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RUSSIAN FEDERATION

REPORT ON THE OBSERVANCE OF STANDARDS AND CODES—IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

July 2016

This Report On the Observance of Standards and Codes on IOSCO Objectives and Principles of Securities Regulation for the Russian Federation was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the Russian Federation. It is based on the information available at the time it was completed on June 14, 2016.

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REPORT ON THE OBSERVANCE OF STANDARDS AND CODES

IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

June 14, 2016

Approved by
James Morsink and James Gordon

Prepared By
Monetary and Capital Markets Department

This report was prepared by Richard Britton and Richard Pratt (external experts) in the context of a joint IMF-World Bank Financial Sector Assessment Program (FSAP) mission in the Russian Federation during February, 2016. The FSAP was led by Karl Habermeier, IMF and Aurora Ferrari, World Bank, and overseen by the Monetary and Capital Markets Department, IMF, and the Finance and Markets Global Practice, World Bank. Further information on the FSAP can be found at http://www.imf.org/external/np/fsap/fssa.aspx, and www.worldbank.org/fsap.

CONTENTS

Glossary

AML	Anti-Money Laundering
AUM	Assets Under Management
BI	Broadly Implemented
CBR	Central Bank of the Russian Federation
CEO	Chief Executive Officer
CIS	Collective Investment Scheme
CRA	Credit Rating Agency
FFFSS	Federal Fiscal and Financial Supervision Service
FI	Fully Implemented
FSC Com	Financial Stability Committee
FSFR	Federal Service for the Regulation of Securities
HFT	High Frequency Trading
ISA	International Standards of Accounting
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
JSC Law	Joint Stock Company Law
KYC	Know Your Customer
MC	Management Company
MED	Ministry of Economic Development
MICEX	Moscow Exchange
MMoU	Multilateral Memorandum of Understanding
MoF	Ministry of Finance
MoJ	Ministry of Justice
NAUFOR	The National Association of Securities Markets Participants
NAV	Net Asset Value
NCC	National Clearing Center
NFE	Nonbank Financial Entities
NI	Not Implemented
OTC	Over The Counter
PI	Partly Implemented
RAS	Russian Accounting Standards
RTS	Russian Stock Exchange
SD	Specialized Depository
SRO	Self-Regulating Organization
UIF	Unit Investment Fund

EXECUTIVE SUMMARY

1. The Central Bank of the Russian Federation (CBR) has recently completed a two-year process of assuming the powers and functions of the previous "standalone" regulator of the securities markets and the insurance industry. This has included absorbing 1,300 new staff and inducting them into the organizational structures of the central bank. In addition to its new supervisory functions covering a disparate group of markets and professional market participants, it has also assumed a developmental role for nonbank financial markets with an emphasis on developing proportionate regulation and optimizing the regulatory burden on market participants. This is a challenging medium to long-term role while also seeking to ensure that standards are raised and that undesirable elements are removed from the market as rapidly as possible.

2. As is reflected in the ratings for many of the principles, there is much that CBR needs to accomplish if it is to approach good international practice as a securities regulator. The assessors have observed many positive elements in the work that supervisors are undertaking on a daily basis and in the longer-term work of developing policy that can be translated into the supervisory agenda. The fact remains that there is a significant amount of work to achieve full compliance. The departure from IOSCO requirements sometimes results from the absence of specific requirements in the legal framework, or insufficient implementation in practice. An additional cause is the complex legislative structure that is highly detailed, consists of many overlapping and in some cases inconsistent provisions that impose many detailed obligations but fail to impose the overarching duties required by IOSCO. The result is not easy to understand or enforce, leaves gaps, and yet creates substantial compliance costs. While some have argued that the absence of overarching provisions is an inevitable consequence of the principles of Russian law, others have correctly pointed out that there are some overarching obligations already in the legal framework and steps are being taken to develop the approach to legislation on these lines.

3. Some of the most recent regulatory changes, such as those on credit rating agencies, are clearly based on international standards. In other areas, further initiatives will be required. These include conflicts of interest identification and improving standards of management in professional market participants. It will also require the creation of legal gateways which will enable supervisors with the necessary skills sets to provide guidance as to what CBR's reasonable expectations are on a range of issues. These include the necessary components of risk management and internal control systems and the fair treatment of clients. Client facing rules require improved checks and balances within licensees which seek to ensure that clients, particularly unsophisticated retail clients, are advised on and sold products which meet their personal (often multi-dimensional) needs in a way which the current limited criteria for customer profiling fail to do. Further initiatives

are also necessary in areas such as the prospectus and continuous disclosure regimes for listed companies and the need for easy to understand disclosure documentation for unit investment funds that still provide sufficient, and sufficiently accurate information to enable the man or woman in the street to understand the risks and rewards and to make an informed investment decision. The retail investor base is small, and such initiatives could make a significant contribution to the numbers participating.

4. CBR faces a major challenge in enforcing the regulatory regime and will need additional resources. Over the financial sector as a whole, there are 19,000 nonbank licensees within the responsibility of CBR. With some 250 members of its inspection team, it was able to carry out scheduled, or routine inspections of just 97 of these in 2014. Most inspection resources were devoted to 499 unscheduled inspections (investigations into complaints or allegations of regulatory breaches). There is scope for greater use of supervisory tools other than inspections. Moreover, the move to place more responsibility on self regulatory organizations (SROs) may reduce the burden on CBR staff in the long term while increasing it in the short term as the new regime is developed. There will be a need for more resources to enable CBR to conduct a fully effective enforcement regime.

5. In other areas where change is underway, the ultimate goal may be clear, but the route will be difficult to follow. One example is accounting standards, where the move to IFRS is taking place while a requirement to publish accounts according to Russian Accounting Standards remains. On insider trading and market manipulation, investors globally will expect to see results from the new law, at least in terms of criminal prosecutions presented in court, in the near term.

INTRODUCTION

6. An assessment of the level of implementation of the IOSCO Principles in the Russian Federation was conducted from February 3–16, 2016 as part of the Financial Sector Assessment Program (FSAP) by Richard Pratt and Richard Britton, both external Monetary and Capital Markets Department experts. The last International Organization of Securities Commission (IOSCO) assessment was conducted in 2011 when the statutory regulator was the Federal Service for Financial Markets (FSFM). Its powers and functions were subsumed into CBR in September 2013 and the integration process was completed in the course of 2015.

7. CBR has created a three-year strategy on financial market development and stability; one of its goals for the period of 2016–18 is creating conditions for the growth of the

financial industry. It has identified as critical to the achievement of that goal "enhancing financial market regulation, inter alia through proportional regulation and optimization of the regulatory burden on financial market participants." Consistent with that goal is the adoption of international standards as established by IOSCO and appropriately adapted to the Russian market and legal system.

8. The assessment was conducted based on the IOSCO Principles and Objectives of Securities Regulation approved in 2010 and its Methodology adopted in 2011 and updated in 2013. Principle 38 was not assessed since this principle is now covered under the principles for Financial Market Infrastructures (PFMI). As a result, issues related to the central counterparties are not covered in this assessment.

9. The assessors relied on a number of information sources: a review of relevant laws, regulations, directions, instruction codes, and other documents provided by CBR; bilateral discussion with senior CBR staff in the weeks preceding the mission and a self-assessment prepared by CBR. In Moscow the assessors met with Mr. Sergei Shvetsov, First Deputy Governor of the CBR, senior CBR staff, senior officials at the Ministry of Finance and the Ministry of the Interior, and with the Moscow Stock Exchange and other representatives of the private sector.

10. The assessors want to thank CBR staff for their full cooperation as well as their willingness to engage in open conversations regarding their supervisory and regulatory work. The assessors also want to extend their appreciation to the other public authorities and market participants with whom they met.

REGULATORY STRUCTURE

11. CBR is the supervisor and regulator of the financial services sector; it is also the central bank. It is established under the Federal Law No. 86-FZ of 7/10/2002, "On the Central Bank of the Russian Federation (CBR)" (Central Bank Law). It is a legal entity. Its authorized capital and other property is in state ownership. Its assumption of powers and functions over the nonbank financial sectors was achieved by Federal Law No. 251-FZ of 7/23/2013 "On Amendments to Certain Russian Federation Legislative Acts in Connection with the Transfer to the Russian Federation Central Bank of Powers of Regulation, Oversight and Supervision in the Area of Financial Markets," which transferred to CBR the powers and functions previously exercised by the Federal Service for Financial Markets (FSFM). The Central Bank Law sets out the governance and management structure of CBR and its powers, duties and functions, including its powers to determine staff hiring and

remuneration policies, its duties and functions to act as the central bank, conduct monetary policy, oversee payment systems and to conduct integrated supervision of the financial services sector. It is also responsible for supervising the conduct of takeovers and mergers of companies that have issued securities to the public.

12. Other government-appointed bodies have relevant regulatory roles. The Ministry of Economic Development (MED) is the body responsible for administering the Joint Stock Companies Act, although disclosure requirements for companies offering securities to the public are the responsibility of CBR. The Ministry of Finance (MoF) is responsible for setting accounting and auditing standards and it relies upon advice from the National Organization for Reporting Standards and the Audit Council respectively, both of which are independent of the profession. Auditors are relied upon to enforce accounting standards and enforcement of audit standards is undertaken by the Federal Financial and Fiscal Service (for public interest companies) and Self-Regulatory Organizations (for all audit firms). The SROs of auditors are supervised by the MoF. The Federal Anti-Monopoly Service can intervene in markets supervised by CBR.

MARKET STRUCTURE

A. Market Intermediaries

13. The intermediaries licensed by CBR are brokers, dealers, investment managers, custodians, and registrars. Investment advisers are not separately licensed. Underwriting is considered to be an activity encompassed within the definitions of brokering and dealing.

14. Most intermediaries hold multiple licenses. According to the National Association of Professional Securities Participants (NAUFOR), 59.7 percent of the licensees held licenses as brokers, dealers and investment managers. Of these, 65 percent also had licenses as depositories. Data from CBR confirm this. On January 21, 2016, there were 826 brokers, dealers, asset managers and custodians, most of which had multiple licenses.

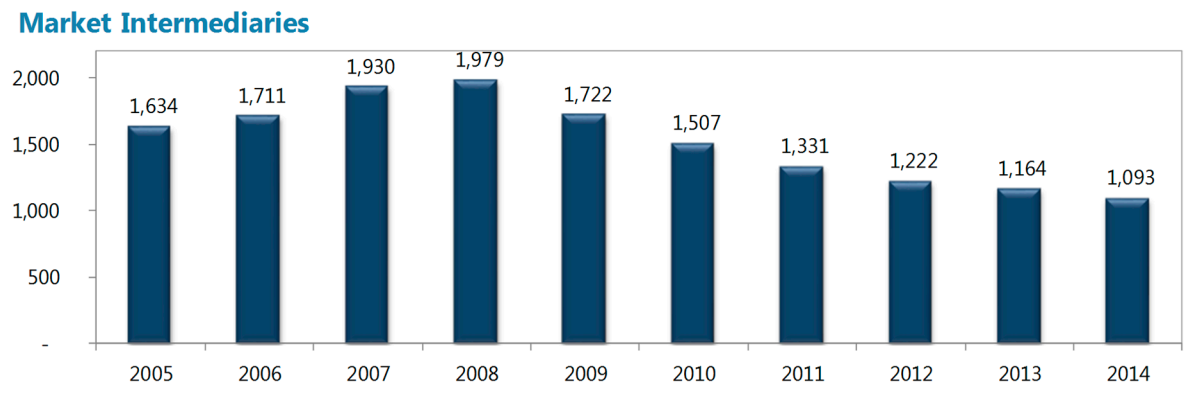
Table 1. Securities Licensees

Licenses Issued	Number
Broker	624
Dealer	641
Investment Manager	533
Depository	498

Source: CBR.

15. The number of intermediaries has been declining as is shown in the figure below.

Figure 1. Market Intermediaries

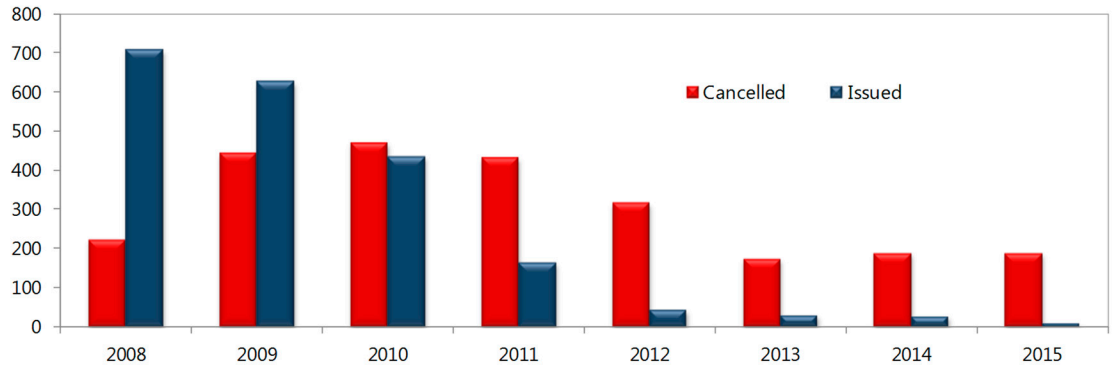


Source: NAUFOR Annual Factbook 2014.

