sets of measures. First, it needs to define the accountabilities of the financial market regulator and the competition enforcement organs clearly. Secondly, it needs to require the financial market regulator and the competition enforcement organs to exercise their powers according to defined substantive and procedural principles of good administration (including the principles of respecting the statutory bounds of discretion, good faith, good motive, fair hearing, public participation, reasoning, consistency, reasonableness, fairness and compensation). Thirdly, it needs to subject all the rules, decisions and actions of the financial market regulator and the competition enforcement organs to judicial review expressly.<sup>2309</sup> Fourthly, it needs to indicate the applicants and the judicial organs that will have the power to make the judicial review; collect and standardize the substantive and procedural grounds of review; define the procedure and remedies of review; and demarcate the line of jurisdiction between the reviewer and the financial market regulator and competition enforcement organs. The list of applicants may include the regulated financial institutions and actors, a defined number of the consumers as a group, and other interested parties including the government. Fifthly, it needs to adopt comprehensive administrative procedure law that can guide the judicial review of all regulatory and administrative actions.<sup>2310</sup>

### 5.3.2.3 Control by Peripheral Institutions

#### i. The International Experience

A number of countries also use different types of peripheral institutions to check the operations of their regulatory and competition authorities and make the

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2308 The pieces of laws also purport to discourage interference. IGE, 1961a, at art. 56 & 57; IGE, 1962c, at art. 105; IGE, 1965c, at arts. 182-184 & 371ff; TGE, 1993a, at art. 17(3); and FDRE, 2003g, at arts. 38, 43(5), 138 & 154(2).

2309 Judicial review of a regulatory action is necessary for a number of reasons. Firstly, the modern principle of separation of powers or divisions of functions recognizes it provided that the reviewing judge shall balance between the need to control the regulator's discretion from arbitrary exercise substantively and procedurally and the need not to interfere in the exercise of discretion of the regulator. Secondly, the principle of rule of law dictates that the carrying out of regulatory action is legitimate only if the empowerment of the action and the substantive and procedural requirements for it are complied with. Thirdly, the judicial review of regulatory actions is not necessarily undemocratic and the reality in many countries is that it is recognized despite arguments against it. Fourthly, the judicial review of regulatory actions ensures the protection of constitutionally recognized human rights of the subjects of regulation. Fifthly, the regulators or the state must compensate the subjects of regulation for injuries to their rights irrespective of the legality of the regulatory action. Baldwin and Houghton, 1986, at pp. 267-283, 239 & 269; Asimow, 1983, at pp. 253-276; Galligan, 1976; Harlow, 1976; Daintith, 1979; Jaffe and Henderson, 1956, at pp. 345-364; Sheltema, 1997, at p. 2; Zhang, 1997b, at pp. 258 & 261; Grey, 1979, at pp. 108-109 & 114-132; Galligan 1982, at pp. 257-263 & 270; Jacobini, 1991, at pp. 5, 7-10 & 15-16; Fuke, 1997, at pp. 21-22; and FDRE, 1995, at arts. 13, 50, 53, 84 & the preamble.

2310 The country has been considering a draft federal administrative procedure law since 2002 although it has not enacted it yet.

regulatory processes participatory through non-binding advises and recommendations. They use the institutions of:

- ombudsman (Scandinavia),
- complaint registering machineries (England),
- mediation offices (the Netherlands and Switzerland),
- censorship offices (China), and
- advisory bodies representing interest groups such as in insurance (Australia, Belgium, Finland, France, Germany, Italy, Norway, Portugal, Spain, Turkey, United Kingdom and Japan).<sup>2311</sup>

Many countries also provide for the peripheral institutions of Ombudsman, Human Rights Commission, Judicial Protectorate, Procurator Office, Comptroller General, and Inspectorate by their constitutions.<sup>2312</sup>

#### ii. The Case of Ethiopia

Ethiopia has also introduced Ombudsman Office that can check the operations of governmental authorities as a federal peripheral administrative control mechanism.<sup>2313</sup> It does not, however, define the exact roles of the Office against the financial market regulator and the competition enforcement organs. It needs to define these so that the office can also control the financial market regulator and competition enforcement organs and contribute to consumer protection.

### 5.3.2.4 Control by the Public

#### i. The International Experience

The countries that have strong hold of the principles of good administration and public consultation such as the United States and the EU member countries also often rely on the mechanism of controlling regulators and competition authorities

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2311 Jacobini, 1991, at pp. 25 - 37, 75, 88, 101-103, 113 & 125-132; Gorden, 1996; Brown and Bell, 1993, at pp. 252-270; Fuke, 1997, at pp. 16-20; Kobayakawa., 1997, at pp. 6-9; Zhang, 1997, at p. 94; Zhang, 1997a, at pp. 77-86; Lotulung, 1997, at pp. 168-176; Bedner, 1997; Harding, 1997, at pp. 133-162; Drupsteen and Dekker, 1997, at pp. 212-225; Schueler, 1997, at pp. 223 & 231-234; Weber, 1997, at pp. 243-251; Pfennigstorf, 1996, at p. 63; and Solomon Abay, 2001, at p. 143.

2312 See the 1929 Constitution of Austria; the 1999 constitution of Finland; the constitution of Sweden (as last amended in 1979); the 2005 constitution of Swaziland; the 1976 constitution of Portugal; the 1982 constitution of Turkey (as last amended in 2004); the 1997 constitution of Poland; the 1991 constitution of Romania; the 1991 constitution of Slovenia (as amended in 2000); the 1977 constitution of Soviet Union; the 1994 constitution of Tajikistan; the 1996 constitution of Ukraine; the 1994 constitution of Belarus; the 1982 constitution of China (as amended in 1988, 1993, 1999, and 2004); the constitution of North Korea; the constitution of Sri Lanka (as amended in 2000); the 1997 constitution of Thailand; the 1983 Constitution Act of Vanuatu; the 1992 constitution of Vietnam; the 1992 constitution of Angola; the 1992 Constitution of Ghana; the 1995 constitution of Uganda; the 1979 constitution of Zimbabwe (as last amended in 1993); the 1996 constitution of South Africa; the 1980 constitution of Guyana (as amended in 1996); the 1976 constitution of Trinidad and Tobago (as amended in 2000); the 1853 constitution of Argentina (as amended in 1860, 1866, 1898, 1957 and 1994); the 1980 constitution of Chile; and the 1981 Constitution Order of Antigua and Barbuda accessed through the Constitution Finder database of the T.C. Williams School of Law of the University of Richmond available at <http://confinder.richmond.edu/>.

2313 FDRE, 1995, at art. 55(15); and FDRE, 2000a.

by the public while others have also worked towards this.<sup>2314</sup> Hence, the regulators and competition authorities are also socially controlled by public opinion as consequence of their accountability to the public and the principle of participatory decision making by giving the public opportunity to participate in the policy formulation, rule making, adjudication and non-adjudication decisions of the regulators and competition authorities.

## ii. The Case of Ethiopia

Ethiopia does not oblige its financial market regulator and competition enforcement organs legally to include public consultation during the making of their decisions, rules and actions. It only invites public comment during parliamentary hearing of their annual reports and establishing laws. It needs to require them to include public consultation in their regulatory and competition enforcement processes in order to check their operations as well as enable public participation in the development and enforcement of the regulatory and competition regimes.

### 5.3.3 The Treatment of Individual Consumers

#### i. The International Experience

Most of the countries focus on the consumer as a group and protect the individual consumer only indirectly. They make it clear in their supervisory laws that their financial regulators and competition authorities are to be guided by the interests of the public, not of the individual, and take the position that the individual consumer of a financial service can not be 'aggrieved party' for purpose of challenging decisions and orders of the regulators and competition authorities in the courts.<sup>2315</sup> They involve the individual consumer in the process only when he/she is invited as source of information, member of decision-making or advisory body, party in class action, or complainant against decisions and financial situations of the regulated institutions.<sup>2316</sup>

Some of the countries also allow the individual consumer to take his/her grievance against the regulators and the competition authorities to peripheral institutions.<sup>2317</sup>

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2314 Jacobini, 1991, at pp. 25-37, 75, 88, 101-103, 113 & 125-132; Gorden, 1996; Brown and Bell, 1993, at pp. 252-270; Fuke, 1997, at pp. 16-20; Kobayakawa., 1997, at pp. 6-9; Zhang, 1997, at p. 94; Zhang, 1997a, at pp. 77-86; Lotulung, 1997, at pp. 168-176; Bedner, 1997; Harding, 1997, at pp. 133-162; Drupsteen and Dekker, 1997, at pp. 212-225; Schueler, 1997, at pp. 223 & 231-234; Fuke, 1997, at pp.18-20; Weber, 1997, at pp. 243-251; and Solomon Abay, 2001, at pp. 167-174.

2315 Pfennigstorf, 1996, at p. 62; and Möschel, 1991, at pp. 113-115.

2316 Ibid.

2317 Some states of the US, for instance, have special offices within the insurance department (and outside) that represent the interests of the insured individual (such as during rate review). UK, the Scandinavian countries and some others also provide for similar protection. The peripheral institutions in most countries, however, make non-binding but influential decisions. Only the UK institutions make binding decisions. Pfennigstorf, 1996, at p. 63; and note the discussions under the preceding subtitles.

## ii. The Case of Ethiopia

Ethiopia allows all parties aggrieved by measures of the competition enforcement organs to take appeals to the Federal High Court.<sup>2318</sup> It does not, however, make it clear if it allows the individual consumer of financial service to challenge the decisions and orders of the financial market regulator in court. It looks, from practice, that the individual consumer does not have the right to do so unless he/she has direct tort claim under the extra-contractual liability law of the country.<sup>2319</sup> The country needs to have clear rule on the matter. It needs to strengthen the complaint handling, judicial review and public consultation mechanisms and encourage the regulated institutions and consumers to participate in the design and implementation of regulation and control of regulatory legality as these have been done in the other countries.<sup>2320</sup> It need not, however, suffocate the financial market regulator and competition enforcement organs by individual suits for judicial review. It only needs to allow suits for extra-contractual compensation when the regulators and competition enforcement organs violate the bounds of their legal authorizations and cause extra-contractual damage on individuals.

