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A New International Financial Architecture - Reflections on the Possible Law-Based Dimension

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A "New International Financial Architecture?"—Reflections on the Possible Law-Based Dimension

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I. Introduction

The onset of the recent series of financial crises in East Asia and worldwide was generated by fundamental economic, political, and financial market errors and weaknesses, and also by exaggerated and disproportionate market reaction to these vulnerabilities, as their extent was revealed at this time.[1] For example, in each case in East Asia, once the domestic crisis was triggered by forced abandonment of an exchange rate peg, it was apparently the combination of pegged exchange rates, high leverage ratios, weak banking and financial systems, declining demand both domestically and elsewhere, and increased competition from other countries such as China and India that transformed a correction into a collapse, and that precipitated "contagion" to other countries experiencing a similar range of underlying vulnerabilities. These vulnerabilities, in turn, appear to stem, in large part, in each affected country from a combination of macroeconomic imbalances, weak financial institutions, widespread corruption, moral hazard, lack of system and institutional decision-making transparency, improper sequencing in the liberalization process, and an inadequate legal

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1. A good explanation of this viewpoint is that of Charles Wyplosz of the Graduate Institute of International Studies, Geneva, and the Centre for Economic Policy Research in London. *See* Charles Wyplosz, Globalised Financial Markets and Financial Crises, Conference Paper for Coping with Financial Crises in Developing and Transition Countries: Regulatory and Supervisory Challenges in a New Era of Global Finance, Forum on Debt and Development, Amsterdam (Mar. 16–17, 1998), *available at* <http://heiwww.unige.ch/~wyplosz/fondad.pdf>. *See also* Rudi Dornbusch, *Asian Crisis Themes*, (Feb. 1998), *available at* <http://web.mit.edu/rudi/www/papers.html>; Paul Krugman, *What Happened to Asia?*, (Jan. 1998), *available at* <http://web.mit.edu/krugman/www/ DISINTER.html>; and S. Radelet & J. Sacho, The Onset of the East Asian Financial Crises, (1998).

foundation.[2] This article observes that most, if not all, of these vulnerabilities can be viewed as *law-based failures* and should be addressed to a significant degree within that context.

In effect, a main emphasis of this article concerns the importance of ongoing and meaningful (bottom-up) economic, financial, and commercial law reform throughout emerging and transition economies and the related enhancement of legal education in these subject-matter areas. In this sense, this article suggests further that in looking forward, these emerging countries need to consider the critical importance of a law-based "building block" approach in addressing the long-term implications of the current financial crises.

Yet in looking to the future to see what emerging economies should be doing prospectively, preemptively, and over the long-term to help ensure sound economic, political, and financial markets fundamentals are in place in order to avoid or, at least, to minimize the effects of a future crisis, domestic efforts cannot and should not occur in isolation. These need to be the result of the collective international, regional, and domestic initiatives taken in this regard. Whether these efforts and initiatives amount to, or should amount to, a "new international financial architecture" (NIFA) is the subject of significant current debate.[3] In trying to decipher the meaning and practical implications of the NIFA, this article postulates that at minimum, any meaningful and effective NIFA should comprise a significant *law-based* component or dimension.

Rather than looking in detail at the factual background to recent financial crises, this article instead, first, will focus on the main vulnerabilities that caused or exacerbated the recent crises. Then, it discusses the web of interlinked "quasi-legal, global standards" that are being developed to assist countries to prepare their individual financial systems for the realities of a world of globalized financial markets, and of other broader elements of financial sector law reform. Consideration is also given to the relationship of such standard-setting process to the broad and ongoing global phenomenon of convergence in financial markets and supervisory standards.

In addition, this article addresses some of the main thematic strands of law-based reform. After reflecting on some of the main areas of the unfinished agenda for meaningful financial sector reform in the emerging economies, this article concludes that the NIFA nomenclature is a vague, but critical "code word" or point of reference for the ongoing search for coherency, meaning, effectiveness, and some semblance of structure within what essentially has become a highly fragmented and volatile "non-system."

