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Financial Market Regulation in Sweden: Finansinspektionen – a Toothless Paper Tiger?

Matthias Kranke

Abstract

As early as in 1991, the Swedish Financial Supervisory Authority (*Finansinspektionen*, FI) was established as an integrated financial supervisor. Although the establishment of FI preceded that of the British *Financial Services Authority* (FSA) by about half a decade, the latter has figured much more prominently in academic debates. This paper is therefore intended to shed light on the Swedish case of financial supervision, that is, on how the integration of 1991 can be explained and how FI is organized. Most attention is directed to the crucial question as to whether or not criticisms of weak or even toothless supervision by FI are justified. Applying rational choice theory to the issue shows that, in terms of institutional design, FI very much relies on a complier-centered strategy, which provides the agency with sufficient means to enhance compliance among market participants and, thus, to ensure qualitatively good supervision. Thus, the author concludes that FI is enabled to supervise the Swedish financial market much better as well as on a much stronger basis than general criticisms suggest.

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Table of Contents

| | |
|---|-----------|
| 1. Introduction | 3 |
| 2. Institutional Design under Rational Choice | 5 |
| 2.1 Basic Assumptions of Rational Choice Theory | 5 |
| 2.2 Designing Institutions Rationally | 6 |
| 3. Finansinspektionen – an Overview | 8 |
| 3.1 Why Create an Integrated Financial Supervisor? | 8 |
| 3.2 Organizational Structure, Duties, and Responsibilities..... | 10 |
| 4. Finansinspektionen – Rather Rational than Weak? | 12 |
| 4.1 Accusations of Weakness | 12 |
| 4.2 Threads of Rationality | 13 |
| 5. Conclusion..... | 17 |
| References | 19 |

1. Introduction

Political scientists have over time become more and more aware of the political implications deriving from specific modes of regulating markets. If we start from the basic definition of regulation as “an activity in which the discretion of individuals or institutions is restricted by the imposition of rules” (Moran 1986: 185), we ascribe importance to political decisions in the form of legislation for the development of markets of any kind. It is therefore reasonable to regard political authority and private pursuits in markets as related to each other in a reciprocal relationship, which makes markets as integral to governance as states (Underhill 2003: 761–766). As a result, “[...] the market is also closely tied to the issue of political legitimacy, particularly in a democratic context” (ibid.: 779).

The above-mentioned aspects do also apply for financial markets in particular because of their utmost significance in various political fields (see Gottwald 2003). Strongly affecting the overall macroeconomic performance and “outcomes” concerning, for example, the distribution of wealth, capital/financial markets may well be referred to as “the ‘central nervous system’ of modern political economies” (Heilmann 2003: 1). The financial market can in turn be conceived as one of the most crucial fields of regulation through political authority. Analyzing financial market regulation therefore yields considerable insights into how markets are politically organized and enriches our understanding of their evolution, structure, and mode of action, thereby providing a key to a better comprehension of a political-economic issue which figures so prominently in academic debates.

A wide range of theories of regulation, comprising teleological, instrumental, cultural, and administrative ones, has been provided to explain regulatory changes in the area of financial markets (see Moran 1986). Political institutions have traditionally been paid much attention to. Since they exert strong influence on, or define, the regulatory framework, their existence indeed merits special investigation. Not only can they bring “veto player” potential to bear (see Tsebelis 2000, 2002), but also change the institutional setting by abandoning, refurbishing, or creating institutions with specified tasks. Institutionalist literature in general, ranging from historical to sociological to economical to finally political institutionalism, has sought to illuminate the evolution of diverse forms of institutions (see Goodin 1996).

