# 1 Crisis and the Reform of International Financial Regulation[1]

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What began in the summer of 2007 as a problem in a relatively unknown segment of the US housing finance market has very quickly turned into the most severe global financial crisis since the 1930s. The impact of this crisis has escalated far beyond its point of origin, affecting countries around the world, and spilling over from the financial system into the real economy. The implications of this shock are wide-ranging and still difficult to fully understand. In this volume, we explore one of the most important consequences so far: the influence of the crisis on the international regulation of financial markets.

The severity of the global financial crisis has revealed major weaknesses in the international architecture for prudential financial regulation that has been constructed since the mid-1970s.[2] Policymakers have responded with a flurry of ambitious initiatives to reform international standards and strengthen the international financial regulatory regime. How has international financial regulation changed in response to the crisis to date? What explains the blitz of international regulatory initiatives we have witnessed to date in response to this crisis? Are we witnessing an important turning in the regulation of global finance?

This volume brings together scholars of the politics of international financial regulation to address these questions from a number of different perspectives. The first section of the book analyzes change across a number of sectors of global finance, including the regulation of banks, credit rating agencies, accountancy, hedge funds, and derivatives. The second section examines the international regulatory response from the vantage point of key powers in global finance in Europe, the US and Asia. The contributors to both sections also embrace a number of distinct theoretical approaches for understanding international financial regulatory change. Taken together, the book presents the first detailed political analysis of the international regulatory response to the global financial crisis which started in 2007.

We begin this introductory chapter by describing in broad brush strokes three key patterns of international regulatory change witnessed so far in response to the crisis: i) an expansion of the perimeter of international regulation, ii) efforts to strengthen its institutional architecture, and iii) a departure from a trend over the past decade or so of delegating regulatory and supervisory responsibilities to private market actors. We then outline three distinct analytical lenses which the contributors to this volume use to explain these international regulatory changes: inter-state power domestic politics, and transnationalism. We conclude by outlining the disagreement among the authors about the broader significance of the international regulatory initiatives launched so far.

## WHAT HAS CHANGED?

How has international financial regulation changed in response to the crisis to date? To answer this question, it is helpful to first review the evolution of international regulation from the mid-

1970s up until the current crisis. There was no founding act setting the basis for the existing international prudential regulatory architecture; it evolved instead in an incremental and ad hoc manner, and usually in response to various crises. The story of this evolution has been told expertly elsewhere and we will not repeat it here (see for example Davis and Green 2008). Instead, our objective is to summarize three key themes of the story in order to establish benchmarks against which to measure change since the current crisis began.

**Evolution from the Mid-1970s to the Current Crisis**

The first theme has been a gradual expansion in the range of issues covered by the international financial regulatory regime. International regulatory coordination first took place in the banking sector in mid-1970s through the creation of a committee of national banking supervisors that came to be called Basel Committee on Banking Supervision (BCBS). After formalizing the division of responsibilities in the supervision of international banks in the 1975 Basel Concordat, the BCBS created the Basel Capital Adequacy Accord of 1988 (Basel I) to define minimum capital standards for international banks, and then updated it between 1998-2004 (Basel II). Regulatory coordination soon extended to securities markets and related sectors such as credit rating agencies via the International Organization of Securities Commissions (IOSCO) created in 1983, as well as to insurance markets via the International Association of Insurance Supervisors (IAIS) created in 1994. In 1990, central banks of the same G10 countries that constituted the membership of the Basel Committee also created the Committee on Payment and Settlement Systems (CPSS) which produced some core principles for "systematically important payments systems" as well as (jointly with IOSCO) for securities settlements systems and central counterparties.

In the wake of the international financial crises of the late 1990s, the perimeter of the prudential financial regulation expanded further to include corporate governance, accounting, and auditing standards. The Organisation for Economic Cooperation and Development (OECD) drafted in 1999 its "Principles of Corporate Governance". In the accounting sphere, the International Accounting Standards Board (IASB) – a private body created in 2001 - established the International Financial Reporting Standards (IFRS) that have been now been embraced by over 100 countries, including the European Union (since 2005) and increasingly the US. Another private sector body – the International Auditing and Assurance Standards Board (IAASB) – emerged as the most relevant standard-setter in the auditing sphere. The standards of these three bodies – as well as those of the BCBS, IOSCO, IAIS, and CPSS – were increasingly promoted across the world by the G7 and international financial institutions after the late 1990s.