II. Submerged Fragilities Necessitate a Law-Based Approach

As alluded to above, the underlying fragilities or vulnerabilities in recent financial crises resulted, in large part, from a *combination* of macroeconomic imbalances, weak financial

2. *Cf. Implications of Asian Financial Crisis: Hearing Before the House of Representatives, Comm. on Banking and Fin. Serv.*, (Jan. 30, 1998) (Statement of Alan Greenspan, Chairman, Bd. of Governors of the Fed. Reserve Sys.) [hereinafter *Implications of Asian Financial Crisis*].

3. *See, e.g.*, Michel Camdessus, From the Asian Crisis Toward a New Global Architecture, Address Before the Parliamentary Assembly of the Council of Europe, June 23, 1998, *available at* (visited Oct. 8, 1999) <http:www.imf.org/external/np/speeches/1998/062398.htm>; and Michel Camdessus, The Role of the IMF: Past, Present, and Future, Remarks at the Annual Meeting of the Bretton Woods Committee (Feb. 13, 1998) *available at* (visited Oct. 8, 1999) <http://www.imf.org/external/np/speeches/1998/021398.htm>. For a more recent authoritative and comprehensive elaboration on the NIFA, see Report of G7 Finance Ministers to the Köln Economic Summit (June 18–20, 1999) [hereinafter Cologne Report].

institutions, widespread corruption, inadequate legal foundations, moral hazard problems, improper sequencing in the liberalization process, and political instability or uncertainties in each of the affected countries. Such vulnerabilities, in and of themselves, present a strong argument for a law-based approach to the NIFA. To illustrate this point, this section will touch upon, in a preliminary manner, the latter three vulnerabilities. The subjects of weak financial institutions, corruption, and inadequate legal foundations are touched upon in Parts III and IV.

A. Moral Hazard and the Role of the Banking System

Most analyses agree on a fundamental role of the banking system in explaining recent financial crises. This line of reasoning suggests that a significant problem in these cases was excessive bank lending following financial market liberalization. Domestic banking crises are common in developing countries for a variety of reasons; often they are the result of bad lending practices, exacerbated by political influences on bank lending or actual policy lending to state-owned enterprises or politically favored enterprises, and, in many cases, underpinned by corrupt or questionable and non-transparent business practices. These problems are further exacerbated when banks' primary source of funds is borrowing in an unhedged foreign currency, because in the event of currency pressures, domestic on-loans go into default, worsening domestic lenders' balance sheets as their own currency position worsens due to external unhedged borrowing. Given investor overreaction leading to denial of roll-over treatment for existing debts, a domestic crisis quickly takes on regional and even international proportions. Importantly, all of these problems are exacerbated by a financial system that is fragile, and poorly regulated and supervised.

It has long been realized that financial intermediaries whose liabilities are guaranteed by the government pose a serious moral hazard problem: the U.S. savings and loan debacle is the classic example.[4] The case in recent financial crises, however, is more murky because financial institutions' creditors did not receive explicit guarantees, but rather perceived that they would be protected from risk due to implicit guarantees, enforced by the politicization of the respective financial systems. In any event, if institutions believe that because of political connections or pressures they will not be allowed to fail, this may plant the seeds for excessive financial risk-taking and eventual bad debt problems.[5] A viable legal infrastructure, with effective implementation and enforcement, underpinning a banking system should significantly reduce these moral hazard concerns.

As to the existence of a deposit insurance scheme and moral hazard, in this author's view a properly constructed and implemented deposit insurance scheme, on balance, brings more benefits of public confidence than systemic risks to a banking system. Such a system should be a "risk-based one," funded by the banking sector, and should be of limited amount, and should not be a 100 percent insurance guarantee for all depositors.

B. Improper Sequencing of Liberalization

Analysis suggests that financial market liberalization may be the best predictor of financial crisis: this has been true in Latin America and the United States in the 1980s, in Europe

4. *See* Krugman, *supra* note 1. For a detailed discussion, see G.N. Olson, *Banks in Distress: Misdirection in Public Policy and Law* (forthcoming 1999).

5. For discussion of these moral hazard situations arising within the Thailand context, see T. Traisorat, *The Thai Crisis of 1997–98: An Opportunity to Re-address the Fundamentals*, Thammasat Univ. L. J.

in the early 1990s, in Mexico in 1994, in Asia in 1997, and in Russia in 1998.[6] In recent financial crises, financial liberalization lifted some restrictions before putting in place a sound regulatory and legal framework.[7] Again, a sound legal infrastructure might well have mitigated such adverse effects of rapid liberalization.

