Enforcing International Financial Standards in Brazil:  
Limits and Possibilities for Adoption of IOSCO Principles

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Abstract: Foreign capital and institutional investors play a key role in the Brazilian capital and financial markets. Internationally promoted regulatory patterns, especially IOSCO principles, have been increasingly influencing administrative rule making by the Brazilian Securities and Exchange Commission (CVM) as well as the adoption of transnational rules in Brazil by means of self-regulatory activity. Even though there is a certain level of convergence of market regulatory standards at the transnational level, implementation and enforcement of rules remains essentially domestic. We analyze two case studies regarding the transposition of international standards into the Brazilian legal system, which illustrate this tension between the transnational and domestic dimensions of financial markets regulation. The first case concerns a CVM rule on disclosure of executive compensation and its interpretation by local courts. The second case refers to the adoption of suitability rules.

Keywords: Financial markets, capital markets, transnational regulation, Brazil, IOSCO principles.

Contents

1 Introduction ______________________________________________________________ 4
  1.1 Background___________________________________________________________ 4
  1.2 Scope and limitations ___________________________________________________ 6
  1.3 Research questions _____________________________________________________ 7
2 International Policy Formation _______________________________________________ 8
  2.1 International Financial Architecture: a brief outlook___________________________ 9
  2.2 Regulatory fragmentation _______________________________________________ 10
  2.3 IOSCO _____________________________________________________________ 12
3. Brazil in the International Financial Architecture _______________________________ 16
  3.1 Brazil and IOSCO ______________________________________________________ 17
  3.2. Brazil and other international and regional organizations and fora___________ 17
4 Brazilian Case Studies

4.1 Background note on the recent development of the Brazilian capital market

4.2 Case Study I: Executive compensation transparency

4.2.1 How is executive compensation regulated by IOSCO?

4.2.2 Matching domestic expectations: first steps for the Brazilian regulation

4.2.3 Constitutionality test: How did the Brazilian Judiciary Power participate in the implementation of the new regulation?

4.3 Case Study II: Suitability requirements

4.3.1 The suitability principle in the international regulation

4.3.2 Suitability regulation in Brazil

5 Case Analysis

5.1 How transnational principles enter into national systems

5.2 The content of domestic rules inspired by international principles

5.3 Domestic enforcement of such rules and how it impacts the implementation of the new rules

6 Concluding remarks

References
1 Introduction

1.1 Background

The Brazilian stock market has grown steadily since 2004. Figures representing the public offerings volume indicate that Brazilian companies have been raising funds via issuance of shares in the equity market. In 2004, the raised volume amounted to BRL 8.8 billion (approximately EUR 3.5 billion). In 2007, public offerings peaked reaching an amount of BRL 70.1 billion (EUR 27.8 billion). In the next year, despite the global financial crisis, the total public offerings volume was equivalent to BRL 34.3 billion (approximately EUR 13.6 billion) and, in 2009, this amount increased further to BRL 46 billion (approximately EUR 18.2 billion).

In terms of capital raised via share issuance, BM&FBovespa ranks as the biggest securities exchange in Latin America, third among emerging markets and fifth worldwide. In the secondary market, the daily trading value amounted to BRL 1.6 billion (approximately EUR 0.6 billion) in 2005 and, four years later, to BRL 5.3 billion (approximately EUR 2.1 billion), peaking at BRL 5.5 billion (approximately EUR 2.2 billion) in 2008. Nowadays, in terms of the average daily trading value, BM&FBovespa ranks seventeenth among securities exchange in the world market, fifth among emerging countries and first in Latin America.

Foreign investors have played a crucial role in the expansion of the Brazilian stock market, especially, in public offerings. In 2009, 66.7% of the participating investors were foreigners; in 2008, 65.6%; in 2007, 72.3%; in 2006, 72.8%; in 2005, 61.7%; and in 2004, 69.2%. With respect to the trading value, foreign investors’ share corresponds to roughly

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35% since 2005. During this same time period, domestic institutional investors participated in approximately 26% to 30% of the trading value. In a nutshell, in the Brazilian secondary market, foreign investors and institutional investors amount to over 60% of the daily trading volume.

Moving away from the stock market towards the Brazilian regulatory framework, it is also possible to realize remarkable changes since 2000. Such changes did not arise out of ordinary State legislative activity, but rather stemmed from BM&FBovespa’s (at that time, simply Bovespa) private regulations creating different levels of corporate governance by the end of 2000, which were strongly inspired in international good practice standards and policy discussions. This was followed by amendments to the Brazilian Stock Corporations Act (Law No. 6,404/1976), which strengthened minority shareholders’ economic and political rights, as well as to the Brazilian Exchange Act (Law No. 6,385/1976), which extended the regulatory competence of the Brazilian Securities and Exchange Commission (CVM) and provided CVM with greater autonomy. Still on the federal legislative level, an important reform took place in 2007 with the adoption of IFRS for preparing financial statements. On the administrative level, CVM issued relevant ordinances, mostly inspired by international regulatory patterns. Furthermore, in the meantime, Bovespa was demutualized and internationally accepted self-regulating models were implemented.
1.2 Scope and limitations

The introductory note above suggests that some interest does exist in Brazil towards the adoption of regulatory patterns which are internationally promoted, especially, in view of the importance of foreign capital and institutional investors for the proper functioning of the Brazilian domestic market. In this paper, we intend to describe how transnational regulation is adopted in Brazil, as well as to give some thought on the hurdles involved in this implementation process.

In order to pursue such goal, we have made two choices. The first one refers to the international institution we selected to verify the transposition of rules. The second choice concerns the adopted methodology with the aim of drawing some conclusions.

Our object of study comprises the principles issued by the International Organization of Securities Commissions (IOSCO). This choice is justified, on the one side, by the influence which such organization exercises in the regulatory activity of CVM; and, on the other side, by the recent increasing participation of Brazil in IOSCO. An inherent limitation associated with the choice to study specifically IOSCO stems from the plurality of sectoral standard setters often addressing complex and interrelated financial market matters.

As such, it is important to bear in mind that possible interferences among such international regulators are not to be ignored but rather acknowledged. In other words, IOSCO is not to be perceived in vacuo, but rather as part of a network formed by national regulators, other standard setting bodies and international organizations, whose members participate in more than one (if not in all) of such structures. Although, one could expect that the power exercised by dominant states in one or more international financial regulation fora could play a role in shaping the international agenda, we will not carry out a political analysis of IOSCO in this sense13.

13 Also, any relations between the interstate, domestic and transnational political arenas could help explaining how consensus is achieved and why certain values and objectives become priorities for international financial reforms. These considerations matter, however, an essentially political analysis of the financial regulatory

No. 471/2008, which has simplified securities issuance with “restricted efforts”; CVM Ordinance No. 457/2007, which adopted the international accounting standards set by IASB (International Accounting Standards Board); CVM Ordinance No. 481/2009, which regulates the request to have voting rights in shareholders’ general meetings exercised by an appointed attorney-in-fact, considering that there are (not many, but still some) Brazilian companies which ownership is not concentrated; CVM Ordinance No. 361/2002, which has regulated the several types of public offerings; and CVM Ordinance No. 461/2007 and 468/2008, which have set rules for the organization of stock exchanges so as to enable demutualization, as well as reviewed regulatory competence issues related to the stock exchange and its relationship with CVM.
Turning to our second choice, we have opted for the case study methodology as the only feasible way of demonstrating how transnational principles are adopted in the Brazilian legal system and how Brazilian players and institutions (both public and private) cause the application of rules, which are strongly inspired by international standards, to be reinforced, mitigated or even avoided. Case studies should not vouch for making general, universal conclusions. However, a detailed factual analysis of specific cases allows us to better understand the underlying dynamic in the adoption of international standards including the constraints and possibilities for the enforcement of such rules, as well as to possibly conclude that the resulting rule may turn out to be different in terms of its content as compared to the initially intended rule.

