Is New Governance the Ideal Architecture for Global Financial Regulation?

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A central challenge for international financial regulatory systems today is how to manage the impact of global systemically important financial institutions (G-SIFIs) on the global economy, given the interconnected and pluralistic nature of regulatory regimes. This paper focuses on the Financial Stability Board (FSB) and proposes a new research agenda for the FSB's emerging regulatory forms. In particular, it examines the regulatory architecture of the New Governance (NG), a variety of approaches that are supposed to be more reflexive, collaborative, and experimental than traditional forms of governance. A preliminary conclusion is that NG tools may be effective in resolving some *kinds of problems in a pluralistic regulatory order, but they are unlikely to be suitable for* all *problems. As such, this article proposes that analyses of the precise conditions in which NG mechanisms may or may not be effective are necessary. It concludes with some recommendations for improving the NG model.*

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I. Introduction

The central transnational regulatory challenge of the moment is how to monitor and manage large cross-border institutions that can jeopardize the health of the entire global economy. So-called global systemically important financial institutions (G-SIFIs) are cross-border institutions that are so large or interconnected with other financial institutions that they are potentially "too big to fail." Equally importantly, such institutions are subject to multiple, overlapping, and even sometimes conflicting legal regimes.

From a legal point of view, the challenge G-SIFIs pose to global financial regulation is the problem of the interdependence of regulatory regimes in a global system that is inherently pluralistic in nature. The threat of regulatory arbitrage that underlies much of the push for the harmonization of financial regulation—the threat of a race to the bottom among jurisdictions—is plausible only if legal regimes are sufficiently fungible and interconnected on the one hand, and yet sufficiently different in regulatory substance or approach on the other, that in some circumstances they can become viable alternatives from market participants' point of view. Conversely, where markets are interconnected, one approach to regulatory oversight in one jurisdiction produces externalities in other regulatory regimes.

This paper takes stock of the way the international financial regulatory system is now tackling this challenge as exemplified by the initiatives of one of the prime organs of global financial regulation today, the Financial Stability Board (FSB). (See Griffith-Jones, Helleiner, and Woods [2010].) The Group of 20 (G20) launched the FSB as its technocratic arm of policy creation and implementation in 2009,[1] transforming an earlier Group of Seven (G7) institution, the Financial Stability Forum, into a more robust organization with increased membership, increased institutional capacity (increased permanent secretariat staff, standing committees) and a broadened mandate to take a more macroprudential focus on G-SIFIs in particular.[2]

Article 1 of the FSB's charter emphasizes its core functions and methodologies—coordination, standard-setting, implementation of global standards, and identification and assessment of cross-border financial risks:

> The Financial Stability Board (FSB) is established to coordinate at the international level the work of national financial authorities and international

1. G20 London Summit, April 2, 2009, "Declaration on Strengthening the Financial System."
2. Structurally, the FSB consists of a plenary of representatives of regulators, central banks and finance ministries in member jurisdictions and international organizations, which makes decisions by consensus, including approving peer review reports and choosing new members; a steering committee; a secretariat; and three standing committees, one of which (the Standing Committee on Standards Implementation) is responsible for conducting peer reviews (described further below). Agreements are negotiated in individual committees through the circulation of draft text usually produced first by the secretariat.

   Member jurisdictions are allowed one, two, or three voting participants depending on "the size of the national economy, financial market activity and national financial stability arrangements of the corresponding Member jurisdiction" (FSB Charter Article 10). At present, there are 24 member jurisdictions plus the Bank for International Settlements, the World Bank, the International Monetary Fund, the Organisation for Economic Co-operation and Development (OECD), the Basel Committee on Banking Supervision (BCBS), the Committee on the Global Financial System (CGFS), the International Accounting Standards Board (IASB), the International Association of Insurance Supervisors (IAIS), the International Organization of Securities Commissions (IOSCO), and the Committee on Payment and Settlement Systems (CPSS) (FSB Charter Appendix A).

> standard setting bodies (SSBs) in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies. In collaboration with the international financial institutions, the FSB will address vulnerabilities affecting financial systems in the interest of global financial stability.[3]

One cannot but be impressed with the sheer volume of initiatives the FSB has undertaken since its relaunch in 2009, and by the remarkable leadership, energy, and acumen behind these. In this paper, I take the FSB as a target of critical analysis precisely because it represents arguably the state of the art in international financial governance: it is an experimental, purposeful, and energetic institution that deploys the most innovative international financial regulation methodology today.

The FSB's approach, like that of most domestic and international regulators, is to tackle discrete and pressing problems through tailored policy initiatives: for example, determining which banks should be designated as G-SIFIs, drafting rules on executive compensation, or deciding how much and what kind of capital such banks should be required to set aside. These are important and complex questions that leave little time for an "eagle's-eye view" of all of this activity taken as a whole. And yet, built into the structure of the Basel Accords and of the numerous activities of the FSB, there nevertheless is an inchoate but distinct ambition that this activity will ultimately add up to a larger global financial governance project, something more than the sum of the parts.

Thus, it is important to carefully consider the sum of all these parts, to reflect on where this broad flurry of activity is leading, and to evaluate whether the implied target of these activities is sufficient to prevent or abate financial crises to come. The question of regulatory *form*—of the nature, strengths, and weaknesses of the emerging global financial architecture—remains surprisingly underexamined both by academics and by policymakers. For example, to date, the FSB has never clearly articulated, let alone defended, its model of regulatory form—what I will call the New Governance (NG) architecture.

To date, the academic literature has also not done a sufficient job of providing leadership in addressing these larger questions. Academic experts in financial regulation, perhaps because they are so closely engaged in conversation with policymakers, have tended to approach problems in international financial governance at a more granular, policy-by-policy level, without regard for the larger architecture. These experts have focused on pointing out the strengths or shortcomings of particular policy initiatives and have assumed that international coordination will take care of itself.[4] In many cases, academics implicitly accept and even build off of the FSB model seemingly without noticing the choice, or discussing its implications (e.g., Romano [2012]). If one reads this literature as a whole for what it might tell us about the larger questions

3. Financial Stability Board (2009a).
4. Gordon and Mayer (2011), for example, argue for the harmonization of regulation that impacts on systemic risks such as capital requirements, bail-ins, and so on, without discussing the mechanism by which harmonization should take place.

addressed in this paper, however, these specific inquiries into discrete policy initiatives raise questions about the NG architecture.

From another disciplinary perspective, there are those working on international law and governance, principally in fields of nonfinancial law such as international labor law, international environmental law, and public international law, who applaud the emerging structure of global financial regulation (Miyano [2008])—largely because this structure has been borrowed (possibly without sufficient reflection) from innovations in many of the public law fields in which they work. These proponents, however, generally lack extensive expertise in financial law, and thus their analyses of the specifics of the global financial regulatory architecture remain thin. And yet the comparison with other legal fields is not entirely misplaced: the entanglement of regulatory systems is a problem that global financial regulation shares with a host of other major international regulatory areas, from environmental regulation, to counterterrorism, and many more. This challenge has been discussed extensively in the public international law literature (Twining [2003]).

We know that regulatory architecture—the form regulation takes—rules versus standards, hard law versus soft law, penalties versus rewards, *ex ante* versus *ex post* regulation, administrative, judicial, or legislative rule-making—impacts the efficacy of regulatory initiatives, the legitimacy of regulation, and its distributive effects. For example, self-regulation is a regulatory architecture that was once taken for granted by many as the best way of achieving certain regulatory objectives, and yet it is widely acknowledged today that self-regulation has clear limitations. Indeed, the understanding that regulatory architecture matters is precisely the premise of NG initiatives (described in Section III): for its proponents, NG offers a more effective and just regulatory form for achieving the same substantive policy goals that one might pursue through either "command and control" regulation or self-regulation.

This paper aims merely to initiate a debate and propose a research agenda regarding the emerging form of the architecture of international financial governance. It does so by bringing together what is known in other legal and social scientific fields about the particular regulatory technologies deployed by the FSB. The aim of this paper is not to propose an alternative architecture, but rather to lay the groundwork for thinking through the alternatives by suggesting how we might approach a more careful diagnosis of the potential problems with the current taken-for-granted approach.

Although this paper is not the place for a full exposition of my own views on possible alternatives, I ask the reader to put aside for a moment one assumption that often stands in the way of a full consideration of the current predicament. It is often taken for granted, implicitly or explicitly, that the current system is the only plausible alternative to an older form of international legal governance sometimes disparaged as "command and control" regulation. This older view is, to some extent rightly, seen as outmoded, impractical, and ill suited to current regulatory challenges.[5] However, it is sometimes then assumed that any criticism of the current approach to regulation is also an implicit argument for a return to command and control, or conversely,

5. Legal scholar Jodi Short has argued that many criticisms of command and control regulation in the United States may stem more from a general U.S. anxiety about state power and coercive government than from an objective evaluation of past policies (Short [2012, pp. 637, 642, 681]).

that a criticism of command and control regulation is in itself an argument for NG regulation, as if there can only be two possibilities—NG or command and control. A more rational and illuminating approach might consider the strengths and weaknesses of the NG approach on its own terms. Only after we evaluate the efficacy of the current model can we determine whether it is indeed the best possible option and how it might be reformed.

The analysis proceeds as follows. In Section II, I describe the pervading understanding of the "problem" of G-SIFIs at successive layers of complexity, and I then describe what kind of practical policy response to this problem is entailed in the regulatory approach of the FSB. In Section III, I analyze the problems and solutions outlined in Section II from the standpoint of the body of regulatory theory that most directly corresponds to (and has most directly influenced) this approach. This body of regulatory theory—the so-called NG literature—claims developments in global financial governance as a prime example of its applications, and has indirectly influenced the architecture of global financial governance by means of models borrowed from initiatives in Europe such as the "open method of coordination" (OMC) of the European Union (EU) and efforts in the United States to establish models of reflexive administrative law such as the U.S. National Environmental Policy Act.

In Section IV, I evaluate NG as implemented by the FSB as an architecture of international financial governance. Experts in financial regulation in both the academy and government who have focused on the effects of particular NG initiatives prior to and since the financial crisis are far less enthusiastic than proponents of NG about its practical prospects for success in this area. Indeed, much of the initiative for current transnational rule-making derives from concerns about the potential pitfalls or limitations of pre-financial crisis, NG-style initiatives as applied prior to 2008 in the United States and Europe to the relationship between regulators and financial market participants. And yet, ironically, at the very moment at which the FSB is busy creating rules and procedures to supplement the failures of pre-2008 domestic regulation that, in many North Atlantic countries, was inspired in important parts by the NG model, the FSB is itself applying much of the same regulatory architecture with little critical evaluation to the relationship between international and domestic regulators—as a tool of international regulatory coordination. To make matters worse, in the process of transposing NG into a tool of international regulatory coordination, some of the most innovative aspects of NG seem to have been lost, diluted, or disregarded in practice.

As described in the conclusion (Section V), a preliminary hypothesis emerges from this analysis: NG mechanisms may be effective in resolving *some* kinds of problems caused by the interrelationship of legal regimes in a pluralistic regulatory order, but they are unlikely to be suitable to *all* problems. This in turn suggests an agenda for future research: detailed study of the precise conditions in which new governance tools may or may not be effective in international financial governance is sorely needed.

II. The FSB Approach to Global Financial Architecture

This section describes the G-SIFI problem and the FSB's response as a problem of transnational regulation. Sections II.A and B summarize the practical challenges G-SIFIs pose as a variation on a quite standard problem in international law and institutions—a problem of coordination in pluralistic conditions. Section II.C describes what is most innovative and deserving of analytical attention about the FSB's approach to this problem.