A second important theme in the evolution of the international prudential regulation has been that the setting of these standards has taken place in a relatively fragmented, weak, and exclusive institutional context. While postwar multilateral trade negotiations have been conducted under the single framework of the GATT/WTO, international financial regulation developed within the much more fragmented alphabet soup of institutions noted above. To be sure, there were some efforts to address the fragmentation before the current crisis. In 1996, the BCBS, IAIS and IOSCO created the "Joint Forum" to discuss issues of overlapping concern across banking, insurance and securities markets. Three years later, the Financial Stability Forum (FSF) was created to bring together in one place for the first time all the relevant international standard setters (the BCBS, IAIS, IOSCO, IASB, CPSS), international economic organizations (the IMF, WB, OECD, BIS, the ECB, the Committee on the Global Financial System), as well as key national financial authorities. The Bank for International Settlements (BIS) has also played an increasingly central position within the patchwork of sectoral regulatory bodies, housing the BCBS, the IAIS, the CPSS, the Joint Forum, and the FSF. Despite these developments, the fragmentation of the institutional context of international financial regulation remained considerable.

The international financial regulatory regime also lacked supranational institutions with the kind of power that the WTO has. Proposals to create such institutions have been consistently rejected by policymakers in favour of international institutions whose formal roles are confined primarily to facilitating networks of informal cooperation, information-sharing and consensus formation. The implementation of financial regulation and supervision continues to be firmly located at the national level, with most international financial regulatory agreements simply taking the forms of "best practice" standards, "memorandum of understanding", general "framework" and "principles" which are not legally binding between regulators, do not require ratification by legislatures, and allow significant flexibility of implementation at the national level (see for example Kahler and Lake 2009). While the trade regime has been characterized by a trend towards greater "legalization" since the Uruguay Round, international financial regulatory agreements remain examples of "soft law" – with the important exception of financial regulation within the European Union (Goldstein, Kahler, Keohane and Slaughter 2000; Singer 2007: 9-10).[3]

International financial regulation has also been developed in an institutional context which has also been more exclusive than that for international trade. To be sure, some of the international financial standard-setters, such as IOSCO, have a broad country membership which comes close to matching the WTO's. But others, such as the BCBS, CPSS, and FSF, were very narrowly constituted before the current crisis. Despite the adoption of its standards around the world, the BCBS included only industrialized countries as of 2007: the G7 countries plus Benelux, Spain, Sweden, and Switzerland. The CPSS's membership was restricted to the G7 countries, Belgium, the Netherlands, Singapore, Hong Kong, Sweden and Switzerland, while the FSF included just the G7 countries, Australia, Hong Kong, the Netherlands, Singapore, and Switzerland. Even within the more widely representative IOSCO, the key regulatory initiatives stem from its Technical Committee that had members from only the G7 countries, Australia, Hong Kong, Mexico, the Netherlands, Spain, and Switzerland. In short, the financial regulatory regime remained characterized by a clear distinction between "rule-takers" and "rule-makers".

The third important theme in the evolution of the international prudential regulation relates to a change in its content in the decade or so before the current crisis: the assignment to private market actors of an increasingly significant role in the regulation and supervision of financial markets. In some contexts, this trend manifested itself through the endorsement and legitimization by the FSF and G7 of standards set by private actors, such as the accounting and auditing standards drafted respectively by the IASB and IAASB, or the codes of best practices for the hedge fund industry set by hedge fund managers' groups. Another manifestation was that regulators began to shift part of the responsibility for monitoring markets into the hands of private investors themselves by requesting private and public actors to publicly disclose more information regarding their activities. The Basel II agreement even elevated this “market discipline” to one of its three pillars of regulation, alongside formal capital requirements and supervision. That agreement also allowed large banks to use their own information and risk-management schemes to determine the amount of reserve capital to put aside for credit risk and assigned credit rating agencies a formal role in credit risk assessment for banks of all kinds. In sum, in the words of the former head of the BIS Andrew Crockett, a “paradigm shift” in the thinking behind prudential policies led authorities to “increasing efforts to work with, rather than against, the grain of market forces” (Crockett 2002: 977).

**Change Since the Crisis Began**

How has the post-2007 crisis influenced these trends and patterns of international financial regulation since the mid-1970s? Very soon after the outbreak of the crisis, a plethora of reports and regulatory initiatives offering diagnoses of the crisis and presenting recommendations were published by national regulatory agencies, financial industry associations, and international standard-setting bodies (see Eleni Tsingou`s discussion in Chapter 2). The Financial Stability Forum coalesced this extensive body of work into an internationally-coordinated response, releasing in April 2008 a road-map of international regulatory reform involving more than 60 recommendations (FSF 2008a). This wide-ranging policy agenda was quickly endorsed by the G7 and then subsequently refined by the FSF and other standard-setting bodies in the lead up to the first-ever G20 leaders summit in November 2008 (FSF 2008b).

At that summit, the G20 leaders made the issue of international regulatory reform the most prominent issue on their agenda (G20 2008). In addition to endorsing much of the work of the technocrats, they set out priorities for the reform agenda with a tight deadline of 31 March 2009. These priorities were largely met by the time of the second G20 leaders summit in London in early April, which then set further priorities with specific deadlines for the various technocratic bodies to meet (G20 2009). Many of the London summit's priorities on regulatory issues had been developed by two G20 working groups, each co-chaired by a developed and developing country representative, which presented very detailed reports and recommendations, alongside those of the FSF (G20 Working Group 1 2009; G20 Working Group 2 2009; FSF 2009a).