16. This trend has continued, as CBR has been reviewing the status of intermediaries that undertake very little business. By the beginning of 2016,[1] according to CBR, the total number of intermediaries had fallen to 826, a reduction of 18.7 percent over the year. CBR has noted that the steady and substantial reduction in the number of intermediaries has not had any appreciable effect on trading volume.

17. The trend of license granting and cancellation has varied considerably since 2008. The number of new licenses has reduced over time and the number of licences cancelled has exceeded those granted since 2010.

Figure 2. Licences Issued and Cancelled



Source: NAUFOR Annual Factbook 2014 (for 2008–14), CBR (2015).

[1] January 21, 2016.

18. According to NAUFOR, 536 organizations traded on the exchanges in 2014, of which the top ten firms accounted for 63.9 percent of the volume of trading, up from 61.9 percent the previous year. The most active trader in non-government securities was CBR which accounted for 21.4 percent of the total turnover, down from 22.7 percent in 2013. CBR was particularly dominant in the market for corporate bonds (where its share was 32.9 percent, as opposed to 3.4 percent of the market for shares). The Sberbank Group (in which CBR has a shareholding of 50 percent plus one share) accounted for 15.5 percent of the market in shares (where it was the most significant trader) and 10.0 percent of the market in corporate bonds, where it was second largest to CBR.[2]

19. Top ten traders in non-government securities by volume are shown in the Table below.

Table 2. Top Government Securities Traders

	Name of Organization	Share of Volume (In percent)
1	CBR	21.4
2	Otkrytiye Group	9.7
3	Sberbank Rossii Group	8.9
4	VTB Group	8.5
5	BCS Group	3.9
6	Gazprom Group	3.2
7	Renaissance Group	2.5
8	Vnesheconombank Group	2.1
9	Bank Saint Petersburg JSC	1.9
10	BC REGION LLC	1.9
	TOTAL	63.9

Source: CBR.

B. Collective Investment Schemes

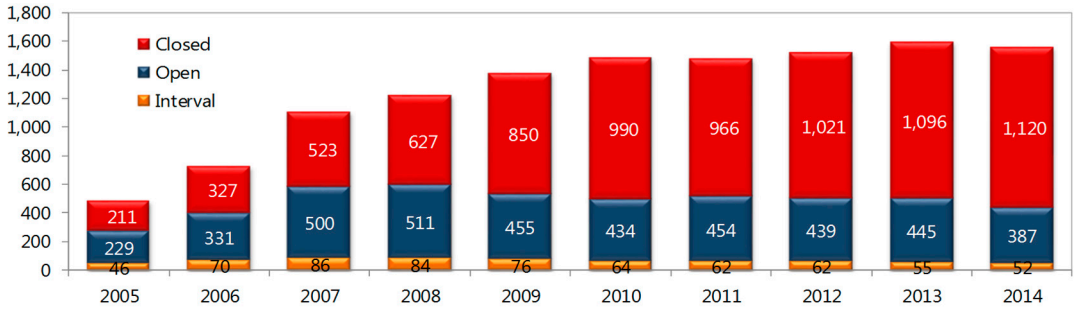
20. At the end of 2014, there were 1,584 unit investment funds (1542 as of 3Q2015), a decline of 2.3 percent from 2013. The number of open-end mutual funds, which are focused on retail investors, decreased by 5.5 percent, while the number of closed-end mutual funds decreased by 2.2 percent. Closed-end funds remained the most common type of fund, amounting to

[2] Source: Sberbank.

72 percent of the total number of unit investment funds. The assets under management (AUM) decreased by 3.1 percent to RUB 569 billion (470 as of 3Q 2015). The AUM of open and interval funds decreased by 24 percent to RUB 92.6 billion.[3] This was the first time the value of open and interval funds had dropped below RUB 100 billion since 2010. AUM represented 0.13 percent of GDP.

21. The most significant structural change for 2014 was related to mixed investment funds.[4] These funds became the largest group. comprising 63.9 percent of the total net asset value of open and interval funds.

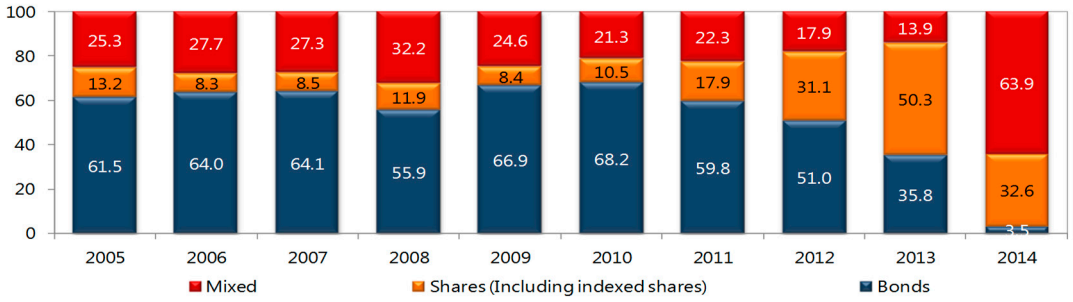
Figure 3. Number of Unit Investment Funds



Source: investfunds.ru.

Figure 4. Structure of Open and Interval Unit Investment Funds

(In percent)



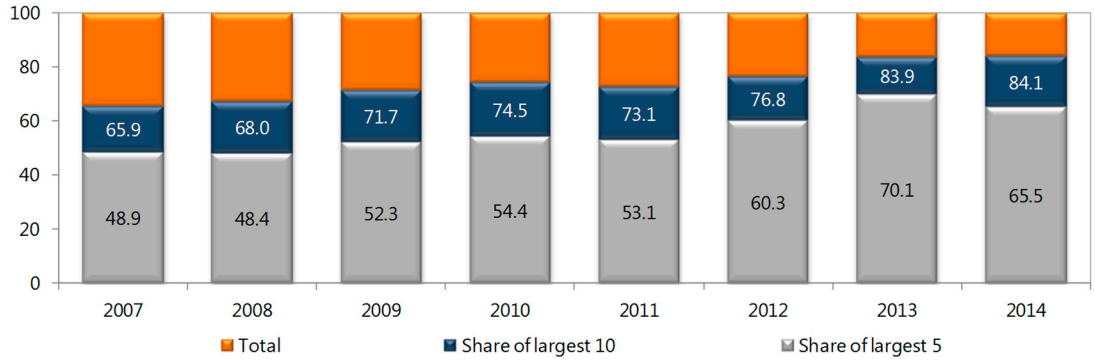
Sources: Investfunds.ru, NAUFOR estimates.

[3]The holder of units of an interval fund has a right to redeem all, or any part, of their units, but only on the dates established by the fund's trust management rules.

[4] Mixed funds invest in other funds or in a mix of shares, bonds, and cash.

22. Since 2007, the share of the ten largest management companies of total AUM has been on an upward trend. At the end of 2014, the AUM of the ten largest management companies made up 84.1 percent of the total market of open and interval funds. Notably, the second largest management company is part of the largest Austrian banking group (by balance sheet size).

Figure 5. Share of the Ten Largest Management Companies
(In percent)



Source: investfunds.ru, NAUFOR estimates.

Table 3. Largest Asset Management Companies (end 2014)

No.	Managing Company	AUM (In millions of rubles)	Share in the Total NAV (In percent)	Number of Funds
1	Sberbank Asset Management CJSC	20,074.0	21.9	19
2	Raiffeisen Capital LLC	16,304.1	17.8	18
3	URALSIB LLC	8,933.9	9.8	19
4	Alfa-Capital LLC	7,706.6	8.4	17
5	Trust Investment Company, LLC	6,918.7	7.6	3

Source: BCR.

C. Markets

23. The Moscow Exchange Group (MEG) is the largest exchange group in Russia, operating trading markets in equities, bonds, derivatives, the foreign exchange market, money markets, and precious metals. MEG also operates Russia's central securities depository (National Settlement Depository) and the country's largest clearing service provider (National Clearing Centre). The

exchange was established in December 2011 by merging the Moscow Interbank Currency Exchange (MICEX) and the Russian Trading System (RTS). MEG's shares are publicly traded on the exchange. As of November 2014, the largest shareholders of the Exchange were CBR (11.75 percent), Sberbank (9.9 percent), Vnesheconombank (8.4 percent), European Bank for Reconstruction and Development (6.1 percent), and Shengdong Investment Corporation (5.6 percent). Commodities trading is provided by five exchanges (St. Petersburg International Mercantile Exchange; "Exchange Saint-Petersburg" CJSC; Moscow Energy Exchange; Saint-Petersburg Exchange; NAMEX).

24. In 2014, the behavior of the markets was determined not primarily by fundamental factors such as poor economic indices but by the evolving geopolitical situation such as sanctions imposed against Russia by the United States (U.S.) and European Union (EU), the fall in oil prices, and capital outflows. The stock market showed negative results in almost all respects. The turnover ratio of the domestic share market was 36.0 percent in 2014, which was slightly greater than that in the previous year. However, comparing with the maximum level observed in 2009, the domestic share market liquidity decreased by 2.6 times.

Investor profiles

25. Although the number of private investors rose from 838,000 people to 906,000 people, the number of active private investors' customers decreased slightly to 62,500 from 62,900 people in the previous year. Private (resident) investors, who make up 90.3 percent of the total number of transactions on the Moscow Exchange, invest predominantly (89 percent) in shares. The number of corporate investors increased in 2014 by 8.8 percent to 19,800. However, the number of active corporate investors decreased to 1,422 companies or some 4.0 percent of the total number of investors.

Table 4. Capitalization of Russian Market (Equities) on MEG in 2010–14

Period	In billions of rubles	In billions of U.S. dollars (Estimate)	Capitalization as percent of GDP
2010	29,253.2	1,379.2	63.2
2011	25,708.0	1,096.2	46.1
2012	25,212.5	1,079.4	40.4
2013	25,323.8	1,041.1	38.0
2014	23,155.6	517.3	32.6

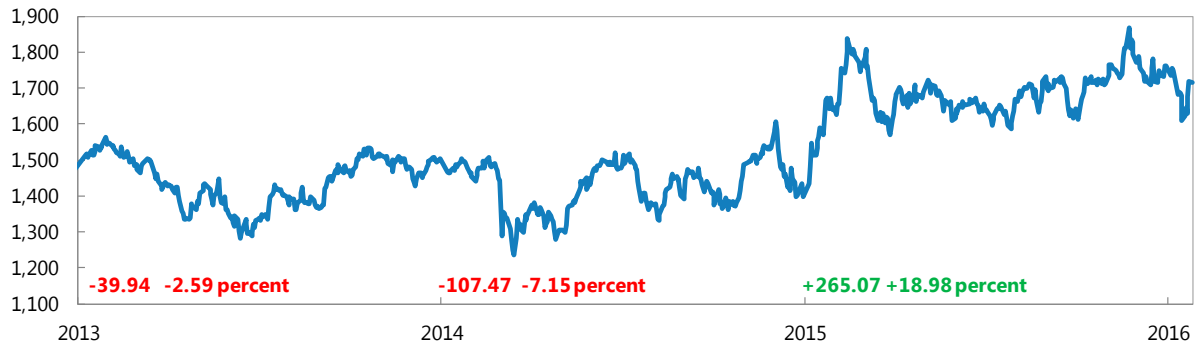
Source: MICEX.

Table 5. Number of Listed Companies on the Moscow Exchange 1/

Period	Moscow Exchange Group	
	Number of Share Issuers	Number of Share Issues (ordinary, preferred) in Quotation Lists
2011	320	119
2012	275	118
2013	273	110
2014	254	106

Source: Micex.
1/ Despite the trend of reduction in the total number of open joint-stock companies, there are currently 30,360 such legal entities. Less than one percent of them are represented on the stock exchange.

Figure 6. MICEX Composite Index 2013–14



Source: MICEX.

26. After a strong start to 2015 the market (as represented by the MICEX Composite Index) traded in a narrow range for the rest of the year.

27. Corporate Bond Market. In 2014, new issues of corporate bonds totaled RUB 1.8 trillion, which was 6.6 percent more than in the previous year. The share of off-market (OTC) placements grew sharply to 68 percent. The number of bond issuers on the Moscow Exchange remained unchanged at 323 companies. The total value of exchange transactions (at cost, without taking into account repurchase agreement (repo) transactions and placements) involving corporate bonds was

RUB 4.3 trillion, which was 30 percent lower than in 2013. Secondary market trading in on-exchange bonds made up 30 percent of the secondary market volume. 45 percent of the turnover was in the bonds of 10 issuers.