There are some more and some less prominent examples of institutions established for the purpose of financial supervision. Among the best-known financial supervisory authorities is probably the *U.S. Securities and Exchange Commission* (SEC): it was founded already in 1934 and is assigned to oversee the securities industry in the tripartite sectoral supervisory framework (separate authorities for the oversight in all three financial sectors, i.e., banking, insurance, and securities) in the US. The British *Financial Services Authority* (FSA), not set up until 1997, is often cited as the prime exponent of integrated supervisory bodies. The German *Bundesanstalt für Finanzdienstleistungsaufsicht* (Federal Financial Supervisory Authority, BaFin), founded in 2002, falls into the same category. So does the Swedish equivalent, the Swedish Financial Supervisory Authority (*Finansinspektionen*, FI), which was established in 1991. At least the SEC and the FSA have attracted some academic attention outside these countries – to a high degree attributable to New York’s and London’s outstanding status as global financial centers – whereas the role of FI has scarcely been reviewed in the non-Swedish literature in a comprehensive manner despite the fact that FI preceded the so well-known FSA and might thus have served as an inspiring example of integrated financial supervision. In support of this observation, Taylor and Fleming (1999: 2) note that, even after the Scandinavian countries Norway (in 1986), Denmark (in 1988), and eventually Sweden had all taken the final steps towards integrated financial supervision as part of a longer evolutionary process, public debate still remained rather limited in academic circles (yet existent in the press) compared to the UK, where the creation of the FSA later in that decade led to quite an intensive debate.

This paper is meant to narrow that gap by examining FI’s institutional design in a single-case study. In doing so, I make use of both English and Swedish literature, including a few essays published in journals, working papers, articles in daily newspapers or magazines, and publications by official institutions like FI itself. Without immersing myself all too deeply in the great many regulatory details, I wish to direct the reader’s attention to the fundamental pattern of design. I contend that rational choice theory has a story to tell as to how the evolution of FI can be understood with emphasis on the notion of harm avoidance by private agents; more specifically, there is plentiful evidence that the institutional design implicitly encourages a complier-centered strategy. Further interest in this context relates to its institutional “strength”

or capability given that reproaches for “toothless supervision of financial enterprises” (*Affärsvärlden* 1993: 18; my translation) have come up from time to time.

This paper is organized as follows. Expounding the tenets of a rational choice perspective, Section 2 provides the theoretical foundation for the analysis of institutional design. Section 3 presents the ideas behind FI’s creation, its legal competences, and its organizational structure in brief. These aspects are put together in Section 4, where FI’s institutional design is surveyed and – hopefully – also explained sufficiently from that specific theoretical viewpoint. Section 5 summarizes the main findings of the preceding sections.

2. Institutional Design under Rational Choice

2.1 Basic Assumptions of Rational Choice Theory

The following theoretical description draws heavily upon Pettit (1996), who offers quite a sophisticated version of rational choice theory, to the extent that it borrows terms from his general approach to understanding institutional design under rational choice premises and distills the fundamental components which later on are made use of with respect to the financial supervisory institution in question.

In very general terms, rational choice perspectives are guided by the idea that people pursue actions in whatever situations – may they be market-like or not – in an economistic, that is, rational or “egocentric” manner. It is the very notion of self-interest, or self-interested desires that reifies all strands of rational choice theory. Such interests typically include first and foremost economic gains, but self-interested desires for social acceptance may as well be another sort (*ibid.*: 61, 65). Accordingly, rational choice theory may be defined as “the theory that people’s behavior can be explained as rationally determined or constrained by certain self-interested concerns: in particular, concerns with economic gain and social acceptance” (*ibid.*: 65). This kind of perspective points to the rationally induced enjoyment of both action-dependent (e.g., money, services, or public goods) and attitude-dependent goods (e.g., self-esteem or gratitude of others) (*ibid.*: 64). While most arguably bringing, at least in part, actual influence to bear on the generation of people’s behavior in market-like contexts, self-interest is likely to affect behavior in a way merely “virtual” in character (meaning that it then has no causal effect, but is a stand-by cause) as far

as non-market contexts are concerned. In such non-market contexts, non-egocentric behavior usually prevails (ibid.: 68–70).

In sum, rational choice theory states that economic or social self-interest exerts considerable influence on how people tend to behave in numerous daily-life situations.