Various changes to international prudential regulation have been implemented as of mid-2009 as a result of these developments. Since banks were at the centre of the current crisis, policymakers have devoted much attention to bank regulation, including the reform of risk management calculations, the development of liquidity management rules, and higher capital requirements on trading books, securitized products and off-balance sheet activities (see Tony Porter in Chapter 4). But there has also been an important extension of the perimeter of international regulation into new issue areas. At the London summit, the G20 leaders endorsed for the first time a set of international principles – developed by the FSF - for pay and compensation for significant financial institutions, and financial supervisors were tasked with their enforcement (FSF 2009c). Derivatives and hedge funds - two sectors whose regulation had been left to the private sector - were also brought under the official international regulatory umbrella for the first time (see our discussion in Chapter 5). Before the crisis, the regulation of credit rating agencies had been only a marginal issue, but the G20 leaders now insisted that all agencies whose ratings are used for regulatory purposes would be subject to a regulatory oversight regime which was both consistent with a revised IOSCO code which had previously been only voluntary (IOSCO 2008a, see Porter in Chapter 4). More broadly, the G20 leaders have also tasked the IMF and FSF with the job of producing guidelines for national authorities "to assess whether a financial institution, market, or an instrument is systemically important" in order that regulation and supervision be extended to these entities (G20 2009: 3).

In addition to further extending the perimeter of international financial regulation, the G20 leaders attempted to strengthen its institutional basis. They did this partly by establishing collaborative "supervisory colleges" for all major cross-border financial institutions. Much more dramatic, however, was the announcement at the London summit of a major reform of the FSF - now renamed Financial Stability Board (FSB) - to transform it into one of the central pillars of global financial governance. The FSB was assigned the job of collaborating with the IMF in conducting early warning exercises as well as setting guidelines and supporting the creation of the supervisory colleges. It was also tasked with undertaking "joint strategic reviews of the policy development work of the international Standard Setting Bodies to ensure their work is timely, coordinated, focused on priorities, and addressing gaps" (G20 2009: 1). The standard setting bodies were also required to report to the FSB on their work in order to provide "a broader accountability framework" for their activities (FSF 2009d: 2). Finally, all FSB members agreed to implement twelve key existing international standards and codes, and to undergo periodic peer reviews. To perform all these tasks, the informal institutional structure of FSB has become more complex and new institutional layers have been created above the informal discussion occurring in the plenary meetings. The FSB has been given an enlarged secretariat in

Basel, promised a full-time Secretary-General, and a Steering Committee and three Standing Committees (for Vulnerabilities Assessment; Supervisory and Regulatory Cooperation; and Standards Implementation) have been created.

The institutional foundations of the international regulatory regime have also been made somewhat more inclusive of developing countries (see Table 1 and Walter in Chapter 10). One sign of this change was the simple fact that the G20 leaders as a whole were now setting priorities for international regulatory reform, in contrast to the aftermath of the East Asian crisis when this role was undertaken by the G7. With the G20's encouragement, IOSCO's Technical Committee, the BCBS, and CPSS also invited a number of systematically important developing countries as new members.[4] The IASB also guaranteed geographical diversity on its Board for the first time in a manner that guaranteed developing country representation.[5] Most important, however, was the expansion of the membership of the FSF/FSB just before the London Summit to include all G20 countries (Spain and the European Commission were also included). Before the expansion, there were two classes of countries: the G7 each had three representatives (finance ministry, central bank, and supervisory authority), whereas the other five member countries (Australia, Hong Kong, the Netherlands, Singapore, and Switzerland) were only allowed one. With the new 2009 expansion, three classes of countries were created: the BRICs (Brazil, China, India, Russia) joined the G7 countries with three representatives each, while Australia, Mexico, the Netherlands, Spain, South Korea and Switzerland were now assigned two, and everyone else was left with one (Argentina, Hong Kong, Indonesia, Singapore, Saudi Arabia, South Africa and Turkey).[6]

<TABLE 1 ABOUT HERE>

The process of institutional reform should not be overstated. Regulators have continued to rely on networked forms of governance and most of the new international regulatory initiatives remain non-binding, allow significant flexibility of implementation at the national level, and do not delegate enforcement or implementation authority to a third party. There have been only two small signs of a possible departure from the longstanding reliance on soft law. The first is the requirement that membership in the FSB is dependent on implementation of key international standards. Second, at their London summit, the G20 leaders asked the FSB to develop "a toolbox of measures to promote adherence to prudential standards" among non-cooperative jurisdictions (G20 2009: 5). But the willingness of the G20 to deploy this toolbox to promote worldwide compliance and implementation remains to be seen.