In terms of self-fulfilling crises, financial liberalization makes attacks possible and exposes underlying vulnerabilities to the vagaries of international capital markets; this tension between market liberalization and systemic stability, safety, and soundness needs to be better understood and appreciated by all. The lesson is that financial liberalization should be contemplated only when the situation is ripe. First, significant financial weaknesses, such as banking system weaknesses, large external debt, high unemployment, and unsettled macroeconomic conditions, must be eliminated. Second, countries that accept full capital mobility must sacrifice either fixed exchange rates or monetary policy independence. Monetary policy independence requires a reasonably flexible exchange rate, while a tight exchange rate requires the abandonment of monetary policy independence, for instance through a currency board arrangement. Full capital liberalization should be the last step of this process.

C. Political Instability and Uncertainty

In each recent financial crisis, perceptions of political uncertainty and instability were significant causes of the initial confidence crisis among external investors. Perceptions of weakness and inability of the respective governments to deal with underlying economic problems, uncertainty over the capabilities of leaders and, in many cases, upcoming elections caused investors to question the political stability of the various countries that eventually required bailouts. Political problems also impeded the implementation of appropriate political responses to the impending and developing financial problems in each instance.

A lesson from these financial crises is that countries with weak and indecisive governments and institutions in conjunction with other underlying vulnerabilities are more likely to suffer external or internal confidence crises than those countries with perceived strong and decisive governments and capable institutions. Further, such governments and institutions have the potential to severely worsen the effect of any crisis or contagion through their ineptitude and inability to demonstrate firm and clear policy commitments. Sound legal and constitutional systems, and a firm embrace of the rule of law, can help provide political stability even in the face of political uncertainties.

III. Coping With Future Crises: A Preemptive Move Toward a Law-Based Approach

The collective interconnection of major developing emerging countries into the international financial system implies that disturbances in any other market, whether developed or developing, can be rapidly translated in the form of financial contagion into developed or developing markets. Empirical investigations by the International Monetary Fund (IMF) and other international organizations have confirmed that the increase in cross-border capital flows over the past ten years, most notably through portfolio investment, has bound

6. *See* Wyplosz, *supra* note 1, at 2, 10–11.

7. *See* Joseph Stiglitz, *What Caused Asia's Crash? Bad Private-Sector Decisions*, Wall St. J., Feb. 4, 1998, at A22.

national capital markets more closely together and that the cross-border translation of disturbances can occur with unnerving speed. This concept was reinforced by the ensuing contagion from the Mexican and East Asian crises extending to other countries in the region and worldwide, as most countries in these regions, even those with fundamentally sound economic indicators, experienced temporary exchange and equity market disturbances during the respective crises.[8]

According to Alan Greenspan, vicious crisis cycles such as those in Mexico in 1994 and Asia in 1997 and 1998 may in fact be a defining characteristic of today's high-tech international financial system.[9] As a result, while human panic reactions may not be controllable, at least the imbalances that exacerbate them can be addressed, preferably in advance.

According to Stanley Fischer, First Deputy Managing Director of the IMF, in order to avoid crises, a country needs both sound macroeconomic policies *and* a strong financial system.[10] A sound macroeconomic policy framework is one that promotes growth by keeping inflation low, the budget deficit small, and the current account sustainable. Unfortunately, what became apparent all too readily with the unfolding of the East Asian financial crises is that the IMF had no "magic formula," that earlier IMF experiences with central and eastern Europe and Mexico were not readily transportable to East Asia; that there could be no model approach for all troubled East Asian countries; and that uncertainty exists about whether history will judge the IMF approach on East Asia as a curative foundation for recovery or as an exacerbating factor for further economic recession or depression in the region.

The critical role of a strong financial system was becoming clear before the Mexican crisis; it was crystal clear in that crisis and its aftermath; and it has been equally clear in the East Asian crises and their aftermath. In this respect, Greenspan notes his own primary factors that have been present in international and economic disruptions, but which appear in more stark relief today, namely:[11] excessive leverage;[12] interest rate and currency risk;[13] weak banking systems;[14] interbank funding, especially in foreign currencies;[15] moral

8. *See* International Monetary Fund, *International Capital Markets: Developments, Prospects and Key Policy Issues* (1997); *idem.*, *International Capital Markets* (1995) <http://www.imf.org/external/pubs/ft/icm/97icm/icmcon.htm>.

