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The review provides a detailed analysis of main trends in Russia's economy in 2013. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit spheres; financial sphere; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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6.4. Financial Markets: Government Regulation vs Self-regulation in Russia in 2014

From 1 September 2013, the Federal Law 'On the Introduction of Alterations to Some Legislative Acts of the Russian Federation in Connection with the Delegation to the Central Bank of the Russian Federation of the Powers for Regulation, Control and Supervision in the Sphere of Financial Markets'¹ has entered into force, whereby the RF Central Bank (the Bank of Russia) is to be endowed with the powers of a federal body of executive authority over financial markets, which previously were exercised by the Federal Financial Markets Service (FFMS of Russia). As a result of integration of the Federal Financial Markets Service into the Bank of Russia, a special structural subdivision has been created - the Bank of Russia Financial Markets Service.

Although from a formal point of view the RF Central Bank is not a government body, its official functions essentially belong to the sphere of government authority, because the execution of these functions implies certain law enforcement measures, and so to a certain degree it can be viewed as a government regulator. So, what does this transfer of powers mean for those spheres of the economy that were previously subject to regulation by the Federal Financial Markets Service of Russia?

For non-bank financial institutions, one of the 'symbols' of the stronger influence exerted by the government regulator has become the draft federal law 'On Self-regulatory Organizations (SROs) in the Sphere of Financial Markets'² submitted by the Bank of Russia in 2013.³

On the one hand, the aim of the new draft federal law is to provide solution to the problem posed by the absence of uniform regulation rules in the field of self-regulation on financial markets, because the activity of self-regulatory organizations (SROs) in each financial market segment is regulated by the specific law issued with regard to that segment, or is not regulated by any legislative acts at all. On the other hand, the draft federal law's goals are declared to be as follows: to make more prominent the role of SROs in the activity of financial market participants; and to make more effective the interaction between SROs and the regulator⁴.

At the meeting held on 28 November 2013, in the course of discussion on the issues of creating an international financial center in Moscow and improving the investment climate in the Russian Federation, RF Prime Minister Dmitry Medvedev spoke of the necessity to observe proper balance between the interests of participants in the self-regulation process and those of the regulator, where 'a more prominent role may and must be played by professional associations'⁵.

Indeed, any further expansion of the powers of the government regulator over self-regulatory organizations may have a negative effect on their performance, if SROs should be deprived of at least one of the components of self-regulation, namely the right to elaborate and establish the standards and rules of professional (entrepreneurial) activity and to exercise control over

¹ Federal Law of 23 July 2013, No 251-FZ 'On the Introduction of Alterations to Some Legislative Acts of the Russian Federation in Connection with the Delegation to the Central Bank of the Russian Federation of the Powers for Regulation, Control and Supervision in the Sphere of Financial Markets' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 29 July 2013, No 30 (Part I), Article 4084.

² See http://www.minfin.ru/common/upload/library/2013/12/main/FZ_o_SRO.pdf. As amended on 13 November 2013.

³ See Polezhaeva N. A. *Pravovoe regulirovanie deiatel'nosti samoreguliruemyykh uchastnikov rynka tsennykh bumag* [Legal Regulation of the Operation of Self-regulatory Organizations of Professional Participants of the Securities Market] *Self-Regulatory Organizations of Professional Securities Market Participants: Membership Features* // *Zakon i pravo [Law and Justice]* – 2013. – No 8. – P. 50–52. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2380625

⁴ See <http://regulation.gov.ru/index.html>.

⁵ See <http://government.ru/>.

compliance with said standards and rules⁶. However, it is precisely this trend - instead of a trend towards increasing the role of self-regulatory organizations and making more effective their interaction with the regulator - that manifests itself in the draft federal law prepared by the RF Central Bank.

Similarly to the general law on SROs adopted in 2007⁷, the new draft federal law puts forth only the general principles of financial market self-regulation, with no regard for the specificities of each type of self-regulatory organization.