28. Government Bond Market. The value of government bond issues traded on the exchanges continued growing in 2014 and, at year-end, had increased by 26 percent (par value), reaching RUB 4.7 trillion or 6.6 percent of GDP. However, exchange turnover was sharply lower—the secondary market volume (at cost, without taking into account repo transactions and placements) decreased by 36 percent to RUB 3.8 trillion for the year.

29. Sub-federal and Municipal Bond Market. This market segment has been and remains the most illiquid sector of the domestic debt securities market. The value of these bond issues made up less than RUB 500 billion, with the value of trading (without taking into account placements of new issues and repo transactions) being RUB 379 billion.

30. Repo Market. The Moscow Exchange is unusual globally in that it hosts a very large repo business. The value of exchange repo transactions on the Moscow Exchange in 2014 was RUB 183 trillion, which was 10 percent lower than in 2013. The share of corporate bonds in the total transaction volume shrank to 39 percent. The share of direct repos with CBR reached 55 percent at the end of the year**.**

Unit Investment funds

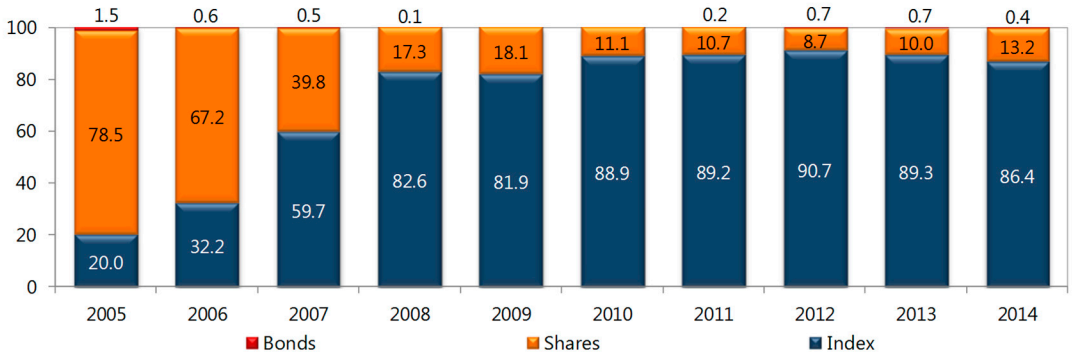
31. In 2014, the value of trading in investment units on the Moscow Exchange was RUB 177.3 billion, +28.6 percent over 2013. A significant innovation was the introduction in 2013 of stock exchange trading in foreign exchange traded funds (ETF). The aggregate volume of transactions in ETF units has grown by seven times for the year and made up RUB 3.5 billion. However, it accounted for about two percent in the total value of transactions in investment units.

Derivatives markets

32. Futures and options trading is dominated by trading in contracts on the MOEX indices. In 2014, the value of trading in futures contracts for securities and stock indices declined for the third year in a row at RUB 28,929 billion (-8.2 percent versus 2013). From 2011, when the maximum trade volumes were recorded, the decrease was 37.3 percent. The proportion between trade in futures and options was unchanged: 87 percent in futures and 13 percent in options.

Figure 7. Structure of Futures Trade on the Derivatives Market of the Moscow Exchange Group

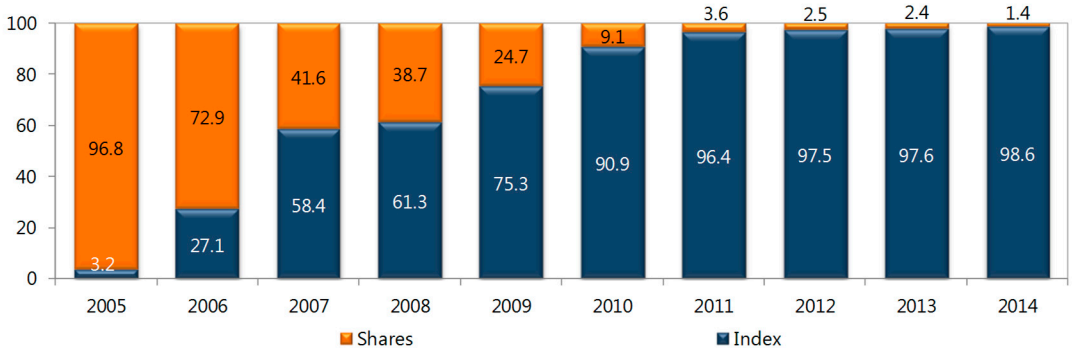
(In percent)



Sources: Moscow Exchange Group, NAUFOR estimates.

Figure 8. Structure of Options Trade on the Derivatives Market of the Moscow Exchange Group

(In percent)



Sources: Moscow Exchange Group, NAUFOR estimates.

D. Preconditions

The legal framework

33. One important precondition for securities markets is a stable and transparent legislative and regulatory framework, but the Russian Federation regulatory framework cannot be so described.

34. The Russian Federation legislative system follows many of the principles of civil law. Like most countries (civil or common law), there is a legislative hierarchy, with the Constitution at the top. As with other Civil Law countries, the Russian Federation incorporates a fundamental Civil Code. CBR is able to issue by-laws on matters within its competence and can do so on its own authority, where there is explicit provision in primary legislation. These by-laws, which all have to be registered with the Ministry of Justice (MoJ), take the form of Regulations, Directions and Instructions. The main difference is their internal structure. Regulations set basic or systemic rules, Directions set other rules, and Instructions tend to deal with the procedural application of the rules. These instruments are binding on all federal governing bodies, governing bodies of the constituent entities of the Russian Federation and local authorities, and all legal and natural persons. In practice, most of them are directed at securities businesses.

35. The assessors have noted a number of issues arising from the structure of the legislation. In particular, it is clear that:

- **The legislation is subject to constant change.** Even primary laws are often amended several times a year. For example, the Securities Law was amended five times in 2015, each amendment resulting in multiple changes to a substantial number of articles. Although the legislative system is highly efficient at showing the legislative history in each act, it remains difficult to keep track of the implications and consequences of all the changes.

- **Not all of the provisions in new or amended legislation result in comprehensive amendments or repeal of previous provisions.** Some examples are given in the text of this assessment and include the law on SROs, which was brought into effect in January 2016, without repealing the existing articles relating to SROs in the Securities Law and the Investment Funds Laws. The provisions regarding the process and criteria for registration of SROs, their rights and duties were different in each of the Securities Law, the Investment Funds Laws and in the new provisions in the new SRO Law and yet all remained in force at the same time. This resulted in membership in SROs being both voluntary and mandatory (at the same time) for professional securities firms. The transition to the new regime has been constructed in a way that results in securities firms being obliged to comply with basic standards that are not yet drafted. CBR have explained the principles for resolving inconsistencies and these are discussed below. However, reliance on such general principles will still leave uncertainty and the existence of such principles is no substitute for a proper analysis of the potential conflicts or inconsistencies between new and previous legislation and the introduction, simultaneously with new legislation of all necessary repeals and amendments to previous legislation.

- **Provisions relating to any one matter can be found in a large number of different legislative instruments.** Again examples are given in the text of the assessment and include the

range of obligations placed on the staff of CBR that extend across several pieces of legislation. Another example concerns the obligations on issuers of securities, which appear in various laws and the Civil Code, all of which have to be read together to get the full picture even though the existing provisions in different laws do not always make reference to the relevant qualifying provisions in other laws. Disclosure requirements relating to substantial shareholdings are set out in the Joint Stock Company (JSC) Law but can only be properly understood by referring to the definition of an affiliated person which appears in other legislation. While the notes to the JSC Law give references for this definition, CBR has stated that the true definition can only be found by referring to two competition laws.

- **The approach to the nature of legislative provisions also changes in different laws.** For example, in many laws, including the Securities Law, the duty of CBR to keep information confidential is explicitly overridden where disclosure is required or permitted by law. In the Investment Funds Law, by contrast, the threat of personal civil liability that hangs over all CBR staff in the event that they make a disclosure (Article 56) is not explicitly overridden by any other legal requirement, although CBR has explained that this should be inferred. The right of CBR to refuse to give a licence if criteria are not met is explicit in some laws but must be inferred in others. For example, the Investment Funds Law explicitly states that CBR has the right to give or refuse licenses based on the criteria. However, the Securities Law does not include such a provision for CBR in respect of brokers, dealers or investment managers, even though it is stated that CBR is the licensing authority and that there are licensing criteria. The power of CBR to give or withhold licenses based on the criteria has to be inferred.

- **The introduction of a new requirement is not always accompanied by the repeal of the existing requirement.** The legally binding requirements in CBR Regulations, Instructions, and Directions, sometimes overlap with existing provisions in Regulations and Orders published by the former securities regulator.

- **Some legislative instruments contain requirements at an inappropriate level of detail.** For example, firms are given legally binding instructions on the persons to whom copies of a quarterly report should be given, how many copies to make, and how to indicate that they have ben read.

36. CBR has explained that there are legal principles for resolving inconsistencies between laws. Like most countries, inconsistencies are resolved on the basis that the later law overrides the former one. Like most civil law countries, there is an additional principle that the more specific law overrides the more general one. Moreover, in the case of conflict, the courts will take the position that the interpretation that restricts liberty the least will prevail. It may well be that in many cases,

this will result in clarity as to which provisions prevail. However, it may well also be that in other cases, this will not be so, and there will be some who are genuinely unclear as to the proper interpretation in any one case, without resorting to judicial decision.

37. CBR has also explained that the recent history of the Russian Federation has resulted in suspicion in the Duma and the public at large of state agencies and this militates against the granting of broad discretion to such agencies. This is the historical background behind the attempt to create a comprehensive set of specific requirements, rather than by setting overarching obligations. Inevitably, this approach leaves overlaps, loopholes and gaps (which are identified in the report), and which have to be addressed by new and amended regulations (which in turn exacerbates the problems caused by detailed requirements that are frequently changed).

38. The consequence of this approach is likely to be to increase costs. One intermediary informed the assessors that the legal department was larger than their trading department. In particular:

- Proper compliance is very costly because of the need to employ staff to keep up with the changes, to identify the overlaps, seek advice on the interpretation of the latter, assess the implications and consequences of the changes, and implement those changes in terms of amended internal procedures, staff training, revised manuals and so on.
- Costs also arise from the payment of fines for failure to comply with detailed rules.
- Detailed requirements in effect micromanage the operations of firms, and are viewed by firms as inhibiting innovation and development.
- CBR is obliged to spend considerable time explaining the intention behind its regulations.
- The focus on detailed rules means that overarching principle based requirements, even where they exist, can be ignored by securities firms as there is a reluctance to take enforcement action for a breach of a principle in the absence of a specific rule.
- The detailed rules will sometimes miss key requirements altogether—for example:
    - the internal controls regulation focuses exclusively on the appointment and duties of a Compliance Officer but does not contain requirements that would be essential to an effective system, such as an obligation to conduct a risk assessment, to prepare policies and procedures that followed from that risk assessment, to develop a management information system that allowed the management to monitor the effectiveness of its policies and procedures in mitigating risk, to train staff in the risk appetite of the firm and the policies and procedures, and to re evaluate the policies and procedures at least annually;

- Provisions on conflicts of interest for securities firms are incomplete and do not include a general requirement to identify conflicts of interest, avoid them, manage them, or decline to act; and

- There are detailed requirements to obtain specific items of information on customer's objectives and circumstances but not an overarching requirement to obtain all information necessary to be able to judge the suitability of services.

- In practice, firms act in a way that is consistent with the detail of the rule but not the underlying intention, for example:

  - There are practices by the audit profession that are consistent with the detailed rules, but not the principle, regarding independence;

  - Disclosures by companies are consistent with detailed requirements but not the general principle that all material matters should be disclosed where they may affect the price of securities (as is evidenced by the absence of profit warnings which although relevant to a securities value is not specifically included in the list of mandated disclosures).

39. The complex regime is difficult to comprehend and enforce. The assessors could not help noticing that regulations were suddenly identified at a very late stage in the mission (or in some cases after the mission). These regulations, such as Regulation 44 of 1998, were clearly relevant to a number of principles, but were not discussed by CBR in the self assessment, or in the discussions (until the final meeting). This suggests to the assessors that CBR do not themselves have a clear and comprehensive picture of the regulations that apply and, it is highly likely that the intermediaries do not. This will mean that it is unlikely that all such regulations can be effectively enforced.

40. A regulatory regime that includes contradictions and inconsistencies can undermine respect for the rule of law. CBR have confirmed that they will not take enforcement action under the SRO law against securities firms for failing to comply with non-existent SRO Basic Standards. However, it is not appropriate to have legal and regulatory provisions that cannot be complied with and must be ignored—even if, or, in fact, especially if, the enforcement authority has stated that they will take no action. If it were to become accepted that there may be some mandatory legal requirements that are impossible to comply with (and can safely be ignored with the agreement of CBR as enforcement authority), then the principle of the rule of law is undermined.

