

Principles of Financial Regulation Reform

The Principles of Financial Regulation Reform seek to restore confidence in the capital market system by addressing:

Transparency

The provision of greater transparency and visibility to investors, regulators and other market participants is of paramount importance. Market structures must insure the appropriate disclosure of all financial security trading activity (listed and over-the-counter), participant accounting (on and off balance sheet), credit rating agency activity and counterparty exposure. Disclosure of this information must protect proprietary property while enabling sufficient access for the various participants (regulators, intermediaries, investors and capital raising enterprises) to adequately understand and assess the risks attached to their activities.

Independence

There is a need to reassert the independent mission of the regulating agencies to protect the investor and stability of the system. Realignment and restructuring the existing regulatory agencies to eliminate forum shopping is desirable. The application of similar rules to institutions performing similar marketplace functions and provision for the necessary flexibility for regulators to respond swiftly to new product innovations and evolving market practices are critical. NRSRO (Nationally Recognized Statistical Rating Organization) regulatory reform requiring greater transparency and independence is needed.

Re-establishment of the SEC's (Securities and Exchange Commission) role as a voice and protector of investors is overdue and critical. The agency requires adequate tools, staffing and financial resources to carry out its mission of investor protection. Regulatory changes need to recognize that investor protections must be tailored to the type of investor and type of investment product, rather than a "one-size-fits-all" approach. For example, enhanced protections for institutional investors may take the form of tools (e.g., enhanced disclosures by issuers) that such sophisticated investors may use to protect themselves, in contrast to "bright line" regulatory requirements to protect retail customers of standardized investment products.

Corporate Governance

Recognition of the role institutional investors perform in the capital markets, and their attendant responsibilities and obligations, is vital. While institutional investors support greater shareholder rights they also recognize the responsibility which comes with such rights and their need to stay vigilant in the capital markets. Providing a forum for institutional investors to communicate with policy makers on developments in the markets enables institutional investors to assist financial market regulators by serving as an "early warning" system on market developments that raise systemic risk and overall market stability, prudential or investor protection concerns.

Investment Opportunities

The ability to invest, consistent with fiduciary responsibilities, in an unconstrained investment opportunity set is critical to enable public pension funds to meet their obligations. Any limitations on the universe of available investments will potentially reduce the ability of these funds to generate the needed returns and may increase the risk of the plan.

Systemic Risk

For this purpose, systemic risk is defined as the potential of widespread financial losses or market disruption caused by:

- The failure of an institution with a likely consequence of further defaults and organizational failure.
- A market with one-sided (purchase or sale) participation that causes destabilizing short-term price shifts with the potential to cause significant organizational or institutional failures.

Mitigation of systemic risk in the financial markets appears best facilitated by an independent entity with funding autonomy, enforceable data collection powers, the capability to analyze the collected data to identify pending risks, and the duty to disclose the metrics indicative of the perceived risks. Information accessible to this entity must include any type of transactional, financial instrument, asset and liability data associated with any market participant. Proprietary information collected in this activity needs to be kept confidential while aggregated metrics must be publicly disclosed.

Utilization of this information to mitigate the perceived systemic risks could be coordinated through the established financial regulatory channels to avoid jurisdictional confusion. Global coordination of this activity is extremely desirable to maximize the efficacy of the effort.

In summary, we believe addressing these reform areas will significantly contribute to the restoration of confidence in the capital market system
(adopted May 1, 2009)

The following funds have also endorsed the principles:

California Public Employees' Retirement System
California State Teachers' Retirement System
Connecticut State Treasurer
Colorado Public Employees' Retirement Association
Maryland State Treasurer
New York Common Retirement Fund
Ohio Public Employees Retirement System
State Retirement System of Illinois
State of Wisconsin Investment Board