To be precise, we focus our analysis on the IOSCO principles in view of two Brazilian case studies relating respectively to disclosure of officers’ compensation and to suitability. International policy formation in the field of financial regulation depends to a large extent on consensus among national regulators and self-regulatory organizations. Although there has been increasingly more cooperation among such regulators and organizations and a certain level of convergence of market regulatory standards at the transnational level, implementation and enforcement of rules remains essentially domestic. Our two Brazilian case studies illustrate this tension between the transnational and domestic dimensions of regulation of financial markets, which in turn are global by their very nature.

1.3 Research questions

The main research question, as the paper title reveals, refers to an implementation test: is the enforcement of transnational regulation by domestic legal systems possible? In case the answer to such question is positive, a further question arises: are there any local particularities which affect the final result of the process for adoption of transnational principles? In order to start answering such question, our analysis is twofold:

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sphere, as mentioned above, is out of the scope of the paper. The bottom line is to emphasize that any “coincidences” in international financial regulation arise for a reason and that a regulatory trend is to be perceived as a product of discussions and work in different organizations and at different levels in such a way that the importance of any of these organizations would better be assessed in relation to a fragmented, weak institutional background (as detailed in Section 2 below) and never separately or isolated from this context.
(i) How does Brazil participate in regional and international financial organizations and fora (especially, in IOSCO)?

(ii) How does transnational regulation enter into the Brazilian domestic legal system? Which domestic players and institutions contribute for the implementation of transnational regulation? Is the final result (i.e. implemented rule) substantially equivalent to the original international rule?

In order to pave the way to such analysis, we first turn to the international dimension and introduce relevant background considerations about international policy formation in the context of financial regulatory fragmentation, so as to better understand the role played by IOSCO (Section 2). Afterwards, we turn to Brazil and how this country participates in IOSCO. We also briefly refer to other international and regional organizations dealing with financial regulation in which Brazil or any of its domestic regulators and/or associations are members (Section 3). Finally, Section 4 presents the two Brazilian case studies illustrating how international financial standards might face the so-called “constitutionality test” before been enforced and how rule making at the domestic level inspired by transnational regulation may arise out of self-regulatory activity and not directly out of traditional administrative legislative competence.

### 2 International Policy Formation

In this section, we introduce an overview of the international financial architecture in order to properly identify IOSCO as one of the standard setting bodies taking part in a dense, complex network of transnational regulators and informal fora related to international financial regulation, which comprises key subject matters that in practice are hard to isolate from one another, such as securities, banking, insurance and accounting. In order to accomplish this purpose we outline a brief historical analysis addressing how the international financial regulatory system developed into a fragmented institutional structure.

After getting a grasp of the international institutional context, we attempt to investigate the insertion of IOSCO in the international financial regulatory reality, as well as to understand the role it plays. In order to analyze the issues covered by IOSCO standards we refer to its most relevant bodies of output, i.e. IOSCO Objectives and Principles of Securities
Regulation (IOSCO Principles), Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation (Methodology) and IOSCO Multilateral Memorandum of Understanding (MMoU).

2.1 International Financial Architecture: a brief outlook

The first relevant insight about the international financial architecture which should be taken into consideration is that the system has developed a clear mismatch: while international financial regulation bears a relatively fragmented, weak institutional structure, finance itself is globally integrated. Not only that, but in contrast to the so-called Bretton Woods system and its single framework of the GATT/WTO, the international financial system is composed by a plurality of mostly informal (non-state based) regulatory mechanisms and regulators. At the same time, the international financial system is one of the most densely regulated areas of international economic law.

Historically, international financial regulatory cooperation first took place in the 1970s with the creation of a committee of national banking supervisors which came to be known as the Basel Committee on Banking Supervision (BCBS). As a second step, regulatory coordination was extended to securities markets and related sectors by the creation of IOSCO in the 1980s and to insurance markets via the International Association of Insurance Supervisors (IAIS) established in 1994. Also during the 1990s the Committee on Payment and Settlement Systems (CPSS) was created in order to produce core principles for systematically important payments systems and, jointly with IOSCO, for securities settlements systems and central counterparties.

After the international financial crisis of the late 1990s, international financial regulation was further expanded to corporate governance (OECD’s “Principles of Corporate Governance” drafted in 1999), as well as to accounting and auditing standards with the creation of two private sector bodies: the International Accounting Standards Board (IASB)

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and the International Auditing and Assurance Standards Board (IAASB) during the early 2000s.

The next relevant step – and a quite intuitive one – refers to the first efforts to address the fragmentation resulting from such “patchwork of sectoral regulatory bodies”\(^\text{16}\). In this sense, the BCBS, IAIS and IOSCO created the “Joint Forum” in 1996 in order to discuss overlapping issues across the banking, insurance and securities markets. Finally, three years afterwards, the Financial Stability Forum (FSF) was set up bringing together the standard setting bodies (BCBS, IAIS, IOSCO, IASB and CPSS), the international economic organizations (the International Monetary Fund (IMF), the World Bank, OECD, the Bank for International Settlements (BIS), the European Central Bank (ECB) and the Committee on the Global Financial System), as well as national financial authorities.

2.2 Regulatory fragmentation

Despite the efforts mentioned above towards mitigating regulatory overlapping by bringing together financial regulators, international economic organizations and standard setting bodies, fragmentation remained a fundamental deficiency in the international financial regulatory system. Not only that, but it also is important to highlight another prominent feature of the international financial regulatory regime, i.e. the inherent limitation of its institutions to be confined to facilitating informal cooperation, information-sharing and consensus formation, but lacking any supranational powers to legally bind countries at the national level. This core critic applies to the whole international financial regulatory system and by default also to IOSCO.

In relation to the regulatory fragmentation problem, it is interesting to note the direct relation which has been established between the FSB and the aim of a greater accountability framework. The Financial Stability Board Charta (FSB Charta) provides for the reinforcement of the original mandate underpinning the creation of the FSF, i.e. addressing the inherent weaknesses of a fragmented institutional network of international regulators.

Indeed, since 2009 the FSB has undertaken the obligation to coordinate the several regulators. Actually, issues such as the necessity to intensify information exchange, to address

\(^{16}\) HELLEINER; PAGLIARI, op. cit., note 13 supra, p. 5.
gaps of the existing international standards and to endeavor greater efforts to enforce these standards have been highlighted since the late 1990s\textsuperscript{17}. In addition, already the FSF was awarded by the G7 the tasks of identifying weaknesses and detecting possible systemic risks in a timely fashion in 1999\textsuperscript{18}.