A. The Challenge of G-SIFIs as a Problem of International Legal Coordination

As mentioned at the outset, the challenge of G-SIFIs is that they are difficult to understand and to control from the vantage point of any singular jurisdiction, and yet their failure can have serious consequences for multiple jurisdictions and the global economy as a whole. The Liikanen Report commissioned by the EU to provide a blueprint for future EU directives on banking regulation defines them as "those institutions whose distress or disorderly failure would cause significant disruption to the wider financial system and economic activity, due to their size, complexity, systemic interconnectedness or lack of good substitutes that can readily take over their activities" (Liikanen *et al.* [2012, p. 38]).

The regulation of G-SIFIs is therefore an inherently transnational problem that demands both practical coordination among regulators and an understanding of how national and international regulatory regimes interact. The proposed responses to the risks posed by G-SIFIs can be divided into the operationally desirable but politically unpalatable on the one hand and the more politically feasible but more difficult to operationalize on the other.

1. Option 1: Break up the G-SIFIs

If certain financial institutions are too systemically important and complex to fail, then the most logical proposal is to break them up into smaller entities.

Prominent academic commentators, including Joseph Stiglitz and Simon Johnson, and even some prominent market participants such as former Citigroup CEO John Reed and former Citigroup Chairman and CEO Sanford Weill, have questioned whether the increasingly large size of financial conglomerates contributes to wider economic welfare to a degree that is proportionate to the externalities they impose on the global economy. Legal scholars, likewise, have proposed that existing anti-trust law might be used to break up some of these conglomerates (Reich [2010]). As the de Larosière Report outlining the EU position on financial regulation explains,

> Given their size and the structural function they have for the financial system as a whole, [SIFIs] are, to some extent, "*too big to manage*" and "*too big to fail*"—which means that they can expose the rest of society to major costs and are subject to acute moral hazard; in some instances, these institutions can even be "*too big to save*", for example when they are head-quartered in a relatively small country or when the organisation of a rescue package is simply too complex to implement.[6]

6. de Larosière (2009, p. 62).

However, most policymakers believe that this approach is for the moment unfeasible due to the opposition of powerful financial institutions (Krugman [2010]). As the de Larosière report makes clear:

> However, although this may be desirable in instances of excessive market dominance under anti-trust law, it is unlikely that large financial institutions will be broken up into component parts.[7]

2. Option 2: Government liquidation or nationalization in conditions of crisis

If the failure of a G-SIFI spreads risk throughout the financial system and imposes costs on taxpayers, another logical proposal would be to give regulators the authority to nationalize or liquidate banks whose capital ratio falls below a certain level (Butler [2009]). However, again, many observers believe this is politically unfeasible at least in the United States due to the public's distaste for government ownership of private assets (Blinder [2009]) and regulators' fear that liquidation is an admission of regulatory failure (Coffee [2011, p. 839]).

3. Option 3: Preparedness

The dominant approach, therefore, has been to focus on drafting firm-specific plans for a more orderly resolution of institutions that pose general systemic or "macro-prudential" risks (Federal Deposit Insurance Corporation [2011]). This is the approach embodied in the U.S. Dodd–Frank legislation (the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010)[8] as well as in the focus on identifying G-SIFIs and requiring that they hold up to an additional 2.5 percent of capital in reserve, in addition to the amount enshrined in the Basel III accords and implemented in recent framework documents promulgated by the FSB (Basel Committee on Banking Supervision [2011]). The new FSB standard on resolution promulgated in October 2011, for example, emphasizes "mandatory resolvability assessment and a recovery and resolution plan for each global SIFI,"[9] as well as "a cross-border cooperation agreement between relevant authorities" (Draghi [2011]).

The centerpiece of this approach is the imposition of additional capital requirements on G-SIFIs both to guard against and ultimately insulate taxpayers from bearing the cost of resolution (Dash [2011]).[10] Other proposals include mandating that financial institutions create "living wills" that purport to define how they would be resolved at times of crisis—an approach now enshrined in U.S. regulations (Enrich 2010)—and shifting the burden of loss to bond holders by mandating that certain categories of bonds stipulate that they convert to ordinary shares when a bank's capitalization drops to a certain level (contingent convertible [CoCo] bonds or bail-in debt) (Hart and Zingales [2010]). There are also proposals to impose additional taxes on G-SIFIs to create a fund

7. de Larosière (2009, p. 62).
8. It is the basis of Title I, Section 165 of Dodd–Frank that directs the Federal Reserve to apply prudential standards to systemically important bank and nonbank financial institutions (Romano and Verstein [2011, p. 48], comments of Tom Baxter, general counsel of the Federal Reserve Bank of New York).
9. A total of 28 G-SIFIs had been designated as of November 2012.
10. Basel III imposes "requirements for globally systemically important banks to hold additional common equity capital above the Basel III minimum standards, rising from 1% to 2.5% of risk-weighted assets commensurate with the systemic impact of their failure, to be fully phased in by 2019" (Draghi [2011]).

that would cover resolution costs or to ask other financial institutions to cover the cost of the bailout of one of their peers after a crisis has occurred (Singh [2011]).

However, problems remain with all of these efforts to prepare for the next failure of a G-SIFI. First, many question whether the preparations are sufficient. Lehman Brothers itself, for example, probably would not have been required to post the additional capital requirements demanded of G-SIFIs under the current regime (Federal Deposit Insurance Corporation [2011]). CoCos raise a host of problems, from how to price such instruments and whether they are open to legal challenge to their possible contagion effects at times of crisis (Pazarbasioglu *et al.* [2011]). More generally, planning for the future is difficult and the experience of past crises is not always a good guide. Living wills, for example, are unlikely to bear much resemblance to actual crisis conditions and hence are somewhat academic exercises (Gilani [2011]).[11] As pointed out by Black (2010), "the solution of an orderly liquidation process for global financial conglomerates is untested, and many doubt whether it will work to prevent future financial crises." In the 2011 Mayekawa Lecture at the Bank of Japan's Institute for Monetary and Economic Studies, Goodhart and Tsomocos (2011, p. 63) likewise conclude, "The experience of the failure of Lehman Brothers was so appalling that most governments thereafter decided that liquidation of a SIFI could not be tolerated."

4. The corollary: Coordination among regulators

The backstop to this preparedness approach, therefore, is better coordination among regulators with the hope that it will lead to greater degrees of trust and better coordination at a moment of future crisis. This focus on building channels for coordination and information-sharing responds directly to the failures of coordination between U.S. and U.K. regulators at the time of the Lehman crisis of 2008. Yet commentators and policymakers alike have decried inadequate levels of information-sharing regarding G-SIFIs among national regulators (Corcoran [2011] and Brummer [2011]).

In particular, the failure of a G-SIFI creates potential conflicts of interest between a G-SIFI's home jurisdiction and the host jurisdictions in which the G-SIFI does business. In a situation of G-SIFI failure, by definition there are not sufficient assets to cover the G-SIFI's liabilities globally and regulators and courts are often tempted to favor their own nationals over other creditors. If the home jurisdiction's courts or regulators can assert control over the G-SIFI's assets worldwide, then they may use available assets to compensate their own national creditors first. Conversely, if a host jurisdiction can, through its courts or by administrative regulation, assert legal jurisdiction over the G-SIFI's assets located within its territory, then the host jurisdiction's courts or regulators may use these assets to compensate creditors located within the jurisdiction first. Because home and host regulators anticipate such behavior at moments of the failure of a G-SIFI, they may be reticent to share information for fear of creating tactical advantages for regulators on the other side.

11. The living-will project exemplifies a response to the threat of future crisis that social scientists have observed in many other arenas, from environmental to security to medical risks. The approach is to prepare what scholars term "fantasy documents" concerning preparedness that outline procedures which in all likelihood bear little resemblance to what would need to be done or would actually be done at the moment of crisis. Social scientists have argued that the true function of such documents is to generate public confidence in the present, rather than to mitigate disaster in the future, and also to create a project that necessitates cooperation and hence gives the parties an opportunity to work together and build relationships (Clarke [1999]).

Hence the problem of coordination between home and host regulators is a central focus of the FSB (Basel Committee on Banking Supervision [2006]). The stated task of the FSB is to "significantly step up cooperation amongst authorities to prepare feasible and credible G-SIFI resolution plans" (Draghi [2011]).

B. The Limits of Harmonization as a Coordination Technique

To understand why NG emerges as an appealing regulatory architecture for the FSB as it addresses coordination problems among regulators, it is necessary to understand what NG innovates against—international harmonization. Up to this point, most attempts at financial regulatory coordination have emphasized a more classical international legal solution to coordination: harmonized rules agreed upon at the interstate level and translated into substantially similar national laws by domestic legislatures or enforced by domestic regulators. The legal mechanism of choice for regulatory coordination of this kind has been the interstate agreement. These agreements have traditionally been negotiated among national financial regulators of the G20 nations[12] through the Basel Committee (Basel Committee on Banking Supervision [2010b]) and then sanctioned by heads of state at G20 meetings.[13] But they are intended to be global in scope—to apply to the G20 nations as well as the non-G20 nations (Helleiner [2010]). The aim is for the content of these agreements to supersede conflicting national law by implementing legislation or changes in regulatory practice in each country (Helleiner [2010]).

Why did this kind of formal harmonization traditionally seem like a necessary form of coordination? As domestic regulators in jurisdictions such as the United States pursued domestic reforms, they confronted a steady drumbeat of threats that markets would respond to additional regulatory burdens by moving business to jurisdictions that did not have heightened regulatory requirements (Gonzalez and Schipke [2011]). National regulators responded to this threat of regulatory arbitrage and of a "race to the bottom" by attempting to ensure that other jurisdictions had roughly the same regulatory burdens as their own (Eubanks [2010]). One concern for the national regulator at the international level has been to ensure that domestic regulatory reform does not lead to a decrease in the size of the domestic financial industry. Thus, international harmonization of regulatory standards has traditionally been seen as the necessary corollary of domestic regulatory reform.

In other words, one emblem at this early stage of international financial governance is that national regulators act on the international plane with quite a nationalist view of their interests: other nations' markets are of concern primarily insofar as they pose financial risks to the domestic market or they become a potential source of competition for the domestic market because of lower regulatory standards. Yet the implication of this nationalist orientation, ironically, is that it becomes necessary to push for global harmonization and standardization over national diversity in regulatory approaches, that is, to favor harmonization rather than pluralism as a modality of international legal architecture.

12. Prior to 2009, such agreements were negotiated among the so-called Group of 10 (G10) nations only.
13. In the past, these proposals were approved at G7 meetings.

In practice, harmonization as an architectural model leads to numerous problems. First, harmonization typically takes the form of substantive *rules*, such as capital adequacy requirements for systemically important financial institutions. One practical reason for the emphasis on harmonizing rules at the Basel Committee and the FSB is that rules are relatively easy to identify, describe, and produce compared to regulatory standards or practices. Yet harmonized rules mean little if the degree of supervision concerning adherence to these rules varies widely from one jurisdiction to another. As argued by Pan (2010), rule making does not in itself translate into better regulatory supervision:

> International law scholars who analyze the performance of transgovernmental networks should distinguish between rulemaking and standards setting, on the one hand, and supervision, on the other. This distinction is important because one of the main achievements of transgovernmental networks has been to drive convergence and harmonization of national rules and standards in the areas of banking, securities, and insurance. Basel I and Basel II, for example, are successful instances where a transgovernmental network has been able to produce a broadly accepted set of regulatory standards. The recent financial crisis, however, demonstrated that the real need for regulatory action is in the area of supervision.[14]

Likewise, Julie Dickson, the Superintendent of Financial Institutions of Canada, has argued that current reforms give too much attention to rule making and not nearly enough attention to the process of supervision itself:

> If we take the view that supervisory judgment has failed time and again, and that we should therefore rely far more on rules than on supervisors going forward, we may create a system with even more risk, as rules often have unintended consequences which can take quite some time to see. As well, our record in getting rules right is not stellar. Stricter rules, like substantially higher capital requirements, can create a false sense of security; an institution will never have enough capital if there are material flaws in its risk management practices. That is why supervision matters.[15]

A related problem with harmonization as an international governance structure is a pervasive lack of support from domestic politicians, banks, the public, and even regulators in many jurisdictions for rule making at the international level. Global agreements require domestic support for implementation, but in many jurisdictions domestic constituencies, from legislators to market participants, have proven to be profoundly skeptical of newly harmonized rules (Tarullo [2008]). The consequence is often the practical impossibility of full compliance with internationally harmonized rules.