## 5.4 The Regulatory Backing

### 5.4.1 The Political Support

#### i. The Theory and International Experience

Regulatory and competition policies are functions of the overall policy framework of a government.<sup>2321</sup> They are also features of a free market oriented economic system. Their enforcement, therefore, necessitates the presence not only of a government that owns and supports this kind of economic system but also of one that has the necessary determination to pursue competition and regulatory policy.<sup>2322</sup> It is also important that the government, the regulator and the competition authority follow common philosophy on the objectives to promote and the roles to play; shoulder common responsibility to materialize the objectives; and have open channels of communication and clear lines of accountability to monitor each other's progress.<sup>2323</sup>

It is also important that the government supports the regulators and competition authorities to avoid jurisdictional conflicts, coordinate their functions, and link these with the functions of the other bodies of government.<sup>2324</sup> The effectiveness of regulatory and competition enforcement also necessitates the existence of government that bears the challenges with the regulators and competition

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2318 FDRE, 2003c, at art. 17.

2319 IGE, 1960a, at arts. 2035 & 2029. Note also the discussion under the 'sanctions' subtitle above.

2320 Note the discussion under the preceding subtitle.

2321 Carmichael and Pomerleano, 2002, at pp. 48-49.

2322 Ibid.

2323 Ibid.

2324 Ibid.

authorities and quickly extends support to them.<sup>2325</sup> The countries that have this commitment on the part of the government have succeeded in practice to enhance regulation and competition in their financial markets.<sup>2326</sup>

## ii. The Case of Ethiopia

Ethiopia has already committed to reduce the roles of its government in the economy, further free market, promote domestic and foreign private investment, decentralize economic management, and enhance public participation in the design and implementation of its development plans.<sup>2327</sup> It has also taken a number of deregulatory measures to promote and strengthen its transition from centrally planned to free market economy and re-established the financial market regulator and competition enforcement organs with new powers and functions.<sup>2328</sup> It has also implemented restructuring measures in the financial market to:

- promote private investment and competition;
- allow market based interest and premium rates;
- abolish control on credit;
- increase the flow of credit and financial services to the private sector;
- liberalize trade in foreign exchange;
- manage the monetary and foreign exchange system;
- control inflation;
- ensure financial security and stability;
- encourage information flow to consumers; and
- accelerate financial development.<sup>2329</sup>

Hence, it has showed some determination to pursue financial regulation and competition commensurate with the free market economic policy.

It has, however, failed to:

- clearly state the goals of its financial market regulation in the specific supervision laws;
- clearly define the functional linkage between its competition organs and the financial market regulator;
- restructure and transform its financial market from bank based to market based system (that will include securities market and private pensions); and
- further the international liberalization of the financial market.<sup>2330</sup>

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2325 Ibid.

2326 Ibid.

2327 PDTCE, 1991; TGE, 1991; EPRDF, 2000; FDRE, 2001b; and FDRE, 2002e.

2328 TGE, 1994; TGE, 1994a; TGE, 1994b; and FDRE, 2003c. Note also the discussions under the 'enforcing organs' subtitle and the 'banking, insurance and microfinance' and 'securities market' chapters above.

2329 Ethiopia, 1998/99-2000/01; Yohannes Ayalew, 2000; and Befekadu Degefe and Berhanu Nega, (eds.), 1999/2000, at pp. 296-302 & 308-317. Note also the discussions under the 'banking, insurance and microfinance' and 'securities market' chapters above.

2330 Note the discussions under the securities market and pension chapters above.

The government needs to correct these shortcomings in order to fully encourage participation of the financial regulator (the NBE), the competition authorities, the business community and the other stakeholders in the furtherance of development of the financial system.

#### 5.4.2 The Legislative Backing

##### i. The Theory and International Experience

Like the political support, the effectiveness of regulatory and competition law enforcement necessitates the presence of government that:

- backs the financial market regulator and the competition authorities with sufficient enforcement powers depending, of course, on the objectives to be promoted, and
- stands willing and acts quickly to support the financial market regulator and competition authorities in the event of need for legislative change to cope with developments in the financial system.<sup>2331</sup>

The regulator and competition authorities also need to have rule-making, investigating, adjudicating and sanctioning powers in order to enable them to act proactively and reactively depending on the type of market failure they have to prevent or correct.<sup>2332</sup> The government may also need to choose between 'black letter law' approach where it leaves little regulatory discretion to the regulators and the competition authorities and 'guideline' approach where it leaves broad regulatory power to them.<sup>2333</sup> The 'guideline' approach is useful to afford flexibility to the regulator and competition authorities so that they can issue and amend technical rules without need to pass legislation in parliament.<sup>2334</sup> Most countries tend to follow the 'black letter law' approach in non-banking regulation and the 'guideline' approach in banking regulation.<sup>2335</sup> The advice from regulatory flexibility point of view is to follow the 'guideline' approach.

##### ii. The Case of Ethiopia

Ethiopia seems to follow the 'black letter law' approach. It leaves regulatory discretion to both the financial market regulator (the NBE) and the competition enforcement organs within a list of powers and functions.<sup>2336</sup> It also delegates the rule-making power to the regulator and the competition enforcement organs only in respect of technical and implementation matters. The approach promotes regulatory stability and certainty during the transition. The country, however, also needs to increase the regulatory autonomy, powers and discretions of both the financial market regulator and the competition enforcement organs as the regulatory capacities of the latter grow so that they can stimulate and respond to

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2331 Carmichael and Pomerleano, 2002, at pp. 49-52.

2332 Ibid.

2333 Ibid.

2334 Ibid.

2335 Id., at p. 52.

2336 Note the discussion under the 'powers and functions' subtitle above.

the changes in the financial market without waiting for parliamentary legislation.<sup>2337</sup>

### 5.4.3 The Funding

#### i. The Theory and International Experience

Effective regulatory enforcement also requires adequate funding. Regulators and competition authorities are mostly funded, in the international experience, through government budget or industry levy.<sup>2338</sup> Each financing approach has shown advantages and disadvantages.<sup>2339</sup> The budgetary approach has the advantage of distributing the cost of regulatory and competition enforcement to the tax payers while the industry levy approach puts the burden on the regulated institutions and their customers.<sup>2340</sup> The budgetary approach has also the risk of unstable funding since the regulators and competition authorities have to compete with other budgetary institutions and programmes for funding while the industry levy approach can ensure consistent funding.<sup>2341</sup> The budgetary approach has also the risk of making the regulators and competition authorities dependent on the government while the industry levy approach can ensure autonomy.<sup>2342</sup> The industry levy approach may not, however, also work when the market in which it is implemented is thin.

#### ii. The Case of Ethiopia

Ethiopia finances the financial market regulator (the NBE) and the competition enforcement organs by state allocated capital and annual budgetary allocations, respectively.<sup>2343</sup> It authorizes the NBE to:

- operate like profit making bank by using initial capital allocated to it by the government;
- maintain integrity of the allocated capital at all times;
- generate income and profit;
- finance some of its operations by industry levy;
- draw audited annual balance sheet and profit and loss statements;
- transfer some of its annual profits to a general reserve fund that supplements its capital; and
- transfer its net annual profits in excess of the general reserve fund and other expenses to the government.<sup>2344</sup>

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2337 The 2008 and 2009 banking and microfinance supervision laws are better than the 1994 and 1996 laws in this regard (Compare the powers and functions of the NBE in TGE, 1994; FDRE, 2008a; TGE, 1994a; FDRE, 2008b; TGE, 1994b; FDRE, 1996g; and FDRE, 2009). Note also the discussion under the 'powers and functions' subtitle above.

2338 Carmichael and Pomerleano, 2002, at pp. 52-53; and Wellons, 1999, at pp. 38-39.

2339 Carmichael and Pomerleano, 2002, at pp. 52-53.

2340 Ibid.

2341 Ibid.

2342 Wellons, 1999, at pp. 38-39.

2343 TGE, 1994, at arts. 9-14; and FDRE, 2008a, at art. 6.

2344 TGE, 1994, at arts. 9-14; and FDRE, 2008a, at arts. 6, 7 & 8. It has re-established the NBE with initial capital of five hundred million Birr (TGE, 1994, at art. 9; and FDRE, 2008a, at art. 6(1)). The

It also expects it to finance the regulatory functions by using its own funds except in the cases where it is fixed by law that the funding has to be borne by the regulated institutions.<sup>2345</sup>

It makes the federal competition enforcement organs part of the ministry of trade and industry which is financed by budgetary allocation.<sup>2346</sup> It does not make them live by their own finances although it authorizes them to levy fees on users of their services.<sup>2347</sup>

The position of Ethiopia on funding of the NBE is commendable in light of:

- the need to ensure autonomy of the NBE,
- the need not to burden tax payers with the costs of financial regulation,
- the thinness of the financial market to sustain funding by industry levy,
- the need to have stable source of regulatory funding,
- the need to increase regulatory responsibility and efficiency of the NBE,
- the need to share the cost of regulation with the regulated financial institutions and make them watch-dogs of regulatory efficiency, and
- the need to charge the regulated financial institutions with the cost of regulatory non-compliance.

The approach needs to be extended to the financing of the competition enforcement organs and the future securities market and pension regulators in order to obtain similar advantages.

However, the supervision departments of the NBE suffer from fund constraint. The NBE allocates fund to them as units sharing with its other departments hence making them get no adequate funding for purpose of their regulatory design and enforcement functions. It does not also authorize them to finance their operations through separate industry levy. The fees they impose on the regulated institutions are accounted to the consolidated fund of the NBE and the supervision departments can not access this for direct use. The NBE needs to recognize financial independence of the supervision departments.

The competition enforcement organs also need to be re-established as authorities with financial and operational autonomy from the government with accountability to parliament.

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NBE also generates income through interest, commissions, service fees and industry levies (Note the financial statements in the annual reports of the NBE).

2345 The banking, insurance, microfinance and insurance auxiliary supervision laws require the banks, insurers, microfinance institutions and insurance auxiliaries to finance the costs of their initial registration and licensing, license renewal, branching appraisal (and permission), inspection, examination, and receivership or takeover. TGE, 1994a, at arts. 5(7-8), 20(4) & 22(5); FDRE, 2008b, at arts. 35 & 51; TGE, 1994b, at arts. 6(4), 25(2-3), 26(5), 31, 38 & 44; FDRE, 1996g, at art. 24; and FDRE, 2009, at arts. 5(1)(a), 6(2), 7, 18, 19(3) & 28(1).