To be more precise, Article 5(2) of the FSB Charta\textsuperscript{19} determines that “standard setting bodies will report to the FSB on their work without prejudice to their existing reporting arrangements or their independence. This process should not undermine the independence of the standard setting process but strengthen support for strong standard setting by providing a broader accountability framework”. In this sense, it could be said that the FSB occupies an enhanced position among the transnational networks dealing with international financial regulation. Nowadays, the FSB is considered by many scholars as the nucleus of the new international financial organization or as “one of the central pillars of global financial governance”\textsuperscript{20}.

This is, once again, essential for the perception that IOSCO’s role in international financial regulation depends upon a dynamic interrelation with other institutions forming the regulatory network. In this sense, it is possible to assert that IOSCO is not to be regarded as the epicenter of global financial regulation – nor does it hold any \textit{de facto} monopoly over international securities markets regulation. In order to illustrate this argument, it is enough to mention, for instance, that the IMF has been since the 1970s active in the control of financial markets\textsuperscript{21}, even though its stated main goals as set out in Article I of the Articles of Agreement of the IMF comprise solely (i) promoting international monetary cooperation, facilitating the expansion and balanced growth of international trade, (ii) promoting exchange stability, (iii) assisting in the establishment of a multilateral system of payments, and (iv) making resources available (with adequate safeguards) to members experiencing balance of payments difficulties.

\textsuperscript{17} See the report “Cooperation and Coordination in the Area of Financial Market Supervision and Surveillance” by Hans Tietmeyer, President of the German Federal Bank (\textit{Deutsche Bundesbank}) at the time, February 11, 1999.
\textsuperscript{18} RUDDIGKEIT, op. cit., note 12 supra, p. 8.
\textsuperscript{19} The FSB Charta is available at <http://www.financialstabilityboard.org/publications/r_090925d.pdf>.
\textsuperscript{20} HELLEINER; PAGLIARI, op. cit., note 13 supra, p. 8.
\textsuperscript{21} RUDDIGKEIT, op. cit., note 12 supra, p. 11.
2.3 IOSCO

IOSCO was set up in its present form in 1986, when the first agencies to join the organization decided to create a General Secretariat for IOSCO. Historically, IOSCO has its roots in the Inter-American Association of Securities, which was created in 1974 and transformed into a global cooperative body by decision of eleven securities regulatory agencies from North and South America during a meeting in Ecuador in April 198322. As IOSCO is not formed by a treaty or interstate agreement, it is not considered a true international organization by most scholars23.

Since its early years, IOSCO has displayed a broad country membership with securities regulators from Europe and Asia joining the organization already by the mid 1980s. Such fact evidences that securities law enforcement has by then emerged as an international regulatory issue basically due to financial markets integration, as well as to the expansion of cross-border trading along with the escalating innovation of financial products, which in its turn reinforces the consolidation of such increasingly integrated market. At the same time, cyclic financial crises have repeatedly evidenced the growing need for an international consistent answer to overspilling negative consequences and to the resulting global contagion of financial markets24.

Traditionally, it is pointed out that by the very nature of the relevant issues related to securities regulation and their less obvious distributional effects central bankers and financial regulators enjoy a considerable degree of autonomy from domestic legislative assemblies. As a result, the range of actors involved in discussions about financial regulation is much less representative than in other economic areas as trade politics for instance. This argument can be easily extended to the international arena if we consider that IOSCO member regulators have been more accountable to self-regulatory organizations (SROs) and private market participants than to traditional government oversight mechanisms, which yields to a poorly

22 Available at: <http://www.iosco.org/about/index.cfm?section=background>.  
defined sense of public interest. Indeed, IOSCO may be considered as a case of power diffusion in favor of private actors, as there is little independence from the private interests it supervises and works with.

In this vein, it is significant to note that IOSCO works in close consultation with private international regulatory bodies as the World Federation of Exchanges (WFE) and the International Capital Markets Association, which is a self-regulating association of dealers on primary and secondary international capital markets. In addition, it is possible to infer from the last annual reports published by IOSCO that its officials find it important to incorporate industry inputs into the standard setting process so as to focus on policy matters of relevance to practitioners and industry bodies. This strongly suggests the hermetic *modus operandi* of international securities regulation and harmonization as it has been exercised by IOSCO. Nevertheless, it is important to mention, as noted by Helleiner and Pagliari that the large-scale use of taxpayers’ money to rescue financial institutions during the last financial crisis has greatly politicized financial regulation causing legislative bodies to get more involved in the subject matter as popular pressure for stronger regulation unleashes.

Another important consideration refers to the fact that IOSCO, by definition, seeks to regulate most prominently the activities of international financial conglomerates, which businesses comprise both banking and securities divisions. Even where an argument can be made that sophisticated financial institutions adopt Chinese wall mechanisms and prevent conflicts of interests while having its different departments assisting clients, the bottom line is that IOSCO’s standards do not cover all the activities performed by such institutions. As a result, once more, the problem of regulatory fragmentation and inherent gaps, on the one hand, and overlapping rules, on the other hand, are to be taken into account while assessing IOSCO’s object of regulation.

Considering that a full analytical assessment of what is meant by international securities regulation in the framework of IOSCO is hardly feasible, we intend to now explore the three main IOSCO’s bodies of output. Firstly, we refer to the IOSCO Principles, which

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26 The annual reports referring to 2004-2010 are available at <http://www.iosco.org/library/index.cfm?section=annualReports>.

27 HELLEINER; PAGLIARI, op. cit., note 13 supra, p. 18.

were adopted by the organization in 1998 and have been updated in 2003 and 2008 and aim at providing jurisdictions with guidance to improve the quality of their securities regulation.

The IOSCO Principles are one of the 12 key standards or codes recognized by the FSB as core to sound global financial regulation along with the Code of Good Practices on Transparency in Monetary and Financial Policies (IMF); the Code of Good Practices on Fiscal Transparency (IMF); the Special Data Dissemination Standard and the General Data Dissemination System (IMF); the Insolvency and Creditor Rights (World Bank); the Principles of Corporate Governance (OECD); the International Financial Reporting Standards (IFRS) and the International Standards in Auditing (ISA); the Core Principles for Effective Deposit Insurance Systems (BCBS/ International Association of Deposit Insurers, IADI); the Principles for Financial Markets Infrastructures (CPSS/IOSCO); the FATF Recommendations on Combating Money Laundering and the Financing of Terrorism & Proliferation (Financial Actions Task Force, FATF); the Core Principles for Effective Banking Supervision (BCBS); and the Insurance Core Principles (IAIS).

At the burst of the recent financial crisis, IOSCO’s Executive Committee requested its Implementation Task Force (ITF) to revise and update the IOSCO Principles to take into account the lessons learned from the meltdown. In June 2010 this resulted in the addition of the following eight new principles addressing matters such as systemic risk, credit rating agencies, hedge funds and auditor oversight:

i. “Principle 6: The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate”

ii. “Principle 7: The Regulator should have or contribute to a process to review the perimeter of regulation regularly”

iii. “Principle 8: The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed”

iv. “Principle 19: Auditors should be subject to adequate levels of oversight”

v. “Principle 20: Auditors should be independent of the issuing entity that they audit”

vi. “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”

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29 Available at: <http://www.iosco.org/about/index.cfm?section=background>.
30 Available at: <http://www.financialstabilityboard.org/cos/key_standards.htm>.
vii. “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”

viii. “Principle 28: Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight”

The second body of output to be commented is the Methodology31, which is used by national jurisdictions for self-assessment purposes and by the international financial institutions in their financial sector assessment programs (FASPs), a joint initiative of the World Bank and the IMF. Within this context, the overall objectives of applying the Methodology are32:

i. assist authorities in the country in comparing their securities regulatory system with an internationally accepted benchmark, the IOSCO Principles;

ii. provide the authorities, as well as the IMF and the World Bank, with input into the overall assessment of the risks and vulnerabilities of a country’s financial system; and

iii. help the authorities, as well as the IMF and the World Bank, to identify the reforms needed to enhance the functioning and soundness of securities markets, especially with respect to the regulation of securities markets, and to make informed policy decisions about the reforms needed.