It should be noted that the general law on SROs had initially been elaborated exclusively as a law on self-regulatory organizations operating on financial markets. However, it was not properly coordinated with the Bank of Russia and the FFMS of Russia, and so was not applicable to part of the existing financial markets⁸.

One of the innovations to be introduced by the draft federal law, which makes questionable the freedom of SROs, relates to expanding the sphere of legislative regulation of the standards and rules applicable to self-regulatory organizations, and expanding the corresponding powers of the regulator as well (Article 4, 5, 6).

In accordance with the draft federal law prepared by the RF Central Bank, the self-regulatory organizations operating on financial markets will be obliged to develop and adopt mandatory internal standards of SROs, and also to develop, approve and coordinate with the Bank of Russia mandatory uniform basic standards for each type of SRO.

In order to be granted the status of a SRO, a not-for-profit organization will be obliged to adopt the basic standards previously coordinated with the RF Central Bank. Besides, those standards may also become mandatory for all financial organizations of a certain type, irrespective of the fact of their membership in a SRO.

The Bank of Russia is planning to be able both to establish the lists of internal and basic standard (to be developed and adopted by self-regulatory organizations in a mandatory procedure) and to determine the scope, content and forms of the relations between public organizations requiring regulation. These standards must be compatible not only with Russian legislation, but also with the normative acts issued by the Bank of Russia (while the requirements stipulated therein are as yet unknown).

The existing legislative norms applied specifically to each sector⁹ usually overlook the issue of the regulator's participation in the elaboration and enforcement of these standards and rules, leaving them within the discretion of the self-regulatory organizations.

⁶ See Item 1 of Article 2 of Federal Law of 1 December 2007, No 315-FZ 'On Self-regulatory Organizations' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 3 December 2007, No 49, Article 6076.

⁷ Federal Law of 1 December 2007, No 315-FZ 'On Self-regulatory Organizations'.

⁸ See V. S. Pleskachevsky's speech at 3rd All-Russian Forum of Self-regulatory Organizations, entitled 'Self-regulation in Russia: Experiences and Prospects for Development' held in the framework of *Russian Business Week 2013* (organized by the Russian Union of Industrialists and Entrepreneurs (RSPP)), 19 March 2013.

⁹ Federal Law of 22 April 1996, No 39-FZ 'On the Securities Market' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], No 17, 22 April 1996, Article 1918; Federal Law of 29 November 2001, No 156-FZ 'On Investment Funds' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 3 December 2001, No 49, Article 4562; Federal Law of 7 May 1998, No 75-FZ 'On Non-state Pension Funds' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], No 19, 11 May 1998, Article 2071; Law of the Russian Federation of 27 November 1992, No 4015-1 'On the Organization of Insurance Business in the Russian Federation' // *Rossiiskaia gazeta* [The Russian Newspaper], No 6, 12 January 1993; Federal Law of 2 July 2010, No 151-FZ 'On Microfinancial Activity and Microfinancial Organizations' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 5 July 2010, No 27, Article 3435; Federal Law of 18 July 2009, No 190-FZ 'On Credit Cooperation' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 20 July 2009, No 29, Article 3627; Federal Law of 30 December 2004, No 215-FZ 'On Housing Saving Cooperatives' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 3 January 2005, No 1 (part 1), Article 41; Federal Law of 8 December 1995, No 193-FZ 'On Agricultural Cooperation' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 11 December 1995, No 50, Article 4870.

In this connection it should be noted that the participants in the self-regulation process are usually more willing to comply with the requirements established by their own organizations rather than with the standards and rules imposed on them from above. Thus, for example, the self-regulation model that was applied in the US securities market prior to 2007, relied on two major self-regulatory organizations: the New York Stock Exchange (NYSE) and the National Association of Securities Dealers, Inc. (NASD).