41. The reluctance to draft general, overarching requirements is gradually diminishing. The assessors have noted that there are some more general obligations (such as the requirement to have adequate risk management and to have systems to identify and monitor conflicts of interest). Indeed, CBR found an old regulation issued in 1998, which contains very general and broad brush requirements on conflicts of interest. However, in these cases, there is no supporting detail and so it

is not easy to judge the expectations of CBR. Moreover, even though these general requirements exist in some cases, some CBR staff continued to insist, from time to time in discussion and in comments in this report that such general requirements would be regarded as simply declaratory in the Russian legal system and would not be legally binding.

42. A reasonable balance between high level obligations, supported by a list of detailed but not exclusive examples, can clearly be struck and has sometimes been struck in the securities legislation.

43. The assessors understand that CBR is considering embarking on a simplification exercise and would encourage them to do so as soon as possible. In particular, it would be most helpful if:

- All new legislative instruments identified existing conflicting provisions (especially where these exist in laws administered by CBR) and repealed or amended them, so as to remove the potential for inconsistency;
- Provisions which deal with a particular subject should, so far as possible, be brought together, or at least cross referenced, so that those seeking to comply with their obligations can be confident that they can find them in a single place, where they relate to the same matter;
- The degree of detail that is required should be reviewed, so as to limit the extent to which the actions of securities firms are micromanaged;
- Greater use should be made of the kind of high-level obligations that are beginning to appear in legislation, so that those subject to the law can see the overall objective of the regulations and do not have the scope for slipping through the gaps created by different detailed provisions;
- Such overarching requirements should be supported by sufficient detail that focuses on the key elements that CBR regard as essential;
- CBR should seek to limit the number of amendments (an objective that should be easier to meet if there is less minute detail in individual instruments).

Business laws

44. Business laws in Russia are based on chapter 4 of the Civil Code, the 208-FZ Federal Law on Joint Stock Companies and the 14-FZ Law on Limited Liabilities Companies. The latest major amendments to business legislation were introduced with Federal Law 99-FZ and Federal Law 210-FZ, from 2014 and 2015 respectively, which changed the types of companies allowed in the Russian Federation, increased the protection of investors holding Russian local securities, and improved the conditions for participation in corporate actions (for example by allowing e-voting and

e-proxy voting). The Insolvency Law was amended in 2014 to incorporate changes in the insolvency procedures for financial institutions. In 2015, amendments to the Federal Law No.7-FZ "On Clearing and Clearing Activities" empowered the National Clearing Center (NCC) to effectively segregate member positions from their client positions. The current legal structure meets the requirements for close-out netting of contracts under the International Swaps and Derivatives Association master agreements and the global master repo agreement of the International Capital Markets Association. Other important Federal Laws to register and conduct business are those related to state registration of legal entities and individual entrepreneurs, fundamental principles of Russian legislation on notaries, trade, consumer rights protection, and combating money laundering and the financing of terrorism (AML/CFT), as well as the Land code, the CBR Law, and the Tax code. One of the most significant changes in these laws was the introduction of the requirement for financial institutions in 2013 to identify their clients, clients' representatives, and beneficial owners and to collect information on the reputation of them and on their business purposes. The definition of the "beneficial owner" was also clarified, and it currently is consistent with the Financial Action Task Force (FATF) Forty Recommendations Glossary.

45. The judicial power is formally independent from the legislative and the executive powers. The judiciary is primarily regulated by the Constitution of Russia, the Code of Criminal Procedure, the Code of Civil Procedure, the Code of Administrative Procedure, the Code of Arbitration Procedure, and the 1996 Federal Constitutional Law on the Judicial System of the Russian Federation. According to the Constitution of the Russian Federation, the judiciary should protect all men (and women), and citizen's rights and freedoms. In addition, the Constitution confirms that courts alone can administer justice and requires that all judges shall be independent and obey only the Constitution and the law. The courts are financed solely from the federal budget in order to ensure a complete and independent administration of justice.

46. The judicial power is exercised by means of constitutional, civil, arbitration, administrative, and criminal proceedings. Examination of cases in all courts is open. Judges adopt the Code of Judicial Ethics which asserts the need to guarantee everyone's right to a fair consideration of a case by a competent, independent, and impartial court. The judicial system is composed of the Constitutional Court of the Russian Federation, the Supreme Court of the Russian Federation, federal courts, district courts, magistrate courts, military courts, and arbitration courts.

47. All judges of the Supreme Court are appointed by the Council of the Federation of the Federal Assembly of the Russian Federation upon recommendation of the President of the Russian Federation. All other judges, including military and arbitration, are appointed by the President of the Russian Federation.

48. The World Bank Global Competitiveness Report for 2014–15 ranks Russia as 109th out of 144 in judicial independence. In terms of the efficiency of the legal framework in settling disputes and in challenging regulations, Russia ranks 110th and 99th, respectively, and in the area of protection of property rights, Russia ranks 120th.

Legal profession

49. The legal profession is governed by the Constitution, the Law on the Status of Judges, the Law on Attorneys' Practice and the Bar, and the Foundations of the Legislation on Notary. The main legal professions in Russia are the public prosecutor, investigator, judge, attorney (advokat), and notary.

50. The public prosecution service consists mainly of the Prosecutor General's Office of the Russian Federation, the prosecutor's offices of the subjects of the Russian Federation, city, district and other territorial prosecutor's offices, and military and other specialized prosecutor's offices. The Prosecutor General of the Russian Federation must be appointed and removed from office by the Federation Council of the Federal Assembly of the Russian Federation by the recommendation of the President of the Russian Federation. The term of office of the Prosecutor General is five years. Prosecutors and investigators employed in the prosecution bodies should not be members of any elective or other bodies set up by state authorities and local self-government bodies.

51. The Investigative Committee of Russia is the main federal investigating authority in Russia. From 2011, this committee is not included in the structure of government authorities, and only the President of the Russian Federation carries out any control over the Committee. The Chairman is appointed and dismissed by the President without the approval of any body of legislative power and reports annually to the President on its activities.

52. All judges of the Supreme Court are appointed by the Council of the Federation of the Federal Assembly of the Russian Federation upon recommendation of the President of the Russian Federation. All other judges, including military and arbitration, are appointed by the President of the Russian Federation.

53. Lawyers must have a license to practice law in order to appear in court on criminal matters. Under the 2002 Law "On Attorneys' Practice and the Bar," each of the Russian regions has a single bar body called Bar Chamber. Lawyers need to be a member of one of such Bar Chamber to be recognized as an attorney.

Credit bureaus

54. Russia has 21 functioning credit bureaus according to the State Register of Credit Bureaus. These bureaus process and store credit histories and provide credit reports and related services. As of December 2014, the number of borrowers whose information is recorded in the credit bureaus is 61 million (60.7 million are individuals and 358,000 are legal entities). Some credit bureaus are owned by banks.

55. Credit bureaus are supervised by CBR and have been the subjects of reforms to strengthen the financial and real sector. The Federal Law "On Credit Histories" entitles the CBR to keep the central catalogue of credit histories which informs users, subjects of credit histories, and

some other persons defined by law about the location of the credit histories. CBR has the power to request and receive credit history reports from credit bureaus.

MAIN FINDINGS

Principles relating to the regulator (Principles 1–8)

56. CBR is making significant advances in the regulation and supervision of financial markets since taking over responsibility for this sector. Full integration of the 1,300 staff of the FSFM was achieved only in 2015. In terms of governance, there are some concerns about the direct involvement of government at the Board level and in setting the bank's budget. A more significant concern is the lack of legal protection for staff in the proper performance of their supervisory duties. The Central Bank Law and other legislative requirements seek to impose high standards of personal conduct and ethics on CBR staff, but greater clarity would be beneficial. On other matters, such as systemic risk in securities markets and perimeter policing, CBR meets IOSCO standards with only minor issues to be dealt with in the latter case. More needs to be done on developing an effective regime to deal with conflicts of interest and misaligned incentives.

Self-regulatory organizations, enforcement, and cooperation (Principles 9–15)

57. CBR has a comprehensive set of enforcement powers and is moving to a more risk-based approach to supervision and enforcement, but the resources devoted to supervision and particularly inspections are inadequate. CBR has enforcement powers that cover most of the requirements of the principles. These powers are now being used with determination to identify and remove securities firms which conduct little or no securities market activity (and which probably should not have been licensed in the first place). For the remaining firms, CBR focuses on identifying breaches of the many detailed rules and applying penalties for such breaches. Most onsite visits to firms are "unscheduled"—i.e., are investigations arising from complaints or suspicions of breaches arising from other sources. The number of routine inspections is very low. In 2014, for the 19,000 nonbank licensees for whose supervision CBR is responsible in all financial sectors, there were 499 unscheduled inspections (i.e. investigations) and only 97 scheduled inspections.[5] Only 250 inspectors are available to inspect all these licensees. This number of routine scheduled inspections is far too low for this to be described as an effective compliance program. Securities firms themselves report that CBR inspectors are beginning to engage in useful qualitative discussions of the effectiveness of risk management as a whole. This is a positive development. CBR is moving towards a new regime

[5] No figures are available for inspections of securities firms specifically. These figures are taken from the 2014 CBR Annual report.

where front line enforcement will be the responsibility of SROs and this will involve the transformation of the role of such organizations. This transformation needs careful management. Market abuse was criminalized only in 2013 and criminal penalties available only in 2015, and as yet only administrative penalties have been imposed.

58. CBR is a signatory to the MMoU and is actively responding to requests for information, even though some ambiguities in the law need to be removed. CBR became a signatory to the IOSCO MMoU in 2015. It has received and responded to requests for information. The Central Bank Law has been amended specifically to allow for CBR to use its powers to obtain confidential information in response to requests from foreign authorities. In most cases, but not all, the duties of confidentiality placed on the regulatory authorities contain an explicit gateway to allow disclosure when permitted by law and this practice needs to be comprehensive. The drafting of the Central Bank Law prohibits the provision of unsolicited assistance and this restriction on the otherwise wide powers of CBR need to be removed.

Issuers (Principles 16–18)

59. Disclosure provisions on issuers are reasonably comprehensive, but the continuing disclosure obligations need to be strengthened. Companies that have issued shares or bonds to the public are required to publish prospectuses and are also required to publish quarterly and annual reports. The requirements for prospectuses and for periodic reports are comprehensive. There is a general obligation to disclose all material facts relevant to a decision to invest in a prospectus and a corresponding continuing obligation to disclose all material facts that might affect the price of a security. In practice, however, disclosures are mostly limited to those included in a list of specifically required disclosures in the law, which includes routine matters such as the holding of a general meeting, or the terms and conditions of securities, but excludes many significant matters such as a material change in prospects or risks, or important events affecting performance and profits. These significant disclosures would be categorized as “any other matter” in the law and CBR has confirmed that they would expect significant disclosures to be made under that category, although very few disclosures (just over 1 percent of the total) are made on this basis. There is no formal derogation from the disclosure obligation for state or commercial secrets, although such omissions from disclosure are made and accepted without any effective statutory safeguards. The exchange does not monitor continuing disclosure obligations by issuers, although CBR states that it is under an obligation to do so. It is important to strengthen the obligation to promptly disclose any matter that might reasonably be expected to affect the value of securities, monitor compliance, and to enforce it by taking appropriate action.

60. Requirements to adopt IFRS are already in place for many companies, with the remaining companies with securities offered to the public, coming into IFRS by 2019, but in practice, the requirement is often observed in form rather than substance. A complex set of provisions in various laws, when taken together, impose a requirement on all listed companies and all companies that publish consolidated financial statements to adopt IFRS. Other companies that issue securities to the public will have to adopt IFRS on a schedule ending in 2019. However, the market perception is that of those currently subject to the IFRS requirement, only those 60–70 companies that seek listings on foreign markets presently comply with this requirement in substance. For all other companies, the general practice is to use Russian Accounting Standards (RAS) as the basis for the narrative and other disclosures in the prospectus, annual reports, and quarterly reports. Formal financial statements, prepared according to both RAS and IFRS are included in the Appendix. RAS standards are described by the CBR as differing from IFRS in a number of ways, mostly with regard to a focus (in practice, although not in principle) on form rather than substance, which could result in very different results, especially at times of volatility in the value of assets. It will be important to ensure full compliance with IFRS in all financial reporting.