9. *Implications of Asian Financial Crisis, supra* note 2.

10. Stanley Fischer, How to Avoid International Financial Crises and the Role of the International Monetary Fund, Address Before the 15th Annual Cato Institute Monetary Conference (Oct. 14, 1997) *available at* (visited Oct. 8, 1999) <http://www.imf.org/external/ np/speeches/1997/101497.htm>.

11. *Implications of Asian Financial Crisis, supra* note 2.

12. Exceptionally high leverage is often a symptom of excessive risk-taking that leaves financial systems and economies vulnerable to loss of confidence. This concern is particularly relevant to banks and other financial intermediaries whose assets typically are less liquid than their liabilities and so depend on confidence in the payment of liabilities for their continued viability. Further, excessive leverage can create problems for lenders that can in turn spread to other borrowers that rely on those lenders. This is particularly the case in Korea and in Japan. *Id.*

13. Banks, because of their nature, lend long and fund short, thereby incurring interest rate or liquidity risk. This exposes them to shocks, especially those institutions with low capital-asset ratios. These problems are exacerbated when financial intermediaries borrow in unhedged foreign currency, with the result of potential bank runs following the collapse of the domestic currency. *Id.*

14. When banks are undercapitalized, have lax lending standards, and are subject to weak supervision and regulation, they become a source of systemic risk, both domestically and internationally. *Id.*

15. Despite its importance for distributing savings to their most valued use, short-term interbank funding, especially cross-border, may turn out to be the "Achilles heel" of an international financial system that is subject to wide variations in confidence. *Id.*

hazard;[16] weak central banks;[17] underdeveloped securities markets;[18] and inadequate legal structures.[19] As put forth above, this author would suggest that in fact most, if not all, of these problems are related to "law-based failures."

A. Law-Based Approach: Some Personal Reflections

A law-based approach invariably should entail a broad rule-oriented framework where unfettered discretion, non-transparency and cronyism must give way. But such a framework should not only be broad in its scope, it should be deep in its implementation. As such, a comprehensive and coordinated framework will need to entail and to interconnect the legislative, administrative, supervisory, examination, enforcement, and judicial administration processes of the country.

Yet, a law-based approach to the economic regulation of the financial sector is not simply about laws and legal processes: law is merely one societal *means* to achieving and legitimizing appropriate policy objectives. In the area of financial sector reform, this chapter suggests that a law-based approach also should be an interdisciplinary approach, where law is the thread that weaves together economic, political, and social objectives with a transparent and fair implementation process, and where the lawyers should work closely with the economists, policymakers, operational people, and the accountants.

The source of the new rules is a rather complex proposition. On the one hand, they have been evolving, over the past two decades, through a complex matrix of "soft-law" initiatives by and among a variety of international financial organizations and institutions. On the other hand, they have been shaped by the particular realities of economic law efforts in individual countries. Associated with all of this have been the diverse influences of varying regional and subregional configurations.

In any event, the commitment to a law-based financial sector reform program needs to be a *long-term societal commitment* whereby the notion of a process based upon a *rule of law* becomes ingrained within and throughout the fabric of civil, political, and economic societies in emerging economies, in a substantive manner and not merely as a facade.

Achieving and sustaining this long-term commitment will depend, in large part, on the development of a strong and vibrant educational infrastructure involving new university educational approaches to the teaching of financial law-related subjects on an interdisci-

16. The expectation that monetary authorities or international financial institutions will come to the rescue of failing financial systems and unsound investments has clearly engendered a significant element of moral hazard and excessive risk-taking. Further, the dividing line between public and private liabilities too often becomes blurred. Interest and currency risk-taking, excessive leverage, weak financial systems, and inappropriate interbank funding are all encouraged by the existence of an excessive safety net (e.g., U.S. S&L crisis) or perceptions of the existence of an excessive safety net (e.g., East Asia). *Id.*

17. To effectively support a stable currency, central banks need to be independent, i.e., their monetary policy decisions are not subject to the dictates of political authorities. *Id.*