The former organization was created on the initiative of market participants, who also established the standards and rules for their operation. The NYSE's members were anxious to uphold their organization's reputation, and so their services were in great demand among holders of securities and other clients. The NASD, on the contrary, was created with the active assistance of the US Administration (Maloney Act of 1938), and its members did not participate in the elaboration of standards and rules. The relevant standards and rules were agreed upon between the self-regulatory organization's board and the government regulator, and represented in the main references to normative acts issued by the regulator. So, the NASD did not enjoy one of the main advantages of self-regulation – the possibility for its members to take part in the development of standards and rules, conducive to ensuring a high level of professional requirements.

If the provisions stipulated in the draft federal law put forth by the RF Central Bank are implemented into actual practice, SROs may find themselves in a situation similar to that faced by the NASD, further complicated by the fact that the government regulator will probably also participate in the decision-making concerning the appointment of heads of self-regulatory organizations (of which more will be said later).

The second innovation to be introduced by the draft federal law developed by the Bank of Russia may be detrimental to the interests of SROs in the sphere of financial markets - and consequently, to their members' interest - has to do with imposing constraints on the supervisory functions exercised by SROs. At present, the constitutional (or charter) documents of some self-regulatory organizations contain provisions concerning supervision over the operation of their members¹⁰.

The RF Central Bank has specified that SROs may supervise the activity of their members only on condition that the corresponding powers have been delegated to them by the Bank of Russia (Article 7). In this connection, the procedure for the delegation of such powers, as well as the procedure and grounds for the termination of such powers are to be established by the RF Central Bank individually for each type of self-regulatory organizations (all organizations of the same type may only be granted an identical set of powers). The delegation to SROs of supervisory powers does not entail the loss of such powers on the part of the Bank of Russia.

Besides, the following functions are also performed by a self-regulatory organization in an event of being endowed with the relevant special powers by the Bank of Russia: receipt of reporting documents from members of SRO; attestation of their heads, their members and their personnel; participation as observers, via representatives, in the audits of their members conducted by the RF Central Bank and government bodies.

Thus, the RF Central Bank is building a new system for regulating the operation of SROs on financial markets, with the regulator's active participation. It is noteworthy that the extent of that participation is to be determined by the regulator itself - a circumstance that may have a negative effect on the realization of the interests of self-regulatory organizations and their members, because no guarantees are envisaged in the draft federal law that the Bank of Russia will actually grant SROs full access to the procedure of development and implementation of their professional standards and rules, or to supervision over their enforcement.

In contrast to the currently applied model of self-regulation in the sphere of financial markets, which is based on the principle of a voluntary association, the draft federal law proposed by the

¹⁰ See Subitem 'e' of Item 2.1 of the Charter of the Russian National Association of Securities Market Participants (NAUFOR); paragraph 4 of Item 2.2 of the Charter of the Professional Association of Registrars, Transfer Agents and Depositories (PARTAD).

RF Central Bank establishes that membership in a SRO should be mandatory (Article 9). At the same time, licensing is not abolished, although it actually makes sense only if membership in a self-regulatory organization is voluntary.

According to the draft federal law submitted by the Bank of Russia, the following types of self-regulatory organizations may be created in the sphere of financial markets (Article 3): (1) self-regulatory broker organizations; (2) dealers; (3) managers; (4) depositories; (5) registrars; (6) joint-stock investment funds and asset managers of investment funds, mutual funds and non-governmental pension funds; (7) specialized depositories; (8) non-governmental pension funds; (9) insurance companies, insurance brokers, mutual insurance companies; (10) micro-financial organizations; (11) credit consumer co-ops; (12) housing saving co-ops; (13) credit history bureaus; (14) actuaries; (15) rating agencies; (16) agricultural credit consumer co-ops.

At present, membership in a self-regulatory organization is mandatory only for agricultural credit consumer co-ops¹¹ and credit co-ops, with the exception of second-tier credit co-ops¹².

The introduction of the principle of mandatory membership can be motivated by the interests of holders of securities and other clients of financial organizations, because it helps in establishing additional control over the activity of SROs. However, the mandatory double control (licensing and self-regulation) coupled with broader powers granted to the government regulator is by no means a guarantee of the best possible protection of clients' interests.