2.2 Designing Institutions Rationally

The basic theoretical assumptions of rational choice theory have been outlined above so that we can now turn to institutional design as it presents itself if created along rational choice lines. In Pettit's (1996: 55) view, institutional design refers to "interventions in any of the arrangements that coordinate the behavior of individuals in society". With the notion of people's self-interest established, compliance with relevant, fundamental societal norms of behavior has to be seen as "not inevitably forthcoming on a spontaneous basis" (ibid.: 71). Individuals' specific interests in situations may be varied to a large extent, but, at any rate, non-compliant behavior is always within the bounds of possibility from a rational choice perspective. That is not to say that what is good for the individual necessarily has to compromise what is good for the public – as a matter of fact, Adam Smith, for instance, was convinced of their potential compatibility –, but rather that a trade-off between the promotion of self-interest and of the public good is far from impossible (ibid.: 71). Therefore, the possibility of non-compliance on the part of a larger group of individuals demands that institutions be designed in such a manner that deviants are either inhibited from pursuing their self-interests to the detriment of society or, at least, not encouraged to do so. Two general rational choice strategies are available to attain this goal: the deviant-centered and the complier-centered strategy.

The deviant-centered strategy focuses, as the name already indicates, on the deviant individual, the so-called *knave*: if self-interest leads people not to comply with norms but to deviate from them instead, institutional interventions are to ensure that potential or actual deviants are kept on or brought back onto the "right" track. For this purpose, the expected self-interest benefit for complying must be raised to a level which suffices to outperform the expected self-interest benefit for deviating. Taking into account "the perfectly self-interested individual" (ibid.: 72), the deviant-centered strategy suggests extreme measures, that is, harsh or draconian penalties and high rewards, so as to make compliance, not deviation, become the knave's interest. Con-

sequently, it entails a motivation “overload” for most of the individuals, namely those inclined to comply due to a more non-egocentric mode of deliberation, which is characteristic of the “homo sociologicus”. To name but a few of the problems that such an approach encounters: the deviant-centered strategy of institutional design gives rise to the old-age challenge of “Quis custodiet custodes?” (“Who will guard against the guardians?”); it also ignores that people in many areas do comply absent extreme sanctions in a non-egocentric fashion and that, the presence of extreme measures notwithstanding, compliance merely occurs on a conditional as distinct from a categorical basis; and it might thus cause many to switch from a pattern of non-egocentric to one of egocentric deliberation, thereby facilitating, among other adverse effects, an increase in the habit of checking on the probability of detection (the lower the likelihood, the more likely deviation) (ibid.: 72–78).

By contrast, “[t]he complier-centered strategy is driven by the need to deal with a more ordinary sort of individual: someone who deliberates in most contexts in a nonegocentric way [...]” (ibid.: 78), whereby a different institutional framework is furthered. The actual concern being the best way possible of building on these positive dispositions in the first place and the coping with the knave in the second place only, the complier-centered strategy embraces three vital principles, all of which are needed for the strategy to function as desired; that is, it has to enhance compliant behavior among the “ordinary” while also dealing with the knave effectively (ibid.: 78–79).

The first principle emphasizes “screening before sanctioning” and alludes to screening devices employed to operate on agents (to find the “appropriate”, e.g., in recruitment processes) as well as options (i.e., by regulating access to resources of whatever kind). In other words, it is about screening in and screening out alike (ibid.: 79–81). However, apart from screens, it is necessary to still rely on sanctioning devices as long as individuals are believed to be guided by self-interest. Screens are thus required to be complemented by sanctions to which can be resorted if non-compliance prevails. The second principle introduces low-level sanctions which are supportive of such a type of deliberation in order to retain and reinforce compliant behavior – unlike the deviant-centered strategy with its drastic penalties and high rewards, it tries to avoid disrupting the desired non-egocentric deliberation (ibid.: 81–85). The third and last principle offers the strongest weapon at the institutional dis-

posal. Besides the aforementioned deliberately supportive sanctions, it is essential that also some with motivational effects be put in place. “The idea is that sanctions, in particular penalties, can be devised in an *escalating* hierarchy” (ibid.: 86; my emphasis). With a view to containing the knave’s socially detrimental behavior as best as possible by means of more severe sanctions because penalties at the lowest level are incapable of keeping the knave in line, this principle is urgently needed to safeguard the complier-centered strategy. Without a credible threat of such an “ultima ratio”, the strategy as embodied in the first two principles would remain “fatally vulnerable to the damage that a knave could do” (ibid.: 86). It is not until this last grade that the focus is shifted to how to deal with the deviant individual (ibid.: 85–87).