18. Recent adverse banking experiences have emphasized the problems that can arise if banks are almost the sole source of financial intermediation. Their breakdown induces a sharp weakening in economic growth. Therefore, a wider range of non-bank institutions, including viable debt and equity markets, are important safeguards of economic activity when banking fails. *Id.*

19. An effective competitive market system requires a rule of law that severely delimits government's arbitrary intrusion into commercial disputes. While defaults and restructuring are in some circumstances unavoidable and in fact a beneficial element of renewal in a market economy, an efficient bankruptcy statute is required to aid in this process, including in the case of cross-border defaults. *Id.*

plinary basis, and to new approaches to bureaucratic and judicial training. In a sense a new partnership must be forged among the academic, bureaucratic, judicial, and practical business and financial worlds in order to ensure that this interdisciplinary educational infrastructure comes into being and becomes an integral part of the overall financial sector reform process, which embodies not simply an enactment stage, but also an effective administrative implementation stage, an effective administrative and judicial enforcement stage, and meaningful monitoring and readjustment mechanisms. Here, key governmental bureaucracies having interdisciplinary components and leading universities having strong law, economic and accounting faculties can play the most constructive and catalytic roles.

B. The Rise of a Global Public Financial Law

1. *The Historical Context*

Prior to the 1970s, many governments and financial market regulators operated on the premise that financial market stability required limitations on competition and a segmented market structure that segregated international banks, securities firms, and insurance companies. In particular, the perception of the banking and securities industries as separate and distinct generally eased the supervisory oversight of these industries. This has occurred principally due to the clearly delineated and understood legal and market distinctions between these different types of financial institutions.[20]

However, in the late 1970s, and particularly in the 1980s and now the 1990s, technological and financial innovation began to facilitate competition within and across these industry segments. This initiated the process of regulatory adaptation to *de facto* changes in market structure and financial institutions. Restrictions on permissible activities were relaxed gradually and market access for domestic and foreign competitors expanded, resulting in net efficiency gains to the international financial system. Nonetheless, international banks still engaged primarily in traditional forms of intermediation, namely the business of taking money from investors and depositors and lending it to corporate and residential borrowers. Credit risk was the major risk incurred by these financial institutions, since interest rate risk could be managed by ensuring that the contractual interest rate on the loaned funds varied with the cost of funds.[21]

In the mid-1980s, in the midst of the Lesser Developed Country (LDC) sovereign debt crisis, the vulnerability of individual banks and the international financial system increased exponentially, and bank exposure to credit risk dominated the regulatory agenda.[22] The LDC debt crisis, which in fact transformed itself into a world debt crisis, led to international prudential efforts, centralized in the Basle Committee on Banking Supervision, to strengthen systemic defenses to credit risk through the issuance of risk-based capital standards in the 1988 Capital Accord.[23] The Capital Accord focused on the credit risk of

20. *Cf.* Roy C. Smith & Ingo Walter, Global Banking (1997).

21. *See* Janet L. Yellen, Address Before the Conference on Recent Developments in the Financial System, Jerome Levy Economic Institute of Bard College (Apr. 11, 1996), *available in* LEXIS Banking Library.

22. *See* Prospects for International Lending and Reschedulings (Joseph J. Norton, ed. 1988); C.T. Ebenroth, *Innovations in LDC Debt Conversions*, *in* International Finance in the 1990s: Challenges and Opportunities (Joseph J. Norton & Ray Auerback eds., 1993).

23. *See* Basle Committee on Banking Supervision, *International Convergence of Capital Measurement and Capital Standards* (July 1988) [hereinafter the Capital Accords].

international banks because such banks, as the main providers of payment services, were the primary interconnective media of economic transactions, and because liquidity and credit exposures were naturally concentrated within the banking system. In addition, banks normally channeled the intermediation of short-term funds into long-term non-marketable assets, thus making banks more susceptible to credit risk and public confidence problems than other institutions.[24]

2. *The Changing Context*

In the past decade, traditional bank intermediation has changed dramatically: large non-bank institutions, including securities firms, finance companies, insurance companies, pension funds, and other collective funds and trusts, have become major players in the intermediation process and forced banks to expand their range of financial activities into the other previously segmented industries. Hence, in the 1990s, international banks have been significantly expanding the scope of their activities into areas that directly impact and/or reallocate credit risk, thereby exposing them to differentiating types of risk not previously under supervisory scrutiny.[25]