2346 FDRE, 2003c.

2347 Ibid.

#### 5.4.4 The Skill Base

##### i. The Theory and International Experience

The effectiveness of regulatory and competition enforcement is also dependent on the regulatory culture and skill of the staff of the regulators and competition authorities.<sup>2348</sup> Culture wise, it is important that the staff have full awareness and commitment to implement the objectives and philosophy of the regulatory and competition authorities and put more attention on output than input.<sup>2349</sup> Skill wise, it is important that the staff have full training and experience to deal with complex issues of regulatory and competition policies and laws.<sup>2350</sup>

The governments and regulators around the world appreciate this and pursue a ‘private-sector-style’ structure in the management of their regulatory and competition authorities as opposed to the traditional ‘public-service-style’ in order to reward staff excellence, commitment and output orientation.<sup>2351</sup> However, the regulators and competition authorities also often face staff constraint since most of the highly qualified and committed staffs usually prefer to work for the regulated industries rather than for the regulators due to varieties of reasons, including the salary differentials between the regulators and the regulated industries.<sup>2352</sup>

##### ii. The Case of Ethiopia

The supervision departments of the NBE also suffer from staff constraint.

First, all of them are understaffed for the responsibility they shoulder. The Banking Supervision Department had only nineteen staffs (excluding the department manager) by the time of the writing of this study one of whom was principal inspector while three were senior inspectors, four were inspectors, seven were junior inspectors, two were clerks and other two were secretaries.<sup>2353</sup> The insurance supervision department had seventeen staffs (excluding the department manager) two of whom were principal inspectors, one was senior inspector, ten were inspectors and junior inspectors, three were secretaries and one was office boy.<sup>2354</sup> Only fifteen of the staffs of the banking supervision department (excluding the department manager, the two clerks and the two secretaries of the department) have handled the regulatory work on the fifteen banks that have over six hundred seventy six branches while also only thirteen of the staffs of the insurance supervision department (excluding the department manager, the three secretaries and the one office boy of the department) have handled the regulatory work on the twelve insurers that have over two hundred five branches and the

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2348 Carmichael and Pomerleano, 2002, at p. 53.

2349 Ibid.

2350 Ibid.

2351 Ibid.

2352 Ibid.

2353 Note the human resource record of the department.

2354 Note the human resource record of the department.

insurance auxiliaries which are over one thousand in number.<sup>2355</sup> The microfinance supervision department has also relied on fourteen staffs (excluding the department manager and the secretaries of the department) to conduct the supervision work on the thirty microfinance institutions scattered across the country.<sup>2356</sup>

Secondly, the staffs in the departments are less experienced and motivated to conduct off-site and on-site examinations on the financial institutions, to assess and forecast the risks in the financial market, and to design regulatory policy.<sup>2357</sup> Most of them are accountants by profession who have few years of regulatory work experience while very few are economists or managers.<sup>2358</sup> One of the staffs of the banking supervision department had second degree in economics (banking and finance) while another one had second degree in business administration, one was certified accountant, eight had first degree in accounting, two had first degree in management, one had diploma in business administration and another one had diploma in banking by the time of the writing of this study.<sup>2359</sup> Ten of the staffs had less than two years of work experience in regulatory matters while the other five had four up to eight years of experience.<sup>2360</sup> Seven of the staffs of the insurance supervision department had first degree in accounting while five had first degree in management and another one had first degree in economics.<sup>2361</sup> Five of them had additional diploma in insurance from the Ethiopian Insurance and Banking Institute (EIBI) while three were attending their studies at the Chartered Insurance Institute of London (CII).<sup>2362</sup> Five of the staffs of the microfinance supervision department had second degrees (two in economics, two in business administration and one in microfinance) while the rest had first degrees (one in economics, two in accounting, and six in management).<sup>2363</sup> Four of the staffs had nearly ten years of regulatory work experience in the department while the rest had less than two years of experience as microfinance regulators.<sup>2364</sup> The heads of the insurance and microfinance supervision departments had also less than two years of regulatory experience while the heads of the banking supervision department and the financial market supervision division of the NBE (which consists the banking, insurance and microfinance supervision departments) had more than ten years of experience in the departments.<sup>2365</sup> They were also economists while one was manager.

Thirdly, the departments suffer from low employee retention rates due to reasons including the non-competitiveness of the salary structure and working conditions

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2355 Note the human resource records of the departments; and Table 1(Chap. 2).

2356 Note the human resource record of the department; and Table 1(Chap. 2).

2357 Note the human resource records of the departments. Also NBE BSD, 2005, at p. 53; NBE ISD, 2005, at p. 88; and Degefe Duressa Obo, 2009, at p. 208 for general assessment of the limitation.

2358 Ibid.

2359 Note the human resource record of the department.

2360 Ibid.

2361 Note the human resource record of the department.

2362 Ibid.

2363 Note the human resource record of the department.

2364 Ibid.

2365 Note the human resource records of the departments.

of the NBE (compared to the private sector). The government has recognized this problem and enacted a special law for administration of the employees of the NBE in December 2008.<sup>2366</sup> The NBE has also started to award its employees with long time service certificates and medals in 2009 with a view to encouraging the employees who serve it for more than ten years.<sup>2367</sup>

The competition enforcement organs of the country also suffer from similar problems. They have employees with less than seven years of work experience in competition matters.<sup>2368</sup>

Hence, the departments of the NBE hardly analyse the off-site reports and on-site examinations of the financial institutions while the actions of the competition enforcement organs have been more reactive and adjudicatory than proactive.<sup>2369</sup>

The country needs to rectify the situation in order to materialize effective regulation.

## 5.5 The Use of International Cooperation and Principles

### 5.5.1 The Use of International Cooperation

#### i. The International Experience

The national laws of many of the countries have become inadequate when their financial markets are increasingly diversified, internationalized, become to be dominated by institutional investors, and affected by illegal activities including tax evasion and money laundering for illicit purposes.<sup>2370</sup> The regulatory inadequacy has been compounded by failures of the national financial markets to regulate themselves, incompleteness and incompatibilities of the national procedures and solutions to solve international problems, and absence of coherent international regulation to fill in the gap.<sup>2371</sup> The use of international cooperation has, accordingly, become increasingly important to coordinate regulatory rules, practices and enforcement.<sup>2372</sup>

Hence, the Bank for International Settlements (BIS), the IMF, the World Bank, the WTO, the UNCTAD, the OECD, the World Savings Banks Institute (WSBI),

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2366 FDRE, 2008d.

2367 Note the NBE news cited as NBE, 2009-10.

2368 Note the human resource records of the Trade Practice Commission and the Competition Secretariat of the Ministry of Trade and Industry of the country. See also Booz Allen Hamilton, 2007, at pp. 58-65.

2369 NBE BSD, 2005, at p. 40 (as revised); NBE ISD, 2005, at p. 88 (as revised); Booz Allen Hamilton, 2007, at pp. 58-65; and unpublished annual reports of the supervision departments of the NBE and the competition enforcement organs. Note also the discussion under the 'powers and functions' subtitle above.

2370 Gilligan, 1999, at pp. 22-26; Möschel, 1991, at p. 36; Alexander, et al., 2006; and Banyár and Mészáros, 2009.

2371 Gilligan, 1999, at pp. 22-26; Pradeep S. Mehta, 2002, at p. 83; Alexander, et al., 2006; and Banyár and Mészáros, 2009.

2372 Gilligan, 1999, at pp. 22-26; Pfennigstorf, 1996, at p. 38; World Bank, 2002, at pp. 148-149; Pradeep S. Mehta, 2002, at pp. 83-84; Alexander, et al., 2006; and Banyár and Mészáros, 2009.

the International Accounting Standards Committee (IASC) (renamed later as International Accounting Standards Board), the International Federation of Accountants (IFAC), the BIS Committee on Payment Settlement Systems (CPSS), the G-7 Financial Action Task Force on Money Laundering (FATF), the G-7 Financial Stability Forum (FSF), the International Corporate Governance Network (ICGN), the Global Corporate Governance Forum (GCGF), the Basle Committee on Banking Supervision (BCBS), the International Association of Insurance Supervisors (IAIS), the International Organization of Securities Commissions (IOSCO), the International Organization of Pension Supervisors (IOPS), the International Association of Deposit Insurers (IADI), the International Competition Network (ICN), and the G-20 have served as forums for international cooperation.<sup>2373</sup>

The IMF, World Bank, OECD, IASC, IFAC, CPSS, FATF, BCBS, IAIS, IOSCO, IOPS and IADI have developed a number of principles and standards for the financial systems, including the following:

- 'Code of Good Practices on Transparency in Monetary and Financial Policies' (IMF);
- 'Code of Good Practices on Fiscal Transparency' (IMF);
- 'Special Data Dissemination Standard' (IMF);
- 'General Data Dissemination System' (IMF);
- 'Principles and Guidelines on Effective Insolvency Systems' (World Bank);
- 'Principles of Corporate Governance' (OECD);
- 'International Accounting Standards' (IASC);
- 'International Standards on Auditing' (IFAC);
- 'Core Principles for Systemically Important Payment Systems' (CPSS);
- 'Forty Plus Nine Recommendations of the Financial Action Task Force on Money Laundering' (FATF);
- 'Core Principles for Effective Banking Supervision' (BCBS);
- 'Core Principles for Insurance Supervision' (IAIS);
- 'Objectives and Principles of Securities Regulation' (IOSCO);
- 'Principles of Private Pension Supervision' (IOPS); and
- 'Core Principles of Deposit Insurance' (IADI).<sup>2374</sup>

A number of regional institutions, organizations and committees have also assisted the coordination of the national financial market rules, practices and enforcements through regional technical cooperation, advisory services, information exchange arrangements, conferences, dialogues, and training programs. They include the following:

- the Caribbean Group of Banking Supervisors (CGBS) (established in 1983);

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2373 Yılmaz Akyüz, 2002, at pp. 28-116; Möschel, 1991, at pp. 36-38; Pfennigstorf, 1996, at pp. 40-42; Andrews, 2006; Degefe Duressa Obo, 2009, at pp. 1-3; Ewing, 2006, at pp. 296-313 & 653-673; and websites of the institutions (accessed in May 2007 and August-December 2010).

2374 Yılmaz Akyüz, 2002, at pp. 28-116; IOPS, 2006; BCBS-IADI, 2009; websites of the institutions (accessed in May 2007 and August 2010); and the discussion under the 'use of international principles' subtitle below.