14. Pan (2010, pp. 264–265).
15. Dickson (2010, p. 624).

Likewise, the lack of will for coordination among regulators themselves—the sense of national competition that often pervades the sense of the common good—also impedes harmonization efforts. Unwillingness on the part of national regulators to adhere to internationally harmonized standards is likely to be even stronger in cases of emerging markets not represented at the FSB or the G20.

For all of these reasons, even many of the proponents of international legal harmonization agree that full or substantial harmonization of regulatory standards in the short to medium term is most likely impossible. Yet many commentators and policy-makers go further to argue that even if it were achievable, harmonization is the wrong objective—that it is not desirable in the first place.

First, different jurisdictions face different conditions and different problems. For example, as Jeffrey Gordon commented in April 2011 at a round-table discussion on Dodd–Frank held at the Yale Law School, the U.S. focus on the liquidation of G-SIFIs reflects options available to U.S. regulators given the size of the U.S. economy and of the Treasury relative to the size of failing financial institutions that may not be available to other countries. For other countries, the focus rather must be on preventing the failure of institutions that are "too big to save" through higher capital adequacy requirements and bail-ins.[16]

Equally importantly, where systemic risk is created by "herd mentalities" in which market participants pursue common strategies, different regulatory approaches may act as a stopgap against contagion by incentivizing different business models (Smits [2010] and Low [2010]). As Takafumi Sato, former commissioner of Japan's Financial Services Agency explained in an op-ed article in the *Financial Times* in 2009, "A global community adopting a uniform platform is vulnerable to a virus, as we have witnessed during the current financial pandemic. Capital adequacy regulations should be designed to foster diversity in business models, demanding the right level of capital for the business type of the bank in question" (Sato [2009]; see also Riles [2011]). As Gordon and Mayer (2011, p. 1) noted regarding the 2008 Lehman crisis, "[O]ne saving grace . . . was that most countries in the world had not adopted state of the art, 'most advanced' regulatory and governance practices."

On these points, policymakers and academics interested in international financial regulation would most likely benefit from more active engagement with state-of-the-art international regulatory theory more generally. The inability of regulators to deliver on promises made at international forums in the face of domestic pressure from legislators or market participants is a well-documented problem in international law and institutions (Vezirgiannidou [2009]). Competition among national representatives and the lack of will for coordination among regulators—the sense of national competition that often outweighs the sense of the common good—is also a problem that repeats itself in numerous international regulatory fields. These problems have been addressed in various ways and with varying degrees of success at different periods in international legal history—from state-to-state agreements to the construction of international

16. Of course, individual jurisdictions are free to adopt higher capital requirements than those stipulated by Basel III and some are taking steps to do so. As the Vickers Report comments, however, jurisdictions that do so risk putting themselves at a disadvantage due to regulatory arbitrage (Independent Commission on Banking [2011, p. 9]).

institutions to the development of customary international law (Krisch and Kingsbury [2006]). Moreover, an extensive literature on global legal pluralism now demonstrates that legal pluralism is a given condition of transnational legality that cannot ever be eliminated. In fact, this literature demonstrates that pluralism has numerous advantages and hence must be incorporated into transnational legal governance (Michaels [2009], Berman [2009], Teubner [1997], and Radaelli and Meuwese [2009]). Hence the challenges posed by global harmonization initiatives in international financial regulation are not unique to this field. I turn now to the question of how the FSB confronts these challenges.

C. Three Key Elements of FSB Methodology

The FSB has acquired credibility as a site for coordinating financial regulatory standards and for creating soft law mechanisms to ensure compliance. However the FSB's formal legal authorities are extremely limited. Article 2 of the FSB charter grants the FSB the authority only to "assess vulnerabilities affecting the global financial system," to "promote coordination and information exchange," "monitor and advise on market developments," and "advise and monitor on best practice in meeting regulatory standards." As if to make the point absolutely clear, Article 16, the final article of the charter, states, "This Charter is not intended to create any legal rights or obligations" (Financial Stability Board [2009a]).[17]

So with these limited powers, how does the FSB tackle a coordination problem that the standard international legal tools have proven to be incapable of resolving? Its approach is innovative. It aims to address, on the one hand, the interrelated quality of domestic regulatory systems, and on the other hand, the political difficulties associated with achieving and implementing international consensus on harmonized rules (Moschella [2010]) through a new set of institutional tools borrowed directly from recent institutional innovations in the EU (Radaelli and Meuwese [2009]) and the United States. Three principal kinds of initiatives deserve attention: standard-setting projects; peer review; and cross-border, firm-specific coordination.

1. Standard setting

In theory at least, the FSB circumvents some of the problems of harmonization initiatives as embodied in standard international legal frameworks by emphasizing broad standards, "best practices," or "rules of thumb" for regulators rather than hard and specific rules.[18,19] Standards—what some commentators such as Arner and Taylor (2009, p. 7) have referred to as the FSB's "soft law approach" to contrast this architecture with rules and regulations—are seen as preferable tools of global financial regulation because they allow for pluralism (for differences in national strategy and emphasis) within a framework of certain common baselines and shared regulatory values. Standards are also viewed as more flexible than rules and hence more able to accommodate future problems that may not be foreseen at the moment of rule drafting.

17. The de Larosière report goes further and calls for reforming the FSB into a more robust institution that would more closely resemble the IMF; see also Arner and Taylor (2009).
18. The FSB charter refers five times to the purpose of the FSB as to develop or implement "standards," but makes no reference at all to "rules" or "regulations" (Financial Stability Board [2009a]).
19. Some people involved in the work of the FSB do not take the view that the FSB distinguishes between "standards" and "rules" and that it adopts a standard-setting approach rather than a rule-making approach.

This focus on standards over rules is not unique to the FSB. The June 2004 Basel II Accords were already largely principle-based agreements.[20]

Yet, in practice, these standards seem to shade into a regime that takes on more and more of the trappings of traditional international legal rules and norms (Karmel and Kelly [2008]). In the area of G-SIFIs, for example, the FSB in October 2011 promulgated what then Chairman Mario Draghi ambiguously described in his letter to the G20 prior to the Cannes Summit as "[a] new international standard—[on the resolution of financial institutions] as a point of reference for consistent reform of national resolution regimes." In this slippery language, a mere standard or "point of reference" also becomes something more than that, the basis for "consistent reform" and "a new international standard."

2. Peer review

The FSB moves beyond earlier institutions, however, with its focus on peer review. Peer review is a soft law technique for implementing harmonized regulatory standards. Countries report on their progress in implementing particular standards, and these reports are in turn evaluated by a committee of peers. The peer review technique was borrowed directly from recent institutional innovations in the EU where, as the name suggests, it was modeled on the academic practices for evaluating scholarship.[21] The secretariat engages those who fail to comply in a "confidential dialogue" that can ultimately lead to public "naming and shaming" (Walter [2010]). An FSB "scoreboard" on its website "tracks progress across the full range of reforms" (Draghi [2011, p. 3]). Redacted versions of peer review results are published on the FSB website. Beyond this, there are no clear penalties for failure to participate in the peer review process or comply with international regulatory standards.

Peer reviews are of two types: "country peer reviews" focusing on one individual country's success in implementing standards, to which countries agree to submit as a condition of their membership in the FSB, and "thematic peer reviews" focusing on one particular problem or regulatory initiative across different countries.[22] The FSB describes the procedure as follows:

> FSB peer reviews will be based on reports drafted by small teams composed of experts from FSB member jurisdictions and international bodies, supported

20. After establishing specific principles regarding requirements for capital reserves, which local regulators such as the U.S. Securities and Exchange Commission (SEC) formally integrated into national programs like the Consolidated Supervised Entities (CSE) Program, Basel II left the details of risk assessment to the individual institutions themselves (Ford [2010a]). On the wider relationship between rules and standards in regulatory practice see Kennedy (1976) and Schauer (2005).
21. The peer review process itself was first developed in the mid-17th century, when the Royal Society of London began to circulate potential journal articles among experts in the relevant field for comments on a piece's suitability and worth (Klug [1999]). By the 20th century, the practice had become widespread across academic disciplines, as publishers found that a group of independent experts with similar knowledge could provide the best judgment of a work's merit in a rapidly changing field, and further, that they were most helpful in improving the quality of a paper through comments and feedback. Like academic journals that made a practice of delegating authority to a community of practicing peers, within the realm of financial regulation, the peer review technique has been used to reimagine accountability outside the box of static compliance to authoritative rules.
22. For an example of a recently completed national peer review, see Financial Stability Board (2012a). For an example of a recently completed thematic review, see Financial Stability Board (2011a).

by the FSB Secretariat. The substantive review by peers will take place in the Standing Committee on Standards Implementation. The final responsibility for approving FSB peer reviews lies with the Plenary, as the decision-making body of the FSB. In keeping with the FSB's commitment to lead by example, peer review reports will be published, along with any commentary provided by the reviewed jurisdictions for inclusion. Following publication of the report, jurisdictions' implementation of agreed actions will be monitored by the FSB and, if implementation lags, peer pressure may be applied.[23]

The FSB's own official objectives for peer review span a number of analytically disparate purposes, from the rather benign goal of information exchange and the more interventionist goal of evaluating FSB members' adherence to their commitments, to norm building (what the FSB terms "fostering a race to the top"), to evaluating and rethinking the content of international regulatory standards and approaches themselves. The last of these is important to the peer review ideal: as NG proponents Sabel and Zeitlin explain, the peer review process creates a kind of accountability that "anticipates the transformation of rules in use" (Sabel and Zeitlin [2008]). In the future, the FSB promises even "more intense monitoring in priority areas: the Basel capital and liquidity framework; over-the-counter derivatives market reforms; compensation practices; G-SIFI policy measures; resolution frameworks; and shadow banking" (Draghi [2011, p. 3]).

FSB peer reviews are largely paper reviews in which a committee of 4–9 representatives of member jurisdictions and international organizations appointed by the FSB Standing Committee on Standards Implementation (SCSI) reviews member states' responses to a questionnaire, supplemented by other documentation such as the results of prior peer reviews or other academic or legal materials the committee may request or procure. The FSB handbook on peer review also anticipates that peer review committees would provide the public with an opportunity to comment on the review process through their website (Financial Stability Board [2011d]).