The final change in international financial regulation to date has been with respect to the public-private balance. In sectors where self-regulation had been actively fostered by public authorities over the past decade – such as derivatives, hedge funds, credit risk management by banks - officials are now bringing regulation under greater public control. In areas where the enforcement of international standards had been delegated to voluntary efforts and market pressures – such as credit rating agencies – policymakers are also assuming the task of monitoring and enforcing compliance. This trend is also apparent in the accounting realm where the G20 has encouraged the private standard-setting body, the IASB, to accept greater public oversight. In January 2009, the IASB responded by announcing the creation of a new international monitoring board to appoint the trustees who oversee its operations. The members of this board are public authorities: the US SEC, Japan's Financial Services Agency, the European Commission, and IOSCO's Emerging Markets and Technical Committees (as well as the BCBS as an observer) (see Andreas Nölke in Chapter 3).

One further sign of this trend has been the concern that policymakers have expressed about the "macroprudential" costs of relying too heavily on market price-based assessments of risk and value. Regulators have accepted the criticism that Basel II's support for these assessments encouraged banks to engage in excessive risk-taking during booms, while reinforcing constraint during economic downturns. To address this pro-cyclicality, the G20 leaders lessened the reliance of Basel II's market risk framework on value-at-risk (VaR) models and external ratings, endorsed non risk-adjusted leverage ratios, and backed "a requirement for banks to build buffers of resources in good times that they can draw down when conditions deteriorate" (G20 2009: 2). To support the latter, the G20 leaders at the London summit also called on accounting standard setters to improve standards for loan-loss provisioning. In addition, the extensive application of market-based fair value accounting has been criticized by the FSF for having "contributed to an increase in the procyclicality of the system" (FSF 2009b: 5). Following up on this critique, the G20 leaders asked accountants to "improve standards for the valuation of financial instruments based on their liquidity and investors' holding horizons" (G20 2009:5) (see Nölke in Chapter 3). Unlike the regulatory policies in the period before the crisis, these new courses of action have explicitly sought to *tame* market forces, rather than to work with them.

## EXPLAINING INTERNATIONAL REGULATORY INITIATIVES

What *explains* the blitz of international regulatory initiatives we have witnessed to date in response to this crisis? The contributors to this volume outline a number of different potential answers to this question. The range of responses stems from the fact they embrace quite different analytical lenses to explain international regulatory change. In this section, we suggest that these lenses can be divided into three broad categories – inter-state power, domestic politics, and transnationalism – each of which builds on past literature that has analyzed the evolution of international financial regulation since the mid-1970s. These three categories are not necessarily meant to be mutually exclusive; on the contrary, they are in several cases complementary. This is witnessed by the fact that some authors draw on several of the analytical lenses simultaneously, while others suggest that the usefulness of each lens has changed according to different phases of the crisis. Each lens also encompasses considerable diversity with it. While each category points in a different direction, taken together they help to clarify the distinct ways in which the authors approach explanations of contemporary international regulatory change in finance.

**Inter-State Power**

The first analytical lens suggests that international financial regulation has evolved primarily in response to the power and interests of leading states. Past scholarship working within this statist tradition has noted that the expansion in the perimeter of international financial regulation has been most extensive in those sectors where leading states have reaped benefits from more stringent regulation. In the areas where they would bear greater costs from international coordination, dominant states have often exercised their influence by narrowing the scope of more ambitious regulatory initiatives – what Wood (2005) calls “spoiling” behavior – or by vetoing them altogether.

This scholarship has also investigated what forms of power allow leading states to shape international regulatory outcomes. In the past, leading financial powers – traditionally the US and Britain – have been able to influence international regulatory outcomes by exercising a unique “market power” that stems from the international importance of their financial markets, financial firms and/or currencies. This power has been exercised directly through the threat of denying access to all-important London and New York financial markets to non-cooperative states as well as indirectly when domestic regulatory changes in these countries prompt competitive responses abroad (Kapstein 1994, Singer 2007, Oatley and Nabors 1998, Helleiner 1994, Strange 1986, Simmons 2001). The US and Britain have also historically derived a kind of “soft power” from their status as overseers of their leading markets, a status that has given their approach to financial regulation and supervision a certain prestige and cachet as a model to be emulated (Walter 2008). In addition, control over international institutions has provided dominant states with an important channel of influence over the standard-setting process, and it has also been used to push for foreign compliance in sectors where regulatory divergence generates significant externalities for dominant powers (Simmons 2001, Drezner 2007). For this reason, analysts have argued that the fragmented, weak, and exclusive institutional context emerged since the mid-1970s reflects the interests of the leading states, which have preferred to set international standards in like-minded “clubs” that they control rather than in a universal multilateral forum where smaller states might try to block their initiatives (Drezner 2007, Wade 2008).