Auditors, credit rating agencies and other evaluative services (Principles 19– 23)

61. The Ministry of Finance (MoF) is at the head of an oversight regime that allows auditing self-regulatory bodies to contribute to, but not take final decisions on, auditing standards and includes enforcement by both the Ministry of Finance and SROs of auditors. The MoF appoints an Audit Council that is independent from but can consider detailed proposals relating to audit standards prepared by SROs. This independent Audit Council takes final decisions on what to propose to the MoF. As a matter of policy, the MoF accepts the Audit Council recommendations. The Audit Council also approves standards of ethics and independence to be enforced by SROs and the MoF (through the Federal Fiscal and Financial Supervision Service (FFFSS)). SRO enforcement activity is monitored by the MoF. FFFSS enforcement is focused on the auditors of public interest companies (including all listed companies). All auditors and audit firms must belong to one of five competing SROs and, to gain membership, must meet qualification requirements and continuing professional development obligations. Independence provisions in the Law consist largely of descriptions of prohibited relationships. The Code of Ethics and Independence Rules adopt a more principle-based approach. Both the FFFSS and the market agree, however, that it is not easy to enforce the independence rules on the basis of these principles. The market perception is that many audit firms adopt practices that clearly breach the substance of the independence principles but not necessarily the specific provisions in the law. It will be important to enhance the enforcement regime so as to address this problem.

62. A new Credit Ratings Agency (CRA) Law is currently in place but cannot yet be fully enforced and there are no effective requirements for other evaluative services. The new CRA law is reasonably comprehensive and is clearly designed to meet the provisions of the IOSCO Code of Conduct and the IOSCO CRA Principle. All of the requirements relating to registration, disclosure, conflicts of interest, methodology, and internal governance are there. There are some enhancements that should be made with respect to CBR's powers to collect further information from license applicants and the imposition of stronger integrity requirements and overarching recordkeeping provision. CBR is also working on detailed regulations, and these were not all fully in place at the time of the assessment. Therefore, no CRA could register, and the law could not be enforced. CBR does not have a process for identifying new evaluative services that may warrant regulation. It proposes to bring investment advice into regulation, but until it does, there are no specific requirements for analysts employed by brokers. Detailed independence requirements for appraisers (for example, of assets of issuers and collective investment schemes) are in a Code of Ethics and Independence prepared by SROs, and these were not supplied to the assessors.

Principles for collective investment schemes (Principles 24–28)

63. The market sector is small and does not raise systemic risk concerns; hedge funds and money market funds are not a significant factor. Operators of collective investments schemes require a license from CBR, as do custodians (specialized depositories), the use of which is mandatory. Integrity tests for licensees should be enhanced. Operators and custodians are subject to capital and organizational requirements. Operators are also subject to conduct of business requirements, but improvements should be made. Agents who market shares or units are also subject to licensing. CBR supervises all three groups. The regulatory framework places strong reliance on the specialized depositories to ensure that the operators (management companies) comply with the rules of the funds, the law, and regulatory acts of CBR. Risk-based supervision is being applied in a comprehensive and constructive way. The legal form of CIS is well established, as are the rights of share and unit holders. There is a disclosure regime with mandatory standards for documentation, but improvements should be made.

Market intermediaries (Principles 29–32)

64. All market intermediaries must be licensed and are subject to an evaluation by CBR, but the criteria need to be enhanced and the capital requirements tailored to risk. CBR is the licensing authority (although it cannot impose a license condition). The criteria cover competence, integrity, and financial standing, but the detailed provisions on integrity, in particular, are too narrow and inflexible, giving insufficient discretion to CBR to determine what matters are relevant to the

individual and the post in question. The legal entity for which a license is sought must demonstrate compliance with a range of matters including internal controls, risk management, and capital. Capital requirements are flat rate and not risk-based. CBR should develop appropriate criteria for judging the adequacy of risk management and internal controls, and should be able to make a judgement on the willingness and capacity of the applicant to comply with their obligations. Capital requirements should be risk-based, and CBR should institute early warning reporting for deterioration of capital while enhancing its powers to take action to avoid default. CBR will need to develop a contingency plan for such occurrence.

Principles for the secondary markets (Principles 33–37)

65. Exchanges and non-exchange trading systems are permitted, and both are required to be licensed. Currently there are none in the second category and no applications are pending. The largest exchange, MOEX, has a near monopoly in many of its markets, particularly equities. Exchanges must be fit and proper to conduct operations, maintain capital, and have rules to ensure they conduct fair, orderly and transparent markets. There must be fair access to the markets, and they must comply with CBR requirements for conducting their operations. They also must monitor the conduct of their members and secure compliance of companies admitted to trading with the listing rules; these areas merit closer examination. There are no effective controls or disclosure of on-exchange short selling. More generally, the supervisory system is relatively new and has yet to be fully tested in highly stressed market conditions. Criminal enforcement of breaches of insider dealing and market manipulation is also new and untested. CBR's taking of adminstrative action in such cases is developing a reasonably successful track record.

Table 6. Summary Implementation of the IOSCO Principles	
Principle	**Findings**
Principle 1. The responsibilities of the Regulator should be clear and objectively stated.	At the level of the Federal Laws, the powers and authority of CBR are set out comprehensively and with reasonable clarity. However, the complex interaction of laws, regulations, directions, etc., coupled with frequent changes and very detailed requirements, has resulted in numerous cases of one group of market participants being subject to obligations to which others are not, for no obvious reason. It is doubtful that even with substantial and highly skilled compliance departments, most licensed firms (or their SROs) are able to stay fully compliant on a consistent basis. Investors, too, face substantial difficulties in understanding what their rights are in their relationship with market participants or through ownership of a particular financial product.
Principle 2. The Regulator should be operationally independent and accountable in the exercise of its functions and powers.	Although the independence of CBR is set out in the Central Bank Law and the Board of Directors' functions are limited under that law to certain administrative matters excluding regulatory policy making and enforcement matters, the right of the Ministers of Finance and Economic Development to attend board meetings with a right to participate in discussions and express opinions to be recorded in the minutes risks creating the impression of possible political involvement in CBR's operational activities. There is a lack of legal protection for staff when performing regulatory functions such as carrying out investigations into possible breaches of the law and normative acts of CBR made under it.
Principle 3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.	Although CBR has control of its operational budget once it has been agreed, the overall size of the budget is established by a decision of the National Financial Board of which the CBR member (the Governor) has one vote among 12. The others are from the Presidential administration, the federation government, and the legislature. Since staff salaries and administrative expenses constitute the major part of the bank's expenses, there is potential for the Presidential administration, federal government, and the legislature to exercise definitive influence over the resources the bank has for regulation and supervision. CBR's costs of regulation are met from income sources other than fees levied on nonbank financial market participants, which go to the government. The retained profit of CBR appears sufficient to enable CBR to meet its responsibilities as a securities market regulator as well as its responsibilities as a central bank and supervisor of banks, insurance companies, and non-state pension funds. It has the necessary powers.

Table 6. Summary Implementation of the IOSCO Principles (continued)	
Principle	**Findings**
	Staffing policies and training appear to be well established and resourced, and CBR's initiatives in investor education are well regarded by others working in this area.
Principle 4. The Regulator should adopt clear and consistent regulatory processes.	Among industry participants there was a mix of opinions on the commitment of CBR to "real" consultation. There was a clear majority view that CBR is serious in seeking views of market participants and the public, and that engaging with CBR by responding to public consultations or participation in CBR workshops is worthwhile and can secure improvements in proposed regulatory approaches. CBR has reasonable processes intended to secure procedural fairness and transparency.
Principle 5. The staff of the Regulator should observe the highest professional standards, including appropriate standards of confidentiality.	Staff are subject to obligations to maintain high standards in their professional and personal conduct. CBR appears to have made substantial efforts to enable staff to understand their duties and responsibilities as set out in the multitude of laws, regulations, instruction, and orders to which they are subject, and the penalties for breaches, etc. As for the legislative provisions themselves, the assessors were working from translated texts and identified some issues. There may be other ambiguities and weaknesses in the Russian text that the assessors have not identified. Currently, there is a two tier system whereby specific restrictions apply only to a limited number of staff. Staff below middle management are subject only to more general provisions in a multitude of laws, regulations, ordinances, etc. There is substantial scope for clarification.
Principle 6. The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.	The Financial Stability Committee of CBR has a clear focus on nonbank financial entities (NFEs) and systemically important financial market infrastructures, including the dominant central counterparty for securities markets. Within CBR nonbanking sector departments, staff appear to be fully engaged in the work on systemic risk. Although the published Financial Stability Review is primarily banking focused, it addresses systemic issues in securities markets when they arise.
Principle 7. The Regulator should have or contribute to a process to review the	Perimeter review of firms and products appears to be undertaken, and the appropriate sources of information have been identified and utilized. There may be scope for further formalizing the process to ensure that issues are not overlooked when first observed.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
perimeter of regulation regularly.	
Principle 8. The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.	CBR is not sufficiently proactive in identifying and evaluating potential, as distinct from actual and current, conflicts of interest and misalignment of incentives. It lacks a process to facilitate this process. Currently, its responses are primarily reactive. The responsibility for identifying and taking action regarding losses caused by the mis-management of a conflict of interest by a professional market participant is placed on the client, who may be unaware that they have suffered a loss.
Principle 9. Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.	The conflict of laws means that CBR cannot enforce the old SRO regulatory regime. The new SRO law could not be fully enforced at the time of the assessment because of transitional provisions. SRO's primary purpose is defined in the law as being the protection of members' interests, market development and efficiency, not investor protection. There are some gaps in CBR's powers to ensure procedural fairness and effectiveness by SROs. There are some gaps in SRO duties and obligations.
Principle 10. The Regulator should have comprehensive inspection, investigation and surveillance powers.	CBR has a comprehensive set of powers. There is no overall record keeping obligation imposed on securities firms, although there are extensive and detailed requirements.
Principle 11. The Regulator should have comprehensive enforcement powers.	CBR has a broad range of investigation and sanction powers, and although the level of fines is modest, the fines related to income should be dissuasive. Criminal prosecutions of market abuse offences are still very rare. Beneficial ownership information may not always be available in practice.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
Principle 12. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.	The enforcement regime is found to be not fully effective. The planning of inspections of intermediaries is neither risk-based, nor routine and periodic, given that very few scheduled inspections are undertaken. There have been no inspections of the exchanges. Supervision is focused on finding and punishing violations rather than monitoring and enhancing risk management. Inspections resources are very limited, with only 250 inspectors for 19,000 nonbank entities across CBR as a whole and used primarily for unscheduled inspections (investigatins) rather than routine compliance checks. Periodic reports submitted by intermediaries are concerned mostly with financial information and do not include risk management indicators.
Principle 13. The Regulator should have authority to share both public and non-public information with domestic and foreign counterparts.	There are powers to share information via the MMoU and other agreements. There is no power to initiate sharing of information on an unsolicited basis. The confidentiality provisions in the Investment Fund Law conflict with the disclosure provisions in the Central Bank Law. Information on beneficial owners may not always be available.
Principle 14. Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts.	CBR is a signatory to the MMoU and actively meets its obligations.
Principle 15. The regulatory system should allow for assistance to be provided to foreign Regulators who need to make inquiries in the	CBR is a signatory to the MMoU and actively meets its obligations.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
discharge of their functions and exercise of their powers.	
Principle 16. There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions.	There is no effective general ongoing obligation to disclose any material fact that could affect the value of securities. In practice, disclosures of material information, other than the items specifically listed in the law, are rare with only just over 1 percent of disclosures falling into this category, even though this category effectively includes many of the most important disclosures, such as changes in prospects or risks. There is no explicit derogation from the disclosure obligations for state and commercial secrets, and no effective safeguards when disclosures are not made. There is inadequate provision for advertisements outside the prospectus.
Principle 17. Holders of securities in a company should be treated in a fair and equitable manner.	The necessary protections for majority and minority shareholders are broadly in place. The provisions relating to shareholders acting in concert with others is limited to specified affiliated persons.
Principle 18. Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality.	The legal obligation to apply IFRS rests on complex interaction of laws and is not yet comprehensive. Most companies that are obliged to use IFRS continue to use RAS-based financial statements as the basis of the narrative and other disclosures in prospectuses and periodic reports. RAS do not qualify as internationally accepted standards, because of continued dominance of form over substance in practice. The absence of any examples of companies being required to resubmit accounts because of failure to compile them properly according to IFRS indicates limited enforcement.
Principle 19. Auditors should be subject to adequate levels of oversight.	The oversight regime is headed by the MoF and Audit Council as public interest bodies, independently of the auditing profession.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
Principle 20. Auditors should be independent of the issuing entity that they audit.	The independence principles defined in the Code of Ethics and Rules of independence of auditors are not yet fully implemented in practice. There are no requirements that the governance arrangements of a public company should result in effective oversight of the appointment of auditors by the risk committee of issuer. There are no requirements to disclose the resignation of an auditor. There is no mandatory requirement for rotation of auditors or the senior officials engaged on an audit.
Principle 21. Audit standards should be of a high and internationally acceptable quality.	International Audit Standards are, in effect, applied to public companies in the Russian Federation.
Principle 22. Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision.	The new CRA law is comprehensive and broadly meets IOSCO requirements. However, there are a number of regulations that had yet to be issued at the time of the assessment, and so the law could not be effectively implemented, and there were no CRAs yet registered.
Principle 23. Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.	There is no process for identifying areas of activity that may fail to be regulated under this principle. There are insufficient provisions to address conflicts of interest of analysts employed by brokers. Detailed provisions on appraisers contained in the SRO Code of Ethics have not been supplied to assessors.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
Principle 24. The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a CIS.	Managers and selling agents are licensed by CBR to the standards applied to all professional market participants. As such, integrity tests should be enhanced. Risk-based supervision has been applied in a comprehensive and constructive way, as lessons learned by CBR as to risk management and internal control practices in well-run fund management companies (MC) are being used to increase standards in less well-run MCs. Some detailed rules of dealing in securities by fund managers are missing.
Principle 25. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.	The legal forms and structures of collective investment schemes and investor rights are set out in the law and mandatory model fund rules, which are the equivalent of a prospectus or offering document. The custodian (specialized depository) has onerous responsibilities to ensure that the manager operates the fund within the law, CBR regulatory acts, and the fund rules. The depositories are licensed by CBR and are subject to detailed regulation of their structure, operations, and regulatory reporting requirements.
Principle 26. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a CIS for a particular investor and the value of the investor's interest in the scheme.	Disclosure requirements for unit investment funds (UIFs) are reasonably comprehensive, and CBR has the right to demand the retraction of disseminated information which does not satisfy the requirements of the Investment Funds Law or regulatory acts of the CBR; to demand dissemination of corrected information; and to prohibit dissemination. There is, however, no overarching general obligation on MCs to provide a wide range of current information in the fund rules or elsewhere which would enable potential investors to make an informed investment decision; nor an obligation to provide that information in a way that an ordinary person will understand.
Principle 27. Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a CIS.	Valuation of the NAV of funds appears to be carried out to a high standard and with effective checks and balances. Procedures for dealing with a fund which is forced to suspend redemptions appear satisfactory, and the powers of CBR in this situation, and if a winding up proves necessary, appear sufficient but are untested.