The expansion of banks into non-traditional activities has spawned the realization that financial risks could be desegregated, separately priced and traded in global financial markets. This realization is having important implications for international financial market supervision and regulation. Particular types of risk are no longer confined to specific institutional categories. As such, financial institutions have come to recognize that unbundled risks can be recombined in ways reflecting the risk profiles of financial institutions that until recently have been characterized as separate and unique. This explosion of financial product innovation raised, and continues to raise, a host of new legal and practical issues, both public and industry, that needed to be addressed within the expanding parameters of public financial law.[26]

The recent Basle Committee amendments to credit risk-based capital requirements are of great importance to international financial institutions.[27] These amendments have been arguably overshadowed, however, by the coordinated but unbalanced efforts of international banking supervisors and securities regulators towards regulatory convergence for similar activities and in certain areas of risk management, particularly market risk. Yet, the globalization of financial activities leads inescapably to the reality of greater communication, cooperation, and coordination among bank supervisors and securities regulators on a broader, international basis.[28]

24. *See IMF Background Paper I, Capital Adequacy and Internal Risk Management*, INT'L CAP. MARKETS: DEVELOPMENTS, PROSPECTS, AND POL'Y DEVELOPMENTS, Aug. 1995, at 136–37 n.2. *See also* JOSEPH J. NORTON, DEVISING INTERNATIONAL BANK SUPERVISORY STANDARDS 190–200 (1995) (explaining in detail the 1988 Capital Accord).

25. *See, e.g.*, A. Crockett, *The Future of Banking Regulation*, EUROMONEY, Sept. 1995, at 272–73.

26. *Cf.* John Howard Jackson, *Regarding International Economic Behaviors—Reflections on the Broader Settings of International Financial Markets and Institutions*, *in* EMERGING MARKETS AND THE ROLE OF INTERNATIONAL FINANCIAL ORGANIZATIONS, ch. 2 (Joseph J. Norton & Mads Andenas eds., 1996).

27. *See* Basle Committee on Banking Supervision, *Basle Capital Accord: Treatment of Potential Exposure for Off-Balance Sheet Items* (Apr. 1995), *available at* <http://www.bis.org> [hereinafter Capital Accord Amendment].

28. *Cf.* GEORGE SOROS, THE CRISES OF GLOBAL CAPITALISM (Geoff Shandler ed., 1998).

C. Global Principles and Standards

Following the Mexican financial crisis of 1994 and 1995 and the U.S. and international rescue operation that it required, leaders of industrial nations recognized the need to develop mechanisms to deal with the potentially systemic dangers of such financial crises.[29] In response to an initiative at the Lyon Summit of the Group of Seven (G-7) in June 1996, representatives of the countries in the Group of Ten (G-10) and of emerging market and transition economies jointly sought to develop a strategy for fostering financial stability through the analysis of key experiences in previous crises and to elucidate basic standards and principles to guide individual nations in developing stronger financial systems.[30] This study concluded that a financial system that is robust is less susceptible to the risk of a crisis in the wake of real economic disturbances and is more resilient in the face of crises that do occur.

1. *The Standard Setting*

As a result of the international attention to the requirements of sound financial systems, the G-7 directed a number of international organizations to develop agreed minimum principles and standards necessary to be implemented in order to encourage and improve confidence in and viability of domestic financial systems. The aim of such standards is to promote sound financial institutions, to minimize systemic risk, and to encourage savings and investment activity through increased confidence in financial markets, both domestically and internationally. It must be noted at the outset, however, that these international principles and standards are just that: minimum internationally agreed upon guidelines that leave wide latitude in their implementation and effectiveness.

The development of this emerging consensus on the requirements for financial stability can be seen as the result of two separate series of events since the collapse of the Bretton Woods system in 1972. These series of events can be classified along two axes, one based on the experience of the developed economies and one based on experiences within emerging economies. First, the growth of international cooperation and the establishment of minimum standards in the area of regulation of financial institutions has come to be viewed as essential in order to maintain and to strengthen the confidence and integrity of the international financial system. This trend is reflected in the evolving role of the Basle Committee on Banking Supervision as a response to various crises involving international financial institutions since the 1970s, and the increasing importance and effectiveness of its pronouncements in the area of financial institution regulation and supervision.[31] Further, international cooperation in this area continues to be of increasing importance to the developed economies as financial technological innovation and internationalization continues at a rapid rate, as demonstrated by recent intense focus on the areas of derivatives and payment and settlement systems throughout the world.[32]

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29. *See* Douglas Arner, *The Mexican Peso Crisis: Implications for the Regulation of Financial Markets*, 2 NAFTA: L. & Bus. Rev. Am. 28 (1996).