In analyzing the current crisis, some of the contributors to this volume point to the enduring role of the US and Britain in driving international regulatory change. David Singer in Chapter 6 highlights the endurance of the central role played by the US, suggesting that, in the absence of clear American leadership, ambitious international regulatory initiatives are likely to give way to the promulgation of increasingly vague principles and guidelines. Our analysis in Chapter 5 highlights how the preferences of US were a key determinant of the "end of self-regulation" of hedge funds and derivatives. We also point to the role of Britain, although our cases suggests that Britain's autonomy in international regulatory politics is increasingly constrained by the strengthened capacity of bodies such as the European Central Bank, the European Commission and the European Parliament who are increasingly emerging as key players in this area.

The growing leadership role of European Union as a whole is explored in depth by Elliot Posner in Chapter 7. Since the beginning of the crisis, EU representatives have demonstrated a greater eagerness to use their influence to export EU models to the international level, turning Europe from a regulation-taker into a regulation-maker. According to Posner, the crisis hit just as EU had increased its capacity to influence international regulatory outcomes because of intensified regional integration and Europe's combined financial market size. At the same time, Hubert Zimmermann's analysis (Chapter 8) highlights the tensions between the diverging approaches to financial regulation advocated in recent years by two key financial powers within the EU: Germany and Britain. While the former has argued for more stringent regulation in various international and European settings, it has frequently encountered the resistance of the latter which has advocated a lighter-touch approach to the regulation of finance.  This pattern suggests that Europe's ability to exercise international leadership may depend on its capacity to reconcile the different regulatory philosophies of key member states.

The European Union is not the only emerging power in international regulatory politics. The transfer of economic wealth towards East Asia in the last decade has given this region both more global financial clout as well as a greater ability to chart a more independent course. Many believe that the current global financial crisis is reinforcing this broader power shift by undermining the dominance of US and British financial firms and markets as well as damaging the "soft power" that stemmed from the reputation of London and New York as financial centres. Andrew Walter notes (in Chapter 10) that a decade ago the East Asian crisis eroded the confidence of policymakers in that region and pushed them away from exploring alternatives to Anglo-American regulatory models. Is this crisis have the opposite effect of encouraging East Asian states to the lead in international regulatory politics?

Interestingly, the contributions to the volume suggest that the two dominant powers of East Asia are not yet ready to take on a new leadership role in this area. Although China has been brought for the first time into the inner circle of global regulatory standard setting, Walter argues that it has shown few signs so far of wanting to use this newly acquired status to challenge the status quo in international financial regulation. Indeed, China has been less critical towards existing international standards in banking regulation than other countries, including the US. Similarly, Saori Katada (Chapter 9) argues that the time for Japan to take the lead in redesigning the international financial regulatory architecture has come and gone. Japan's voice in this area has remained muted during this crisis, and its role of representing East Asian voices in global financial debates has also been weakened by the inclusion of China in the main international regulatory bodies. More generally, East Asia lacks the kinds of significant regional institutions to coordinate international financial regulatory initiatives that Europe has built.

**Domestic Politics**

While many power-centered analyses assume dominant states are driven by a coherent "national interest", others have drawn instead on two-level game analogies to explore the domestic sources of their preferences (Kapstein 1994, Oatley and Nabors 1998, Singer 2007, Tarullo 2008). Past literature has shown how the range of domestic societal actors engaged in debates about international financial regulation is usually much narrower than in other economic areas such as trade politics. This feature stems from the complexity of the issues involved, its more indirect and less obvious distributional consequences, and an institutional context that in most advanced industrialized countries gives central bankers and financial regulators considerable autonomy from domestic interests and legislative assemblies.

The only societal actors that consistently take an active interest in the debates are financial market participants for whom the distributional consequences of international regulations are more immediate. They may have concerns about adjustment costs to new standards or may see international regulatory coordination as a way to gain market share (Drezner 2007, Mattli and Woods 2009; Oatley and Nabors 1998; Wood 2005: 157-8). Given their opposition to intrusive regulatory measures and their support for market-driven solutions, the trend of delegating regulatory responsibilities to private market actors over the past decade has been frequently presented as an example of the capacity of the financial industry to "capture" the policymaking process. The influence of the financial industry is also boosted not just by the resources it can mobilize for lobbying or financing electoral campaigns, but also by its control of technical expertise and its frequent interaction and shared similar professional norms and background with regulators.