Table 6. Summary Implementation of the IOSCO Principles (continued)	
Principle	**Findings**
Principle 28. Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight.	Hedge funds are not a source of potential or actual systemic risk in the Russian Federation, and as such intensive regulation as set out in the Key Questions to this principle is not required. Furthermore, hedge funds and hedge funds managers are regulated at the same level as other funds targeted at qualified investors.
Principle 29. Regulation should provide for minimum entry standards for market intermediaries.	The licensing power is exercised carefully and with thorough examination of applications. However, there is no regulation of investment advisers (and they are not required to submit advice only through licensees). The license criteria are not comprehensive, especially with regard to integrity. There is no power to impose a license condition. There is no general requirement on a licensee to report any change that might affect their suitability to be licensed.
Principle 30. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.	Capital requirements are not sufficiently tailored to the quantum and nature of risks, nor to risks from outside regulated entity. There is no liquidity requirement for intermediaries. There is no requirement to maintain knowledge of capital at any time and calculate capital daily. There is no requirement that auditors should check that the amount of capital is sufficient to match the risks faced by the intermediary. There is no requirement to report a deterioration of capital to CBR. CBR powers to intervene to protect investors are limited (unless a broker is, in effect, in default, when the Insolvency Law provisions can be used).

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
Principle 31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.	There are some detailed requirements on client asset segregation, internal controls, and risk management. There are no overriding obligations to act with due care and diligence with respect to clients, to give priority to client interests, or to have systems and controls to protect the integrity of the dealing process, or the integrity of the market. There is no requirement to have systems and controls that ensure the fair, honest, and professional treatment of clients. There is no obligation to conduct a risk assessment, tailor policies and procedures to that assessment, have information systems to check effectiveness of controls, to review effectiveness annually, or to re-evaluate risk annually. There is no effective overriding obligation to identify and prevent or manage and disclose conflicts of interest and, if necessary, refuse to act. There is no overriding obligation to segregate duties, where necessary to avoid internal conflicts of interest. There is no overriding obligation to collect sufficient information from a client to ensure services are suitable for the client's risk appetite and objectives. There is no obligation to disclose enough information to enable an investor to make an informed decision. There is no specific requirement for a client to be provided with a written client agreement that includes fees and charges. There is no effective requirement on an investment manager to segregate client money. There are insufficient safeguards to protect clients of brokers who use client money for their own purposes. There are insufficient provisions for requiring the intermediary to identify the client and beneficial owner of the account. Client money accounts are reconciled only monthly, and client assets reconciled only quarterly, and this is insufficient. It is not appropriate to place primary responsibility for compliance with the law and regulations on the compliance officer; this should be on the management of the intermediary.

Table 6. Summary Implementation of the IOSCO Principles (continued)

Principle	Findings
Principle 32. There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.	There are powers available to deal with an intermediary in default in the Insolvency Law, and these are sufficient once the conditions are met to make them available. There is no documented contingency plan for dealing with failure of an intermediary. There are no early warning systems for potential default. There are only limited powers to take action to protect investors prior to default by intermediary.
Principle 33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.	As is typical of most jurisdictions, applications to open a new exchange or non-exchange trading system are rare events. From discussion with exchange supervision staff at CBR, it was apparent that the licensing of the merged MICEX and RTS was thorough and skillful and with an awareness of significant issues.
Principle 34. There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.	Although the elements of supervision as set out in this principle appear to be met as far as this can be achieved from the obligation on exchanges to provide substantial ongoing documentation flows to CBR, the system of supervision has yet to be rigorously tested by an onsite inspection of MOEX, a period of intense stress in the markets, the unexpected insolvency of a major listed company, or the failure of one or more large members.
Principle 35. Regulation should promote transparency of trading.	There appear to be no obvious omissions in the transparency regime on MOEX's markets. The unusual ability of the exchange to have developed markets in products largely traded OTC in other countries such as corporate bonds, foreign exchange, and repos means that there is more transparency in these markets than is typical elsewhere. The absence of dark pools, even informal ones such as broker crossing networks, means that a factor which elsewhere complicates initiatives to maintain or increase levels of transparency in equity markets, and limit the creation of two tier markets, is missing. However, High Frequency Trading (HFT) is a significant factor in equity trading.

Table 6. Summary Implementation of the IOSCO Principles (concluded)

Principle	Findings
Principle 36. Regulation should be designed to detect and deter manipulation and other unfair trading practices.	The Law and the regulatory and technological resources appear to be in place for an effective regime to detect, deter, and punish insider dealing and market manipulation. It is a new law, and no cases have yet come to court to make a judgment as to their effectiveness. While the fines are unlikely to be dissuasive, the loss of three years' salary should be. The prison sentences and other sanctions should have a high deterrent effect, if persons contemplating insider trading or market manipulation consider that there is an unacceptably high possibility of being detected and convicted in a criminal court. CBR is developing a reasonably good track record in detecting breaches and taking administrative action.
Principle 37. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.	With one exception, the regime to monitor large exposures appears comprehensive, well-planned, and well-managed. It uses multiple data sources, mostly in real time. Flows of relevant information to the appropriate departments within CBR work well and should generate warning signals in time for CBR and NCC to take appropriate action. FSD's threshold for concern—a single exposure which equals or exceeds 100 percent of an entities' own funds—is too high. Recent improvements to the bankruptcy law and the associated clearing law have been formally recognized internationally. There is a lack of effective controls on short selling of equities on MOEX, including the absence of a surveillance regime, and no mechanism for providing information on short selling to market participants or CBR. The NCC takes effective measures to protect itself from exposure to naked short selling by MOEX members and their clients, which is one necessary element of the IOSCO requirements, but it is not sufficient.
Principle 38. Securities settlement systems and central counterparties should be subject to regulatory and supervisory requirements that are designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.	Not assessed.

RECOMMENDED ACTION PLAN AND AUTHORITIES' RESPONSE

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles

Principle	Recommended Action
Principle 1	• The draft Guidelines for the Development and Stability of the Financial Market of the Russian Federation for the Period of 2016–18 has, as one of its goals, "creating conditions for the growth of the financial industry." It has identified as critical to the achievement of that goal "enhancing financial market regulation, inter alia through proportional regulation and optimization of the regulatory burden on financial market participants." It would be consistent with that goal for CBR, perhaps in conjunction with the MoF and industry representatives, to set up a program with the objective of achieving a substantial simplification of the regulatory framework while retaining and enhancing those elements of regulation, supervision, and enforcement which are necessary to achieve the other goals set out in the draft Guidelines, namely "improving the living standards for the Russian population through the use of financial market instruments;" and "facilitating economic growth through granting the competitive access of Russian economic agents to debt and equity financing."
Principle 2	• The authorities should consider measures to secure immunity for CBR staff in the case of decisions properly made on the basis of due diligence. • Given the other opportunities for consultation between Government and CBR at Governor and Board level, as set out in the CBR Law, the authorities should consider whether the right of the Ministers of Finance and Economic Development to attend Board meetings and express recorded opinions is necessary or appropriate.
Principle 3	• The authorities should consider whether the process by which a very substantial proportion of CBRs' operational budget is set by the executive and legislature of the Russian Federation in the National Financial Board is consistent with true operational independence of CBR in the performance of its supervisory and regulatory responsibilities.
Principle 4	• CBR should keep its consultation process under review to ensure that it engages the willing support of the nonbank licensees for its development of more effective regulation of the financial markets sector.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
Principle 5	• CBR should review the multitude of legislative and regulatory requirements to which staff are subject to remove any ambiguities and with the longer-term aim of codifying them in a comprehensive Code of Professional Ethics. There is substantial scope for clarification. • The currently two-tier system whereby specific restrictions apply only to a limited number of upper-level staff should be reviewed.
Principle 7	• Further formalizing the process of perimeter review might include appointing a senior manager and staff with specific responsibility and appropriate reporting lines for the topic. Consideration should also be given, if not already in place, of providing specialized training for the Territorial Units of the bank to enable them better to recognize Ponzi schemes and other outright fraudulent practices.
Principle 8	• The assessors have noted the difficulties in drafting legal provisions stating general principles of behavior, but strongly urge the authorities to seek a solution which would enable the Russian regulatory framework to move closer to international standards regarding an effective framework which both requires and assists licensees to identify, manage, and mitigate conflicts of interest and misaligned incentives that arise in their businesses.
Principle 9	• Provisions in previous laws relating to SROs that conflict with provisions in the new law should be repealed. • The new SRO law should be amended to provide that: ○ the primary purpose of SROs as being to promote high standards of conduct to protect investors and promote fair markets; ○ an explicit condition of registration of an SRO should be the ability to demonstrate to CBR that the SRO has the willingness and capacity to provide adequate standards of professional behavior and investor protection; ○ an SRO should adopt provisions that prevent any member of the SRO, or any employee from abusing their position to gain unfair competitive advantage; ○ an SRO's internal rules should include provisions on procedural fairness that match those of the CBR itself, and a prohibition on the inappropriate use of information, for example for personal gain;

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
	○ an SRO's internal rules should ensure that all similarly situated members and applicants should be treated equally; ○ the membership criteria for the new SROs should not constitute a barrier to entry to the securities or fund management business; ○ an SRO should be required to submit its internal rules to CBR for approval, and CBR should be able to approve, deny approval, or insist on changes to the SRO's internal rules, where necessary, to ensure that they match appropriate standards of fairness, effectiveness, and professionalism; ○ an SRO should be required to keep records, for a minimum of five years, which demonstrate that it is complying with its charter and its statutory responsibilities, and which record the operation of its functions; ○ CBR has the power to conduct onsite inspections of SROs; ○ the power of CBR to collect information from SROs overrides any confidentiality duty imposed by the SRO law or any other statute; ○ CBR has the power to approve, deny approval to, or insist on changes to SRO internal rules; ○ CBR has the power to conduct inspections of SROs and should state explicitly that the duty to disclose matters to CBR overrides any duty of confidentiality to members. • CBR should develop a new supervisory regime with SROs, where Basic Standards replace (not add to) existing regulations, and all supervisory tools are used. CBR should develop an oversight methodology for monitoring SRO activity.
Principle 10	• The Securities Law, Investment Funds Law, and Organized Trading Law should include an overriding record keeping obligation that requires all securities businesses to keep such records as would be necessary to demonstrate their operation of their business, to demonstrate compliance with the law and regulations, to document their relations with clients and third parties, and to keep such records for five years.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action

Principle 11	• CBR should seek an amendment to the AML Law so that a person subject to the relevant obligations should:
	  ○ Always ask a natural person if they are acting on their own behalf or on behalf of another; and
	  ○ Refuse to act if they are unable to identify the beneficial owner of a legal entity.
	• CBR should consider reviewing the powers in Article 11 of the Investor Protection Law and seeking amendments as appropriate so as to ensure that they are capable of being used in practice.