- the Association of Securities and Exchange Commissions of the Americas (COSRA) (created in 1992);
- the Association of Supervisors' of Banks of the Americas (created in May 1999);
- the Inter-American Development Bank (IDB) (created in 1959);
- the European Savings Banks Group (established in 1963 as the 'Savings Banks Group of the European Economic Community' and renamed as the European Savings Banks Group in 1988);
- the Banking Supervision Committee (BSC) of the European System of Central Banks (ESCB) (established in 1998);
- the Committee of European Securities Regulators (established in June 2001);
- the Committee of European Banking Supervisors (CEBS) (established in November 2003);
- the European Insurance and Occupational Pensions Committee (EIOPC) (created in November 2003 replacing the EC Insurance Committee that was created in December 1992);
- the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) (established in November 2003);
- the Asian Development Bank (ADB) (created in 1966);
- the Offshore Group of Banking Supervisors (OGBS) (formed in 1980);
- the Association of Financial Supervisors of Pacific Countries (AFSPC) (created in late 2002);
- the EMEAP Working Group on Banking Supervision (WGBS) (operational as of July 2004);
- the Islamic Financial Services Board (IFSB) (created in November 2002 and operational as of 10 March 2003);
- the Regional Group on Banking Supervision of Transcaucasia, Central Asia and the Russian Federation (operational as of 2005);
- the Group of French-Speaking Banking Supervisors (Groupe des Superviseurs Bancaires Francophones - GSBF) (established in 2004);
- the SEANZA Forum of Banking Supervisors (operational as of September 2004);
- the African Development Bank (ADB) (created in 1964);
- the Committee of Banking Supervisors of West and Central Africa (CBSWCA) (created in April 1994);
- the African Capital Markets Forum (created in 1996);
- the SADC Subcommittee of Bank Supervisors (SSBS) (created in 2004 under the Committee of the Central Bank Governors (CCBG) of the Southern African Development Community (SADC)); and
- the African Stock Exchanges Association (ASEA) (registered in Nairobi on 13 November 1993).<sup>2375</sup>

The WTO, IMF, World Bank and UNCTAD have also promoted the principle of competition along with their trade liberalization (WTO), international financial

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<sup>2375</sup> Alexander, et al., 2006; BCBS, 2006, at pp. 27-72; EC, 2004a; EC, 2004b; EC, 2004c; EC, 2005a; Degefè Duressa Obo, 2009, at pp. 1-3; and the websites of the organizations and committees (accessed in May 2007 and August 2010).

stability (IMF), and economic development (World Bank and UNCTAD) related objectives although they have not developed an international competition regime yet.<sup>2376</sup>

The BCBS, IAIS, IOSCO, IOPS and ICN are serving as the most specialized institutions for international cooperation in the fields of banking, insurance, securities and pension regulation and competition law enforcement.<sup>2377</sup>

The BCBS, formed in 1974, serves as forum for international cooperation by:

- exchanging information on national supervisory arrangements;
- studying the effectiveness of techniques for supervising international banking businesses; and
- setting minimum supervisory standards.<sup>2378</sup>

It encourages cooperation between the banking supervisory authorities in the G-20 and other countries.<sup>2379</sup> It circulates recommendation and advice to the supervisory authorities around the world and organizes international conferences for the banking supervisors.<sup>2380</sup> It works with a number of banking supervisory groups including the Offshore Group of Banking Supervisors and the supervisory groups of the Americas, Caribbean, Middle East, Central Asia and Transcaucasia, SEANZA (South-East Asia and Australasia), Central and Eastern Europe, and Africa.<sup>2381</sup> It also conducts training programmes on banking supervisory issues.<sup>2382</sup> It has also set up a Financial Stability Institute (FSI) since 1999 in cooperation with the BIS to conduct multi-level training programmes.<sup>2383</sup>

The IAIS, formed in 1994, serves as global forum for cooperation to promote insurance regulation and financial stability.<sup>2384</sup> It holds annual conferences to enable insurance supervisors, industry representatives and other professionals to discuss on developments in the insurance sector and on topics affecting insurance regulation.<sup>2385</sup> It trains insurance supervisors in cooperation with the World Bank Group.<sup>2386</sup> It has also developed Multilateral Memorandum of Understanding

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2376 Note the objectives and principles in the GATS, the Articles of Agreement of the IMF, and the constitutions of the World Bank and UNCTAD. Particular international competition rules and authority are not developed yet although there has been discussion on the matter within these institutions and others including the OECD and the International Competition Network (ICN) (Note the competition pages in websites of the organizations).

2377 Note the histories, works and memberships of the institutions (which are growing from time to time) from BIS, 2007; BCBS, 2007; IAIS, 2007a; IOSCO, 2007; IOPS, 2007a; ICN, 2010; ICN, 2010a; ICN, 2010b; and ICN, 2010d.

2378 BCBS, 2007, at p. 1.

2379 *Id.*, at pp. 4-5.

2380 *Ibid.*

2381 *Ibid.*

2382 *Id.*, at p. 6.

2383 *Ibid.*

2384 IAIS, 2007a.

2385 *Ibid.*

2386 *Ibid.*

(MMoU) since February 2007 to enhance cooperation and information exchange among insurance regulators.<sup>2387</sup>

The IOSCO, formed in 1983, serves as forum for international cooperation to:

- standardize regulation of securities markets;
- exchange information on regulatory experience; and
- provide assistance in the application of international standards in the regulation of securities markets.<sup>2388</sup>

It has developed multilateral memorandum of understanding (IOSCO MOU) since 2002 to facilitate cross-border exchange of information among the securities market regulators, endorsed the IOSCO MOU in 2005 as benchmark for international cooperation, and expanded the signatories of the IOSCO MOU by 2010.<sup>2389</sup> It has also adopted consultation policy to facilitate continuous interaction among the securities markets, the regulators and the international community.<sup>2390</sup>

The IOPS, formed in July 2004, serves as forum for policy dialogue and exchange of information for promoting good practices in the regulation of private pensions.<sup>2391</sup> It serves as:

- standard-setting body for pension regulation;
- forum for international co-operation between pension supervisors, policy makers, researchers and the private sector; and
- forum for statistical collection and analysis.<sup>2392</sup>

The ICN, formed in October 2001, serves as forum for international cooperation to address competition concerns.<sup>2393</sup> It works to:

- encourage the dissemination of competition law experience and best practices,
- develop procedural and substantive principles and standards for competition law enforcement;
- promote the advocacy roles of competition authorities;
- increase international cooperation among competition authorities, practitioners and others;
- increase international convergence in competition law and practice;
- facilitate the work relationship between firms and competition authorities; and
- achieve better competition law enforcement and advocacy.<sup>2394</sup>

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2387 Note the IAIS Multilateral Memorandum of Understanding on Cooperation and Information Exchange (IAIS MMOU) (February 2007) and the IAIS MMOU (as modified on 18 November 2009) from IAIS, 2007 and IAIS, 2009.

2388 IOSCO, 2007.

2389 Ibid.

2390 Ibid.

2391 IOPS, 2007a.

2392 Ibid.

2393 Ewing, 2006, at pp. 296-313 & 653-673; ICN, 2010; ICN, 2010a; and ICN, 2010c.

2394 Ibid.

It does this by making its membership open to national and multinational bodies entrusted with the enforcement of competition law; organizing projects, seminars, workshops and annual conferences; inviting participation of competition experts from the consumer, business and academic communities and the legal profession; and disseminating its work products and documents through its website and an ICN public email distribution list.<sup>2395</sup>

The international institutions also cooperate and work together on cross sectoral matters. The BCBS, IAIS and IOSCO have developed Joint Forum for purpose of this.<sup>2396</sup> The BCBS also works with the International Association of Deposit Insurers (IADI) on matters of deposit insurance.<sup>2397</sup> It also works with the regional organizations across the Americas, Europe, Asia and Africa on matters of banking and related regulation.<sup>2398</sup> The IOPS works with the other international organisations involved in pension policy development and dialogue, including the OECD, World Bank, IAIS, IMF and the International Social Security Association (ISSA).<sup>2399</sup> The ICN also works with the bodies working in the competition field including the WTO, UNCTAD, and the OECD.<sup>2400</sup> The IMF and World Bank have also developed a joint Financial Sector Assessment Program (FSAP) to assess the financial systems of their member countries.<sup>2401</sup> The World Savings Banks Institute (WSBI) and the European Savings Banks Group (ESBG) also work with savings and retail banking institutions and the BCBS to encourage the expansion and appropriate regulation of microfinance and corporate social responsibility.<sup>2402</sup>

The G-20 is also serving as forum for strengthening the international financial architecture and fostering sustainable economic growth and development.<sup>2403</sup> It has served as forum for international cooperation among the developed and the transition and emerging market countries in finding out the solutions to the 2008 financial and economic crisis.<sup>2404</sup>

A new organization of emerging market countries called BRIC is also established to coordinate the financial and economic developments in its member countries.<sup>2405</sup>

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2395 ICN, 2010c; ICN, 2010d; and ICN, 2010e.

2396 BCBS, 2006, at pp. 4-5; and the information about history, mandate and publications of the Forum from IOSCO, 2007b.

2397 BCBS-IADI, 2009; and IADI, 2007-10.

2398 BCBS, 2006, at pp. 27-72.

2399 IOPS, 2007a.

2400 ICN, 2010c.

2401 The FSAP was launched in 1999. Participation to it is voluntary. More than two-thirds of the members of the institutions have participated in it. IMF, 2005; IMF, 2007-10; and IMF, 2007-10a.

2402 Degefe Duressa Obo, 2009, at pp. 1-3; and websites of the institutions (accessed on May 29 2007 and August 23 2010).

2403 G-20, 2009; and Wikipedia, 2010a.

2404 G-20, 2009; BBC, 2009a; BBC, 2009b; AP, 2009b; AP, 2009c; Reuters, 2009a; and Wikipedia, 2010a.

2405 The first official meeting of the organisation was on 16 June 2009. Its current members are Brazil, Russia, India, China and South Africa. Its membership is expected to rise in the future. Wikipedia, 2011.

The international and regional institutions have, accordingly, been useful to develop the financial markets and regulatory and competition law systems in the developed and transition and emerging market countries. A global regulatory and governance structure that can regulate systemic risk in the financial markets is not, however, developed yet.<sup>2406</sup> The 2008 financial and economic crisis has increased the need for this.<sup>2407</sup>

## ii. The Case of Ethiopia

Ethiopia cooperates with the IMF and the World Bank and tries to see if its financial regulatory actions are in line with the internationally accepted principles and standards.<sup>2408</sup> It, however, does this outside the Financial Sector Assessment Program (FSAP) of the IMF and the World Bank.<sup>2409</sup> It also lacks formal membership and cooperation with the international organizations working in the area of financial market regulation and competition including the BCBS, IAIS, IOSCO, IOPS and ICN.