3. Finansinspektionen – an Overview

3.1 Why Create an Integrated Financial Supervisor?

Before the creation of FI, the Swedish financial market was overseen by two complementary supervisory authorities, one for banking and securities (*Bankinspektionen*) and the other for insurance (*Försäkringsinspektionen*). Thus, prior to 1991, a system fairly akin to tripartite sectoral supervision was in place. It was then changed to a system of integrated supervision by the merger of those supervisory bodies into a single institution, FI. Several general and some specifically Swedish reasons for integration can be given.

Market developments in recent years are among the most often mentioned general rationale for the integration of sectoral supervisory agencies into a single supervisory body like FI. Briault (1999: 11; see, with the exact same words, Grünbichler and Darlap 2003: 6), like many others, regards “increasing integration both among different types of financial institutions and across borders” as constituting a major incentive to integrate financial supervision. The former aspect of integration towards financial conglomerates engaging especially in banking and insurance activities, known as “bancassurance” business, is in this context of outstanding importance (ibid.: 12–13; Taylor and Fleming 1999: 9). On any account, the result has been that “traditional distinctions which used to apply across types of firm, types of product and types of distribution channel” (Briault 1999: 12) have extremely blurred, which makes sectoral supervision less meaningful or at least more complicated.

The second crucial motivation for integrated supervision is the aspect of increasing regulatory efficiency and effectiveness, for example, by taking advantage of resulting economies of scale and scope, improved resource allocation, a higher capability of resolving conflicts, higher consistency of the rules imposed, increased accountability, simultaneous achievement of such elemental functional, somewhat overlapping objectives as prudential and conduct of business regulation, or possibly reduced risk of moral hazard (ibid.: 18–26; see also Briault 2000). The following should be noted here, however: being currently the FSA Managing Director of Retail Markets and having worked at the FSA since the day of its inception, Clive Briault can be expected to have a very strong personal interest in depicting a single financial regulator, and the FSA in particular, as an institution too important not to be built up; this does definitely not imply that his reasoning is of no account, but as there are certainly not only strengths but also weaknesses associated with integrated supervision (see Lannoo 2002: 4–5), it is nothing but helpful to know about his professional background.

As for the more specific rationale for the introduction of integrated financial supervision in the Swedish case, Briault (1999: 11; my note) as well as Grünbichler and Darlap (2003: 6; my note) literally state in unison that FI was indeed created in July 1991 in response or as a reaction to “actual and prospective market developments, including [the above-named] increasing integration both among different types of financial institutions and across borders”. Likewise, Taylor and Fleming (1999: 7) see enhanced banking-insurance linkages as having worked in that direction (see also Yamdagni 1991). This argument is also reflected in the “Government’s proposal 1990/91:177 on the integration of the banking and insurance inspectorates, and so forth” (*Regeringens proposition 1990/91:177 om sammanslagning av bankinspektionen och försäkringsinspektionen, m.m.*; Swedish Parliament (*Riksdagen*) 1990/91: 8; my translation): “one example in this ongoing transformation is the formation of so-called ‘bancassurance’ groups or financial conglomerates, which mainly entails that the traditionally clear boundaries between banking and insurance businesses are continuously dissolving.”

The country’s financial system in addition affected by a severe banking crisis at the beginning of that decade, Swedish politicians seemed quite eager to abandon the fragmented regulatory structure and hence to tackle potential future problems within the scope of integrated supervision, which they deemed more appropriate or effective

and efficient (economies of scale and scope) in the light of upcoming challenges to be met (Taylor and Fleming 1999: 7). The then-government argued as follows: “an integration of supervisory activities within a single agency would facilitate higher preparedness for new tasks and for the bundling of resources in critical situations. [...] Furthermore, integrating supervision would improve the capacity to coordinate, extend and strengthen competence in the area of information technology (IT). Through increased application of IT, supervision can be made more effective” (Swedish Parliament 1990/91: 9; my translation). Moreover, this official position considers similar organizational changes in other countries, namely the previous move towards financial integration in Norway and Denmark (ibid.: 19; Taylor and Fleming 1999: 7).