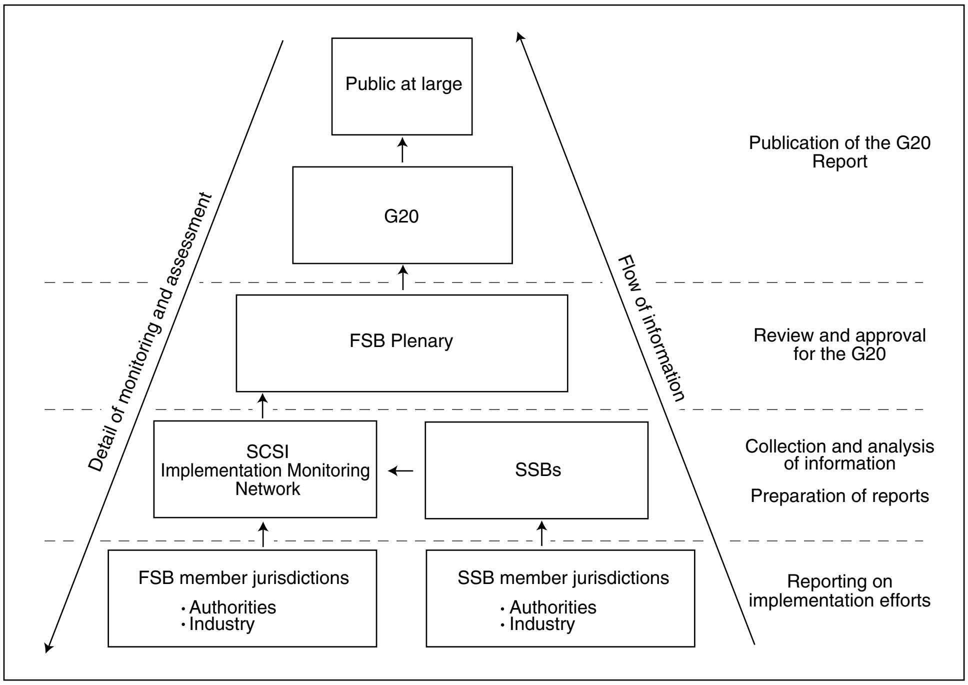
The committee then drafts a report of approximately 15 pages and submits this to the SCSI, where it is discussed (and representatives of the country under review are given an opportunity to respond). Ultimately the report is submitted to the FSB Plenary for approval and then is posted on the FSB website. An FSB diagram of this process somewhat romantically portrays an amorphous entity it terms the "public at large" as the ultimate judge and arbiter of national regulatory compliance (Figure 1).[24]

In sum, peer review as practiced by the FSB is a governance regime that carries only a possible reputational sanction. What defines this particular implementation of peer review as a mode of governance therefore is not so much the sanction as the regularized practice of periodic and extensive self-evaluation and reporting requirements. On this front, the FSB has instituted a busy schedule of self-reporting requirements whereby

23. Financial Stability Board (2010).

24. As Cristie Ford (personal comment) points out, the diagram bears an ironic resemblance to Ayres and Braithwaite's "enforcement pyramid" (Ayres and Braithwaite [1992, pp. 35–38]). The resemblance is ironic, because Ayres and Braithwaite's pyramid is intended to point out that informal sanctions are effective only in the shadow of more formal penalties for noncompliance.

Figure 1 Structure of Information Flows for G20 Reporting



Source: Financial Stability Board (2011c, p. 5).

national regulators must complete questionnaires concerning their regulatory activities and their compliance with international standards.

For example, a questionnaire developed for a thematic review on risk governance contains approximately 50 detailed questions, to be answered by already-busy national regulators in just over one month. The questionnaire is posted on the website, but responses are not made public. Although the questions are framed as merely for information-gathering purposes, many assume a clear normative framework and set of policy preferences, and the survey prompts national regulators into a kind of self-evaluation according to the policy preferences. For example, question 1.1 reads:

> Please describe your jurisdiction's overall approach to assessing firms' risk governance frameworks (e.g. legislation, regulation or supervisory guidance)? Please provide links to relevant documents. Has your jurisdiction evaluated whether such guidance is consistent with the BCBS or OECD principles on corporate governance or other recommendations provided by the industry?[25]

The message is clear. Member states should be evaluating themselves according to international standards. Regulators completing this survey may find it rather embarrassing to have to answer any part of this question in the negative. Moreover,

25. Financial Stability Board (2012c, p. 3).

"risk governance" is defined quite specifically in the questions to include the internal institutional structures in place within private firms for monitoring and managing risk, such as the competence and authority of risk management departments and the authority of boards, and also the regulatory practices for monitoring these structures. Regulators completing this survey may also find it quite uncomfortable to have to admit to their global peers that financial institutions in their jurisdiction do not have exactly this kind of organizational structure for managing risk. Hence the peer review process of answering these questions also encourages regulators to set up similar levels of review among the market participants they regulate.

3. Supervisory colleges

A third architectural innovation worthy of mention is the "supervisory colleges" aimed at the cross-border regulation of individual financial institutions and in particular the coordination of home and host regulators. Again, the model for this initiative was a similar experiment of the same name conducted by regulators in the EU (de Larosière [2009, p. 61]). The goal is to

> enhance information exchange and cooperation between supervisors to support the effective supervision of international banking groups. Colleges should enhance the mutual trust and appreciation of needs and responsibilities on which supervisory relationships are built.[26]

What is new here, from the standpoint of international law, is that regulation is not generally applicable to all, but rather is specific to a particular non-state actor: regulators convene to develop specific protocols for information sharing concerning a specific financial institution. Rules, procedures, and information sharing across borders are being developed tailored to, and applicable only to, one particular target of regulation. For example, a supervisory college concerning Citibank would assemble regulators[27] in each jurisdiction with intimate knowledge of and authority over Citibank in their jurisdiction and develop protocols for information sharing in times of crisis, build relationships among individual regulators, and devise regulatory policies, procedures, and strategies tailored to Citibank's particular situation. In the environmental or security context, in contrast, one does not create environmental regulations that apply to only one polluter or security laws that apply to only one terrorist organization (even if in practice general rules are often created in response to a specific case). Thus, the model dispenses with the traditional formal model of regulation in favor of something more pragmatic, and it also recognizes that regulation is conducted by real people—and that personal relationships among regulators are as significant a source of regulatory stability and strength as, for example, sanctions against governments for failure to share information might be.

26. Basel Committee on Banking Supervision (2010a, p. 2).

27. Ford describes the regulatory advantages of enforcement teams that are *ad hoc,* specific to the context of a firm, and flexible to the needs of the job (Ford [2005, pp. 819–821]).

D. Conclusion to Section II

In sum, the FSB responds to the challenges of an interrelated but plural global regulatory environment with some new tools and approaches borrowed largely from the European experience in coordinating among diverse regulatory authorities within the EU. These tools and approaches are not particularly legal in nature—indeed, the FSB has minimal formal legal authority over its members. They are rather pragmatic and problem-oriented. And they are sociologically and institutionally grounded: they emphasize relationships, reputations, and the gradual evolution of norms and standards through repeat encounters.

III. The New Governance Approach

Although the FSB initiatives described in the previous section eschew traditional legal approaches, therefore, they draw powerfully on one popular body of regulatory theory known as New Governance (NG). As described in this section, NG theories of the government's role in coordinating optimal regulatory outcomes developed first in the context of domestic regulatory problems as a new way of thinking about the continuing role of the state in the context of free market challenges to all forms of regulation, but they were later picked up as a tool for interstate coordination among disparate regulators and regulatory regimes in the EU in regulatory contexts other than finance such as labor and environmental standards.[28] These initiatives received enthusiastic academic attention as innovative and novel approaches to age-old problems concerning the lack of enforceability and hence "soft law" character of international law. From there, European regulators with personal experience of this model imported these methods into the FSB and other emerging nodes of contemporary global financial governance.

For NG theorists, the implicit but pervasive application of their theory by the FSB and related institutions has naturally been a source of enthusiasm and pride. In Section IV, I will evaluate the strengths and weaknesses of NG as a mode of global financial governance. However, because most financial regulators and experts in financial law are not very familiar with the NG debates that lie beneath the surface of current initiatives in their field, this section first lays out the key elements of the NG approach to regulation, its theoretical origins, and its distinctive characteristics.

A. What Is New Governance?

The term New Governance captures a variety of regulatory approaches that emphasize a shift away from traditional "command and control" regulation toward more reflexive, collaborative, and experimental forms of governance. Instead of mandating certain behavior through regulations and directives, NG regulates through "a continuous dynamic process governed by the relevant stakeholders" (Bingham [2010, p. 300]). Here, the task of government is to *coordinate* and *facilitate* collective information sharing and learning:

28. Other strands of NG techniques were developed in the United States in a variety of policy areas including environmental protection, health care, public school reform, and public housing (Karkkainen [2004, pp. 474–475]).

> [N]ew governance regulation, unlike command and control regulation, is regulation based on an iterative process between private party experience and a regulator that serves variously as clearinghouse, catalyst, monitor, prod, and coordinator.[29]

As de Búrca and Scott explain in the introduction to their collection of essays on NG in the EU and the United States,

> The concept of new governance is by no means a settled one. It is a construct which has been developed to explain a range of processes and practices that have a normative dimension but do not operate primarily or at all through the formal mechanism of traditional command-and-control type legal institutions. The language of governance rather than government in itself signals a shift away from the monopoly of traditional politico-legal institutions, and implies either the involvement of actors other than classically governmental actors, or indeed the absence of any traditional framework of government, as is the case in the European Union and in any transnational context. In a practical sense, the concept of new governance results from a sharing of experience by practitioners and scholars across a wide variety of policy domains which are quite diverse and disparate in institutional and political terms, and in terms of the concrete problem to be addressed. Yet in each case, the common features which have been identified involve a shift in emphasis away from command-and-control in favor of "regulatory" approaches which are less rigid, less prescriptive, less committed to uniform outcomes, and less hierarchical in nature.[30]

While the term has been applied to a broad range of processes and practices, according to Ford, there are three related convictions that underlie most NG strategies implemented in the EU and the United States: (1) an emphasis on "learning by doing" that includes structured learning processes which pull experience into the creation of regulation in self-reflexive ways; (2) a recognition of the necessity for regulatory revisability, as documented in practices such as notice-and-comment rules that allow quick decisions by relevant actors; and finally, (3) humility about the fact that regulators cannot know more about everyday operations than the practitioners themselves (Ford [2010a]).

1. Valuing diversity and pluralism

One classic element of the NG approach to regulation is to set broad targets and allow regulated entities to reach those targets in their own ways. As explained by de Búrca and Scott (2006),

> the idea of new or experimental governance approaches places considerable emphasis upon the accommodation and promotion of diversity, on the importance of provisionality and revisability—in terms of both problem definition and anticipated solutions—and on the goal of policy learning. New

29. Ford (2010a, p. 445).
30. de Búrca and Scott (2006, p. 2).

> governance processes generally encourage or involve the participation of affected actors (stakeholders) rather than merely representative actors, and emphasize transparency (openness as a means to information-sharing and learning), as well as ongoing evaluation and review. Rather than operating through a hierarchical structure of governmental authority, the "centre" (of a network, a regime, or other governance arrangement) may be charged with facilitating the emergence of the governance infrastructure, and with ensuring coordination or exchange as between constituent parts. A further characteristic often present in new governance processes is the voluntary or non-binding nature of the norms.[31]

2. A pragmatic approach to conflict between state and market

Another key value of the NG approach is its emphasis on experimentation and collaboration. The experimental and collaborative approach has its links to U.S. management studies, accounting techniques, theories of pedagogy, and even ethical, cultural, and religious norms, as well as to the U.S. tradition of philosophical pragmatism (Simon [2004]). However, in the United States, the more concrete impetus for this new approach to regulation lies in the search by center-left academics and policymakers in local, state, and national government for a pragmatic response to market-based critiques of the legitimacy of state regulation. On this point, the NG argument is that markets cannot always be counted on to produce the kind of efficient and welfare-maximizing coordination that neoliberals imagined would emerge through the institution of price:

> Optimal coordination will not always emerge, however, as if led "by an invisible hand." Even in settings where coordination is essential, it may fail to materialize, may emerge in a form that could have been improved upon, or may not be amenable to displacement despite the world changing around it. There consequently may be a role for regulation in encouraging, fostering, and facilitating efficient coordination [notes omitted].[32]

Yet, on the other hand, NG is not a call for a return to state control: it takes seriously neoliberal critiques of the inefficiencies and injustices of state "command and control" and therefore seeks a "third way" between free markets on the one hand and state regulation on the other. As explained by Wilkinson (2010),

> Attempting to escape from the sterility of many traditional social scientific dichotomies—state versus market, regulation versus deregulation, democracy versus expert, and technocratic governance, and so on—experimentalism draws on our potential for reconstructing and reimagining governance—both locally, and in a variety of national, transnational, supranational, and international settings—according to the generic value of self-government.[33]

31. de Búrca and Scott (2006, p. 3).
32. Ahdieh (2010, p. 581).
33. Wilkinson (2010, p. 676).