It does not also work with regional associations on the matters of financial market regulation. This does not happen for two reasons. Firstly, no regional organization of financial market regulators is active currently in the Eastern African Region. Both the Common Market for Eastern and Southern Africa (COMESA) and the Intergovernmental Authority on Development (IGAD) are overwhelmed by general economic integration and regional peace matters as opposed to financial market regulation issues.<sup>2410</sup> The monetary cooperation realm of COMESA and the COMESA Bankers' Association are not also working on matters of financial market regulation although they have started their operations by promising to work on banking practices and regulations among others.<sup>2411</sup> The Eastern and Southern African Banking Supervisors Group (ESAF) is also dissolved as of November 2004 by decision of the Committee of the Central Bank Governors (CCBG) of the Southern African Development Community (SADC) so that the CCBG will have subcommittee on banking supervision in line with the SADC regional integration process only.<sup>2412</sup> Secondly, the peace and policy situation in the Eastern African Region is not conducive for the financial market regulators of the region to initiate direct cooperation on financial market regulatory issues. The countries of the region suffer from recurring political disagreements and policies of non-liberalized financial markets.<sup>2413</sup>

2406 Alexander, et al., 2006; Banyár and Mészáros, 2009, at pp. 154-164; and Chorafas, 2009, at pp. 202-205 & 239-242.

2407 Christoph Ohler, 2009; J. Balvin Hannibalsson, 2009; Chorafas, 2009, at pp. 202-205 & 239-242; Chapman, 2010, at pp. 250-252; Moschella, 2010; OECD, 2009f; World Bank, 2009b; IMF, 2009; IMF & FSB, 2009; WTO, 2009; G-20, 2009; AP, 2009b; AP, 2009c; BBC, 2009; BBC, 2009a; BBC, 2009b; and Bloomberg, 2010.

2408 Note the country reports of the IMF and World Bank for Ethiopia from their websites; and NBE BSD, 2005 & NBE ISD, 2005 as revised.

2409 Note the IMF-FSSA Country Reports from IMF, 2007-10; and IMF, 2007-10a.

2410 COMESA, 2006; and IGAD, 2007.

2411 Note the COMESA Monetary Cooperation Programme and the works of the COMESA Bankers' Association from COMESA, 2007 and COMESA-BA, 2007.

2412 BCBS, 2006b, at p. 68.

2413 Note the conflict situations surrounding Ethiopia, Eritrea, Somalia, Sudan and Egypt.

The country needs to appreciate the importance of cooperation with the international organizations in order to build its regulatory capacity, enhance its regulatory functions and fight against illicit financing, and encourage membership and cooperation of the financial market regulator (i.e. the NBE) to the BCBS, the IAIS and the other relevant international organizations in the short run and to the IOSCO and IOPS when it creates the securities market and private pension regulators in the future. It also needs to encourage the membership and cooperation of its competition enforcement organs with the ICN in order to build its competition law enforcement capacity and functions.

## 5.5.2 The Use of the Basel and IAIS Principles

### i. The International Experience

The BCBS has pursued principles and standards in the areas of international supervisory coverage, capital adequacy, and effective banking supervision as part of its effort to foster international monetary and financial stability under the BIS.<sup>2414</sup>

It has pursued two basic principles in its effort to close the gaps in international supervisory coverage, namely that no foreign banking establishment should escape supervision; and that supervision should be adequate.<sup>2415</sup> It has issued several documents to meet the principles as of 1975, including the following:

- the May 1983 Principles for Supervision of Banks' Foreign Establishments that laid down the principles for consolidated supervision of international banking groups (known as the 1983 Concordat);
- the April 1990 Supplement to the 1983 Concordat that was issued to improve the flow of prudential information among the banking supervisors in different countries;
- the July 1992 Minimum Standards for consolidated supervision of international banking groups; and
- the June 1996 document for overcoming impediments to conducting effective consolidated supervision of the cross-border operations of international banks.<sup>2416</sup>

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<sup>2414</sup> The BIS was established on 17 May 1930. It served as forum to promote discussion and policy analysis among central banks and the international financial community; centre for economic and monetary research; and counter-party, agent or trustee for central banks in international financial transactions. It exists as forum for international monetary and financial cooperation. The BCBS was established under the BIS by the central-bank Governors of the Group of Ten countries. Its members are the central banks (and banking regulators) of Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Spain, Sweden, Switzerland, United Kingdom and the United States. Its secretariat is at the BIS in Basel. It reports to the central bank Governors and heads of the banking supervisory authorities of the Group of Ten countries. It also acts under their endorsement of its initiatives. BIS, 2007; and BCBS, 2007.

<sup>2415</sup> BCBS, 2007, at p. 2.

<sup>2416</sup> Ibid.

It has developed a Capital Adequacy Accord and a Revised Capital Adequacy Framework in its effort to develop multinational capital adequacy measurement standard. It proposed the first capital measurement system in 1987 and this was approved by the G-10 Governors in July 1988 as the Basel Capital Accord to provide for the implementation of credit risk measurement with a minimum capital standard of 8% by 1992.<sup>2417</sup> It initiated amendments on the Accord between 1991 and 1996 to give it greater precision and expand its coverage from credit risk to market risk.<sup>2418</sup> It proposed the revised Capital Adequacy Framework in June 1999 to improve on the way regulatory capital requirements reflect the underlying risks in the banking book, better address the recent financial innovations, and thereby replace the 1988 Capital Accord with a system that consists of the following three pillars:

- minimum capital requirements (that seek to refine the standardized rules of the 1988 Capital Accord and expand them to credit, market and operational risks);
- supervisory review requirements (that seek to assist the banks' internal assessment processes); and
- disclosure principles (that seek to strengthen the use of market discipline as complement to the supervisory efforts).<sup>2419</sup>

It issued the Framework on 26 June 2004 after interaction with banks, industry groups and supervisory authorities that are both members and non-members to the Committee.<sup>2420</sup> It also published a consensus document governing the treatment of banks' trading books under the new Framework in July 2005 after having worked with the International Organization of Securities Commissions (IOSCO) and integrated this with the June 2004 text by document released in June 2006.<sup>2421</sup> The 1988 Capital Accord and the Revised Capital Adequacy Framework have served as benchmarks for national rule-making and bank performance in both the BCBS member and non-member countries.<sup>2422</sup>

It has developed 'core supervisory principles and methodology' in its effort to assist the development of effective banking supervision.<sup>2423</sup> It developed the first Core Principles for Effective Banking Supervision in 1997 in collaboration with the G-10 and non-G10 supervisory authorities and the first Core Principles Methodology in October 1999 to facilitate the implementation and assessment of the core principles.<sup>2424</sup> It has issued the core principles to set minimum standards for sound supervisory practices in the following seven areas:

- preconditions for effective banking supervision (Principle 1);
- licensing and structure of banks (Principles 2 to 5);

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2417 Ibid.

2418 Id., at p. 3.

2419 Ibid.

2420 Ibid.

2421 Ibid.

2422 Id., at pp. 3-4

2423 Id., at p. 5.

2424 BCBS, 1997; BCBS, 1999; and BCBS, 2007, at p. 5.

- prudential regulation and requirements (Principles 6 to 15);
- methods of ongoing supervision (Principles 16 to 20);
- information disclosure requirements (Principle 21);
- powers of supervisors (Principle 22); and
- cross-border banking (Principles 23 to 25).<sup>2425</sup>

It has issued the Core Principles Methodology to provide guidance for assessment of the compliance of national systems to the core principles by different parties including the IMF, the World Bank, regional supervisory groups, regional development banks and consulting firms.<sup>2426</sup>

It has revised both the Core Principles and the Methodology in October 2006 after consultation with representatives from its member countries, the non-member central banks and supervisory authorities, the IMF, the World Bank, the IAIS, the IOSCO, the FATF, the CPSS, the regional groups of supervisors, the international trade associations, the academia, and other parties.<sup>2427</sup> The revised 'Core Principles' currently defines 25 principles in the following seven areas:

- objectives, independence, powers, transparency and cooperation (principle 1);
- licensing and structure (principles 2 to 5);
- prudential regulation and requirements (principles 6 to 18);
- methods of ongoing banking supervision (principles 19 to 21);
- accounting and disclosure (principle 22);
- corrective and remedial powers of supervisors (principle 23); and
- consolidated and cross-border banking supervision (principles 24 and 25).<sup>2428</sup>

It also elaborates on the following as preconditions for effective banking supervision and requires the banking supervisors to react against their shortcomings:

- sound and sustainable macroeconomic policy;
- well developed public infrastructure;
- effective market discipline; and
- appropriate level of systemic protection (or public safety net).<sup>2429</sup>

The revised Methodology sets the techniques, criteria and considerations for assessment of compliance with the principles.<sup>2430</sup> It is, like the first methodology, meant for multiple use, including the making of:

- self-assessment by the banking supervisors themselves;
- the IMF and World Bank assessments of the quality of supervisory systems under the Financial Sector Assessment Program;

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2425 BCBS, 1997.

2426 BCBS, 1999.

2427 BCBS, 2006; BCBS, 2006a; and BCBS, 2007, at p. 5.

2428 BCBS, 2006, at pp. 2-5.

2429 Id., at pp. 6-7.

2430 BCBS, 2006a, at pp. 2-42.

- review by private third parties such as consultants and researchers; and
- peer review such as by the regional banking supervisory groups.<sup>2431</sup>

The Committee has also issued principles and standards on questions relating to the following:

- credit risk and securitization;
- liquidity and operational risks;
- risk management;
- transparency and disclosure; and
- money laundering and terrorist financing.<sup>2432</sup>

It has published papers on:

- supervision and management of banks' interest and foreign exchange risks, international lending and country risks, and off-balance-sheet exposures;
- implementation of customer due diligence;
- supervision of large exposures;
- use of risk management guidelines (such as for derivatives);
- adoption of sound practices for loan accounting and disclosure;
- enhancement of corporate governance;
- valuation of loans; and
- supervision of electronic banking.<sup>2433</sup>

It has also worked on a number of technical banking and accounting issues in cooperation with the International Accounting Standards Committee, the International Auditing Practices Committee of the International Federation of Accountants, and the International Chamber of Commerce.<sup>2434</sup> It has also worked on issues common to the banking, insurance and securities markets and developed principles for supervising financial conglomerates, among others, in collaboration with the IAIS and IOSCO.<sup>2435</sup>

It has also issued the following principles and consultative documents in the aftermath of the 2008 financial and economic crisis:

- 'Principles for Sound Liquidity Risk Management and Supervision' (September 2008);
- 'Principles for Sound Stress Testing Practices and Supervision' (May 2009);
- 'Core Principles for Effective Deposit Insurance Systems' (June 2009, issued in cooperation with the International Association of Deposit Insurers - IADI);
- Consultative Document on Microfinance Activities and the Core Principles for Effective Banking Supervision (February 2010);

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2431 Id., at pp. 1-2.