3.2 Organizational Structure, Duties, and Responsibilities

FI is an independent public regulatory agency under the general jurisdiction of the relevant government ministry which is the Ministry of Finance (*Finansdepartementet*). Entitled to set the broader parameters of financial oversight, the Ministry of Finance authorizes FI to supervise companies operating in the Swedish financial market. The funding is provided from two different sources: most of the financing is actually guaranteed through the general government budget (to achieve cost neutrality, an industry levy paid directly to the government is used to cover most of the expenses – but the government in turn allots to FI an amount of funds at least identical to the sum raised by the levy); a smaller part is paid by corporations for specific duties of FI (FI 2005: 3–5; Swedish Bankers’ Association (*Svenska Bankföreningen*) 2004: 12; Taylor and Fleming 1999: 13–15; International Monetary Fund (IMF) 2002: 12, 72; Anonymous 1997). According to an employee at FI, roughly 80 percent stem from the first source, another 20 from the second. Quite recently, the ministry has been appointed to investigate FI’s required role in the future. It did so by conducting a survey called “Inquiry into Finansinspektionen’s Role and Resources” (*Utredningen om Finansinspektionens roll och resurser*), which suggests increased financing through charges (Ministry of Finance 2003: 139–142).

With the triple objective of ensuring the stability and efficiency of the financial sector, sufficient consumer protection, as well as general confidence in the financial market and its institutions (Swedish Parliament 1990/91: 17; FI 2005: 3, 10; European Central Bank (ECB) 2003: 13), FI’s major operational areas comprise supervision, regulation and licensing, and financial stability analysis (FI 2005: 4–6; Lumpkin 2002: 28;

Taylor and Fleming 1999: 12; Mwenda and Mvula 2003: 45). Worth mentioning is the fact that FI did not relinquish its internal organizational structure along the pillars of banking, insurance, and securities evident in three “sectoral” departments, albeit resembling today’s operational foci (three subdivisions for supervision, regulation, and analysis per department), until 2000 (Lumpkin 2002: 28; for the time before 2000, see Taylor and Fleming 1999: 16; Anonymous 1997). Nowadays, FI has functionally distinct departments ranging from, for example, Communications to Prudential Supervision. It is headed by a government-appointed Director General (at present Ingrid Bonde), who is responsible for the day-to-day operational work and also serves as the chairperson of the supervisory board, called Board of Directors, which is composed of nine government-appointed members (including the Director General) plus two employee representatives; it is authorized to decide the application of sanctions to firms and make rules in accordance with the delegated powers of the relevant statutes (FI 2005: 4; Taylor and Fleming 1999: 14; IMF 2002: 73).

As the responsibility for the active promotion of a safe and efficient financial system is shared between FI and Swedish Central Bank (*Sveriges Riksbank*), clarification pertaining to FI’s concrete supervisory function is needed. In the Swedish Central Bank’s (2003: 70–71) view, FI’s primary activity lies in institutional supervision, which is to guarantee the stability of individual institutions, whereas “system supervision” (systemic risk is the Central Bank’s main concern) and monitoring plus evaluation of the financial infrastructure are of secondary importance only. This description is largely consistent with the official self-presentation. “Companies offering financial services,” FI says (2004; my note), “must be financially stable and have functioning internal controls and a healthy balance between capital and risks. We prioritize supervision of the largest corporate groups [...] [for the reason that] [r]isks are not distributed evenly in the financial sector since companies under our supervision are of different sizes and types.” A classification that contains four risk categories based on financial companies’ size and the nature of their business with gradually declining extent and intensity of investigations pursued by FI has been developed to achieve the intended effect of stability of individual institutions; and the Ministry of Finance (2003: 44; my translation) asserts, “This has also brought about a focus on (mainly rather big) financial companies which are of outmost importance for systemic stability. FI has identified thirteen corporations/business groups as being systemically important, and particular responsible inspectors have been appointed for those.” Corre-

spondingly, Lumpkin (2002: 28) highlights that “[...] emphasis is placed on ‘group-wide’ supervision and risk analysis”.