The revised version of the Methodology has been approved for consultation with the IOSCO membership by the Executive Committee of IOSCO on April 19, 2011.

Thirdly, we refer to the MMoU, which was adopted in May 2002 following decades of increasing bilateral cooperation between IOSCO members. The MMoU is considered the international benchmark for enforcement cooperation and exchange of information among regulators. To pursue full implementation of the IOSCO MMoU, IOSCO has resolved to ask all ordinary members and associate members, with primary responsibility for securities regulation in their jurisdictions, to apply to become full signatories to the IOSCO MMoU by January 1st, 2013.

An important insight with regards to the description above refers to the limits of the relevant body of outputs. The IOSCO Principles are pitched at a very general level, which evidences that IOSCO efforts have been characterized by a certain avoidance of potentially

controversial substantive standards\textsuperscript{33}. In fact, this stems from the already mentioned principle of consensus, which is common to transnational networks as IOSCO. However, to the extent that reversing financial globalization is not possible, that a global government is hardly desired and that the establishment of a single global financial regulator is not enforceable in the medium term, transnational and transgovernmental networks are considered indispensable.

Based or not in the fact that coordination (once achieved) is self-sustaining, the bottom line is that there are no dispute resolution nor enforcement mechanisms for the compliance with IOSCO’s standards. As a result, some scholars consider that such system does not attempt to substantially harmonize securities laws and further that such persisting discrepancies cause foreign judgments not to be recognized and enforced whenever they go beyond a “comfort zone”, which could be defined as areas in which domestic preferences are somehow aligned\textsuperscript{34}.

3. Brazil in the International Financial Architecture

In this section, we analyze Brazil’s participation in international and regional organizations and fora with the mere intent to illustrate two main perceptions: on the one hand, that Brazil broadly takes part in the international financial regulatory structures both at the transnational and at the regional level, and on the other hand, that Brazil now plays an increasingly prominent role as a big emerging economy which passed the financial health and soundness test after the last financial crisis.

Instead of trying to gauge the extent to which Brazil actually shapes the international financial regulatory agenda or defines the content of international standards and principles, which would presuppose a deep assessment of Brazil’s most direct interests in the context of financial regulation, we will simply refer to the main organizations in which the country or any of its domestic regulators and/or associations are members.

\textsuperscript{33} VERDIER, op. cit., note 22 supra, p. 150.

\textsuperscript{34} VERDIER, op. cit., note 22 supra, p. 147.
3.1 Brazil and IOSCO

CVM participates as a founding member of IOSCO, as well as through the chairmanship of the Inter-American Committee and of the Working Group responsible for enhancing the regulation of investment funds. CVM is an ordinary member of IOSCO and is also active within IOSCO’s Emerging Markets Committee and Executive Committee. Since April 2011 the president of CVM, Ms. Maria Helena Santana, chairs IOSCO’s Executive Committee. CVM has executed over 25 bilateral memoranda of understanding and the MMoU on October 21, 2009. Also (and only) in 2009, CVM was admitted as a member of IOSCO’s Technical Committee.

Furthermore, BM&FBovespa, BM&FBovespa Market Supervision (BM&FBovespa Supervisão de Mercado, BSM), the Brazilian Financial and Capital Markets Association (Associação Brasileira das Entidades dos Mercados Financeiro e de Capitais, ANBIMA) and CETIP (Brazilian OTC Clearing House) are members of IOSCO’s Consulting Committee gathering self-regulatory organizations (SRO Consultative Committee). To be precise, Mr. Jose Carlos Doherty – ANBIMA’s Chief Regulatory Officer – is currently Chairman of the SRO Consultative Committee.

3.2 Brazil and other international and regional organizations and fora

Firstly, it is important to note that a membership broadening trend has been taking place after the burst of the last financial crisis and in view of the perception that regulatory financial bodies were undemocratic and of reduced effectiveness since developing countries were not represented in the most relevant fora\textsuperscript{35}. Even IOSCO with its historically broad country membership was not an exception as the Technical Committee, where key regulatory initiatives stem from, had only exclusively OECD countries as members until very recently. Indeed, only by early 2009 was the membership expanded to include Brazil, India and China. Before that, Mexico was the only developing country which was a member of IOSCO’s Technical Committee. While the broadening of country membership has been mostly well

regarded by some scholars, others consider that a potential downside will be that consensus is
to become even more difficult to reach in the years to come\footnote{HELLEINER, Eric; PAGLIARI, Stefano. The End of an Era in International Financial Regulation? A Postcrisis Research Agenda. \textit{International Organization}, 65, p. 169-200, Winter 2011, p. 185.}.

Secondly, it should be emphasized that Brazil’s participation in fora of the international monetary and financial order is be understood in light of recent changes in its economy and its performance in the global financial crisis, which conferred it much more of the so-called “soft-power”, even though Brazilian participation in the world economy is still relatively small. This is evidenced by the fact that Brazil became a country member of the FSB having three representatives on board: the Ministry of Finance (\textit{Ministério da Fazenda}), Central Bank of Brazil (\textit{Banco Central do Brasil}, BACEN) and CVM.

Furthermore, we would like to highlight CVM’s participation in two prominent international organizations which scope is not restricted to securities regulation. Within the World Trade Organization (WTO) framework, the part of that agreement of foremost interest for the purposes of the present study is the General Agreement on Trade in Services (GATS) and its specific Annexes on Financial Services. CVM has been participating of the negotiating process concerning financial services since the 1997 round. Currently, CVM participates on the Brazilian Delegation on the new mandate for achieving a higher degree on the international commerce of financial services. Additionally, Brazil is an observer member of OECD, within which CVM follows the meetings of FATF.

At the regional level, we would like to mention Brazil’s participations in the following organizations: Mercosur (Common Southern Market), Council of Securities Regulators of the Americas (COSRA), and IIMV (Iberoamerican Institute of Stock Exchanges). CVM takes part in three Mercosur forums, the Services Group, the Working Group on Financial Issues (SGT-4) and the Working Group on Investments (SGT-12), which is coordinated by BACEN. Within the SGT-4, the Securities Market Commission has already prepared a document setting out minimum regulatory standards for the region, which has been later approved by the Common Market Council (CMC) as Decision No. 08/93. Such document contains minimum required regulations regarding securities issuers, investment funds, exchange and brokers, independent auditors, as well as systems for clearing, settlement and custody.

Another significant and recent development refers to CMC’s Decision No. 31/10, which refers to minimal regulation of the securities market on the preparation and disclosure
of financial statements for transactions taking place in the Mercosur region with tradable securities of companies with public offering authorized by any of Mercosur’s member countries. CMC’s Decision No. 31/10 was adopted in Brazil by means of CVM Resolution No. 659 of February 24, 2011. According to this regulation, companies with authorized public offering which would like to trade their securities in Mercosur should, as of the fiscal year beginning in 2012, submit their quarterly and annual financial statements, adopting the IFRS in force, according to the pronouncements issued by IASB.

