

WHY THE IRAQ SECURITIES COMMISSION IS ORGANIZED AS AN INDEPENDENT REGULATORY COMMISSION

The interim Iraq Securities Commission (ISC) was created by CPA Order No. 74 as an independent regulatory commission. The draft Law Regarding Securities (draft law) would create a permanent ISC to replace the interim ISC. The permanent ISC also would be organized as an independent regulatory commission. Set forth below is an explanation of the principal reasons that the independent regulatory commission model is proposed for regulation of Iraq's securities market and how the model is implemented in the draft law.

1. The independent regulatory commission model is the prevailing regulatory model in most countries of the world. Many countries have separate governmental regulatory bodies responsible for banking, securities, insurance and pension regulation. Many others use a consolidated financial regulator, which in some countries consolidates all banking and non-bank financial regulation. In others, the consolidated regulator is responsible only for all non-bank financial regulation. While the specific means of organizing the regulator and establishing its accountability and oversight varies among countries, the prevailing practice is to establish the financial regulator as an independent body separate from other governmental ministries. In this respect, the degree of independence has similarities to the independence given to countries' central banks responsible for monetary policy.

2. The independent regulatory commission model is supported by international best practice recommendations for securities regulation. The International Organization of Securities Commissions (IOSCO) is the professional membership body of the world's securities regulators. More than 100 countries' regulators are IOSCO members. In 1998, IOSCO issued its "Objectives and Principles of Securities Regulation (IOSCO Principles), consisting of three Objectives and 30 Principles. Principles 2 and 3 regarding the regulator provide:

- 2 The regulator should be operationally independent and accountable in the exercise of its functions and powers.**
- 3 The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.**

The following excerpts from Sections 6.2, 6.3 and 6.4 of the IOSCO Principles explain what is envisioned by Principles 2 and 3.

6.2 Clear Responsibility

The capacity of the regulator to act responsibly, fairly and effectively will be assisted by:

- a clear definition of responsibilities, preferably set out by law;
- strong cooperation among responsible authorities, through appropriate channels;

- adequate legal protection for regulators and their staff acting in the bona fide discharge of their functions and powers.

6.3 Independence and Accountability

The regulator should be operationally independent from external political or commercial interference in the exercise of its functions and powers and accountable in the use of its powers and resources.

Independence will be enhanced by a stable source of funding for the regulator.

In some jurisdictions, particular matters of regulatory policy require consultation with, or even approval by, a government, minister or other authority. The circumstances in which such consultation or approval is required or permitted should be clear and the process sufficiently transparent or subject to review to safeguard its integrity. Generally, it is not appropriate for these circumstances to include decision making on day-to-day technical matters.

Accountability implies:

- a regulator that operates independently of sectoral interests;
- a system of public accountability of the regulator;
- a system permitting judicial review of decisions of the regulator.

Where accountability is through the government or some other external agency, the confidential and commercially sensitive nature of much of the information in the possession of the regulator must be respected. Safeguards must be in place to protect such information from inappropriate use or disclosure.

6.4 Adequate Powers and Proper Resources

The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.

What this means in practical terms is the subject of elaboration in this document. It includes powers of licensing, supervision, inspection, investigation and enforcement, all of which are discussed in later sections.

It necessarily requires adequate funding for the regulator in order to enable the regulator to exercise its tasks. The level of resourcing should recognize the difficulty of retaining experienced staff who have skills that are valuable to the private sector.”

The draft law, including its provisions regarding establishment, organization and accountability of the permanent ISC, has been prepared to comply with the IOSCO Principles.

3. The independent regulatory commission model permits the organization of a securities regulator with the requisite knowledge, expertise and authority to regulate a highly technical and sophisticated facet of the Iraqi economy. Securities markets are highly complex and rapidly changing. While it is possible for the Iraqi Parliament to provide in the draft law for the basic legal authority that is necessary for the ISC to regulate the securities market, it is impossible to provide or anticipate in the law the specific types of regulations that will be necessary as the market grows and evolves. Accordingly, it is essential that the ISC have and be able to exercise the expertise necessary to adopt regulations necessary to implement to the law on a timely basis. Article 15 of the draft law provides this rulemaking authority.