FI has been vested with the power to utilize various instruments, among them administrative fees, fines, and, ultimately, the withdrawal of licenses so as to enforce corporations’ compliance with regulatory rules (e.g., statutes or ordinances). It can also decide to reject board members and the Chief Executive Officer (CEO) as being “improper”. Other disposable, but rather “soft” measures include the licensing of financial institutions, the issuing of regulations and general guidelines as a supplement to current legislation, the issuing of permits for financial operations, the inspection of institutions, the request of certain information, the delivery of a warning, and the laying down of institution-specific standards and directions (FI 2005: 5, 15–16; FI 2004; Taylor and Fleming 1999: 12; Swedish Bankers’ Association 2004: 12).

These competences form a central component of financial supervision in Sweden so that they shall be taken as a clue to FI’s institutional design in terms of Pettit’s rational choice approach. Concentrating mainly on risk avoidance and prevention to ensure financial stability, FI is designed in great conformity with this perspective insofar as these competences allow the identification of a particular rational-choice inspired strategy supposed to make for the desired stability: FI conducts a complier-centered strategy as the next section will demonstrate.

4. Finansinspektionen – Rather Rational than Weak?

4.1 *Accusations of Weakness*

It may seem a little exaggerated to argue that it has been a commonplace since FI’s formation to criticize it for either too unclear a set of “rules of the game” (after the so-called pension affair; on this, see Björck 1991) or a lack of resources in terms of employees’ average expertise and experience (see *Affärsvärlden* 1993), but such critical statements have occasionally been made.

The 2002 Financial System Stability Assessment of Sweden released by the IMF (2002) is much more concrete by specifying potential and actual debilities of the financial system, including shortcomings of financial supervision. In particular, it accentuates two weaknesses as regards FI’s capacity to enforce regulatory codes and

standards. First of all, although looking upon the general prerequisites for supervision favorably, it considers sufficient regulation and supervision quite difficult, not to say hardly feasible, in that FI has limited resources at hand and also lacks staff experienced and well-skilled enough to utterly fulfill the regulatory tasks in question; the problem of too little adequate equipment is, second, aggravated by FI's restricted legal enforcement authority (e.g., to take interim or corrective measures) (ibid.: 7, 19, 54–56). This assessment leads to the complaint that “[...] FI has relied on moral suasion in coordination with possible sanctions to influence corporate behaviour” (ibid.: 19). As a consequence, it proposes strengthening FI's authority over financial companies and supplying more resources (ibid.: 56). Proposals of this kind are largely reiterated in the survey (Ministry of Finance 2003: 93–97, 119–129) and supported by the Central Bank (2003: 68–69).

As for the lamented degree of enforcement abilities, it is to be recognized that these critical evaluations focusing on the specified aspects were done in the light of the situations in 2002 (IMF assessment) and 2003 (Utredningen's survey). A few changes in FI's institutional design have been undertaken ever since: FI (2005: 12–13, 16) itself notes that it has been granted expanded sanctionary powers such as the application of fines to financial companies which do not comply with the rules imposed. These crucial changes, even if they appear to have been rather small scale, must be borne in mind when tracing features in FI's design conforming with rational choice logic.

4.2 *Threads of Rationality*

As has been shown in the preceding sections, FI focuses its supervisory activities on monitoring the financial system particularly with regard to the overwhelming goal of safety, or stability. It pursues an approach of “group-wide” supervision and risk analysis, whereby the companies which, being the most crucial players in the financial market, are viewed as constituting the biggest threat to financial stability are supervised with exceptional intensity.