Secondly, CVM is one of the 26 members of COSRA, which is a forum formed in 1992 for mutual cooperation and aiming at enhancing the efforts of each country in North, South, and Central America (including the Caribbean) to develop and foster the growth of sound securities markets. Thirdly, Brazil is a member of the IIMV, a non-profitable organization which was set up on May 20, 1999 and which main objectives are to promote a better knowledge of the structure and regulatory environment of the securities market of the region, to develop transparency and integrity in this market.

4 Brazilian Case Studies

The present section is dedicated to our two case studies describing the implementation of the transparency principle applied to executive compensation in the Brazilian legal system, on the one hand, and the adoption of suitability requirements as a result of self-regulatory activity, on the other hand. First of all, however, we outline some relevant considerations regarding the development of the Brazilian capital market during the past twenty years in order to provide some context to the case study analysis following the next and final section of the paper.

4.1 Background note on the recent development of the Brazilian capital market

Since the 1990s there has been a gradual opening of the Brazilian capital market to foreign investments, following the opening of the Brazilian economy after a long period of dictatorial regime. After the privatization of important state controlled companies during the
1990s and the enlargement of the domestic capital market during the second half of the 2000s, a growing number of international investors have been active in the Brazilian capital market.

As referred in Section 1 above, there is evidence of internationalization of Brazilian securities regulations. This is to be evidenced, for instance, in view of the enactment of a federal statute adopting the IFRS, as well as of administrative regulations issued by CVM on enhanced information disclosure by listed companies, on regulation of credit rating agencies and on short selling. Moreover, self-regulation mechanisms including the creation of BM&FBovespa’s Novo Mercado, which is a listing segment adopting international patterns of corporate governance, also reinforce this trend.

Considering that it would not be reasonable or feasible to try to understand the implementation of international standards in its entirety, which by nature is a complex phenomenon, we believe that carrying out specific case studies already is enough to meet the goal of pointing out relevant questions related to what we could call internationalization of the Brazilian financial regulation. The two case studies are summarized below.

4.2 Case Study I: Executive compensation transparency

4.2.1 How is executive compensation regulated by IOSCO?

The global financial crisis of 2008 has proven that executive compensation programs and their cornerstones are key issues of utmost importance for understanding the incentives behind the predatory behavior of financial institutions in the financial system. As a consequence, executive compensation has since then been often included among regulatory recommendations and guidelines issued by international organizations to their members.

The international regulation of executive compensation in terms of its adequacy and transparency or disclosure of the compensation amounts and respective criteria started in the FSB. In 2008, the then FSF recommended that “regulators and supervisors work with market participants to mitigate the risks arising from remuneration policies.” The Compensation Workstream Group was set up with a mandate to “draft sound practice principles for large financial institutions”. In 2009, the FSB published its “Principles for Sound Compensation
Practices”37, setting the aim “to ensure effective governance of compensation, alignment of compensation with prudent risk taking and effective supervisory oversight and stakeholder engagement in compensation.” However, the document emphasizes in Item I that “the benefits of sound compensation practices will be achieved only if there is determined and coordinated action by national regulators, facilitated if necessary by suitable legislative powers and supported by national governments.” Among the measures suggested to assess the relationship between compensation and risk, the document recommends that the remuneration amounts be published so that stakeholders, especially the shareholders, may be able to better supervise executive compensation (Principle 9)38.

Turning to IOSCO, disclosure to the investor of all data which might affect his or her investment decision has been recommended in the IOSCO Principles (1998 through 2010 versions). Until 2010, however, there was no document which specifically suggested a broad disclosure of the compensation schemes of listed companies’ officers. In February 2010, IOSCO published a new document entitled “Principles for Periodic Disclosure by Listed Entities”39. According to these principles, data regarding the administrators’ remuneration is included among the relevant information to be disclosed by listed companies. Such data would be relevant for the investor to perceive the existing incentives in order to achieve given goals of the issuer company (“they can assess the incentives created by this use of the issuer’s resources”), as well as to realize whether such incentives are aligned with the investor’s interests and how performance may be oriented to the returns generated for shareholders40.

To be precise, disclosure of the following information is suggested: (i) a description of the issuer’s decision-making process for its compensation policies, including the composition and mandate of any remuneration committee; (ii) the most important design characteristics of the compensation system including how those characteristics may be tied to performance and, where appropriate, risk; and (iii) quantitative information on compensation, broken down as appropriate to indicate incentives underlying the compensation, together with any necessary

38 “9. Firms must disclose clear, comprehensive and timely information about their compensation practices to facilitate constructive engagement by all stakeholders. Stakeholders need to be able to evaluate the quality of support for the firm’s strategy and risk posture. Appropriate disclosure related to risk management and other control systems will enable a firm’s counterparties to make informed decisions about their business relations with the firm. Supervisors should have access to all information they need to evaluate the conformance of practice to the Principles.”
40 Item d Compensation Disclosure of the referred document.
qualitative information. In this case, quantitative information is to be broken down on any
defined individual basis indicating fixed and variable, paid and deferred, as well as cash and
share compensation41.

4.2.2 Matching domestic expectations: first steps for the Brazilian regulation

Since 1976, the Brazilian corporate statute determines that the officers’ compensation is to
be annually approved in the general shareholders’ meeting42. The shareholders have to resolve
and fix the global or individual amounts, including any kind of benefits and allowances, taking
into account officers’ responsibilities, the time they dedicate to their tasks, their competence,
professional reputation and the amount at which their services would be valued at market prices43.
In practice, shareholders approve officers’ compensation in their global amount, i.e. the total
amount employed to pay all members of the company’s management bodies (Administrative
Council and Board of Directors). Therefore, it was neither mandatory to disclose how this global
amount was to be divided among the members of the management bodies, nor which amounts
were part of fixed compensation and which were variable.

In March 2009, CVM submitted – to public comments and suggestions – a project of
administrative regulation setting more stringent rules on information to be disclosed by listed
companies44. One of the issues covered by this regulation referred to the publication of
information on executive compensation.

The initial proposal comprised disclosure of the individual remuneration of each officer.
In the referred notice, however, CVM sustains that it would like to find out whether the market
considers such individual disclosure of information convenient and necessary45. Moreover, CVM
demonstrates it is aware of three important arguments against the proposed individual disclosure
requirement, i.e. (i) a cultural issue46, (ii) a different treatment as towards non-listed companies,
which would boil down to competition asymmetries, and (iii) a safety issue47.

41 Note 38 supra.
42 Article 132, Law No. 6,404/1976.
43 Article 152, Law No. 6,404/1976.
46 This argument refers to the fact that Brazil is culturally different compared to countries in which the individual
disclosure is mandatory. In other cultures it is more common and natural to share information regarding one’s
assets and income, and well paid individuals are considered successful and competent. In Brazil, people tend not
It is interesting to mention the results of this public consultation initiative. Only 7 interested parties were in favor of the new proposed rules and 24 were against them. Among these last 24 responses, 15 were in favor of the disclosure of remuneration paid to each management body, but not to each individual member. Not only there were not many replies in favor of the individual disclosure with identification of the respective companies’ officers, but even these few supporters, which understood that the new rules would in theory be beneficial to the Brazilian securities market, have asserted that it was still not the appropriate time for the adoption in Brazil of such transparency standards. In other words, it was generally understood that the downside of disclosing individual compensation information would not be compensated by potential benefits.