Ford puts it most powerfully:

> The challenge, then, is to imagine an alternative within which regulatory design is not always a drag on human capacity and imagination, in the way that old style non-reflexive command-and-control regulation can be, and yet that puts sufficient brakes on risk-blind hubris, socially detrimental self-aggrandizement, and predictable human flaws in decision-making and information processing.[34]

What this excursion into the political origins of the NG concept highlights is that the architecture now used by the FSB to coordinate among national regulators was developed first to address a problem in relations between *state* regulators—federal, state, or municipal government—and *private* parties that were the target of regulation. Thus, as with the EU "open method of coordination" (OMC), the deployment of NG techniques by the FSB stretches those techniques further to address the state-state relations—relations between national regulators, mediated by an international organization, and the compliance of national governments with international law.

3. Institutional roots in EU comitology

In the late 1990s, this approach was adapted by EU staff into a technocratic process for consensus-building among national regulators in particular regulatory areas known as the OMC peer review process:

> Regulation in this model begins with councils or networks of EU officials and member states that set framework goals, timetables, and metrics for gauging and comparing performance. National ministries and regulators then have the discretion to advance these goals and translate guidelines into local practice as they see fit. But they are obliged to report their performance on those metrics, to participate in peer reviews that compare how member state methods perform, and to periodically revise goals, metrics, and procedures in light of those comparisons. Again, the emphasis is to abandon fixed rules and bureaucratic enforcement in favor of local experimentation and deliberative processes that expose new possibilities and foster interactions in which states learn from, discipline, and set a continually corrected baseline for one another. . . .[35]

The OMC originated with the European Employment Strategy as defined in the Amsterdam Treaty of 1997. The initial motivation behind the OMC was the need for EU legislators to address unemployment issues in a way that accounted for national diversity in technological and industrial expertise (Trubek and Mosher [2003]). Under the OMC policy guidelines, EU member states set short- and long-term goals as well as specific quantitative and qualitative indicators or benchmarks to guide the process. These broad guidelines are then translated into national and regional policies, and periodically monitored through a peer review process organized around forms of mutual learning (Eberlein and Kerwer [2004, p.123]). Unlike more traditional governance models, the point of the OMC was not to create a single common framework, but

34. Ford (2010a, p. 447).
35. Schneiberg and Bartley (2008, p. 49).

rather to encourage experiential sharing among EU member states and to establish best practices across diverse national contexts.

By avoiding strict regulatory requirements, and instead making space for experiments that are adjusted to local situations, the OMC has allowed the EU to encourage policy improvement while fostering principle-based convergence. There is now evidence that by using targets and the peer review process, EU member states have begun to gain a better understanding about how to combat cross-border problems such as unemployment (Trubek and Mosher [2003]). Since 1997, the OCM guidelines have been applied to tackle a broad range of regulatory issues in the EU, and hence in effect have replaced the traditional one-size-fits-all central policy as the regulatory approach of choice at the EU level.

In theory at least, NG as applied by the EU represents a substantial innovation over traditional approaches to international law and institutions, as it is a practical response to the political difficulties in creating binding rules at the international level.[36] Its focus on consensus,[37] reflexivity, and discourse draws on work in international relations theory on the effect of "epistemic communities" of global actors on norm creation,[38] while its emphasis on effectuating learning across public and private divides within a particular sectoral or regulatory area evokes Anne-Marie Slaughter's work in international relations on "the disaggregated state" and the displacement of traditional states with transnational issue networks in the New World Order.[39]

4. Regulation by information

One central NG technique that is particularly prevalent in the emerging global financial governance regime is "regulation by information."[40] The FSB's "scoreboard"

36. In the United States, similar efforts have since been used to grapple with a federal system that governs policies across 50 states. Examples of the NG model in the United States include among others, the Green Building Council's Leadership in Energy and Environmental Design (LEED) standard, a voluntary certification process that has helped standardize the metrics of sustainability while reducing the ecological footprint of new construction; educational initiatives such as the No Child Left Behind Act, which creates nationwide goals and then allows states to develop localized methods for assessing school performance; and in public housing reforms such as Chicago's HOPE VI act, which replaced top-down legislation with partnerships between planners and the actual communities in need of housing projects. As argued by de Búrca (2010), these standards-based reforms represent pragmatic, participatory, and information-centric strategies that are designed to enlist states, private entities, NGOs, and other social actors in an ongoing dialogue. NG, then, aims to reshape both the means and ends of legislation.

37. The emphasis on consensus is particularly prevalent in the European versions of NG. The U.S. versions emphasize deliberation first and consensus second (Cristie Ford, personal comment).

38. For Slaughter (2005, p. 42), the Basel process is a good example of the workings of such "epistemic communities."

39. "[New Governance] rejects an image of law that is state-centered, unified, and hierarchical, underpinned by 'the rule of law' that protects individual rights, strictly separates political and legal powers and enforces a chain of governmental command through formal court-centered processes. It promotes instead an image of law that is decentered, fragmented, and heterarchical . . . " (Wilkinson [2010, pp. 673–674]).

As pointed out by de Búrca and Scott (2006, p. 5), there is considerable division of scholarly opinion about the impact of NG on traditional legal institutions, and about the normative desirability of NG tools. Some view NG as taking power and capacity away from legal institutions (de Búrca and Scott [2006, p. 5]), while for others "Law and new governance are posited as mutually interdependent and mutually sustaining. They potentially play off one another's strengths and mitigate one other's [sic] weaknesses" (de Búrca and Scott [2006, p. 6]).

40. "Regulation by information refers to an array of experiments with disclosure, rating/ranking systems, and certification or labeling initiatives. Such schemes rely on the release and dissemination of information to discipline firms and stimulate enforcement by consumers, investors, or advocacy organizations" (Schneiberg and Bartley [2008, p. 43]).

on its website, for example, regulates by publicly ranking jurisdictions and regulators according to the FSB's standards for compliance.

Regulation by information deploys certain standards or "indicators"[41] to publicly rank or comparatively evaluate countries' performance with respect to a predetermined global standard. This is regulation by information because although some indicators are used as bases for awarding benefits or penalties, "[t]he majority of prominent indicators appear to operate in global governance in even more diffuse ways than this, by influencing professional, public and political opinion to craft new approaches or take different policy orientations" (Davis, Kingsbury, and Merry [2011, p. 20]).

Because they are perceived as technical rather than political, indicators have an aura of objectivity about them. But as Davis, Kingsbury, and Merry (2011) suggest with respect to World Bank indicators,

> A particular feature of global governance indicators is the way they tacitly embody theories about both the appropriate standards against which to measure societies (or institutions) and the appropriate ways in which to measure compliance with those standards. . . . Those theories are generated through dynamic collective processes that differ in significant ways from other political processes. . . . Consequently, using any given indicator in global governance involves tacitly accepting both a very particular set of claims about the standards against which societies or institutions ought to be evaluated and a particular process for generating those claims.[42]

And yet, from NG proponents' point of view, this is very much the value of regulation by information: it turns highly politicized questions—about which it is difficult to reach global consensus—into seemingly technical problems to be delegated to experts. It trades the highly politicized processes of international negotiation for a depoliticized practice of mutual auditing in which the FSB, as a technocratic institution, borrows the characteristics and processes of the auditor: "independence from the matter being audited; technical work in the form of evidence gathering and the examination of documentation; the expression of a view based on this evidence; a clearly defined object of the audit process" (Power [1997, p. 8]).

It is important to appreciate once again that this approach to global financial governance is far more sociological in its orientation than legal. NG addresses age-old challenges of public and national law—challenges such as how to generate legitimacy for international rules and organizations, how to generate effective solutions to cross-border problems, and how to ensure that the international agreements are enforceable—largely by exerting social pressure on regulators. These sociological tools recognize that within the relatively circumscribed, club-like expert community of regulators

41. "An indicator is a named collection of rank-ordered data that purports to represent the past or projected performance of different units. The data are generated through a process that simplifies raw data about a complex social phenomenon. The data, in this simplified and processed form, are capable of being used to compare particular units of analysis (such as countries or institutions or corporations), synchronically or over time, and to evaluate their performance by reference to one or more standards" (Davis, Kingsbury, and Merry [2011, p. 5]).
42. Davis, Kingsbury, and Merry (2011, p. 4).

engaged in international financial governance activities, the club can bring considerable informal pressure to bear on any one of its own members to come into compliance with international standards.[43] As pointed out by Brummer (2012, p. 116), these pressures are experienced as quite real by many national regulators: "A regulator's record of compliance with international standards can affect its reputation, and with it, its ability to create coalitions and alliances in the future."

What is valuable about this approach is its recognition of the role of ideas, expertise, and communities of experts in producing international law (Riles [2000, 2011])—dimensions that are traditionally ignored in international legal theory. This recognition is exemplified in the FSB supervisory colleges, which assume that communities of experts can be their own basis of compliance.

One further advantage of this approach from the FSB's point of view is that it shifts much of the task of monitoring and promoting compliance onto the representatives of regulated entities themselves—onto domestic regulators in the case of the FSB. With the dramatic expansion of peer review, domestic regulators spend increasingly large amounts of time evaluating their performance relative to international standards, collecting and processing data about their performance, and communicating to real or perceived international audiences about their activities (Merry [2011, p. S88]). Over time, this activity is designed to have an impact on regulators' behavior, identity, and worldview. As noted by Dunn (2005, p. 185) in her study of an EU standards-based regulatory project, "[t]his transforms audited managers as acting subjects: they now have strong incentives to constantly monitor and discipline themselves in order to ensure that the EU's production objectives are met."

B. Addressing the Democracy Deficit

The standards for evaluating or ranking jurisdictions are often produced by "expert committees" and hence, in the NG approach, non-elected technocrats yield considerable implicit power through such instruments. As such, NG is open to standard domestic criticisms of international organizations as undemocratic and unaccountable to domestic constituencies.

But for NG proponents, one great promise of the approach is its contribution to the challenges of creating legitimacy and accountability for international institutions directed by non-elected experts. Sabel and Simon (2006) write that peer review actually provides *better* popular accountability than the traditional formal "principal-agent" model of democratic accountability (in which elected "agents" are accountable through elections to the public as "principal") because the deliberative process entailed in peer review—what they term "dynamic accountability"—actually entails a more substantive and meaningful form of accountability than formal electoral accountability:

43. As emphasized by Schneiberg and Bartley (2008, p. 49), however, NG theorists insist that NG is more than sociological coercion through shaming; it also requires some harder enforcement tools

> including the use of comparison and penalty defaults to destabilize established understandings, the fostering of common cognitive frameworks to discipline interest-based bargaining, and the leveraging of higher-order processes by specific (usually domestically based) actors. Furthermore, [NG techniques] feed into (and reflexively evaluate) conventional legislation by nation-states, further blurring lines between soft and hard law processes.