Principle 12	• CBR should devote sufficient resources to the inspection team so as to be able to conduct a risk-based, or routine/periodic scheduled inspection program. • CBR should commence a regular inspection program of the exchanges. • The Securities Law should be amended to place specific responsibility for ensuring compliance with regulatory obligations on management. • The internal controls regulation should be amended to focus on the essential elements of an internal control system rather than just the detailed provisions for the appointment and functions of the compliance officer. • CBR should adopt an approach to enforcement that focuses on the risks to the objectives of securities regulation, identifies the key measures to mitigate those risks, and uses all supervisory tools to ensure compliance with those regulatory requirements. • CBR should develop the periodic reporting requirements so as to gain more information relevant to the adequacy of risk management and compliance by securities firms. • CBR should develop a protocol for mounting investigations into market offences so as to avoid the risk of "tainting" evidence before a full criminal investigation takes place.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
Principle 13	• The CBR Law should be amended to enable CBR to provide confidential information to a foreign regulator on an unsolicited basis. • The Investment Funds Law should be amended to provide an exception to the commercial secrets provision to allow disclosure where required by law.
Principle 16	• The Securities Law should be amended so that it: ○ includes an effective provision that requires the disclosure of any material fact that would reasonably be expected to affect the price of a security or the decision to buy or sell that security; ○ permits derogations from the disclosure obligations for state and commercial secrets but imposes safeguards, which include CBR powers to approve or deny approval to deferral of disclosure and appropriate trading restrictions to protect market integrity, as well as powers to require immediate disclosure when obligations are not met; ○ no longer includes the 50 detailed matters for disclosure from the Securities Law, thereby reinforcing the primacy of the overriding obligation to disclose all material facts; and ○ gives CBR specific powers to require issuers to make disclosures when material events have occurred (or CBR discovers that they may be about to occur), but the issuer has failed to meet its disclosure obligation. • The 50 detailed matters listed in the Disclosure Regulation should exclude routine events which would not affect the price of a security (such as the announcement of a general meeting) and include a material change in prospects, a significant change in risks, a change in the economic circumstances of the country or region in which the issuer does most of its business, a significant change in the trading environment, the signing of a major new contract, the loss of a major contract, a major physical or weather event that affects the continued operation of the company, a significant change in the line of business, a decision to acquire or sell significant assets, or any other major event which is likely to affect the value of the company's assets, or its ability to continue to make profits. • The Investor Protection Law and the Law on Advertising should deal more comprehensively with advertisements so as to ensure that advertisements issued in connection with a public offer should be issued only by the issuer or advisers acting under the issuer's authority, should only contain information that is true and not misleading, should refer to the prospectus. and should be subject to approval by CBR.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
	• CBR should discuss the simplification of the disclosure regime with the private sector to make it more comprehensible and enforceable.
Principle 17	• CBR should seek an amendment to the JSC Law to: ○ Extend the requirements relating to shareholder disclosures and takeovers to those reaching the specified thresholds when actin in concert with any person; ○ Extend the requirements for information to be provided for General Meetings so as to include full information on the consequences of decisions proposed on the agenda; and ○ State explicitly the rights of shareholders to receive remaining assets after liquidation, in proportion to the shareholdings (in relation to all assets and not just in respect of dividends credited but not paid).
Principle 18	• CBR should continue its program of progressively obliging public companies to publish financial statements according to IFRS. In addition, CBR should require those companies that are subject to a requirement to publish accounts according to IFRS to use the IFRS accounts as the basis for the narrative and other disclosures in the prospectus and quarterly reports. • The MoF should consider amending the agreement with the National Organization to give MoF formal oversight powers to enable it to check on the internal processes of the National Organization and thereby ensure they are sufficiently transparent. Such a provision should be included in future agreements with organizations that may win the tender to act as the independent adviser on accounting standards in the future.
Principle 20	• The Auditing Law (or other legislation as appropriate) should be amended to include: ○ A general provision prohibiting financial business, corporate, and personal relations between an auditor or audit firm and the client and any other relationships or behavior that might threaten or reasonably appear to threaten independence;

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
	○ A general provision that prohibits the provision of any non-audit services to an audit client, where such services may be of a nature or scale that would compromise or appear to compromise the independence of the auditor; ○ Provisions requiring governance arrangements that ensure that the selection of auditors and the oversight of auditor independence is, in the case of public issuers, carried out by a body independent of management; and ○ A requirement to disclose the resignation, replacement, or removal of an auditor. • The Audit Council should ensure that audit and ethical standards include the requirement that internal quality controls directly address independence, and that there are mandatory measures to require the rotation of individual auditors if not audit firms, so as to safeguard independence. • The MoF should increase the priority given to independence in substance as well as form, when conducting inspections.
Principle 22	• CBR should complete the process of writing regulations, so that the law can come into effect. • The CRA Law should be amended to include: ○ A general record keeping requirement that is broad enough to ensure that all appropriate records are kept to demonstrate the compliance of the CRA with the regulatory requirements, the operations of the business and the practical implementation of rating methodology); ○ The power for the CBR to require an applicant for registration as a CRA to provide additional information; ○ An obligation on CRAs to maintain sufficient resources to be able to apply the methodology with all relevant information rigorously and robustly; and ○ An expanded integrity test, with a broader disclosure requirement and the discretion of CBR to consider whether the matters disclosed are relevant.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
Principle 23	• CBR should create regulations that specifically address the potential conflicts of interests of analysts when introducing a regulatory regime for advisers. • CBR should review the ethical standards of the SROs for appraisers to ensure that all the requirements of this principle are met.
Principle 24	• While continuing to search for customers carrying out improper transactions, with or without the knowledge of the licensee, onsite inspectors should be equally engaged in seeking evidence of a firm treating its clients unfairly, such as by selling funds or other products not suitable for the client's risk profile, or where a less expensive (but lower commission generating product) would meet the client's need equally well or even better. As retail participation in financial markets increases, mis-selling of financial products is likely to increase, and this will damage the confidence of new investors in financial markets. • Increase the number of annual planned onsite inspections of MCs and SDs. • Introduce rules covering best execution and due diligence. • Introduce more comprehensive integrity tests for individuals in key positions in MCs.
Principle 25	• Although a specialized depository (SD) must be independent of the management company (MC) of a unit investment fund (UIF), it is able to be a company within the same group as the MC. There is potential in these circumstances, despite the current regulation of the activities of SDs, for collusion or a lack of care to occur. A mechanism to mitigate this risk might be to assign, within the risk-based supervisory framework, a High Risk or "red zone" rating to SDs in this position and submit them to the highest intensity of SD supervision. Alternatively, the Investment Funds Law could be amended to secure actual independence of the SD.
Principle 26	• CBR should continue to explore ways, within the constraints imposed by Russian law, to establish general or overarching requirements on MCs to provide a wide range of current information in the fund rules and elsewhere which will enable potential investors to make informed investment decisions; and to provide that information in a way that an ordinary person will understand.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
Principle 27	• There has not been a failure of a fund for a long time, and the relevant laws and regulatory acts have changed, some repeatedly, in recent years. CBR might wish to consider running an exercise ("war game") to test the current legal and operational position against a hypothetical failure of a fund or group of funds.
Principle 28	• The further development of hedge funds, and funds which, while not being formally categorized as hedge funds, can borrow to invest and thus can be highly leveraged, should be closely monitored by CBR with a view to subjecting them to more intensive supervision should they begin to demonstrate systemic risk characteristics.
Principle 29	• The Securities Law and regulations should be amended so as to: ○ Expand the fitness and properness criteria for (and matters to be disclosed by) senior managers and owners especially with respect to integrity; ○ Give CBR the discretion to determine the relevance of the disclosures when considering whether or not to grant permission to take up a post; ○ Give CBR discretion to judge the adequacy of the organization, and governance, including the adequacy of the risk management and internal controls of a license applicant; ○ Impose a general obligation on a license applicant to disclose any matter that might reasonably affect CBR's judgement as to the suitability of the applicant to undertake securities activity and extend this to licensees so as to create an obligation to disclose any matter that might reasonably be supposed to affect a decision as to whether they should retain a licence or continue to act as manager or owner (as appropriate); ○ Give CBR the power to grant a license with conditions, or amend a license to impose terms and conditions as appropriate; and ○ Bring investment advice into regulation. • CBR should develop criteria to assist it in making the qualitative judgements recommended here.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
Principle 30	• The new regulation on risk-based capital that CBR is contemplating should: ○ Set capital requirements that are based on the full range of risks to which a professional securities market firm is subject, taking account of the nature, scope, and scale of its activities, and require that capital be maintained at all times; ○ Impose a liquidity requirement that would ensure that a professional securities firm could absorb some losses and wind down the business in an orderly manner; ○ Create an obligation on a professional securities firm to report a deterioration in excess capital (i.e., the capital held in addition to the minimum requirement) of 50 percent since the last report; and a further obligation to report to CBR if their capital falls below 120 percent of the minimum; ○ Require securities firms to make a daily calculation of capital and place this on the file so that CBR and auditors can select days at random to check that such calculations are being undertaken properly; ○ Set a deadline for the submission of annual audited accounts by professional securities firms; and ○ Set a requirement on securities firms that they must get an annual opinion from their auditors on whether their capital is sufficient for the full range of risks.
Principle 31	• The Securities Law should impose the following obligations on securities firms, in each case, with overall provisions supported by some detail giving clear information about what is required to ensure that the overall obligations are implemented effectively: ○ To act with due care and diligence in the interests of a client, to place the interests of the client above its own, and to have systems and controls that ensure the integrity of its dealing practices and the fair, honest, and professional treatment of clients; ○ The management to have full responsibility for complying with legal and regulatory obligations; ○ The management to undertake a risk assessment of its business, to devise policies and procedures that address those risks, to train staff in those

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action
	○ procedures, to have an information system for assessing effectiveness of those policies and procedures, to review the effectiveness at least once a year, and to reassess the risks at least once a year; ○ An investment manager to hold client funds in a segregated account; ○ All securities firms to identify and prevent, or manage conflicts of interest, by disclosure, internal organizational barriers, or by declining to act; ○ All securities firms to ensure that there is appropriate segregation of duties where necessary to prevent unmanageable risks of conflicts of interest, undetected errors, breaches of internal controls, or abuse more generally; ○ All securities firms to obtain sufficient information about the client's circumstances and objectives to enable them to provide appropriate services and advice; ○ All securities fi~~e~~rms to refuse to accept clients where the reasonable and affordable measures have not identified the beneficial owner and to establish in each case if a natural person is acting on his or her own behalf or on behalf of another; ○ Those firms that hold client money to have effective protection for those assets including segregation and a requirement to reconcile client money in the bank accounts with the internal records on a daily basis; and ○ Those firms that hold client assets to reconcile client assets with internal accounting records weekly for the high-intensity trading client, and monthly for all other clients, except those who do not trade for three months, whose reconciliation should be quarterly. • CBR should amend regulations to impose the following obligations: ○ To have systems and controls to limit the use of client money in the securities firm's own interests (to circumstances where it provides scope for covering temporary and minor shortfalls in the client account), to give prominence to this matter in the client agreement, and to explain the risks to the client; ○ To identify all clients and the beneficial owners; and ○ To provide a client with a written agreement with certain specified contents, such as fees and charges. To give a client enough information to make an informed investment decision.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (continued)

Principle	Recommended Action

Principle 32	• The Insolvency Law should be amended to enable CBR to appoint a provisional administrator if it thinks such action is necessary to protect investors or safeguard market stability from the consequences of a default.
	• CBR should review the powers of the provisional administrator to ensure that they are sufficient to enable it to:
	  ○ Restrict activities by the intermediary;
	  ○ Move client accounts to another intermediary; and
	  ○ Apply other available measures intended to minimize customer, counterparty, and systemic risk in the event of intermediary failure, such as customer and settlement insurance schemes or guarantee funds.
	• CBR should draw up a detailed plan of the specific actions it would take in the event of a failure, including the names and contact details of those who would take the relevant decisions, contact details of the relevant people in other agencies, draft press releases and statement to investors, check lists of steps to be considered to exercise legal powers and protect investors, lists of the necessary physical facilities that may be required, names of possible administrators, and other relevant matters. The plan should be tested from time to time in a trial exercise.

Principle 33	• In considering issues which arise in its ongoing supervision of MOEX, the exchange supervision team should look carefully at the exchange's record of disciplining members and listed companies. The current approach has elements which, while it may be effective in the context of a Russian market with few retail investors, are difficult to reconcile with good international practice.
Principle 34	• The upcoming first inspection of MOEX will be an important stage in CBR's development as a securities market regulator, and it will be critical that the inspectors have the necessary skills and will have been fully briefed by the offsite exchange supervision team to carry out their task efficiently and knowledgeably.
Principle 35	• Although dark pools and informal trading systems do not exist in the Russian market currently, some brokers are internalizing trades in overseas markets and CBR should remain alert for any indications that this practice is being adopted domestically.