Furthermore, those who argued against the new rules stated that such disclosure obligations were in breach of fundamental rights to privacy and intimacy enshrined in Article 5 of the Brazilian Federal Constitution. Another argument was that individual disclosure of remuneration would increase the risk of crimes against officers and their families, endangering their lives and assets.

CVM, at its turn, explained the need for new rules referring expressly to regulatory patterns of other markets and indicating that, according to the best international practices, the highest level of transparency of executive compensation and incentive programs should to be aimed. For this purpose, CVM expressly referred to the document “Corporate Governance in Emerging Markets – Report from Emerging Markets Committee of IOSCO” published in December 2007. In addition, CVM quoted countries which adopt transparency rules for individual officers’ compensation – France, South Africa and the United States. Nevertheless, it recommends a gradual approach towards this matter in the Brazilian regulation.

to disclose information about their assets or income and this trend is stronger the higher one’s income is (Item 11.8).
47 The safety argument can be summarized as follows: in a country penalized with violence problems, the disclosure of individual remuneration information may be reckless and dangerous (Item 11.8).

Finally, the rule created in Brazil ended up requiring that officers’ compensation policy be disclosed, including information about the composition of the compensation, the objectives of each of its components, the reasons justifying the compensation composition as being well tuned to the evolution of the performance indexes, and whether such policy is aligned to short, medium or long run interests. Moreover, disclosure is required for compensation amounts of each management body (but without identifying the individual amounts paid to each officer), as well as for the highest, the lowest and the average of the individual compensation amounts.

CVM justified the rule above as corresponding to a suitable level of transparency which would stimulate further discussion in the market about compensation policies and, at the same time, would provide investors with the necessary information in order to enquire issuers who are not adopting sound practices51.

4.2.3 Constitutionality test: How did the Brazilian Judiciary Power participate in the implementation of the new regulation?

After CVM Ordinance No. 480/2009 entered into force on January 1st, 2010, the Brazilian Institute of Finance Executives (Instituto Brasileiro dos Executivos de Finanças, IBEF) filed a lawsuit aiming at preventing CVM to demand IBEF’s associate members to disclose their officers’ compensation amounts. IBEF pleaded that the new rule was illegal and unconstitutional as it breached the constitutional right to privacy and intimacy, further asserting that publishing such information would endanger the officers’ and their families’ safety. The Fifth District Court of Rio de Janeiro’s Federal Courts approved an injunction in order to avoid the obligation to disclose the referred information. This decision was confirmed by the appellate court, as well as by the Brazilian Superior Justice Court (Superior Tribunal de Justiça, STJ).

While defending its regulatory powers, CVM argued that Brazil must implement international transparency standards; otherwise, this would work to the country’s disadvantage in international capital markets. For the purpose of this paper, it is interesting to

highlight CVM’s argument sustained before the Brazilian courts that it had undertaken obligations vis-à-vis international organizations. In this sense, CVM explained that the disclosure clause was a binding obligation undertaken by Brazil internationally before IOSCO and as a result of G20 meetings.\footnote{Lawsuit No. 2010.5101002888-5 (5th District Federal Court of Rio de Janeiro).}

The Brazilian courts have ruled in favor of the non-disclosure – both as a final decision in the three instances and as an initial decision. Rio de Janeiro’s Federal Court decision demonstrates that domestic peculiarities and constraints have overridden the approach towards an internationalization of the Brazilian regulatory pattern. In this decision, the court specifies that publishing high compensation amounts in a country characterized by strong social inequalities and violence would be problematic. Further, it is asserted that the existence of such a disclosure rule in other countries does not lead to the incorporation of such rule automatically without previously tailoring it to the Brazilian reality.\footnote{The preliminary decision was overruled by the Federal Regional Court of the 2nd Region. For a summary of this decision, please refer to <https://ww2.stj.jus.br/revistaeletronica/Abre_Documento.asp?Link=ATC&Seq=11827523&Resp=201000498520&Data=20100930&Tipo=91&formato=PDF>.}

4.3 Case Study II: Suitability requirements

4.3.1 The suitability principle in the international regulation

In the international level, the suitability duty is not novel. In fact, the protection of the clients’ interests vis-à-vis the financial intermediaries had already been included in IOSCO’s Report on International Conduct of Business Principles dated as of July 1990.\footnote{International Conduct of Business Principles, Report of the Technical Committee of IOSCO, July 1990, available at <http://iosco.org/library/pubdocs/pdf/IOSCOPD8.pdf> (last visited: June 4, 2012).} Also since 1998 IOSCO Principles already comprised the information duty so as to “to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor’s interest in the scheme” (Principle 19), which has not been amended in the 2010 version of the document (Principle 26).\footnote{Available at: <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD82.pdf> (last visited: June 1, 2012).} Furthermore, according to 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”. After the 2008 financial meltdown, however, the duty to assess whether the product and/or service were suitable for the client has been perceived as quite elusive and would, therefore, require greater care and attention from regulators, especially in the case of complex financial products.

Even without having resulted in the issuance of international rules, we would like to mention a study about suitability prepared by the Joint Forum57 dated as of April 2008 and entitled “Customer Suitability in the Retail Sale of Financial Products and Services”. This study analyzes the regulation in 11 countries58 and in the European Union and investigates the suitability practice in 90 financial firms around the world. The main conclusion of the referred study can be summarized as follows: “while suitability and the risks posed by mis-selling are increasingly on the mind of regulations and firms, there remains wide disparity in what is required of firms and in firms’ internal policies and practice”59.

Referring to the Joint Forum’s study, as well as to the shortcomings in the suitability test revealed by the financial crisis, IOSCO’s Technical Committee published a Consultation Report about “Suitability Requirements with respect to the Distribution of Complex Financial Products”60 in February 2012. These suitability principles address the following issues: classification of customers, general duties irrespective of customers’ classification, disclosure requirements, protection of customers for non-advisory services, suitability protections for advisory services, compliance function and internal suitability policies and procedures, incentives to eliminate unsuitable complex financial products and, finally, enforcement actions.

4.3.2 Suitability regulation in Brazil

Since 1999 managers of securities portfolios and investment fund administrators have the duty to verify the suitability of financial products to the investor profile61. Additionally, security brokers have the obligation to deliver to their clients the relevant information about

57 The Joint Forum is formed by the Basel Committee on Banking Supervision, IOSCO and the International Association of Insurance Providers.
58 Australia, Canada, France, Germany, Italy, Japan, the Netherlands, Spain, Switzerland, UK and the United States.
59 Available at: <http://www.bis.org/publ/joint20.htm> (last visited: June 1, 2012).
the risks involved in the transactions\textsuperscript{62}. However, there were by then no rules regarding the proceedings necessary for compliance with such obligations, neither there were any discussions about what is nowadays referred to as “suitability test” (an express used in Brazil without a proper translation into Portuguese).