2432 Note the BCBS 'Publications by category' from BCBS, 2010c.

2433 BCBS, 2007, at p. 4; BCBS, 2009a; and the BCBS 'Publications by category' from BCBS, 2010c.

2434 Ibid.

2435 BCBS, 2007; BCBS, 2009a; and the history, mandate and works of the joint forum of the BCBS, IAIS and IOSCO from BCBS, 2010d; BCBS, 2010e; and BCBS, 2010f.

- Consultative Document on Strengthening of the Resilience of the Banking Sector (prepared in December 2009 and issued for comment on 16 April 2010); and
- Consultative Document on International Framework for Liquidity Risk Measurement, Standards and Monitoring (prepared in December 2009 and issued for comment on 16 April 2010).<sup>2436</sup>

The IAIS has assisted the development of sound insurance markets, the improvement of domestic and international supervision of insurance markets, and the maintenance of global financial stability as of its establishment in 1994.<sup>2437</sup> It has done this by issuing principles, standards and guidance papers on various issues; providing training and support on issues related to insurance supervision; and organising meetings and seminars for insurance supervisors.<sup>2438</sup> Its principles, standards and guidance papers have focused on the:

- organization and practice of insurance supervision;
- corporate governance, internal control, prudential regulation, and conduct-of-business of insurance companies; and
- supervision of re-insurance, cross-border insurance and insurance on the internet.<sup>2439</sup>

It has issued a 'Core Principles and Methodology' for effective insurance supervision and assessment in October 2003 and six sets of principles on the following areas:

- supervision of international insurers, insurance groups and cross-border operations (Insurance Concordat, December 1999);
- conduct of insurance business (December 1999);
- supervision of insurance activities on the Internet (October 2004);
- capital adequacy & solvency (January 2002);

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2436 BCBS, 2008; BCBS, 2009; BCBS-IADI, 2009; BCBS, 2010; BCBS, 2010a; and BCBS, 2010b. The crisis has also triggered discussion on the need for revising the 2004 (Basel II) Capital Framework. The 1988 Capital Accord (Basel I) was recognition of the international expansion of the financial services in the 1980s and 1990s. The 2004 Framework (Basel II) was endorsement of the expansion of the trading of credit and derivatives by banks. The post 2008 call is for adoption of a Basel III capital regime that, as response to the 2008 financial and economic crisis, will i) modify the Basel II risk-weighted asset framework and the requirements on operational risk; ii) introduce new capital buffers, leverage ratios, provisioning requirements, liquidity rules and a principle of equal regulatory treatment of the financial markets; and iii) create regime for the concentration (conglomeration) problem. McIlroy, 2008; Moosa, 2008; Adrian Blundell-Wignall, et al., 2009a; Christoph Ohler, 2009; Goodhart, 2009, at pp. 98-112; Moosa, 2010; Adrian Blundell-Wignall and Paul Atkinson, 2010; Chapman, 2010, at pp. 192-197; and the 2008 up to 2010 publications of the Basel Committee on Banking Supervision posted in the 'banking problems' and the 'Basel II framework' publication categories of the website cited as BCBS, 2010c.

2437 It was established as association of regulators and supervisors of insurance markets. It currently represents insurance regulators and supervisors of more than 180 jurisdictions in more than 130 countries around the world. It includes more than 100 observers representing industry associations, professional associations, insurers, re-insurers, consultants and international financial institutions. IAIS, 2007a.

2438 Ibid.

2439 IAIS, 2003; IAIS, 1999; IAIS, 1999a; IAIS, 2002; IAIS, 2002a; and IAIS, 2004.

- minimum requirements for supervision of re-insurers (October 2002); and
- group-wide supervision (October 17 2008).<sup>2440</sup>

It has issued the standards on the following seventeen areas of particular issue:

- licensing (October 1998);
- on-site inspection (October 1998);
- derivatives (October 1998);
- asset management by insurance companies (December 1999);
- group coordination (October 2000);
- exchange of information (January 2002);
- evaluation of reinsurance cover of primary insurers & security of re-insurers (January 2002);
- supervision of re-insurers (October 2003);
- disclosures concerning technical performance and risks for non-life insurers and re-insurers (October 2004);
- fit and proper requirements and assessment for insurers (October 2005);
- disclosures concerning investment risks and performance for insurers and re-insurers (October 2005);
- disclosures concerning technical risks and performance for life insurers (October 2006);
- asset-liability management (October 2006);
- structure of regulatory capital requirements (October 17 2008);
- risk measurement for capital adequacy and solvency purposes (October 17 2008);
- Internal Models for regulatory capital purposes (October 17 2008); and
- structure of capital resources for solvency purposes (November 02 2009).<sup>2441</sup>

It has issued the guidance papers (as adjunct to the principles and standards) on the following:

- insurance regulation and supervision for emerging market economies (September 1997);
- model memorandum of understanding (to facilitate the exchange of information between financial supervisors) (September 1997);
- fit and proper principles and their application (October 2000);
- public disclosure by insurers (January 2002);
- anti-money laundering and combating the financing of terrorism (October 2004);
- solvency control levels (October 2003);
- use of actuaries as part of supervisory model (October 2003);
- stress testing by insurers (October 2003);
- investment risk management (October 2004);

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2440 IAIS, 1999; IAIS, 1999a; IAIS, 2002; IAIS, 2002a; IAIS, 2003; IAIS, 2004; and IAIS, 2008.

2441 IAIS, 1998; IAIS, 1998a; IAIS, 1998b; IAIS, 1999b; IAIS, 2000; IAIS, 2002b; IAIS, 2002c; IAIS, 2003a; IAIS, 2004a; IAIS, 2005; IAIS, 2005a; IAIS, 2006; IAIS, 2006a; IAIS, 2008a; IAIS, 2008b; IAIS, 2008c; and IAIS, 2009a.

- combating the misuse of insurers for illicit purposes (October 2005);
- risk transfer, disclosure and analysis of finite reinsurance (October 2006);
- preventing, detecting and remedying fraud in insurance (October 2006);
- structure of regulatory capital requirements (October 17 2008);
- risk measurement for capital adequacy and solvency purposes (October 17 2008);
- internal models for regulatory capital purpose (October 17 2008);
- mutual recognition of reinsurance supervision (October 17 2008);
- regulation and supervision of captive insurers (October 17 2008);
- roles and responsibilities of group-wide supervisors (October 17 2008);
- use of supervisory colleges in group-wide supervision (October 26 2009);
- structure of capital resources for solvency purposes (November 02 2009); and
- treatment of non-regulated entities in group-wide supervision (May 11 2010).<sup>2442</sup>

The specific principles serve as fundamentals to effective insurance supervision and form the basis for the standards while the standards describe and elaborate on the best and most prudent practices on the particular issues.<sup>2443</sup> The principles and standards set and describe the practices for a supervisory authority (and well managed insurer) so that the supervisors may use them in assessing the practices of the insurance companies in their jurisdictions.<sup>2444</sup> The guidance papers are issued to assist the supervisors' efforts to raise the effectiveness of supervision.<sup>2445</sup> The 'Core Principles and Methodology' define the essential principles that need to be in place for an insurance supervisory system to be effective; the techniques and criteria for assessing practice against the principles; and the factors that need to be considered in implementing the principles.<sup>2446</sup> They are, like the Basel Core Principles and Methodology on banking supervision, meant for use in the making of:

- self-assessment by the banking supervisors themselves;
- the IMF and World Bank assessments under the Financial Sector Assessment Program (FSAP);
- review by private third parties such as consulting firms; and
- peer review such as by regional groupings.<sup>2447</sup>

The BCBS and IAIS do not, however, possess formal supranational supervisory authority and their conclusions do not have legal force.<sup>2448</sup> They only formulate and recommend broad supervisory principles, standards, guidelines and statements of best practices for implementation by the national regulatory authorities and encourage convergence towards common approaches and

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<sup>2442</sup> IAIS, 2007d.

<sup>2443</sup> IAIS, 2007b; and IAIS, 2007c.

<sup>2444</sup> Ibid.

<sup>2445</sup> IAIS, 2007d.

<sup>2446</sup> IAIS, 2003. They are expected to be implemented according to the domestic context, industry structure and stage of development of the financial system and the overall macroeconomic conditions of the country in question (IAIS, 2003, at Annex 2).

<sup>2447</sup> Id., at pp. 5 & 50.

<sup>2448</sup> BCBS, 2007, at p. 1; and IAIS, 2007a.

standards.<sup>2449</sup> Hence, their standards and principles serve as non-binding, but universally applicable, minimum frameworks for improving domestic and international financial stability and providing bases for further development of effective supervisory and market practices.<sup>2450</sup> Their core principles and the essential criteria for assessment of the principles also serve as base-line for assessing the existence of sound prudential regulation and supervision in a country.<sup>2451</sup>

Countries also use the Basel and IAIS core principles, methodologies, standards and guidelines in practice as minimum benchmarks for assessing the qualities of their supervisory systems and practices and identifying the works to be done to achieve a level of sound supervisory practice.<sup>2452</sup> The IMF and World Bank also use them for their Financial Sector Assessment Program (FSAP) to assess the financial supervision systems and practices across their member countries.<sup>2453</sup>

## ii. The Case of Ethiopia

The NBE is not member to the BCBS and IAIS.<sup>2454</sup> The country has not also joined the IMF-World Bank Financial Sector Assessment Program.<sup>2455</sup>

The banking and insurance supervision regimes of the country also comply little with the BCBS and IAIS core principles on effective banking and insurance supervision.<sup>2456</sup> The weaknesses are mostly in the risk orientation, corporate governance, enforcement and infrastructure of the regulations although a lot has also to be improved in respect of the other aspects of the principles.<sup>2457</sup> The weaknesses of the microfinance supervision regime are not also different from the weaknesses of the banking and insurance supervision regimes.<sup>2458</sup>

Hence, the banking, insurance and microfinance supervision departments of the NBE need to:

- make their supervisory approaches more risk oriented than they are now;
- enhance the corporate governance structures and working environments of the banks; insurers and microfinance institutions;
- increase the effectiveness of their regulatory enforcement; and

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2449 Ibid.

2450 BCBS, 2006, at p. 2; BCBS, 2006a, at pp. 1-2; and IAIS, 2003, at pp. 4-6.

2451 Ibid.

2452 BCBS, 2006, at pp. 1-2; BCBS, 2006a, at p. 1; BCBS, 2009a; IAIS, 2003, at pp. 5 & 50; and IAIS, 2009, at pp. 9-12.

2453 IMF, 2005; IMF, 2007-10; and IMF, 2007-10a.

2454 BCBS, 2007; BCBS, 2009a; and IAIS, 2007e.

2455 Note the IMF-FSSA Country Reports from IMF, 2007-10; and the discussion under the 'use of international cooperation' subtitle above.