Past literature in this "domestic politics" tradition notes that the one exception to this general pattern of societal involvement occurs during, and in the wake of major financial crises when international regulatory issues become more politicized in wider society. A number of contributors to this volume explain the post-2007 international regulatory changes with reference to this wider domestic politicization. In Chapter 5, we argue that the large-scale use of taxpayers' money to rescue financial institutions had the effect of politicizing financial regulation to an unprecedented level in the US and Europe, thus unleashing popular pressures in favour of stronger regulation and increasing the involvement of legislative bodies, such as the US Congress, and the European Parliament. We also highlight how the severity of the crisis generated support for new kinds of regulation even within the private sector both for defensive reasons at a moment of weakened political legitimacy and for more positive reasons of improving the functioning of their industry, restoring confidence, and/or gaining market share. Similarly, Posner (Chapter 7) argues that the politicization of financial regulation within Europe has had the effect of weakening the nexus between EU policy entrepreneurs (who sought a more integrated European polity) and multinational financial firms that had been a key driver behind the process of European regulatory harmonization with international standards over the previous decade, while unleashing new populist pressures for tighter national and international regulation.

In addition to analyzing the influence of domestic societal interests, past scholarship has focused on regulators themselves as domestic political actors, subject to various bureaucratic incentives and national political constraints (Kapstein 1994, Singer 2007). David Singer, for example, has described financial regulators as driven by the need to maintain their positional power, a task that requires them to find a balance between conflicting pressures coming from their legislatures and from domestic private sector interests. In this volume (Chapter 6), Singer also calls attention to the importance of the domestic institutional arrangements mediating domestic pressures on regulators in the country at the core of the crisis: the United States. His analysis of the institutionally fragmented regulatory environment in the US, made of competing agencies and overlapping jurisdictions, leads him to conclude that US regulators are unlikely to assume strong leadership in crafting international standards despite the severity of the crisis.

Walter and Katada suggest that the domestic political context is also important for explaining why China and Japan have not taken a stronger stance in pressing for international regulatory change during this crisis. Walter (Chapter 10) suggests that China's convergence towards the Basel standards since East Asian crisis was not driven by powerful external forces, but rather by a strategic calculation of reformers within the Chinese leadership who used compliance with international standards to promote financial sector reform without undermining their control over the process. China's mainstream stance at the international level during this crisis, he argues, reflects the enduring influence of these domestic goals (as well as much lower levels of domestic politicization pressures of the kind that resulted from bank failures and bailouts in other countries). If Basel II was discredited, the usefulness of this international standard for driving domestic reform would be undermined. Similarly, Katada (Chapter 9) argues that the muted voice of Japan in the regulatory response to the global financial crisis derives in part from domestic institutional changes, such as the separation of regulatory and supervisory functions from the Ministry of Finance into a newly established Financial Services Agency.

By drawing on the "varieties of capitalism" literature, Zimmermann (Chapter 8) and Nölke (Chapter 3) introduce one additional way that domestic politics might be important in explaining international regulatory politics during the crisis. In place of more actor-based analyses, this literature explores the significance of structural differences between distinct national political economies. From this perspective, Zimmermann explores whether British and German positions on international financial regulation can be attributed to their respective liberal market versus coordinated market economies. He argues that the consistent German preferences for stronger international regulation, in particular, can be attributed at least in part to policymakers' desire to preserve their distinctive domestic model of capitalism from globalization pressures. Similarly, Nölke shows that controversies over international accounting standards often reflect the fact that the standards have different functions and are developed in different institutional contexts in these two kinds of economies. He also suggests that the rise of powers such as China and India, whose varieties of capitalism present significant differences from both the Anglo-Saxon and Rhenish economies, might further complicate regulatory politics in this area.

**Transnationalism**

A final broad analytical lens for explaining international financial regulatory change focuses not on the power and preferences of the leading states but rather on the significance of the transnational context with which state actors interact. Some past scholarship in this tradition has focused on the increasingly dense transgovernmental networks in which financial officials operate. These networks are said to be fostering the emergence of transnational "epistemic communities" with shared expert knowledge or even shared ideological commitments to neoliberal thinking. With these networks, officials from international organizations are often seen as important actors promoting certain norms and technical knowledge (Kapstein 1992, Slaughter 2004, Baker 2006, Walter 2008, Abdelal 2007, Chwieroth 2007). From this perspective, the control of technical expertise has permitted transnational networks of financial officials to become increasingly autonomous from both the dynamics of inter-state politics and the constraints posed by the domestic politics (Baker 2006: 140, Porter 2005).

Other transnational scholarship has moved beyond this transgovernmental focus to examine the influence of transnational non-state actors in international regulatory politics. Most prominent have been analyses of the growing transnational lobbying activities of private financial institutions. The emergence of a small number of global associations representing heavily internationally oriented financial firms – and associated private thinks tanks and eminent persons groups – has enhanced the ability of the financial industry to interact directly with international standard-setting bodies and to organize "self-regulation" at the international level that parallels similar self-regulatory arrangements that exist at the domestic level (as described for example in Porter 2006; Mügge 2006a). Paralleling the pattern in domestic politics, the capacity of private sector associations to shape international regulatory outcomes has been boosted by the relative absence of countervailing transnationally organized societal interests engaged in the debates on this topic (see for example Scholte and Schnabel 2002; Porter 2005: ch. 9). The result, some argue, is that the international regulation of financial markets resembles a situation of transnational "regulatory capture" (Underhill and Zhang 2008).