Table 7. Recommended Action Plan to Improve Implementation of the IOSCO Principles (concluded)

Principle	Recommended Action
Principle 36	• In order to enhance the cooperation between the Department for Market Manipulation and Division F over the longer term, the two parties could consider whether there are benefits in developing a MoU which sets out the responsibilities and expectations of both parties. The expectation must be that the work load will increase as knowledge and expertise and technical and analytical resources to detect violations increase. • Given that market manipulation is now a criminal offence, the exemptions in the Insider Trading Law have particular importance. As is the case in the EU under the Market Abuse Directive and in other jurisdictions, such as Japan and the United States, where the equity and bond markets are an important source of debt and equity capital, CBR should review the current regulation and consider what improvements are necessary to impose suitable limits on trading activities in order to ensure that investors' interests are adequately protected.
Principle 37	• CBR should work with MOEX to research good practice on the regulation and disclosure in other markets and adopt measures best suited to the Russian market, while being consistent with international standards. • With one exception the regime to monitor large exposures appears comprehensive, well-planned, and well-managed. It uses multiple data sources, mostly in real time. Flows of relevant information to the appropriate departments within CBR work well and should generate warning signals in time for CBR and NCC to take appropriate action. FSD's threshold for concern—a single exposure which equals or exceeds 100 percent of an entities own funds—is too high and should be reduced, possibly to a maximum of 25 percent.

A. Authorities' Response to the Assessment

Introduction

66. The Central Bank of the Russian Federation (CBR) extends its appreciation to the representatives of the International Monetary Fund who worked closely and remotely on the assessment of implementation of the IOSCO Objectives and Principles of Securities Regulation in the Russian Federation.

67. Financial sector surveillance conducted by the International Monetary Fund represents a distinct opportunity for understanding the key linkages that affect the stability and vulnerability of

the Russian financial sector. The results of the mission have deepened the CBR's understanding of the improvements to be made, helped to articulate policy recommendations, and could be used for better discussions with market participants, which are also called for to provide support for policy and institutional changes.

Principle-by-Principle Response

Principle 6

68. We suggest rephrasing the summary passage referring to Principle 6 in the following way: the *Financial Stability Review* addresses systemic issues in all segments of the financial markets, including securities markets, when they arise, and these issues are given appropriate focus and analysis. Within the CBR, non-banking sector departments' staff appears to be fully engaged in the work on systemic risk. While FSCom is responsible for the assessment and analysis of systemic risks and the stability of the financial system, it also has a special focus on NFIs and systemically important financial market infrastructure.

Principle 9

69. It is significant to reflect that on March 10, 2016, seven SROs were registered under the new SRO law, and moreover four of them are SROs of professional securities firms. CBR thus suggests eliminating the inconsistences in the text of Principle 9 implementation assessment.

70. Furthermore, the assessment states that the CBR must approve Basic Standards no later than three months after the first SRO is registered. This statement is not accurate. Rather, the CBR sets a list of Basic Standards not later than three months after the first SRO is registered (Article 33(9) of the SRO law).

Principle 12

71. As the grade for Principle 12 ("The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program") was downgraded from *partly implemented* to *not implemented*, we suggest taking into consideration the comments below.

72. Please consider that the grade *not implemented* involves the identification of serious deviations from the criteria, and that this judgment is not substantiated. Specified criteria regarding the competencies of the Chief Inspection are implemented without any significant deviations, and therefore are partly implemented.

73. Moreover, please take into consideration the data on the number of inspections: in 2014 the Chief Inspection carried out 37 onsite inspections of professional securities market participants, including 9 (24 percent) unscheduled inspections. In 2015, 27 onsite inspections of professional securities market participants were carried out, including 4 (15 percent) unscheduled inspections. As regards asset management companies, the Chief Inspection carried out 43 onsite inspections, including 36 (84 percent) unscheduled inspections in 2014, and 25 onsite inspections, including 13 (52 percent) unscheduled inspections in 2015.

74. CBR also suggests taking into account the following observations:

75. Inspections are in general conducted at the suggestion of the off-site team and based on facts regarding the deterioration of the financial position, breaches of regulations, complaints by clients and the federal authorities, profile, exposure and concentration of risk, business transparency, among others.

76. BR has adopted the practice of coordinated onsite inspections of financial groups (including those, which are not institutionalized as financial groups). This tool allows CBR to identify risks taken by the groups (individual participants of the groups).
Coordinated inspections allow CBR to uncover procedures used to mask the risks taken by the group, and thereby improve the transparency of financial activities and improve market discipline.

77. Concerning the description of the switch to the risk-based principles, is important to consider the points made below.

78. In 2014–15, the Chief Inspection carried out onsite inspections of professional securities market participants initiated by the Securities Market and Commodity Market Department implementing risk-based supervision. There were mainly inspections of relatively small professional securities market participants about which there was substantial negative information on their financial statement or activities.

79. During most of these onsite inspections, violations were discovered, including of the requirements of the legislation, as well as the absence of assets or their significant overvaluation, typically associated with the use of “structured” operations to comply with capital structure requirements, and with the investment of funds in financial instruments of dubious quality, and with an increased risk of deliberate substitution of high-quality and liquid assets.

80. The Chief Inspection, during onsite inspections of the activities of professional securities market participants, in particular evaluates the quality of internal control and risk-management systems for compliance. In most of the inspected professional securities market participants, no systems had been organized for internal control and risk management, and corporate governance was not compliant with international principles. These facts were considered to be violations of the requirements of the legislation. The assessment of the quality and the level of implementation of declared procedures of internal control systems, risk management, and corporate governance in these professional securities market participants had no chance to be carried out due to total absence of the subject for assessment.

81. Approaches to implementation of this practice are constantly improving. Examples of best practices were reported to Chief Inspection employees during training sessions.

The report of the mission does not accurately mention that a final report of violations, together with an agreed rectification program, is handed to the regulated entity on the departure of the inspection team. The final report must not include an agreed rectification program. Moreover, monitoring of the elimination of violations found during the onsite inspections is not within the competence of the Chief Inspection.

Principle 16

82. Principle 16 states that there should be full, timely, and accurate disclosure of financial results, risk and other information that is material to investors' decisions. This principle was assessed as "not implemented" even though Russian legislation provides for all major requirements for prospectus, financial statements, and disclosure of material facts. This information was provided during the assessment and is mentioned in the report. The legislative provisions are set in Federal Law № 39-FZ "On the securities market" (Article 24(4), Article 30, 30(2), 30.1), and in the Federal Law "On joint stock companies" (Chapter 13). Detailed disclosure requirements for securities issuers are set out in the Regulation of the Bank of Russia dated December 30, 2014, № 454-P. These requirements are set in line with IOSCO International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers, International Disclosure Principles for Cross-Border Offerings and Listings of Debt Securities by Foreign Issuers, Principles for Periodic Disclosure by Listed Entities and Principles for Ongoing Disclosure and Material Development Reporting by Listed Entities, and are enforced by CBR.

83. As for the main shortcomings in the implementation of the Principle 16 mentioned in the report, the following points should be considered:

Advertisements during the securities offering

84. Current Russian legislation provides for the necessary legal mechanisms to ban offering advertisements before a prospectus is published. There is also a requirement in the Securities Law that prohibits unfair and inaccurate advertisements as well as advertisements missing any material information concerning the offering. CBR will take into account the recommendation to require prior approval of securities advertisements by CBR, which is currently missing.

Material facts disclosures

85. The Report does not take into account that Russian legislation requires companies to disclose any material fact potentially able to influence the price of the security issued by such company. Specifically, Article 30(13) of the Securities Law defines the material fact as any event which may cause a substantial change in securities' price. As provided for in Article 30 (4), such material events are to be disclosed. Moreover, the CBR has the power to require the issuer to make such disclosure in case of failure through a CBR order.

86. The list of events in Article 30 (14) of the Securities Law covers most possible situations in which meaningful disclosure is necessary for investors, while the general obligation to disclose any material fact that could affect the value of securities set out in Article 30 (4)(13)(14) covers all the rest. Many of the examples of events cited in the report as not covered by the list are actually covered (that is, signing of a major new contract, the loss of a major contract, significant change in the line of business, a decision to acquire or sell significant assets), while others are not applicable in the Russian tradition—such as profit warnings—as many companies consider only an approved financial statement as a valid document due to disclosure.

Absence of explicit derogation from disclosure obligations and safeguards giving CBR the power to require advance notice of any decision to delay or abstain from disclosures of material facts

87. We find the assessors' statement that there is explicit derogation from the disclosure obligations for state and commercial secrets to be arguable as there are general provisions that all essential information is to be disclosed, and if the information is not disclosed, then the issuer must provide the reason for doing so. When state and commercial secrets shall not be disclosed in accordance with the corresponding laws, and when the issuer refrains from such disclosure of state or commercial secrets, the issuer must nonetheless disclose that this information was not disclosed because it constitutes a state or commercial secret. The recommendation to provide CBR with the power to require advance notice of any decision to delay or abstain from disclosures will be considered.

88. Overall, CBR does not agree with the "not implemented" assessment for this Principle. CBR believes that major safeguards requiring full disclosure that enables investors to take informed investment decisions are implemented in the Russian legislation. There are certain shortcomings in the disclosure regime. However, in CBR's opinion, they are not of a gross nature and do not justify downgrading the previous FSAP assessment, which was "partially implemented," especially considering that there were no changes in the legislation that weakened the disclosure regime.

Principle 17

89. CBR does not agree with the downgrade from "broadly implemented" to "partly implemented" for Principle 17 ("Holders of securities in a company should be treated in a fair and equitable manner"). Russian legislation in fact provides for all major safeguards aimed at implementation of the principle, according to which holders of securities in a company should be treated in a fair and equitable manner. Although the JSC Law provisions relating to takeovers cover actions of the buyer acting with its affiliated persons rather than shareholders acting in concert, the affiliated persons include a rather wide spectrum including individuals, and the affiliated person's lists are obligatory for disclosure, thus ensuring that this provision of the law is really working in practice. CBR takes into account the recommendation on this principle and is working on corresponding amendments to the legislation.

Principle 22

90. The following should be noted in assigning a grade to Principle 22 ("Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision"). With the aim of applying the newly adopted CRA Law, the CBR has issued Regulation № 521-P dated January 17, 2015 "On the Procedure of CBR Maintaining CRAs Register, Foreign CRAs' Branches and Offices, on the Requirements for Procedure and Form of CRAs Notifications Submission." In accordance with the new Regulation, business companies can apply to be registered as credit rating agencies. Furthermore, on February 29, 2016, one business company has already applied to be registered under Regulation No 521-P as a credit rating agency.

91. Furthermore, regarding the requirements on the relevance of work experience, Section 4 of Article 7 of Federal Law 222-FZ lays down requirements for the relevance of work experience in position as a senior manager at a CRA or its structural units or any analytical agency or research

center, or a financial organisation or its structural unit operating in the financial market, or have experience of work with CBR or a federal executive body acting as a regulator of the financial market in a position not lower than a structural unit head for at least one year in case of higher education degree in Economics, Law, Mathematics (technical), and at least two years in the event of a different higher education degree.

Principle 29

92. In reference to the assessors' comment regarding the absence of a regulation on investment advisors, it is important to mention that the draft law amending the Securities Law on investment advisors' activity was already submitted to the State Duma. Provisions of the new law establish a financial consulting implementation framework, including the requirements for investment advisors and self-regulatory organizations of investment advisors, and govern interactions between the investment advisor and clients. They also set out requirements on clients' investment profiles, and determine the rights and duties of a financial advisor.

Principle 31

93. Principle 31 ("Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters") was downgraded from "partly implemented" to "not implemented" owing to findings of a lack of regulation in the following respects.

Conflicts of interest

94. CBR Regulation № 3234 contains specific requirements on brokers to control the risks inherent in direct (or indirect) client access to the exchange; and there is a mandatory system of pre-order validation for every client which allows a broker to set limits to prevent a client from placing orders exceeding those limits. This comment is in response to the statement that there are no provisions relating to the controls necessary to prevent a client with direct access to an exchange from placing an order that exceeds specified limits.

Internal controls

95. According to passage 1.1 of Article 10 of the Securities Law, professional intermediaries operating in the securities market have to organize and exercise compliance and internal audit. In order to organize and exercise compliance, professional intermediaries operating in the securities

market are obliged to appoint a compliance officer or to form a separate division within their organization (compliance service).

96. Professional intermediaries operating in the securities market are required to organize a risk management system with respect to their professional activity in the securities market and operations with own funds. The risk management system has to be commensurate with the nature of the operations of the professional intermediary operating in the securities market and include a risk monitoring system that provides timely information to the Board.

97. Requirements aimed at regulation of compliance, internal audit, and the organization of risk management systems of professional intermediaries operating in the securities market are currently under development.

Protection of clients' rights

98. The Article 3 of the Securities Law imposes obligations on brokerage firms to act with due care and diligence in the interests of a client and to place the interests of the client above their own.