4. The independent regulatory commission model in the draft law is intended to ensure that the ISC will possess the necessary authority and organization to regulate the securities market expeditiously and effectively without undue political or industry influence while still being accountable to the Government. Under Article 6 of the draft law, the permanent ISC is established as an independent commission with the exclusive responsibility and authority to administer the law. The ISC is given a legal personality with administrative autonomy, including the authority to perform all legal acts necessary to achieve the general objectives stated in Article 2 of the law. The ISC's authority includes the right to sue and be sued, and to be represented in legal proceedings. However, the ISC may not engage in any commercial activity, lend any funds, or own or issue any securities. Article 6.D of the law provides that the ISC shall report to the Prime Minister. Article 6.G provides that the ISC shall enjoy the exemptions and facilities accorded to ministries, government departments and official public institutions.

5. The independent regulatory commission model in the draft law is designed to ensure the independence of the ISC by providing for the appointment for fixed terms of five ISC commissioners who may not hold other governmental or conflicting industry positions, and who have protections against removal from office other than for cause. One of the primary differences between commissioners and ministers who head governmental ministries is that the commissioners are not subject to removal prior to the expiration of their terms in the event of a change in control of the Government.

Article 9.A of the draft law provides that the ISC is to be comprised of five commissioners. The commissioners, including a Chairman and a Deputy Chairman, shall be appointed by the Prime Minister for five-year terms renewable once. The Chairman and Deputy Chairman shall be full-time government positions, and the Chairman shall have a grade of Minister and the Deputy with the grade of Deputy Minister. The other three commissioners shall be designated by the Prime Minister as full-time positions or part-time positions and shall be remunerated based on the percentage of their time dedicated to the ISC, as determined by the Chairman, at a grade commensurate with Deputy Ministers. Each commissioner must be an Iraqi citizen and have relevant experience for the position. No Person may be employed by or hold any other position with the Government of Iraq while serving as a commissioner. Article 12.D provides that

a full-time commissioner shall not have any other employment. A part-time commissioner shall not have any other employment that would conflict with his or her responsibilities to the ISC.

Article 9.B is intended to ensure continuity in the governance of the ISC. It provides that a commissioner shall hold office until a successor is appointed or the commissioner resigns. The terms of office of the commissioners first taking office after the enactment of the law shall expire as designated by the Prime Minister at the time of their appointment, with one expiring at the end of one year, one expiring at the end of two years, one expiring at the end of three years, one expiring at the end of four years, and one expiring at the end of five years. Finally, Article 9.C provides that the Prime Minister may remove a commissioner prior to the expiration of his or her term only criminal misconduct; conviction of a violation of this or another law, other than minor infractions; substantial violations of ethics provisions; repeated and inexcusable absence from duty; or if physically unable to perform the duties of a commissioner.

6. Articles 13 and 14 of the draft law is intended to ensure that the ISC has adequate financial resources to ensure its independence, while at the same time ensuring the ISC's financial accountability. Article 13.B provides that the ISC shall present to the Prime Minister within the first three months of each fiscal year, an annual report summarizing the ISC's activities during the preceding year, accompanied by the balance sheet and revenues and expenditures account of the ISC, certified by the Bureau of Supreme Audit. Article 13.C indicates that the budget of the ISC shall be determined annually as part of the overall budget process of the Government of Iraq. The ISC shall submit a budget to the Ministry of Finance. The ISC shall be credited with and entitled to retain and use the financial resources derived from its activities to fund the operations of the ISC. These resources include any fees that the ISC adopts pursuant to the standards set forth in Article 14 of the law, and any forms of assistance, grants or donations from persons who are not subject to regulation by the ISC and which are approved by the Council of Ministers. Article 14 indicates the types of fees that may be levied by the ISC pursuant to rules which must be approved by the Council of Ministers. Finally, Article 13.D indicates that any fees received by the ISC in excess of its annual budget shall be paid to the general treasury of the Government of Iraq. However, the ISC may make an application to the Council of Ministers, supported by appropriate documentation, to retain all or a portion of such excess monies for ISC expenditures that are consistent with the objectives of this law and for the further development of the ISC and that are not provided for in the ISC's annual budget.

7. If Iraq does not create a strong independent securities regulator, its securities market could suffer adverse consequences. Iraq is an emerging capital market that will only grow by attracting new investment capital, both from inside and outside the country. The absence of a strong independent governmental securities regulator will result in less capital investment in Iraq, because of an increase in investment risk, due to the greater risk premium associated with the lack of objective securities regulation which is necessary to give investors confidence in the fairness and integrity of the market.