Taking this argument in a more structuralist direction have been some neo-Marxist interpretations suggesting that international regulatory change reflects the needs of "transnational financial capital", understood as a class backed by the disciplinary power of global markets, the hegemony of neoliberal ideology, and the power of dominant states (Gill and Law 1989, Soederberg 2004).

A number of the contributors to this volume embrace the transnational analytical lens to explain the international regulatory response to the current crisis. Porter (Chapter 4) argues that the key international regulatory responses to the crisis have involved transnational informal groups engaged in technical discussions over standards and risk models that are not primarily about national competitiveness. Their importance is overlooked by conventional theoretical approaches that focus only on sovereign states and their formal treaty-making. He uses this analytical lens to explore the debates surrounding the work of the Basel Committee in amending the international banking standards and IOSCO in amending the code of conduct for credit rating agencies. He argues that the work of these bodies has not involved simply technical issues about risk modeling, but also attempts to improve the integration of risk modeling into governance itself.

Tsingou (Chapter 2) also analyzes the work of some of these transnational bodies, but her analysis goes beyond formal institutions to address the informal governance networks through which privileged access to the policymaking process actually takes place. In her view, reforms to the governance of international standard-setting bodies, such as expansions in country membership, mask the fact that the intellectual and institutional parameters of international regulatory changes during the crisis continue largely to be defined by the same group of key financial actors from public bodies, private firms, academia, and think tanks who were responsible for the pre-crisis arrangements. These experts need to be seen, she argues, as part of a broader "transnational policy community" where the distinction between public and private is blurred and whose overall orientation is similar to that of industry preferences. Despite the public criticisms, this community has demonstrated a great resilience in a time of crisis, claiming exclusive expertise of the issues at hand and continuing to control the agenda. In her words, this transnational policy community "is under stress but not broken", a fact that helps to explain why, in her view, the crisis has produced rather marginal changes in the international regulatory architecture.

Several contributors to this volume highlight more specifically how the financial industry has mobilized its resources on a transnational basis in order to try to restore its tarnished reputation and leave its footprint on the international regulatory response. Tsingou examines how bankers' groups such as the Institute for International Finance (IIF) and the Counterparty Risk-Management Policy Group III have attempted to frame the international regulatory response of intergovernmental bodies. In our chapter (Chapter 5), we point out that the steps taken by the International Swaps and Derivatives Association to bring order into the over-the-counter derivatives markets through self-regulatory measures were important in preventing the imposition of more stringent regulatory measures. Katada (Chapter 9) also argues that the rise of transnational financial industry groups has created new channels for the financial sector to lobby on its behalf, and as a result, Japanese banks have increasingly voiced their opinion on financial regulatory issues through the IIF and the International Banking Federation rather than through their own government.

In a similar vein, Nölke (Chapter 3) analyzes the most famous case of transnational private authority in financial regulation: the International Accounting Standards Board. He argues that the transnational private character of the IASB and its control of technical expertise have permitted this body during the crisis to deflect most of the unprecedented attacks coming from national parliaments, governments, and financial industry groups against the quasi-public role of this private body and against the adherence to the principle of fair-value accounting. Although the presence of two distinct set of accounting rules in the US and Europe could have led to competitive tensions across the Atlantic, Nölke argues that accounting regulators collaborated closely with each other in order to keeping the interference of politicians at bay. In his view, the new layer of public oversight they accepted is rather distant and the departure from the use of fair-value accounting has been remarkably limited. More generally, from a more structuralist perspective, Nölke also argues that the barriers to more substantial change are set by the dominance of the financial sector over the economy in the more "financialized" global economy in recent debates.

**HOW SIGNIFICANT?**

Nölke's judgment raises the final question that this volume addresses: are we witnessing an important turning in the regulation of global finance? Although all the contributors agree that considerable international regulatory change has taken place in response to the crisis, they disagree about the broader significance of the moment we are living through. Some believe that we are indeed at a moment of real change in the evolution of international financial regulation, either because of changes already underway or because forces unleashed by the crisis will soon generate major change. Others are more skeptical, arguing that the changes we have seen so far, and those we are likely to see in the near future, are merely incremental and limited in ambition.