> Peer review imposes on implementing "agents" the obligation to justify the exercise of discretion they have been granted by framework-making "principals" in the light of pooled comparable experience. In peer review, the actors at all levels learn from and correct each other, thus undermining the hierarchical distinction between principals and agents and creating a form of dynamic accountability—accountability that anticipates the transformation of rules in use. . . . To put it differently, what dynamic accountability achieves is a method of controlling and checking the ability of participators to discern or distinguish the right course of action when such control cannot be hard wired into the rules of hierarchy. Within the context of the EU, multiple "agents" or the various administrative authorities responsible for implementing EU law in their respective jurisdictions can be expected to drift from the original intentions of the principal authority. However, with the peer review process, the respective administrative authorities are pushed to explain their decisions, including how specific decisions impact other agents. In this way, the peer review process opens accountability to possibilities that may have been initially overlooked by the principal.[44]

C. Conclusion to Section III

In sum, many of the core values of NG, such as fostering regulatory pluralism, mutual learning, and principled-based self-regulation rather than command and control regulation, are clearly admirable and innovative. In theory at least, NG represents a substantial innovation over traditional approaches to international law and institutions because it recognizes and addresses the political difficulties with creating binding rules at the international level.

And yet, the observations of experts in financial regulation concerning some applications of these approaches, together with social scientific and legal studies of the outcomes of NG approaches in other areas of international regulation, suggest that the reality of NG may differ somewhat from the theory. In the next section, we explore in more detail these studies and their implications for the FSB.

IV. New Governance in Practice: A Critical Appraisal

The previous section described important recent architectural innovations in international financial governance. Yet what are we to make of the following fact: despite all the framework agreements, all the peer review documents, the supervisory college meetings, and networking opportunities, many regulators confess privately to considerable skepticism about how much progress really has been made on cross-border coordination in the case of a failing G-SIFI since the 2008 Lehman crisis. The view of many regulators seems to be that if a systemically important financial institution were to fail today, the level of coordination would be relatively the same, or at best only slightly better, than at the time of the Lehman crisis.

44. Sabel and Simon (2006, p. 400). For a skeptical analysis of these claims that peer review produces deliberation and that deliberation translates into accountability, see Shapiro (2004).

This should, I believe, give us some pause. If these regulators are correct in their skepticism, then one might legitimately ask whether all this novel activity is really delivering enough added value to justify the tremendous time and expense involved. Why is there so little buy-in on the part of various domestic constituencies (Moschella [2010])—market participants, legislators, even domestic regulators—to this new approach to international governance? Does this suggest the need for any skepticism about the almost euphoric claims made on behalf of NG approaches? Surprisingly, to date no serious empirical research on this subject has been undertaken in the area of global financial regulation. The intuitive appropriateness of the NG model has more or less been taken for granted by regulators focused more on the substantive details of the policy agenda.

In the absence of such research, this section draws together what can be known about the strengths and weaknesses of the NG architecture in two ways. To begin with, NG methods were deployed in many sectors of *domestic* financial regulation prior to the crisis of 2008, and the weaknesses of these methods in the domestic context are widely appreciated. Indeed, it is the awareness of these weaknesses that spurs many efforts at more robust international financial regulation. And yet, remarkably, the same methods are now being redeployed on the terrain of transnational financial governance.

This time, the targets of regulation are not private firms but domestic regulators in FSB member jurisdictions, and it is possible that this difference somehow eliminates the problems documented in the domestic context. On the other hand, it is also possible that this difference exacerbates the problems: a review of the implementation of NG by the FSB suggests a number of ways in which in this new application NG has actually lost some of its more innovative aspects. Second, I analyze the known aspects of the FSB governance structure. Where appropriate in this section, I draw analogies to available research on the application of NG techniques in other fields of transnational regulation. This analysis suggests both some potential weaknesses of NG as an architecture of international financial governance overall, and also some possible conditions for determining when the method might be most appropriate and effective and when it might not.

A. Lessons Learned from NG in Financial Regulation Prior to 2008

Few NG experts claim any substantive knowledge of international financial regulation. The exception is Ford (2010b, 2011), whose work lies squarely at the intersection of both fields. Ford's survey of three recent examples of failure or underperformance of NG-style financial regulation prior to the financial crisis, such as principle-based regulatory approaches to shadow banking deployed by the SEC and the Basel II accords, gives us a more limited and pessimistic picture of how NG might be used in financial regulation. One example is regulators' past reliance on market participants' own risk management models to determine the nature and size of risks in the global economy. Although from a NG perspective this might have seemed like a wonderful collaborative approach to regulation, an approach that devolves authority to the market participants and enlists them in the project of governance, Ford (2010a, p. 461) concludes that "[r]egulatory faith in industry actors' competence, if not literally their bona fides, proved to have been misplaced to catastrophic effect."

From this and other examples, Ford finds a number of potential weaknesses in the NG approach, at least as it has been applied to date in real-world financial regulatory contexts. First, information-based governance relies too heavily on regulated parties for information:

> Information-based analysis and reason-giving (essential elements of new governance thinking) also seem to collapse in times of economic exuberance, when those involved are more willing to suspend disbelief. Market bubbles may also be times when regulators' budgets are under pressure, because problems are not at the forefront of peoples' minds. The duty to give reasons and explain is further hampered by extreme complexity of the sort that characterizes modern financial markets.[45]

In response, Ford (2010a, p. 444) argues "for a renewed appreciation of the amount of energy required to move people off their short-term incentives—an amount substantially greater than was put into the monitorship or principle-based regulatory initiatives . . . " She notes

> the ways in which background conditions that are either subtle or taken for granted—including lack of diversity, power imbalances, unequal access to information, and failures of transparency and accountability—have the potential to make reasonably designed regulatory initiatives ineffective, or worse. These are stories in which well-resourced actors were able to control loosely structured, fluid environments in their own interest, with minimal pushback from public-interested voices. In other words, they are situations in which our flawed humanity (tribal, short-sighted, self-interested but often irrational, and prone to satisficing) infiltrated regulatory models, reintroduced power relationships in indistinct but convincing ways, and arguably determined outcomes to a greater degree than did regulatory design.[46]

Second, the enthusiasm in the NG project for local experimentation assumes too quickly that industry representatives will make choices that are in the public interest:

> In practical terms, the "local level" in new governance regulation cannot be a black box. Moreover, we cannot presume that public-regarding or long-term thinking will automatically be produced at this level. Without a considerable oversight mechanism that tests those groups' assumptions, those groups will develop suboptimal resolutions. For example, a local level comprised of self-interested bankers cannot be counted on to self-regulate effectively where no one is acting as an active, public-regarding counterweight in their interpretive community. What this means is that we should perhaps be wary of industry efforts toward "pre-emptive self-regulation." We should not assume that

45. Ford (2010a, p. 473).
46. Ford (2010a, p. 448).

> regulators will necessarily be able to adapt measures that were initially taken to pre-empt regulation into a more consequential project.[47]

Third, the NG emphasis on coordination—with its quite benign image of the differences among interested parties—fails to fully take into account how powerful market participants may be, relative to regulators, both in terms of their influence over the political process and their ability to shape the dominant consensus about how markets should be regulated.

> Regulation cannot be understood without reference to the broader social, political and institutional contexts that contains it. Beyond pure regulatory design, the financial crisis makes clear that questions about the appropriate regulatory mix of strategies do not take place in isolation from questions of power and influence, which directly affect feasibility and effectiveness in practice.[48]

B. Practical Shortcomings in the Application of New Governance by the FSB

Ford's research highlights potential concerns about the efficacy of NG as applied prior to the 2008 crisis to public regulation of private market participants. And yet, just at the moment at which these failures are widely acknowledged, the same regulatory methods are being applied at the international level to coordination among national and international regulators. It is possible that what was less than fully successful at the national level, in the relationship among public and private actors, might succeed at the international level, in the relationship among various categories of public actors. But it seems counterintuitive to assume such success without further evaluation. Moreover, a review of the application of NG by the FSB suggests new challenges to regulatory success and ways in which some of the more innovative or hopeful dimensions of NG actually have been lost in the translation to international governance.

1. Limited participation

NG posits an expanded community of stakeholders in which regulatory legitimacy is generated by including as many possible interested parties in the process of creating and implementing standards. But the FSB remains a closed membership organization that purports to make standards that apply to non-members as well as members. Some important emerging economies, including economies that are touted as possible relocation sites for global financial institutions seeking to avoid North Atlantic regulatory burdens, do not participate in the FSB process. This poses a serious challenge to the FSB's legitimacy.[49] As noted:

> When an organization like the Basel Committee excludes a government (or many governments), it risks being viewed as an undemocratic or unrepresentative regime imposing its will on nonparticipating (and often democratic)

47. Ford (2010a, p. 471).
48. Ford (2011, p. 4).
49. The FSB has sought to respond to this challenge by establishing regional "consultative groups" that hold *ad hoc* discussions with non-member countries (Financial Stability Board [2012b]).

> governments. . . . The very credibility of its standards may consequently be undermined because of the regulatory environment in which it was created, whatever its technocratic merits.[50]

Likewise, the NG approach imagines collective governance in which all viewpoints are heard and coordinated. Yet at the FSB, although decisions are made by consensus, in practice some members have considerably more authority than others with more representatives in the FSB Plenary.[51] At the individual committees in which important policies are often debated and drafted, the representation of North Atlantic regulators on FSB and Basel committees—both as committee members and committee chairs—is still unduly large in relation to these economies' global market share.

2. Limited public-private coordination

As described above, one of the central innovations of NG was its emphasis on new forms of collaboration between public and private actors that would go beyond the antagonistic relations between regulators and market participants posited by both free market and welfare state models of state-market relations. So far, however, this collaborative approach has not been operationalized in the FSB process. This process has mainly engaged representatives of governments and international bureaucracies, and private parties participate only through more attenuated opportunities for public comment.

This exclusion of private actors is unfortunate, because it fails to recognize the practical authority of organizations such as the International Swaps and Derivatives Association in constructing their own forms of international financial governance beyond the state (Riles [2011], Brummer [2012, p. 4], and Teubner [1997]). There are signs that the FSB recognizes this problem and plans to address it. Most recently, the FSB began reaching out more actively to private-sector organizations and market participants.[52] Yet such initiatives remain in the embryonic stage.

3. Standards slide into rules

Another innovative aspect of NG theory was its emphasis on governance through broad standards rather than rules. One advantage of standards, as seen in Section III, is that they aim to encourage local experimentation and a plurality of approaches rather than hard and fast rules that demand compliance. Another advantage of standards over rules in financial governance in particular is that rules predominantly monitor and punish conduct *ex post*, in contrast to principle-based regulation, which is more *ex ante* in style. In practice, however, the FSB regime is increasingly rule-oriented rather than standards-oriented and this leads to a number of problems. Although it speaks in the language of standards, the FSB increasingly is creating what are functional rules.

50. Brummer (2012).
51. A list of the representatives of each country is available at http://www.financialstabilityboard.org/about/plenary.pdf.
52. For example, a "roundtable on risk disclosures by financial institutions [aimed] to encourage the private sector to jointly take forward development of principles and of leading practice disclosures that will be relevant and informative given current market conditions and risks." The FSB plans to create a joint public-private task force on risk disclosure that will engage both with market participants and with other standard-setting national and international organizations "to develop principles for improved disclosures" (Financial Stability Board [2012b]).

One of the problems with rule-based governance—precisely the problem NG sought to address—is that rules can easily be diluted or ignored altogether at the national implementation phase and hence rules impose weighty compliance monitoring costs on regulators. For example, Basel II was never implemented in the United States at all and was only implemented in Europe just before the 2008 financial crisis. Despite the fiercely committal language in FSB reports and communiqués, the FSB lacks any formal power to hold member states to any of the agreements they have made at the international level. This fact has led one Chinese commentator to dismiss the organization as a "talking shop" (Ojo [2011]).

As is well documented in the context of the EU experience with NG techniques in the context of the OMC, another problem with rules is that they encourage private actors to "game" the system or develop other forms of resistance to the regime (Power [1997], Dunn [2005], and Merry [2011, p. S90]). This was also the global experience with capital adequacy standards under Basel II, where market participants devised all kinds of financial products and accounting methods to "game" the regulatory standards.