In 2006 CVM discussed with market players whether an investor should be considered as a qualified investor by the simple fact that he or her had invested at least BRL 300,000 (approximately EUR 120,000). This discussion further developed into a broader one referring to the convenience of administrative regulation imposing the duty to verify the suitability of the product for the client, in addition to the already existing rules which were pitched at a very general level. In the following year of 2007, CVM published a document about the suitability test for public comments. This document referred to how the matter is regulated in the United States, in the European Union and in the UK; however, no normative ordinance was issued as a result of this initiative.

In 2009 the matter was once again raised in policy discussions in Brazil; however, CVM decided to leave suitability out of its ordinance on rules and proceedings for securities transactions in regulated markets and recommended that the issue should be addressed in a future and specific regulation\textsuperscript{63}.

In June 2009, the Brazilian Regulatory and Supervision Committee of the Financial Markets, Capital Markets, Insurance, Pension Plans and Capitalization (Comitê de Regulação e Fiscalização dos Mercados Financeiros, de Capitais, de Seguros, de Previdência e Capitalização — COREMEC\textsuperscript{64}) issued Resolution No. 7\textsuperscript{65}, which intended to guide market

\textsuperscript{62} Article 3, VI, CVM Ordinance No. 387/2003.

\textsuperscript{63} CVM Public Hearing Notice No. 04/2009 followed by CVM Ordinance No. 505/2011 and 506/2011. CVM decided to leave suitability regulation for a separate and new public hearing. Any comments regarding suitability which have been received as a result of the referred public hearing notice were to be analyzed in the future by CVM in another specific study about suitability rules (CVM Public Hearing Notice No. 04/2009, item 3.67, pages 65 and following, available at <www.cvm.gov.br>).

\textsuperscript{64} COREMEC was set up in 2006 as a mechanism for integration of the different regulators, as well as for facilitating sharing relevant information. In this respect commentators compare COREMEC to international fora as IOSCO and FSB. See YAZBEK, Otávio. “A crise financeira e risco sistêmico: a evolução recente da regulação sistêmica no Brasil” [“Financial crisis and systemic risk: recent evolution of systemic regulation in Brazil”]. In: PADUA LIMA, Maria Lucia L. M. Agenda Contemporânea. Direito e Economia. 30 Anos de Brasil. São Paulo: Saraiva, 2012. p. 112-113.

\textsuperscript{65} Available at: <http://www.mpas.gov.br/arquivos/office/3_090630-161947-899.pdf> (last visited: June 1, 2012). Article 2 of this rule suggests that the following should be regulated: (i) assessment of the profile of clients or beneficiaries, including their financial situation, knowledge or experience with the products and services offered or recommended by the supervised institutions, as well as the purpose of the purchase or contract; (ii) assessment of the suitability of the products or services offered or recommended to the profile of the clients and the beneficiaries and their purposes; (iii) updating the information received from clients and
regulatory institutions for setting rules on the duty to assess the suitability of products or services offered or recommended to the needs, interests and objectives pursued by clients.

However, it was only in December 2010 that a suitability regulation was issued in Brazil. The initiative was taken by ANBIMA in its self-regulatory activity. ANBIMA members comprise commercial and multiservice banks, investment banks, fund managers, securities brokers and distributors, as well as private assets managers.

ANBIMA’s Code on Regulation and Best Practices for Private Banking Activities establishes obligations for ANBIMA members to adopt formal proceedings in order to verify the suitability of the investment recommendations in view of the investor’s profile, as well as to adopt proceedings for collecting relevant information regarding the investor’s financial situation, knowledge and objectives.

Furthermore, also in December 2010, ANBIMA’s Committee for Regulation and Open Market Best Practices issued Resolution No. 10, which requires that the negotiation of derivatives over the counter must involve a proceeding for verifying its suitability vis-à-vis the client’s profile before entering into any agreement or contract.

By the end of 2011, CVM published the Public Hearing SDM Notice No. 15/2011 bringing the duty to verify the suitability of products and services to the client’s profile back to its regulatory agenda. This document was – as expressly stated – first and foremost inspired in the European Union Directive 2004/39/EC. CVM also refers to the discussions about the matter in the international arena, mentioning a report published by the BIS and the IOSCO study for the regulation of complex financial products suitability (both referred to above).

Moreover, in January 2012, ANBIMA issues a further regulation on suitability, disciplining the duty to verify the suitability of recommended investments in its Code on Regulation and Best Practices for Investment Funds.

beneficiaries periodically in a suitable fashion in view of the nature of the products and services purchased or contracted; (iv) identifying mismatches between the clients’ or beneficiaries’ profile and the products or services acquired or contracted; and (v) actions to be taken whenever there are mismatches between the clients’ or beneficiaries’ profile and the products or services.

69 Available at: <http://portal.anbima.com.br/fundos-de-investimento/regulacao/codigo-de-fundos-de-investimento/Pages/default.aspx> (last visited: May 28, 2012).
5 Case Analysis

Despite the importance of international fora for transnational rule making, the emergence of applicable regulation and the possibilities for its implementation take place on the domestic level. Both case studies provide us with some tools to consider how the transnational and the national levels interact and what the tension between these two dimensions is. In other words, the discussion above allows us to think about the limits and possibilities in the implementation of transnational principles in domestic markets. The matters to be taken into consideration in order to draw these concluding remarks are threefold:

1. How transnational principles enter into national systems;
2. The content of domestic rules inspired by international principles; and
3. Domestic enforcement of such rules and how it impacts the implementation of the new rules.

5.1 How transnational principles enter into national systems

First of all, we would like to refer to the nature of the domestic players involved in the implementation of transnational principles in the Brazilian legal system. In the executive compensation case, we have verified that it was CVM – in the exercise of its rule making competence – that issued a regulation adopting international standards and even justified the creation of new domestic rules making express reference to international policy fora. This case study illustrates the most common phenomenon, at least in Brazil, which is the issuance of securities regulations by the regulatory agency which has been granted specific normative powers to do so by law. Administrative rule making by CVM certainly facilitates a swift approval of new rules as compared to traditional law making, since political hurdles – as for instance, exposure to conflicting political interests and need to be on the top of the Senate’s political agenda – are avoided.

A different situation was described in the second case study. Initially, CVM took the lead and openly discussed the suitability duty with market players and domestic organizations; however, subsequently, it was ANBIMA in its self-regulatory activity who requested its members to adopt suitability rules. Such private regulation came before any administrative rules were issued by CVM and actually currently corresponds to the most detailed regulation of suitability in Brazil. Recently CVM started considering the adoption of
suitability rules and, should new rules come into force, we will have a hybrid system in Brazil with both private and public regulations. Therefore, we realize that international principles might enter the Brazilian legal system both by means of private or public regulatory activity.

Moreover, the two case studies have demonstrated that both organizations responsible for the transposition of rules – CVM and ANBIMA – actively participate in IOSCO, which international principles have inspired the creation of domestic rules in Brazil. However, we acknowledge this conclusion is not to be generalized, as we could have chosen two other case studies which refer to the implementation of transnational principles in Brazil without the involvement of domestic players or organizations which are take part in international financial fora. The first case regards the adoption of IFRS by Brazilian federal legislation. CVM strongly supported the approval of this new statute aiming at the enhancement of accounting standards to the adopted by Brazilian companies; however, in this case, the transposition of international principles took place upon issuance of a federal legislation and not administrative regulations by CVM. The second case refers to the voluntary adoption of auditing committees by Brazilian listed companies. Except for financial institutions, Brazilian listed companies are not required to implement such internal governance structure. In other words, the adoption of this international corporate governance standard in Brazil is essentially voluntary and conducted individually by each listed company which is interested in implementing more stringent corporate governance rules70.

