



*Melbourne APEC Finance Centre*  
*Ceremonial Launch*

Keynote Address by Prof Allan Fels AO

10 April 2007

I'd like to congratulate Monash on its formal establishment of the new Melbourne APEC Finance Centre and on its having received support from the Victorian Government. This award reflects Monash University's long term commitment to being a highly internationally oriented university as well as its work and strength over many years in relation to financial and economic studies.

I'd also like to congratulate the Victorian Government on its far sightedness and vision in supporting the Centre financially and in other ways. Victoria is very strong in the area of financial services with a number of major financial institutions having their head offices in Melbourne. And Victoria has other strengths including academic strengths in the field of studying financial markets and this has been recognised by the government.

I'd also like to congratulate APEC for recognising the need for national centres of this kind to improve understanding and better governance by APEC countries.

The Centre already has a strong reputation as a trainer of officials in life insurance, pensions and banking, regulation in the Asia Pacific region and this will now be strengthened.

I have been asked to say a few words on governance and regulation.

Questions of governance have been at the core of many of the biggest challenges facing countries in the Asia Pacific region. As the Prime Minister of Thailand at the time, Mr Anand Panyarachun said in 1998, "At the core of our dark experience lies the ugly truth that there is an absence of transparency, accountability, public interest, and public responsibility". At that time of the financial crisis in East, and South East Asia, the need for greater transparency and accountability in the regulation of the financial sector had been one of the underlying problems surrounding the currency, instability, corrupt bankruptcy and falling stock markets of the time. More generally in South Asia, issues about the management of financial services and indeed the whole of government bring basic questions to the fore concerning the relationship of government, the private sector and the community. Similarly economies in transition in central and South East Asia are also facing questions about grappling with and defining the role of the State. In the South Pacific issues of governance are also central to the future.

It can be said that on the one hand the circumstances in each country concerning governance are different. They all have different histories and different populations. Compare the population of China with 1.2 billion people with the population of Nauru with the population of 10,000. However, there are some common principles of governance that seem universally applicable. In particular, there are four key elements that always come to the fore in questions of governance. They are:

- Accountability. Public officials must be answerable for government behaviour, and responsive to the entity from which their authority is derived.
- Participation. Participation refers to the involvement of citizens in the development process. Beneficiaries and groups affected by the project need to participate so that the governments can make informed choices with respect to their needs, and social groups can protect their rights. This is not the same as saying they must do what particular groups want. The general public interest must come first.

- Predictability. A country's legal environment must be conducive to development. A Government must be able to regulate itself by laws, regulations and policies, which encompass well defined rights and duties, mechanisms for their enforcement and impartial settlement of disputes. Predictability is about the fair and consistent application of these laws and implementation of government policies.
- Transparency. Transparency refers to the availability of information to the general public and clarity about government rules, regulations and decisions. It can be strengthened through the citizens' right to information with a degree of legal enforceability. Transparency in government decision making and public policy implementation reduces uncertainty and can help inhibit corruption among public officials.

I would now like to comment on regulation. Every regulator faces four questions.

First, what should be done, what ought to be done.

Second, what may be done, what is allowed to be done by the law.

Third, what can be done, what is actually possible in practice.

Fourth, what cooperation is needed from other parties, including those being regulated, to achieve the goals of the regulator.

These four questions arise in regard to financial regulation as much as in any other field. The first question then is what ought to be done. What would add value to the community, to the public? What would constitute some value added to the public as a result of regulation? Obviously a regulator must achieve some results of benefit to the community. In the case of financial regulation it is to have a financial system which is efficient, stable and enables the market to operate in the most efficient and productive way possible. In regard to Asia, there is an interesting situation. On the one hand, most of the APEC nations are growing very fast. This is generally good in the context of the development of a good financial system. On the other hand, financial systems and financial regulation may not be as sophisticated and developed as in more advanced countries. So there is a big opportunity but there is also a big risk.

But in talking about the contribution to public value I don't want to just talk about the results that regulators achieve. The value they add to the community is also judged by another criterion – how well they use their power. Regulators have conferred on them a substantial amount of state power, the coercive power of the state to regulate, to direct the movement of resources, to prohibit or require their use in certain respects. Accordingly, an important test of how good a regulator is involves not just the results but also the correctness, the justness and fairness of the processes and so on. And a regulator has to avoid either extreme of overusing the power conferred upon a regulator or less often said failing to use the power. Most often we hear about the overuse of power but quite often it is the failure to use power at all conferred by legislation which is the bigger problem in regulation. So to sum up on public value, it is partly the results and it is partly the processes and the proper use of government power that count.

The second question is – what may regulators do? A regulator's role is set by the political or, as I prefer to call it, the authorising environment. It is from the authorising environment that laws, regulations, values, budgets and so on are set that determine what the regulator may do, what the regulator is permitted to do. So in analysing how good the system of regulation is one needs to look at the political climate. Often it is in this field that the biggest challenges arise. There is a lack of real political support in developing countries for regulation. This is because of the dominance of the influence of vested interest groups especially big business. I believe this is one of the most serious problems of regulation in Asian countries. Asking this question gives a lot of insight into regulation in Asia.

Third, there is the question of what can do done, what is possible in practice? What is possible in practice depends upon the resources, the skills and capabilities, and the legal powers of the regulator. Once again, in developing countries there are often weaknesses in these areas which limit the scope for effective regulation.

So to understand regulation and to improve it, it is not just a question of teaching and understanding what ought to be done. It's a question of what may be done and what can be done.

The final question is what cooperation is needed to get results? The fact is that regulators can't get results without the active cooperation of those being regulated. Again, there is a very difficult question in striking the right balance. The regulator cannot simply rely upon voluntary cooperation. On the other hand, simply to use legal powers to prosecute and fine also rarely works alone, does not get results. To get cooperation much more is required, essentially the support of those being regulated. The ideal seems to be to carry a big stick, to use it occasionally but generally to rely on voluntary cooperation by people who know that if they don't cooperate they could face sanctions.

In these few words I have tried to set out a framework of the key questions which arise in regulation. I believe this applies to the financial sector. I believe that in teaching regulation there is often a very heavy emphasis on what should be done on, on what would be ideal. I believe, however, that teaching also needs to look at the political problems stemming from the authorising environment and the capability questions and finally on the cooperation issues. In the way a comprehensive approach will be taken to the analysis of regulation. And if that is done in the MAFC courses I believe the approach will be of great value to those being taught.

I wish Monash and the new Melbourne APEC Finance Centre all success in its ventures.

Thank you.

Allan Fels, Melbourne April 2007