2456 Tables 3(Chap. 5) & 4(Chap. 5).

2457 Note Tables 3(Chap. 5) & 4(Chap. 5); NBE, 2010; and the discussions under the preceding subtitles of this chapter and the various subtitles of the banking, insurance and microfinance chapter above.

2458 Note the discussions under the various subtitles of the banking, insurance and microfinance chapter above and compare the country's microfinance supervision regime with the BCBS 'Consultative Document on Microfinance Activities and the Core Principles for Effective Banking Supervision' (BCBS, 2010).

- align the objectives and instruments of their regulations with the international principles.

### 5.5.3 The Use of the IOSCO, IOPS, ICN and Other Principles

#### i. The International Experience

The IOSCO has issued Objectives and Principles of Securities Regulation in September 1998 and indicated three major objectives of securities regulation:

- protecting investors;
- assuring market fairness, efficiency and transparency; and
- reducing systemic risk.<sup>2459</sup>

It has issued thirty principles of achieving these objectives in the following areas:

- responsibilities of securities regulators (Principles 1 to 5);
- self-regulation of securities markets (Principles 6 and 7);
- enforcement of securities regulation (Principles 8 to 10);
- domestic and international cooperation in securities regulation (Principles 11 to 13);
- responsibilities of securities issuers (Principles 14 to 16);
- rules and standards for collective investment (Principles 17 to 20);
- rules and standards for secondary markets (Principles 25 to 29);
- requirements for market intermediaries (Principles 21 to 24); and
- systems for clearance and settlement of securities transactions (Principle 30).<sup>2460</sup>

The principles focus on the fairness, efficient functioning and stability of the securities markets themselves excluding the broader issues of macroeconomic and financial policy that are associated with systemic instability.<sup>2461</sup>

The IOSCO has also issued an IOSCO Principles Assessment Methodology in 2003 to enable the objective assessment of the level of implementation of its Objectives and Principles in the jurisdictions of its member countries and the development of action plans to correct deficiencies.<sup>2462</sup> It has issued a Multilateral Memorandum of Understanding Concerning Consultation, Cooperation and Exchange of Information among its members on the matters of securities regulation.<sup>2463</sup> It has also enhanced its activities following the 2008 financial and economic crisis to contribute to the resolution of the issues that affect the

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2459 IOSCO, 2003; and IOSCO Resolution No. 41 of September 1998.

2460 Ibid.

2461 Yılmaz Akyüz, 2002, at pp. 50-51. The development of more comprehensive and representative set of principles that cover the latter and aspects of policy towards capital account liberalization and commercial presence of foreign investors in securities markets is also seen to be important for actions of the IOSCO and others.

2462 IOSCO, 2003a.

2463 IOSCO, 2010; IOSCO, 2010a; and IOSCO, 2010b.

securities markets and revised its strategic direction in order to increase its roles to:

- enhance the international regulatory framework for securities markets through international standards;
- identify and address the systemic risks to fair and efficient functioning of markets; and
- advance the implementation of its Objectives and Principles of Securities Regulation.<sup>2464</sup>

The IOPS has issued Principles of Private Pension Supervision for effective regulation of occupational and personal pension plans.<sup>2465</sup> It has addressed three major objectives of pension supervision by the principles:

- promotion of pension (and financial) stability, security and good governance,
- protection of the interests of pension fund members and beneficiaries, and
- encouragement of pension provision.<sup>2466</sup>

It has issued the principles in the following areas:

- objectives, powers, resources and independence of the pension regulator (Principles 1 to 4);
- risk orientation, proportionality and consistency of the pension regulation (Principles 5 & 6);
- consultation of the regulated pensions (Principle 7);
- cooperation between the pension and other regulators (Principle 7);
- confidentiality of information (Principle 8); and
- transparency, governance and accountability of the pension regulators (Principles 9 & 10).<sup>2467</sup>

It has also developed the following guidelines and methodology during and in the aftermath of the 2008 financial and economic crisis:

- OECD-IOPS Guidelines on Licensing of Pension Entities (March 2008);
- IOPS Guidelines for Supervisory Assessment of Pension Funds (December 2008);
- IOPS Guidelines for Supervisory Intervention, Enforcement and Sanctions (November 2009); and
- Methodology for Review of Supervisory Systems Using the IOPS Principles of Private Pension Supervision.<sup>2468</sup>

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2464 IOSCO, 2008; and IOSCO, 2009. It has set its future operational priorities to be i) building the regulatory capacities of its members, ii) enhancing the ongoing development of international regulatory standards to deal with emerging risks and the inadequate functioning of markets, iii) supporting the development of the international enforcement and surveillance framework, iv) improving its liaison with other international financial standard setters, v) enhancing its representation in global decision making forums, vi) strengthening its communications with stakeholders including investors and bodies that represent industries, and vii) promoting international cooperation in the fields of securities market and other financial market regulations (IOSCO, 2009).

2465 IOPS, 2006.

2466 Ibid.

2467 Ibid.

2468 IOPS, 2008; IOPS, 2008a; IOPS, 2009; IOPS, 2010; and IOPS, 2010e.

It has also been working to develop an OECD-IOPS Good Practices framework for Pension Funds' Alternative Investments and Risk-Management Systems starting from 2008.<sup>2469</sup> Its work program for the period from 2008 up to 2011 has also included revision of the 2006 Principles, updating of the Methodology for their Assessment, and development of guidelines for the risk-based regulation and supervision of pensions.<sup>2470</sup> It has also issued document on IOPS Consultation Process and made several publications on technical matters relating to the supervision of private pensions during and after the crisis.<sup>2471</sup>

The ICN has issued the following principles, recommendations and manuals:<sup>2472</sup>

- Guiding Principles for Merger Notification & Review Procedure (2002);
- Recommended Practices for Merger Notification & Review Procedures (2002-2005);
- Best Practices: An Increasing Role for Competition in the Regulation of Banks (2005);
- The Role for Competition in the Telecommunications Services Sector: Suggested Best Practices (2006);
- Recommended Practices for Dominance/Substantial Market Power Analysis (2008);
- Recommended Practices on State Created Monopolies (2008);
- Recommended Practices for Merger Analysis (2008-2010);
- Anti-Cartel Enforcement Manual - Chapters 1 to 6 (2008-2010); and
- Competition Agency Practice Manual - Chapter 1: Strategic Planning and Prioritization (SPP) (2010)

It has also issued several study reports, discussion papers and reference materials for general, substantive and procedural issues including workbooks and handbooks in the fields of cartel, merger, unilateral conduct (market dominance), competition advocacy, agency effectiveness (competition policy implementation), capacity building, and competition enforcement in regulated sectors (including

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2469 IOPS, 2008b; IOPS, 2008d; IOPS, 2009a; IOPS, 2010a; IOPS, 2008c; IOPS, 2010b; and IOPS, 2010e.

2470 It has, accordingly, launched i) a project on Risk-based Supervision (RBS) Toolkit (in 2008) whose goal is to provide guidance for supervisory authorities on how to introduce and develop a risk-based system of supervision for pension funds by 2010 and thereafter; ii) a project on supervising DC pensions (in 2009) whose aim is to draw on previous work and reports of the IOPS and provide an overview of the issues which are particularly important when supervising defined contribution pension systems by 2010 and thereafter; and iii) a project on Regulation and Supervision of Alternative Investments Risk Management (in 2010) whose aim is to examine how the good practices operate and are applied in its member countries. It has also planned i) a project on Information for DC Scheme Members (to be launched in 2011) to examine how supervisory authorities themselves can act as sources of comparative and objective information for pension fund members; ii) a project on Financial Education (to be launched in 2011) whose aim is to make the IOPS participate in the OECD work in the areas of financial education where pension supervisors play an important role; and iii) a project on issues surrounding the coverage of pension fund systems in the context of developing countries (to be presented in 2011). IOPS, 2008b; IOPS, 2008d; IOPS, 2009a; IOPS, 2010a; and IOPS, 2010b.

2471 IOPS, 2006a; and the list of press releases, guidelines, working papers and other publications from IOPS, 2010c and IOPS, 2010d.

2472 ICN, 2010d.

banking and telecommunications) until September 2010.<sup>2473</sup> It currently works through an advocacy working group, an agency effectiveness working group, a cartel working group, a merger working group, a unilateral conduct working group, and an advocacy and implementation network.<sup>2474</sup>

The IMF, World Bank, OECD, International Accounting Standards Committee (IASC) (renamed later as International Accounting Standards Board), International Federation of Accountants (IFAC), BIS Committee on Payment Settlement Systems (CPSS), and G-7 Financial Action Task Force on Money Laundering (FATF) have also issued principles and standards many of which predated the financial crises of the 1990s and are incorporated recently into a global programme of coordination covering both the financial sector per se and the aspects of macroeconomic and disclosure policy.<sup>2475</sup>

The IMF has issued a Code of Good Practices on Transparency in Monetary and Financial Policies that requires:

- clear indication of the roles, responsibilities and objectives of the central banks and financial market regulators other than the central banks;
- creation of open process for the formulation and reporting of decisions on monetary and financial policy;
- publicity of information concerning monetary and financial policies;
- definition of accountability of the central banks and financial market regulators other than the central banks; and
- assurance of integrity of the central banks, other financial market regulators and their staff.<sup>2476</sup>

It has issued a Code of Good Practices on Fiscal Transparency to require:

- transparency of the fiscal roles and responsibilities of governments through clear legal and administrative framework for fiscal management;
- commitment of governments to public disclosure of comprehensive and reliable information on fiscal activities;
- openness of the process of budget preparation, execution and reporting; and
- public and independent scrutiny of fiscal information.<sup>2477</sup>

It has issued:

- a Special Data Dissemination Standard (SDDS - 1996) to prescribe the data to be made public concerning the fiscal, financial, non-financial, and external sectors of the economy by countries that intend to use the international capital markets and to lay down the minimum bench mark to be met on the periodicity and timeliness of the information;

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2473 ICN, 2010d; and ICN, 2010e.