In theory, peer review is meant to address this problem of noncompliance. Yet in practice, peer review also has its limits. First, participation in it is still largely voluntary in many practical respects. Although the FSB charter states that peer review is a requirement of membership, the FSB peer review handbook acknowledges that volunteers will be taken first and in practice to date country peer reviews have been limited to volunteers (Financial Stability Board [2011d]):

> Not only is peer review monitoring far from comprehensive, but the information generated through monitoring is often not shared with the broader international regulatory community or market participants. And even when information is shared, it often goes unused due to the complex format through which it is disseminated. As a result, the risk-adjusted cost of defection can be low, increasing the likelihood of noncompliance when significant distributional tradeoffs arise.[53]

The problems the FSB is now encountering with peer review are replicated in the EU experience with OMC as well. According to the European Commission's own 2008 assessment of the impact of the OMC:

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53. Brummer (2011, pp. 263–264). Brummer's review of the IMF's Financial Sector Assessment Program, which is more established and arguably more rigorous than the FSB's own peer review process, concludes that "despite its importance, the architecture supporting monitoring has historically been quite weak, even with regard to the primary monitoring system—FSAP" (Brummer [2012, p. 157]). In particular, he identifies three key problems.
    (1) Participation is in practice less than compulsory and many countries do not in fact participate. This creates an "adverse selection problem" in which those countries that choose to participate are in practice those with the less serious regulatory problems (Brummer [2011, p. 159]).
    (2) The information used in peer review is provided by member states under review and hence is open to all kinds of bias, incompleteness, or error (Brummer [2011, p. 160]). Note that the FSB is just beginning to attempt to address this problem in a small way by creating more uniform standards for data collection and reporting as concerns linkages among SIFIs in particular, but this also requires mandating that private firms collect data in certain forms and certain kinds of data they may not have collected in the past (Financial Stability Board [2011b]).
    (3) Results of peer review have not been made public sufficiently (Brummer [2011, p. 161]). This is arguably less of a problem in the case of the FSB, which at least releases a redacted version of each peer review report on its website.

> Delivery on the common objectives has been too slow or insufficient . . . there is a widespread consensus that the potential of the Social OMC remains largely unexploited, that a number of weaknesses should be corrected and that strategic reinforcement of the method would go some way towards improving delivery on the common objectives. The analysis points to a lack of political commitment and visibility and a need for better horizontal policy coordination and mainstreaming of social protection and social inclusion concerns in all relevant policy areas.[54]

4. Pluralism slides into harmonization

A related innovation of the NG approach was its emphasis on regulatory pluralism rather than a demand for a single universal regulatory standard. Although this ideal was also central to the FSB's mandate and reflected in the language of "standard setting" rather than "rule making," in practice the FSB is moving toward greater emphasis on securing compliance with harmonized rules and practices than the promotion of regulatory pluralism.[55] Consider, for example, the following official explanation of the new FSB standards on SIFIs that describes a harmonization project rather than a pluralistic project. According to then Chairman Draghi, the new standards were

> designed to address gaps in legal frameworks and tools for effective intervention in failing systemic firms, including those that operate in multiple jurisdictions, and to remove impediments under existing national law to cross-border resolution. Their implementation will require legislative changes in many jurisdictions.[56]

As one FSB report explains, likewise, peer reviews are now "focused on the implementation and effectiveness of international financial standards and of policies agreed upon within the FSB" (Financial Stability Board [2010, p. 3]). This drift away from original commitments to pluralism and toward greater insistence on harmonization has been observed in the context of NG regulation in the EU also.[57]

5. Problems with the sociological approach

One innovation of NG, as we saw, is its emphasis on sociological rather than legal tools for achieving outcomes. Some observers query, however, whether—in the case of international financial regulation—a community of regulators who are collectively committed to careful deliberation and individually susceptible to group pressure when they fail to meet international targets is in fact so easily achieved. Verdier points out that the fantasy of a community of cosmopolitan regulators is not borne out in practice:

54. Greer (2011, p. 196), quoting European Commission (2008) 2170, p. 2.
55. As argued by Slaughter (2005, p. 59), harmonization goals are far more nationally suspect and hence to the extent that the FSB becomes what she terms a "harmonization network" it can expect greater degrees of domestic criticism.
56. Draghi (2011).
57. Dunn (2005) argues, for the context of EU food safety standards, that when coupled with NG "audit technologies" such as self-reporting mechanisms, this drift toward harmonized standards has unintended detrimental effects on the internal character of local institutions—leading to pressures for jurisdictions to abandon differences and conform to a homogeneous model—that go far beyond the kinds of local change envisioned by traditional international legal harmonization projects or indeed the defensible objectives of regulatory policy.

"national regulators are tied to domestic constituencies by incentives and accountability structures that are much stronger than their links to any 'hypothetical global polity'" (Verdier [2009, p. 115]). Brummer argues that the NG model, with its happy image of a community of expert peers, ignores the fact that the dominant modality of interaction is not a "coordination problem," in which regulators share the same basic preferences for regulatory standards, but rather competition. "Regulators, in short, do not always share the same policy preferences. Some policy options will, for example, cost more for some countries than for others. Due to diversity in history, culture, and custom, countries have vastly different starting points as far as what kinds of regulations are already in place" (Brummer [2011, pp. 269–270]). Shapiro likewise argues:

> There are a number of reasons to be agnostic if not atheistic about deliberation. Most fundamentally, there is little reason to believe that people with substantial, long-term, material interests in achieving a particular outcome are going to abandon those interests and their dedication to those outcomes as sweet reason emerges from the talk fest.[58]

6. Learning slides into surveillance

And these limitations to deliberation lead to another problem. One of the greatest values of NG tools such as peer review is the opportunity they provide for comparison and learning.[59] Although proponents of NG promote peer review as a tool for reflexive learning, in practice peer review often slips into a tool of surveillance in which participants evaluate themselves and submit to evaluation according to how closely they conform to a given standard and there is relatively little opportunity to deliberate about the appropriateness of the standard in the first place. Although in theory NG supports a plurality of regulatory approaches, often it is used more to monitor and self-monitor according to a predetermined policy or institutional choice.

The FSB risk governance peer review questionnaire (Financial Stability Board [2012c]) provides a good example of this problem in practice. The questionnaire acknowledges that there is no clear international standard regarding proper procedures for risk governance and that the purpose of the review is to evolve toward consensus concerning a standard. Thus, it would seem to be a natural vehicle for deliberation and consultation. However, the specific questions posed to regulators presuppose an answer as to what the international standard for risk governance should be. For example, the questionnaire introduces the concept of a "risk committee" as "a specialised Board committee responsible for advising the Board on the firm's overall current and future risk appetite and strategy, and for overseeing senior management's implementation

58. Shapiro (2004, p. 350).

59. The opportunity for developing best practices through comparison to others is part of the underlying self-justification of NG. As noted by de Búrca and Walker (2007, p. 536), NG

> speaks to the close tracing of particular interests allowed by the timely adjustment of shifting preferences in local contexts of practice, the epistemic premium of continuously developing and refining best practice, the dignity and compliance-value of participation and negotiated settlement, and the competitive dividend and diversity-respecting importance of the coexistence and coalition of differentiated frameworks of regulation.

of that strategy"—clearly one very particular possible institutional form of risk management among all possible forms. Rather than ask about other possible institutional forms or policy solutions that might serve similar functions in different jurisdictions, the questionnaire goes on to ask, "Do supervisory requirements or expectations exist concerning the role and responsibilities of the risk committee?"—thus assuming that such committee should exist and should be supervised. In this way, the questionnaire becomes a tool of surveillance rather than a tool of deliberation, and a tool for promoting adherence to one specific regulatory response to risk as the new harmonized global standard rather than a tool for coordinating among pluralistic regimes.

When tools for learning become tools of surveillance, then the comparison conducted through peer review remains relatively superficial and opportunities for learning are lost. Equally importantly, the unexamined common sense solutions found in jurisdictions that exercise larger influence at the FSB secretariat continue to dominate to the exclusion of other possibilities and at a cost to the international legitimacy of the organization as a whole. If Sabel and Simon (2006) claim that the deliberative dimension of NG is key to overcoming the democracy deficit in administrative law at the national and international level, then the converse is also true—a failure of deliberation and the transformation of NG instruments into tools of surveillance exacerbates the problems of democratic accountability many commentators see in a process by which a small group of non-elected experts hailing disproportionately from certain geographical areas makes international rules for the rest of the world.

7. Audit culture

Finally, although some Basel negotiators suggest that there are contexts in which NG tools can be effective means of learning and consensus building—that is, that they can be used as opportunities to educate a wider audience of global regulators about the particular conditions of national markets, and also as opportunities to learn more about conditions of other markets that may impede regulatory harmonization—many regulators suggest a degree of frustration with the volume of paperwork produced by NG initiatives, and a concern that the time demands of these assignments do not produce sufficient practical rewards.

Given the sheer volume of new governance activity, this criticism needs to be taken seriously. In an era of seriously curtailed government budgets, time spent on peer review, on international meetings, and on information exchange is time that is not available for other regulatory initiatives. The FSB estimates that each member of a peer review committee should expect to spend the full-time equivalent of approximately six weeks on this work, and while the FSB (interestingly) does not estimate the time costs of such activity to the members under review, one can assume it is at least comparable. Furthermore, many of these reviews in turn make requests for information that place demands on market participants, and these demands have also mushroomed to the point at which risk management staff in some banks claim to spend almost half of their time responding to regulators' requests for information—often so that such information can in turn be passed on to international organizations.

Social scientists have begun to explore the real costs on institutional cultures of "audit cultures" or "audit societies"—governance systems rooted principally in self-reporting strategies. These costs include lost labor resources devoted to wasted reporting efforts, but they also include other problems such as information overload, "anxious preoccupation with how one is seen by others," and an erosion of trust within institutions (Power [1997]; see also Shore [2008])—precisely the opposite of what the FSB seeks to achieve through NG strategies.

The reasons why such processes may begin to seem like "paperwork" rather than true exercises in deliberation relate once again to how these tools become standardized and institutionalized into fairly rigid models. When faced with a questionnaire that asks questions that do not fit the local context, for example, there is little space within the form to explain why the question is not the right one to ask in the first place. This suggests that at a minimum more attention needs to be paid to designing a peer review and self-monitoring process which fosters meaningful dialogue and deliberation by making room for respondents to challenge the terms of the question or the assumptions behind the review itself.

V. Conclusion

The attention of policymakers, market participants, and many of their interlocutors in academia has focused, naturally enough, on the details of particular policy initiatives of the moment without much regard for the greater sum of the regulatory parts. Yet individual policies take shape and come to be implemented within particular regulatory architectures.[60] The predominant architecture deployed by the FSB—the NG architecture—may have been chosen largely by default, and perhaps without sufficient critical analysis or empirical study. The summary of the history of the NG approach in Section III suggests that this lack of reflection is perhaps due to the influence of Europeans and Americans on G20 reforms after the crisis of 2008 and culminating in the relaunch of the FSB. In Europe and the United States, NG techniques have generated considerable excitement in academic and policy circles from the late 1990s up to the present.

However, recent coordination challenges surrounding financial regulation in the EU that surfaced in the past year, together with the weaknesses of the U.S. collaborative approach to regulation demonstrated by the financial crisis of 2008, suggest that at a minimum this model should not be adopted without reflection. The aim of this paper therefore, has been to initiate a debate about the range of available approaches, and the

60. Pan (2010, pp. 245–247) argues that the fragility of the G20 "network" approach to financial governance should be apparent from the last financial crisis:

> International law scholars frequently noted that the international financial architecture relied to a great extent on informal transgovernmental networks as opposed to formal international organizations or other treaty-based mechanisms. Thus, the international financial architecture appeared to provide convincing empirical support for such scholars' claims about the effectiveness of transgovernmental networks in promoting regulatory cooperation among states. In fact, the international financial architecture proved incapable of preventing or managing the causes and effects of the recent financial crisis. . . . The failure of states to provide for an international legal regime capable of conducting prudential supervision of cross-border financial institutions proved to be one of the reasons why the international financial architecture was unable to prevent financial instability in the US from becoming a global financial crisis.

strengths and weaknesses of each, in international financial regulation to be deployed by the FSB in particular as it addresses the challenges of G-SIFIs.