According to its self-assessment (see FI 2005: 16, where emphasis is placed on “purposes of prevention”) and the prevalent view in the Ministry of Finance (2003: 29; emphases in original, my translation), under whose control it is, containing systemic risks necessitates the supervision of individual financial companies or groups of

them: "even though for the most part the goal of promoting stability consists of guaranteeing stability of the financial *system*, it is vital to comprehend that developments which may put the whole system at high risk do not appear from nowhere – what in reality causes a systemic crisis is that financial or operational problems arise in one or more identifiable *companies* and that those problems then spread to other actors. To pay attention to the individual financial enterprise as regards organization, capitalization, and risk management is therefore at the very core of financial supervision [...]." This quotation exhibits a great deal of what may be called "harm avoidance by private agents". Harm avoidance here stands for preventing risks/instability from spreading from individual companies, the private agents, to the system as a whole.

In addition to "prudential supervision", FI is in charge of "market conduct supervision" (Ministry of Finance 2003: 29–30), which stresses efficiency and thus rather refers to the notion of "benefit promotion" (for this term and "harm avoidance", see Pettit 1996: 59–61). Taking into account the official statements presented as well as the findings derived from scientific essays, however, it seems evident that the primary orientation of Swedish financial supervision concerns harm and risk avoidance for the sake of financial stability. Lumpkin (2002: 3) underscores the utmost importance of this end in general terms: "[a] central goal in the design of regulatory and supervisory regimes for financial services is to create a framework that ensures the safety of the financial system as a whole and allows other objectives of supervision [...] to be attained efficiently and effectively." FI's institutional design is for the most part apparently directed to the prevention of harm. This has significant implications for the scope of powers that FI could potentially wield.

Consider the following: unless a supervisory agency aims at harm avoidance, it does not need to possess considerable sanctionary powers; but if it does target at exactly that, it better should be able to exert credible pressure on market agents from a rational choice perspective. As the latter scenario applies for FI, such competences are plainly fundamental to the conduct of a deviant- and even a complier-centered strategy. This is because both strategies rest on dealing with knaves, that is, financial companies which deviate from the expected behavior: extreme measures make up the very core of the former strategy; the latter is still dependent on them, but only resorts to them as a kind of emergency measure.

Several instruments at FI's disposal like the licensing of financial companies or permits of their services clearly function as screening devices, yet with different objectives; the distinction between screening of agents and of options helps to clarify the twofold aim of employing screens in FI's supervisory strategy. On account of its commitment to institutional supervision, FI is keen to only screen in those agents, read: companies, that can reasonably be expected to comply on a categorical basis but to screen out deviant candidates; by the same token, it must also exercise a good deal of caution towards the range of financial services it allows the agents to offer, which again requires careful screening. FI's licensing authority falls without doubt in the category of screening in and out agents. In contrast, service permits are as much option-related screens as is the right to reject board members and CEOs by reason of presumed "unsuitability". Furthermore, FI disposes of instruments conducive to applying screens. Among them are on-site inspections and the request of information, both of which generally provide necessary information for supervision, thus in part reducing the asymmetry of information in FI's favor. The issuing of general guidelines, "[...] which unlike laws are optional, but ought to be followed by financial institutions to be considered carrying on sound activities" (Swedish Bankers' Association 2004: 12), is another supplement to screening. It operates indirectly: if corporate entities want to be licensed or their services to be permitted by FI, they will be inclined to follow such guidelines on a voluntary basis for their own economic sake. The delivery of a warning or the development of institution-specific standards is directed at companies wavering between compliance and deviance, serving to indicate the potential intensification of requirements or to actually tighten instructions.

This response could be interpreted as a preliminary, "soft" kind of sanction once a company has attracted FI's special attention by failing to comply; it must then possibly bear the burden of extra, intensified requirements. This kind of sanction definitely ranks among the least severe measures. The available option of imposing fines on deviant companies has of course a higher enforcement power than the requirement to fulfill additional conditions and has sometimes also been used by FI (see, for fines imposed in 2004, FI 2005: 16). This order shows that feasible sanctions are arranged in an escalating hierarchy so that their imposition can work in a deliberately supportive way, just as the complier-centered strategy demands it. The last level in the hierarchy of sanctions is embodied in the power to withdraw licenses from companies. As the "ultima ratio", this device will be resorted to only if FI assumes the whole

Swedish financial system to be in danger of being afflicted by grave instability due to the difficulties of certain institutions; companies of this kind represent the knaves in rational choice terms. The sanction is designed to contain, if necessary, the knaves' harmful behavior, and the mere authorization to withdraw licenses contributes to ensuring financial stability and safeguarding the financial system.