2474 ICN, 2010d; and ICN, 2010f.

2475 Yilmaz Akyüz, 2002, at pp. 28ff.

2476 Id., at p. 33.

2477 Id., at pp. 33-34.

- a General Data Dissemination System (GDDS - 1997) to guide countries in the provision of comprehensive, timely, accessible and reliable economic, financial, and socio-demographic data to the public; and
- a Data Quality Reference Site (DQRS) and Data Quality Assessment Framework (DQAF) to require the improvement of the quality of data to be disclosed by all member countries of the IMF.<sup>2478</sup>

It has also been revising the codes of good practices and data dissemination standards to contribute to improvement of the financial market operations and attainment of global financial stability in the post 2008 period.<sup>2479</sup>

The World Bank has issued Principles and Guidelines on Effective Insolvency Systems that are intended to complement the legal and commercial systems of the transition and emerging market countries by international best practices; help the countries to tackle issues of cross-border dimension; and facilitate access of the countries to the international financial markets.<sup>2480</sup>

The OECD has issued Principles of Corporate Governance that focus on the definition of business objectives and the relationship among shareholders, board of directors, management, employees, creditors, customers and stakeholders of businesses and the community in the setting up of business objectives and monitoring of performances.<sup>2481</sup> It has addressed general principles on the following matters:

- protection of the rights of shareholders and the efficiency, transparency and fairness (to shareholders) of the markets for corporate control;
- equitable treatment of shareholders including minority and foreign shareholders through disclosure of material information and prohibition of abusive self-dealing and insider trading;
- recognition and protection of legally established rights of stakeholders and encouragement of cooperation between corporations and stakeholders in creating wealth, jobs and financially sound enterprises;
- transparency, timeliness and accuracy of disclosure and annual audits of company performance, ownership and governance by independent auditors; and
- strategic guidance of companies by management, monitoring of management by board, and accountability of the latter to the companies and their shareholders.<sup>2482</sup>

Its intention has not been to harmonize the national differences on matters of corporate governance but to indicate general guidelines on the matters to take care of.<sup>2483</sup> It has also issued Methodology for Assessing Implementation of the

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2478 IMF, 2010; IMF, 2010a; and Yilmaz Akyüz, 2002, at pp. 34-36.

2479 William, et al., (eds.), 2008; IMF, 2010; IMF, 2010a; and IMF, 2010b.

2480 Yilmaz Akyüz, 2002, at pp. 49-50; World Bank, 2001; World Bank, 2009c; World Bank, 2010d; and World Bank, 2010e.

2481 Yilmaz Akyüz, 2002, at pp. 47-48; OECD, 2004b; and OECD, 2004c.

2482 Ibid.

2483 Ibid.

OECD Principles on Corporate Governance in 2006 and undertaken works under action plan launched in 2008 to address the weaknesses in corporate governance that were discovered during the 2008 financial crisis.<sup>2484</sup>

The International Accounting Standards Committee (IASC) (renamed later as International Accounting Standards Board) and the International Federation of Accountants (IFAC) have issued International Accounting and Auditing Standards (respectively) with a view to harmonizing accounting and auditing practices and meeting the needs of cross-boarder businesses.<sup>2485</sup> The IASC has focused on the development of standards acceptable both to the United States and its other member countries.<sup>2486</sup> It was concerned with the reconciliation between the standards it wanted to develop for accounting and financial reporting worldwide and the specific Generally Accepted Accounting Principles of the United States.<sup>2487</sup> The IFAC has focused on the development of standards for internal auditing (i.e. the assessment of the extent and effectiveness of a firms' management, accounting and efficient use of assets) and external auditing (i.e. the auditing of financial statements and supporting evidence of the firm to determine their conformity with applicable standards) although much of its international initiative has been on the harmonization of the external auditing processes because countries often consider the internal auditing processes to be matters for domestic laws and the firms.<sup>2488</sup>

The BIS Committee on Payment Settlement Systems (CPSS) has developed CPSS Core Principles for Systemically Important Payments Systems (2001) and CPSS-IOSCO Recommendations for Securities Settlement Systems (2001) and Central Counterparties (2004) (in cooperation with the IOSCO) to address: the transfer and settlement of funds between financial institutions on their own behalf and on behalf of their customers, the payment and settlement systems for securities and foreign exchanges, and the clearing arrangements for exchange-traded derivatives.<sup>2489</sup> Its initiative has been to develop internationally agreed framework for the design, operation and oversight of the payment and settlement systems and reduce the credit, liquidity, legal, operational and systemic risks associated with the rising volumes of international payments. It has, accordingly, made its principles focus on the following:

- the legal basis for the payments system (first core principle);
- the rules and procedures to enable participants to have clear understanding of the impact of the payments system on financial risks and the management of credit and liquidity risks (second and third principles);

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2484 OECD, 2006b; OECD, 2009; OECD, 2009a; OECD, 2009b; OECD, 2009c; OECD, 2009d; OECD, 2010; and OECD, 2010a.

2485 Yilmaz Akyüz, 2002, at pp. 44-47; IASB, 2010; IASB, 2010a; IASB, 2010b; IFAC, 2010; IFAC, 2010a; IFAC, 2010b; IFAC, 2010c; and IFAC, 2010d.

2486 Ibid.

2487 Ibid.

2488 Ibid.

2489 Yilmaz Akyüz, 2002, at pp. 41-44; CPSS, 2001; CPSS-IOSCO, 2001; and CPSS-IOSCO, 2004.

- the need for settlement of assets with little or no credit risk and for prompt settlement (fourth and sixth principles);
- the robustness of multilateral netting systems (fifth principle);
- the minimization of operational risks through high degree of security and operational reliability (seventh principle); and
- the efficiency and practicality of the payments system (including the trade-off between safety and efficiency), the need for objective and publicly disclosed criteria for participation, the need for fair and open access, and the need for effective, accountable and transparent governance arrangements for the system (eighth, ninth and tenth principles).<sup>2490</sup>

It has also issued Assessment Methodology for 'Recommendations for Securities Settlement Systems' (November 2002), Central Bank Oversight of Payment and Settlement Systems (May 2005), General Guidance for National Payment System Development (January 2006), and General Principles for International Remittance Services (January 2007).<sup>2491</sup>

The G-7 Financial Action Task Force on Money Laundering (FATF) has also issued Forty plus Nine Recommendations that focus on the use of money for drug dealing, terrorism and corruption.<sup>2492</sup> It has addressed the following:

- incrimination of the use of proceeds of serious crimes;
- keeping of records;
- identification of customers;
- reporting of suspicious transactions to competent national authorities;
- development of programmes that can counter money laundering;
- development of internal control systems;
- training of employees;
- exercise of adequate supervision;
- sharing of expertise by supervisors with judicial and law enforcement authorities; and
- strengthening of international cooperation through information exchange, legal assistance, and bilateral and multilateral agreements.<sup>2493</sup>

It has also issued Methodology for Assessing Compliance with the Recommendations and adopted Key Principles for Mutual Evaluation and Assessment (which were prepared in collaboration with FATF Style Regional Bodies (FSRBs), the IMF and the World Bank).<sup>2494</sup> It has also issued guidance documents and best practice papers that are meant to assist the enhancement of mutual evaluations and combating of money laundering and terrorist financing.<sup>2495</sup>

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2490 Ibid.

2491 CPSS, 2005; CPSS, 2006; CPSS-IOSCO, 2002; and CPSS-World Bank, 2007.

2492 Yılmaz Akyüz, 2002, at pp. 53-55; FATF, 1996; FATF, 2001; FATF, 2004; FATF, 2004a; FATF, 2004b; FATF, 2004c; FATF, 2008; FATF, 2009d; and FATF, 2010a.

2493 Ibid.

2494 FATF, 2009; FATF, 2009c; and FATF, 2010.

2495 FATF, 2009a; FATF, 2010b; FATF, 2010c; and FATF, 2010d.

The principles and standards of the aforementioned institutions have, accordingly, served as international catalogue of national rules for the financial sector and competition by covering both the financial sector per se and the aspects of macroeconomic, disclosure and competition policy. The IOSCO Objectives, Principles and Methodologies for Securities Regulation, the IOPS Principles and Methodologies for Private Pension Supervision, and the ICN guiding principles, recommendations and manuals for aspects of competition policy are recognized as non-binding minimum international regulatory benchmarks for the securities and pension markets and regulators and the competition authorities.<sup>2496</sup> The principles and standards of the other institutions have also been used as benchmarks to promote international financial strength, integrity and stability and as preconditions for mutual assistance between countries (including the lending facilities of the IMF).<sup>2497</sup>

The institutions have also been working to help their member countries in the recovery from the 2008 financial and economic crisis and to assist the G-20 industrialized and emerging market countries and others to reshape their systems of regulation, governance and competition.<sup>2498</sup>

## ii. The Case of Ethiopia

Ethiopia does not apply the aforementioned principles, standards and recommendations because of the absence or underdevelopment of the markets and institutions for their application. It only tries to follow some of the IMF codes of good practices and FATF recommendations on money laundering.

It needs to enhance and align its system with the international approach in order to encourage trade, investment and stability in the financial and non-financial markets. It needs to consider the IMF, World Bank, OECD, IASC, IFAC, CPSS and FATF principles, standards and recommendations as it develops the monetary and financial policy, corporate governance, accounting, auditing, payments, settlement and insolvency systems for the existing and future markets. It also needs to consider the IOSCO and IOPS principles and standards as it creates the securities market and private pensions and the ICN guiding principles, recommendations and manuals as it develops its competition regime.

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2496 Note the 'introduction' to the IOSCO principles in the Objectives and Principles document (IOSCO, 2003); the remark about use of the IOSCO principles in the brief history of IOSCO (IOSCO, 2007); the introductory statements to the IOPS principles (IOPS, 2006, at pp. 2-3); Ewing, 2006, at pp. 296-313 & 653-673; and the 'introduction' to the ICN Work Products Catalogue (ICN, 2010d).

2497 Yilmaz Akyüz, 2002, at p. 28.

2498 IMF, 2008; IMF, 2009; IMF, 2010c; IMF, 2010d; IMF, 2010e; IMF, 2010f; Jose Viñals, et al., 2010; World Bank, 2008; World Bank, 2009; World Bank, 2009a; World Bank, 2010; World Bank, 2010a; World Bank, 2010c; OECD, 2008; OECD, 2009; OECD, 2009a; OECD, 2009b; OECD, 2009c; OECD, 2009d; OECD, 2009e; OECD, 2010; OECD, 2010a; OECD, 2010b; OECD, 2010c; IASB, 2010c; IASB, 2010d; IASB, 2010e; IASB, 2010f; IASB, 2010g; IFAC, 2010e; FATF, 2008; FATF, 2009b; FATF, 2009c; FATF, 2009d; and ICN, 2010g.