Nevertheless, as a rule of thumb, it is possible to say that international financial standards enter the Brazilian legal system upon regulatory and self-regulatory activity of CVM, ANBIMA and BM&FBovespa71, all of which are members of IOSCO. To put it shortly, the Brazilian Securities and Exchange Commission is the main responsible organization for the domestic adoption of transnational regulation – though it is not exclusively the only one. Self-regulatory organizations and private players, as well as the Brazilian legislator, also play a role.

*What are the possibility and the limit?* The possibility lays in the transposition of transnational financial principles upon administrative rule making by CVM (whenever within

71 Since BM&FBovespa was not referred to in the two specific case studies under analysis, we could mention, as an example of its private regulatory activity, the creation of “Novo Mercado”; which is a market segment with enhanced corporate governance requirements.
its regulatory competence), as well as upon self-regulatory activity. The limit is to be found in Brazilian domestic mandatory rules. In case of conflict with existing Brazilian laws or even with the Brazilian federal constitution, the adoption of these principles would only be possible if new rules were to be issued following the traditional rule making procedure, which at its turn implies considerable political and time costs.

5.2 The content of domestic rules inspired by international principles

When it comes to assessing the substantive content of domestic rules adopted in view of international principles and the harmonization of financial regulations across the world, the highly controversial one-size-fits-all idea emerges. The case studies above demonstrated that the international standard was adapted to local specificities upon transposition into the Brazilian legal system.

In the procedure of adoption of the new rules and public hearing, CVM acknowledged market restraints and interests and ended up limiting the extent of the transparency rule for disclosure of executive compensation in Brazil. In this case, we realized that the information to be disclosed was limited to the highest, lowest and average amount paid to officers, which compared to the international standard represents a rather lax rule.

In the suitability case study, we verified that currently there is only one IOSCO open principle. On February 21, 2012, IOSCO published the consultation report “Suitability Requirements with respect to the Distribution of Complex Financial Products” setting out nine principles relating to customer protections, including suitability and disclosure obligations, which relate to the distribution by intermediaries of complex financial products to retail and non-retail customers. In any case, with reference to the already existing IOSCO principle, it should be noted that the choice in terms of which mechanism is to be adopted for the implementation of this international standard in the domestic level is left to be made locally. However, CVM expressly refers to the European rule as the main source of inspiration for the proposed regulation submitted to public hearing, even though it also specifically mentions IOSCO principles as well. This case demonstrates that general

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72 The closing date for responses was May 21, 2012.
principles issued by IOSCO may strongly inspire domestic regulations; however, the source
to concretely think about the rule to be adopted is to be found in different legal systems.

*What are the possibility and the limit?* The limit refers to the need to adapt the general
rule to local particularities (which will become clearer when we discuss enforcement below).
The possibility, conversely, lays in the adoption of open international principles allowing
tailored domestic rules to be created accordingly.

### 5.3 Domestic enforcement of such rules and how it impacts the implementation of the
new rules

Are international standards of good corporate governance suitable for the development
of the Brazilian capital market? In the executive compensation case study we verified the
participation of Brazilian courts, which are not part of the Brazilian securities market but are
responsible for the enforcement of securities and corporate regulations in Brazil. Before this
case, all discussions regarding good corporate governance practices were restricted to
organizations strongly related to the functioning of the market – CVM, BM&FBovespa,
entrepreneurs’ and academic *fora*. Furthermore, most governance rules are voluntary arising
out of BM&FBovespa’s private regulations and being spontaneously adopted by listed
companies. An exception was CVM Ordinance No. 480/2009, which introduced disclosure
obligations inspired in transparency of certain information regarding officers’ compensation
following international recommendations.

The case study demonstrates that the participation of another local institution in the
enforcement of domestic rules implementing international principles may result in a different
construction of the applicability of the rule in the domestic level and may further imply the
consideration of different interests, which are also worth to be protected. The international
rule comprised disclosure of information concerning the company, as well as of personal data
of its officers. On the one hand, investors have a legitimate interest of receiving relevant
information about the compensation policy of the invested companies. On the other hand,
officers also have a legitimate interest of keeping their financial data undisclosed.

This conflict of interests was well illustrated in the arguments raised respectively by CVM
and IBEF in the course of the judicial proceedings in Brazil. CVM, among other reasons, argues
that the new rule is accepted internationally as a paramount for good corporate governance and is
related to the development of the Brazilian securities market. IBEF, at its turn, defended the need to keep compensation information confidential due to Brazilian cultural specificities. Both arguments are legitimate and fragile. The case study reveals an attempt of dialogue between international principles and local values. Domestic enforcement of such rules and how it impacts the implementation of the new rules. Moreover, the executive compensation case was the first case study, which has allowed us to consider the restraints and the consequent tailoring of international rules being imported to the Brazilian legal system.

The most important take away is that it is not possible to fully foresee what the outcome will be while implementing imported standards. The issuance of domestic rules inspired by transnational principles is only the first step, as the new rules will necessarily be tested by local institutions responsible for the supervision and enforcement in the domestic level. In fact, it is often to be expected that the final domestic rule will differ from the international rule exclusively inspired in foreign markets – and this phenomenon is to be verified not only in Brazil but in various jurisdictions across the globe. We refer, for instance, to the following cases described by Pistor and Milhaupt in their seminal work *Law & Capitalism*73: Mannesmann in Germany, Livedoor in Japan, SK Corporation in South Korea, China Aviation Oil in China and in Singapore and Yukos in Russia. All of these cases demonstrate that international corporate governance standards are to be adapted to each jurisdiction when questioned by local institutions.

### 6 Concluding remarks

In view of the case studies and discussion above, we now shall address the research questions proposed in Section 1. According to the Brazilian experience, we can say that the enforcement of transnational regulation by domestic legal systems is indeed possible. Furthermore, considering the growing integration of financial markets and the interest in attracting foreign capital flows to domestic markets, it is possible to assert that implementing transnational regulations is not only possible, but also completely aligned to local interests in participating in international organizations and enhancing Brazil’s “soft power” in such fora.

The transposition of transnational regulations into the local system can not, however, take place without certain restrictions. The main restriction lays in the fact that the transnational rule has to “fit” in an existing domestic legal system, i.e. it may not violate constitutional principles and mandatory laws which are already in force. In case of any such a conflict of rules, the restriction may only be overcome if the deep, necessary changes are undertaken in the existing legal system and if the political challenges associated with the legislative procedure are tacked. This is probably the reason why securities and exchange regulatory agencies and self-regulatory entities are the main responsible agents for the transposition of transnational regulations. In any case, there is always the risk that potential conflicts between the new imported rule and the existing local rules are discussed by and before local institutions, as for instance, the local courts.

At the same time, another perceived restriction refers to the local market interests affected by the adoption of new rules inspired by transnational regulation. The more the relevant domestic interests are fine-tuned in line with the good functioning of the market, the easiest should the implementation of transnational models be. This is to be perceived especially in the cases where self-regulatory entities anticipate state regulation and set forth stricter requirements to its members than the obligations provided by the existing laws.

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