It seems that what clients are concerned with is by no means limited to the protection of their interests: their main priority, in fact, is to secure their profits. The presence in the market of several SROs based on the principle of voluntary membership makes them compete between themselves, improve their performance standards and rules for attracting clients, while their clients have opportunities for making a choice between several financial organizations – members of one or other self-regulatory organization.

The draft federal law put forth by the RF Central Bank also establishes that a SRO of a certain type must have, among its members, no less than 30% of financial organizations operating in a given field. Associated members¹³ cannot be included in the total number of members sufficient for the creation of a self-regulatory organization.

According to the new draft federal law, any financial organization may be a member of only one SRO of a certain type. If a financial organization operates in several different fields, it may become a member of several self-regulatory organizations at once, or of one self-regulatory organization uniting several types of SROs. In the latter case, a self-regulatory organization may be created on condition that the number of its members operating in each given field amounts to no less than 30% of the total number of financial organizations it unites. Consequently, it may unite no more than three SROs of each type.

At present, under the general rule, in order to gain the status of a self-regulatory organization, a not-for-profit organization must unite no less than 100 professional entities (or no less than 25 subjects of entrepreneurial activity) of a certain type, in not otherwise specified by the existing federal laws¹⁴. The prevailing legislation whereby the activity of those SROs on financial markets is regulated, which are not subject to the 2007 general law on self-regulatory organizations (SROs of funds and the organizations which, by agreements with funds, keep their pension saving accounts; asset managers; housing saving co-ops), sets no floor for the number of their members. One exception is the SROs of professional securities market participants (no less than 10 members). So, no restrictions are imposed on the number of self-regulatory organizations.

¹¹ Item 3 of 7 Article 31 of Federal Law of 8 December 1995, No 193-FZ 'On Agricultural Cooperation' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 11 December 1995, No 50, Article 4870.

¹² Item 3 of Article 35 of Federal Law of 18 July 2009, No 190-FZ 'On Credit Cooperation' // *Sobranie zakonodatel'stva RF* [Collection of Laws of the Russian Federation], 20 July 2009, No 29, Article 3627.

¹³ For more details on associated membership, see Article 10 of the draft federal law prepared by the Bank of Russia.

¹⁴ Subitem 1 of Item 3, Article 3 of Federal Law of 1 December 2007, No 315-FZ 'On Self-regulatory Organizations'.

Besides, the Bank of Russia intends to establish the procedure for ensuring that heads of SROs comply with the requirements to their professional qualifications. The Bank of Russia is also going to reserve the right to approve or reject the proposed candidacy of a SRO's head (Article 26).

At present, the head of a self-regulatory organization is appointed to that post or dismissed from it by decision of that organization's responsible body.

One more important provision stipulated in the draft federal law is that the heads of SROs (or other persons representing their interests) and the boards of SROs represented by their chairpersons, which may be elected by the self-regulatory organizations from among their heads, may represent the interests of these SRO at the Bank of Russia, but only with the right of an advisory vote.

However, the rights and responsibilities of the said representatives at the Bank of Russia, including their right to act on the issues relating to the core activity of each self-regulatory organization, are to be determined by the Bank of Russia (Article 32).

One of the main functions of a SRO is to represent the interests of its members in their relations with federal bodies of state authority, bodies of state authority of RF subjects, and bodies of local self-government. The participation of the government regulator in appointing the representatives of organizations subordinated to them - in this case heads of self-regulatory organizations - may be contrary to the interests of those organizations.

By way of summing up, it can be said that, in this phase of development, the replacement of one regulator by another has had no influence on the procedures applied in regulating the activity of SROs on financial markets. Market participants still retain a considerable degree of independence in regulating their own activity. Nevertheless, if the provisions stipulated in the draft federal law "On Self-regulatory Organizations in the Sphere of Financial Markets" put forth by the Bank of Russia are adopted and implemented in actual practice, the influence exerted by the government regulator will become stronger, and the burden imposed on financial market participants (financial organizations) - heavier. Moreover, there is a possibility that the very idea of a SRO may vanish as a result of such alterations, although the formal status of these organizations will be preserved.