In the first camp sit our chapter as well as those of Posner and Singer. Our own placement here stems from the fact that the crisis has finally – after many unsuccessful efforts in the past – brought hedge funds and derivatives under the public international regulatory umbrella. At the same time, we acknowledge that the detailed content of the regulation of these two sectors could certainly have gone further and it is not clear whether the changes triggered by the politicization of regulatory politics will endure once the domestic pressures generated by the crisis fade away. Posner's positioning in this camp stems more from his view of the future. He predicts significant change in the coming years because of his argument that the EU is emerging as a major force in the international regulatory politics at the very moment when the crisis has accelerated a backlash against the previous neoliberal program, and coalitional politics within Europe is moving in a direction that favours more ambitious financial regulation. Singer, too, anticipates important transformations in the future. In his case, however, the cause will be the lack of US leadership which, when combined with the expansion of membership in international regulatory bodies, will make significant international regulatory reform very difficult. In this context, he predicts the weakening of international regulation and the emergence of a decentralized patchwork of disparate national and regional regulatory regimes.

In the second camp, we can place the chapters by Tsingou, Porter, Nölke, Walter, Katada, and Zimmermann. Each of these analyses emphasizes continuity over change vis-à-vis the previous international regulatory regime, or at least the limits of the changes we are witnessing. For Tsingou, what is remarkable is the continuing influence of the same transnational policy community that influenced the pre-crisis arrangements despite the severity of the financial meltdown. Porter, too, stresses the enduring role of expert technical knowledge and the incrementalist kinds of changes that it endorses. Similarly, Nölke is struck by the fact that fair value accounting remains largely intact despite all criticisms leveled against it. Both Walter's and Katada's analyses of the limited international regulatory ambitions of China and Japan also deflate any expectations that these alternative power centres will bring radical change to the international status quo. Finally, Zimmermann argues that enduring structural differences in the function of finance within national economies will ensure that any ambitious international regulatory initiatives will be implemented only in slow and uneven ways.

The disagreements between these various analyses partly reflect the fact that they are each focusing on different aspects, sectors and country/regional perspectives relating the politics of international financial regulation. But the disagreements also stem from the fact that we are still living in the midst of this crisis. Although scholars are often tempted to reach definitive interpretations of transformations they are living through, it is worth recalling the evaluation that

Zhou Enlai allegedly made of the French revolution's impact: "It's too early to tell."

And there are indeed certainly many questions raised by the authors of this volume that will only be able to be answered after more time passes. Are we facing a turning point just in the "mode" or also in the "content" of financial regulation (Nölke in Chapter 3)? Will the inclusion of emerging countries into international regulatory bodies significantly change the nature of international regulatory politics? Will the departure from the previous reliance on self-regulation in hedge funds and derivatives significantly shift the substance of regulation? Is the movement towards tightening financial regulation described above destined to lose strength as soon as the memories of the crisis fade, or will these changes have more enduring and long-lasting effects? Do the initiatives described in this volume signal a change in the purpose of financial regulation or has the "implicit contract between finance and the state" (Tsingou in Chapter 2) remained unaltered? In the concluding chapter, these questions are addressed by Zimmermann in a speculative manner through the discussion of some core dimensions of change. As he notes there, however, until we have clearer answers to questions such as these, the debate on whether the facts analyzed in this volume represent a turning point in the international regulation of financial markets must remain open. In the meantime, this volume aims at making an initial contribution towards an area of study that will undoubtedly continue to be important for academics and practitioners in the coming years.

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[1] Thanks for their very helpful comments to all the contributors to this volume as well as Jason Thistlethwaite and David Kempthorne.

[2] We use the term "prudential" regulation in a very general sense in this chapter to refer to financial regulation whose purpose is, at least partly, to promote financial stability. We recognize

that the distinction between prudential regulation and other kinds of financial regulation is often hard to draw clearly. Indeed, as the volume highlights, one of the consequences of this crisis has been that regulators have expanded the scope of what is considered "prudential" financial regulation into new areas.

[3] The content of these "soft law" international agreements has, however, been often subsequently implemented in hard form in national laws at the domestic level.

[4] IOSCO's Technical Committee invited Brazil, India and China to join, while the BCBS expanded in rather faltering two-step process first in March 2009 to include Australia, Brazil, China, India, South Korea, Mexico, and Russia, and then again in June 2009 to include all G20 countries that were not yet members (Argentina, Indonesia, Saudi Arabia, South Africa, and Turkey) along with Hong Kong SAR and Singapore. The CPSS welcomed in July 2009 the following new members: Australia, Brazil, China, India, Mexico, Russia, Saudi Arabia, South Africa and South Korea.

[5] It expanded the membership of the board from 14 to 16 and then required that four members were from Asia/Oceania, four from Europe, four from North America, one from Africa, one from South America, and two others. The IASB's trustees who oversee its operations are also selected with guaranteed regional representation. As we note below, the IASB's also now has a new Monitoring Board. We have left the IASB out of Table 1 because of this complicated governance structure and because of the regional – as opposed to country – representation model vis-à-vis the Board and trustees.

[6] To make plenary discussions manageable with the enlarged membership, delegations with more than one seat have one member seated at the back (but who retains the rights of the table and can be rotated with the others according to topic).