In short, FI can employ a relatively wide range of various instruments to attain its goals with the priority given to financial stability. Since possible measures range from screens concerning both agents and options to sanctions of different intensity, with the screening devices taking center stage, it is fair to say that FI follows a complier-centered strategy. What is more, FI can influence the agents' environment by virtue of its role as a norm-setter (Törnqvist, Lumsden, and Marton 2000: 18; see also *Af-färsvärlden* 1993: 18; Ministry of Finance 2003: 39). Used appropriately, its influence might bring about changes in the agents' behavior in the sense that their mode of deliberation becomes less egocentric and that compliance eventually occurs on a more categorical basis. This alone will hardly be enough to achieve compliance, but it can well prepare the ground for it. All the measures examined complement one another making FI's approach to supervision consistent with the three principles of the complier-centered strategy in rational choice theory.

But what about the accusations of weak, even "toothless" supervision? That FI was granted by means of new legislation (taking effect in July 2004; see FI 2005: 16) the power to impose fines in case of non-compliance marks an important adjustment, for it implicates a significant widening of the scope of disposable low-level sanctions. FI has been enabled to take a comparatively strong low-level sanction before imposing the heaviest sanction of all: the withdrawal of licenses. In this sense, that change did improve FI's supervisory capability considerably by fine-tuning the content of the second principle in its complier-centered strategy. Another recurrent criticism has been related to the insufficient provision of resources, that is, above all funds and staff. This criticism is more difficult to rebut. While financial resources can be reallocated quite fast, usually after one year from one budget to another, compensating for a shortage of experienced and skilled staff constitutes a middle- or long-term challenge. This is so for many reasons: it might turn out be difficult to attract a sufficient number of capable employees due to possibly higher wages in private companies; it will also take some time until staff restructuring starts to really have an impact on the

conduct of supervision inasmuch as new personnel needs to become acquainted with the subject; the staff's learning processes are moreover complicated by the ever-changing nature of the subject. The lack of appropriate staff was yet a major concern in 2003, when the Ministry of Finance was conducting the inquiry into FI's role. It is likely that this problem still exists and hampers effective and efficient application of screens and imposition of sanctions to some extent. For this reason, FI's strategy of supervision will still have to be further supported by additional resources.

5. Conclusion

Some observations shall be summarized here. Even though FI also supervises the financial system in order to promote the conduct of business, most emphasis is placed on ensuring financial stability, which makes prudential supervision its paramount task. It closely monitors individual corporate entities assuming that instability originates in them and in turn affects the whole system. To the end of stability, FI relies on a complier-centered strategy with screens on agents (licensing) and options (permits) installed and a wide range of potential sanctions provided most of which are of lower severity (warnings, extra requirements, and fines) and one of which is "structural" in character (the withdrawal of licenses as the "ultima ratio"). Seeing that, FI is enabled to pursue supervision on a much stronger basis than criticisms of general weakness have indicated.

I should be self-critical as far as these findings are concerned. My interpretation of FI's design from a rational choice perspective is liable to theoretical one-sidedness. A different approach could perhaps also have explained the subject in question and yielded different results. Additionally, the connections between theoretical and empirical aspects in this paper are to some degree based on speculations given the scarcity of theoretically enriched analyses of FI's role in the Swedish financial system.

Political scientists will therefore have to study its role in much greater depth than has hitherto been the case. They could build on empirical overviews like those published by the IMF or the ECB, which have been used in this study. In my view, a two-fold objective is to be achieved: at first, political scientists ought to give, as a supplement to IMF or ECB publications, own empirical reviews of current supervision including

changed and new legislation; the second step should be to provide theoretically deep analyses based on or incorporating the empirical reviews. I deem both of them necessary if we want to more fully understand Swedish financial market regulation. The same applies for regulation in other countries. There is obviously no lack of possible topics. For one thing, the implications of the Basel II rules for FI's supervisory function would qualify for intensive political science research (see Lybeck 2004).

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