Although the NG model deployed by the FSB has solid theoretical foundations and much promise, in its application there are signs of potential pitfalls. This would suggest that regardless of how seductive NG is in theory, we should not assume that it is always the best approach to coordinating among interconnected but pluralistic regulatory regimes in the international financial system without the benefit of further research into the precise conditions in which it furthers goals of regulatory coordination while preserving diversity and promoting legitimacy, and those in which it does not.

Thus, a preliminary hypothesis for future research emerges from this analysis: NG mechanisms may be effective in resolving *some* kinds of problems caused by the interrelationship of legal regimes in a pluralistic regulatory order, but they are unlikely to be suitable to *all* problems. This is, at the very least, a robust international financial governance structure necessitates some other kinds of international legal arrangements alongside NG mechanisms. This hypothesis merits empirical study, and also suggests the need for debate about the full range of possible legal alternatives for a global financial architecture. In short, the general validity of the NG model should not simply be accepted as an untested and unchallenged article of faith.

A. Possible Avenues for Reform

Although we lack sufficient information about current conditions to make firm recommendations, the research into uses of NG techniques in other international institutional contexts, together with lessons learned from the application of NG techniques by national regulators to domestic financial markets, does suggest on a preliminary basis that a number of reforms of or limitations on NG mechanisms might improve their efficacy. These comparative insights provide us with initial hypotheses concerning which reforms or limitations on the NG model for the FSB might be worth pursuing. These include the following.

1. A more inclusive process

Why do market participants remain so skeptical of the relatively modest reform proposals embodied in Basel III? Why do domestic politicians in many countries fail to throw their support behind international regulatory initiatives? Perhaps more attention deserves to be paid to the form through which consensus about such reform initiatives as capital adequacy requirements for G-SIFIs is reached in the first place (Moschella [2010]). Market participants point out that they have very few opportunities even to learn about negotiations at the FSB, let alone to participate in them meaningfully, until after the agreement is complete.[61] While the FSB rule-making procedure allows for a public comment period, market participants argue that the process by which these comments are actually taken into account is opaque and that they have little sense of whether their comments have any impact on outcomes at all. The same is largely true of domestic legislators. Their involvement in the international consensus is often limited to approving or rejecting agreements negotiated by regulators after the fact. In particular, further comparative research needs to be conducted on the consequences

61. In the view of Brummer (2012, p. 198), "the G-20 and the FSB have been relative laggards regarding accountability. Indeed, only the FSB has circulated consultative papers, and thus far has done so only rarely."

of variations in national processes for participating in international regulatory coordination. Some countries, including the United States, make relatively greater room for the involvement of political branches, while the negotiation process in other countries allows for less political involvement. Likewise, some regulators obtain feedback from market participants through more formal notice and comment procedures while others have greater access to informal channels. It may be that such differences correlate with differing degrees of support for international regulation in different countries.

One of the lessons of recent innovations in international law and institutions is that bringing a wider range of actors into the negotiation process, while time consuming and messy, creates far greater success at the implementation stage. Those who participate in international negotiations are more committed to seeing the results of the negotiations bear fruit than those who do not have a chance to participate. One early example of the use of soft law techniques to create global consensus was the United Nations World Conference model, in which national delegations were expected to include representatives from a wide range of government and nongovernmental organizations (NGOs), and in which virtually any legitimate NGO was allowed to participate as an observer to the process (Riles [2000]). While such conferences were originally viewed as lesser forms of international law making than traditional closed-door treaty-making negotiations among state representatives, in practice they have proven to be quite successful in generating broad and deep consensus for reform in individual nations on difficult social topics. These conferences serve important pedagogical and political functions, in addition to their legal function.

Of course, it may not be possible to open up the financial regulatory process to this extent. Financial governance differs from governance areas such as the environment, safety standards labor rights, human rights, and even international trade in the sense that NGOs are by and large industry organizations with budgets that dwarf those of national regulators, and with track records of favoring their own narrowly defined short-term interest at the expense of larger and longer-term interests (McDonnell and Schwarcz [2011, pp. 1643–1644]). Many national regulators express the need for a space for discussion and coordination away from the political pressures they experience from market participants in which to construct rules that serve the wider social good. Regulators involved in the FSB rule-making process have concerns about the impact of openness on the ability to reach consensus, on how confidential information can be shared, and even on potential questions of sovereignty and national security of opening this process to a wider range of public and private actors (Jones [2010]). From the viewpoint of many participants in G20 processes, the consensus-making process is complicated sufficiently at the moment by the rapid increase in member states. Conversely, the civil society groups that do express an interest in financial regulation seem, from the regulators' point of view, to engage in unhelpful populist bashing of financial institutions, making it difficult to bring them into the expert discourse (Kelly [2011]). While these are legitimate concerns, the exclusion of the full range of interested parties from the negotiations creates its own practical costs as well as challenges to the legitimacy of the consensus reached through NG methods (Nickel [2006]).

There is yet another reason to favor openness in the FSB process. As Ford points out, one of the lessons of the failures of NG techniques in financial regulation prior to the crisis of 2008 is that

> the development of active contestation and deliberation within new governance structures cannot be presumed. It must be fostered, ensured, and protected. Reason-giving, problem identification, and careful problem-solving techniques tend to collapse when everyone's interests are aligned.[62]

This suggests that a broader and more diverse FSB membership perhaps could be a benefit rather than a burden to better governance by helping to preserve the plurality and diversity of views that is vital to the success of NG techniques. Ironically the premise of NG—that through such techniques a broad base of stakeholders can and should be enrolled in decision-making processes—has been sidelined as NG has been translated into an international regulatory structure at the FSB.

2. Better procedural regulation of NG processes

We saw that although the ideals behind NG are often laudable, the implementation can stray far from these ideals. We also saw that NG processes impose substantial burdens on national regulators and on the private sector. Finally, we saw that there are increasing concerns about the legitimacy of the authority of a small group of technocrats at the FSB secretariat and of small, unelected subcommittees of the FSB Plenary that are quickly becoming one of the most powerful agents of global financial regulation.

Concerns about similar processes in other international institutional contexts have led legal scholars to ask whether this explosion of law making within international technocratic organizations should not be subject to greater procedural safeguards, just as the rule of law requires subjecting domestic administrative agencies to procedural safeguards. Benedict Kingsbury and his colleagues in the Global Administrative Law Project at the New York University School of Law have identified this "accountability deficit" as a primary target for international legal reform across numerous policy areas.[63]

These safeguards could include, for example greater disclosure about the positions national representatives take at international meetings,[64] and more detailed rules concerning the process of agreement at meetings and the process of producing and evaluating peer review reports that would constrain civil servants' discretion and provide greater opportunities for input from a wider range of participants, more detailed rules concerning standards of proof and evaluation in reaching conclusions, and opportunities for some higher or alternative level of appeal for review of FSB procedures. The FSB handbook on peer review takes a first step in this direction. It asserts that

62. Ford (2010a, p. 486).
63. These developments lead us to define global administrative law as comprising the mechanisms, principles, practices, and supporting social understandings that promote or otherwise affect the accountability of global administrative bodies, in particular in ensuring they meet adequate standards of transparency, participation, reasoned decision, and legality, and by providing effective review of the rules and decisions they make (Krisch and Kingsbury [2006]).
64. Slaughter (2005, pp. 222–223) argues that "public activists must seek to extend US domestic procedural guarantees to transgovernmental activity. . . . In practice, this means requiring regulators seeking to develop US positions at harmonization talks . . . to create a record of all their actions; this record would then be subject to notice-and-comment rule making, allowing all interested members of the public full input."

"FSB peer reviews will follow objective and transparent procedures. The results of the peer review, including any assessments on which it is based, will be published to promote greater transparency by all member jurisdiction" (Financial Stability Board [2011d, p. 3]). The procedures in the handbook remain quite general, however.

3. More narrowly tailored assessment tools

Comparative research in other fields suggests that NG methods are most effective when the problem they seek to address is very narrowly tailored. In such cases, peer review can be more focused, and discussions in supervisory colleges can be more specific and meaningful. As Greer concludes in his survey of the EU experience with OMC in the health safety field:

> In principle, this kind of more specific sectoral initiative can surmount the three obvious problems of the OMC in health: its broad system-level focus, the tendency for OMC work to concentrate in health ministries' international rather than line divisions, and the ease with which comparative health indicators can always be discredited. By drawing on smaller networks with clearer preferences, more specific data concerns, greater lobby support, and professional engagement, it can create coordination and rulemaking where there were only informal shared ideas.[65]

4. Greater resources for monitoring and deliberation activities

Finally, many of the problems associated with implementing NG ideals stem from lack of adequate resources. As Ford suggests, regarding national regulation,

> principles-based regulation may be more "hands-off" in its approach to the procedural details, but this does not mean that it requires fewer regulatory resources. Principles-based regulation may actually require intensive interaction with firms, at least around certain issues or situations. It means having an adequate number of staff, and giving regulators the ability to obtain transparent and reliable information from and about industry. It requires that regulators have and use robust investigatory powers where necessary, conduct regular and adequate compliance audits, and possess the quantitative expertise and relevant experience to independently scrutinize information.[66]

Likewise, at the international level, the FSB would also need greater resources for monitoring and deliberation activities to implement a principle-based regulatory regime.

B. Recommendation

The recommendation is to mount a cross-disciplinary, cross-jurisdictional research project aimed at evaluating the strengths and weaknesses of the FSB experience with NG methodologies to date and at identifying the conditions under which these methodologies are successful and those in which they require supplementation with other methods.

65. Greer (2011, p. 198).
66. Ford (2011); see also Ford (2010a).

What is needed now is a detailed study, based upon several case studies of particular specific regulatory or compliance initiatives, that would provide a detailed, empirical picture of how NG methodologies are currently being used both from the point of view of the FSB secretariat and committee structures and from the point of view of national bureaucracies and national interest groups in several representative jurisdictions. The focus should be on the micro-processes by which consensus over compliance is or is not reached. Research should seek to describe the governance process from various players' points of view, including civil servants, domestic legislatures, executive branch political leaders, and market participants to consider how a device such as peer review might be effective in generating consensus with some constituencies but ineffective with others. The few studies we have suggest that the process of reaching consensus between peer review committees and regulated states is a far more complex process than the official procedures suggest and that there is some room for variation and contestation.[67] The emphasis should be on the relationship between these micro-processes and "issues of implementation, effectiveness, and local impact" across different jurisdictions with different market challenges and regulatory approaches. This requires a detailed objective picture of the social and institutional processes at work in regulatory technologies such as peer review, standards making, and supervisory colleges. What is the experience of regulation by those who are subject to these processes, and how does it shape their behavior? How do these practices alter or realign existing power dynamics in the market, and among nations? Under what precise conditions are such practices effective, and when are they ineffective?

Since the very problem to be studied is the efficacy of questionnaire and committee-based information gathering processes, this study cannot rely entirely on such processes. Rather, what is needed is a combination of observational and interview-based methods. On the basis of this empirical information, it will be possible to determine when NG techniques are the ideal governance tools in international financial governance and when they should be supplemented with other kinds of governance tools.

67. In his study of the work of expert committees at the IMF, Harper (2000, p. 45) calls this relationship between international and national actors "paternalism without power."

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