30. *See* Group of Ten (G-10), *A Strategy for the Formulation, Adoption and Implementation of Sound Principles and Practices to Strengthen Financial Systems, Financial Stability in Emerging Market Economies* (Apr. 1997), *available at* <http://www.bis.org> [hereinafter Group of Ten].

31. *See* Basle Committee on Banking Supervision, *Core Principles for Effective Banking Supervision* (Sept. 1997), *available at* <http://www.bis.org>.

32. *Cf.* Douglas Arner, *An Analysis of International Support Packages in the Mexican and Asian Financial Crises*, J. Bus. L., July 1998, at 380; and Joseph J. Norton, *The Thai Financial Crises Delving Behind the Facade of Financial Sector Reform and the Need for an Interdisciplinary Approach*, 28 Thammasat U. L. J. 246–76 (1998).

The second element of a developing international consensus is the realization of the importance of domestic financial stability for developing countries, especially given their potential vulnerabilities to changes in capital flows within the international financial system. In many ways, this emerging consensus is the result of the 1980s Debt Crisis and the Mexican Peso Crisis of 1994 and 1995, which has since been echoed in an all too substantial form in Thailand, Indonesia, South Korea, Russia, and Brazil.[33] The consensus in this area is that in order to develop economically, emerging market countries must have in place appropriate structures to guarantee financial stability, especially given the increasing mobility of international capital and the reliance of emerging markets on that capital to fund their own development processes.[34]

Public financial law is taking on an increasingly international overlay. Global consistency in the prudential regulation of the similar financial services and activities of international banks and securities firms can only be realized through enhanced initiatives in international supervisory coordination and cooperative information-sharing arrangements.[35] With respect to banking supervision, the Basle Committee has been the vehicle of international regulatory cooperation for banking supervisors and the driving force behind coordinated supervision for global markets. The Basle Committee has embraced the concepts of consolidated supervision and clear division of responsibilities between the home and host country supervisors for cross-border banking groups in this regard.[36]

With respect to securities regulation, the International Organization of Securities Commissions (IOSCO)[37] has been the collective forum for the development of international cooperation and information-sharing among securities regulators. Although IOSCO lacks the supervisory influence enjoyed by the G-10 members of the Basle Committee, the geographically broader-based IOSCO membership has issued several (in 1986, 1989, 1994, 1996, and 1998 respectively) resolutions on compliance with basic IOSCO principles on high regulatory standards, cooperation, and mutual assistance.[38] These IOSCO initiatives on international coordination and cooperative information-sharing have been carried out largely on a bilateral basis between national securities regulators in the form of memoranda of understanding (MoUs).[39]

Enhanced joint undertakings by the Basle Committee and IOSCO have had, and should continue to have, a significant, positive influence on the international convergence, coor-

33. *Cf.* Arner, *supra* note 32.

34. *See, inter alia,* Joseph J. Norton, *International Co-Operative Efforts and Implications for Law Reform, in* BANK FAILURES AND BANK INSOLVENCY LAW IN ECONOMIES IN TRANSITION (Rosa M. Lastra & Henry N. Schiffman eds., 1999).

35. *See* Rosa M. Lastra, *Developments in International Banking Regulatory Cooperation, in* Y.B. INT'L FIN. & ECON. L., 405–18 (Joseph J. Norton ed., 1998).

36. *See* Basle Committee on Banking Supervision, *Supervision of Financial Conglomerates* (Feb. 1999), *available at* <http://www.bis.org> [hereinafter Joint Forum]; *see generally* George A. Walker, *The Law of Financial Conglomerates: The Next Generation,* 30 INT'L LAW. 57 (1996).

37. IOSCO, established in 1983, has roughly over 120 voting, affiliate, and associate members, who are primarily securities regulators, self-regulatory organizations, and related international organizations. The IOSCO Technical Committee, composed of developed country members, and development committees, composed of members from countries with emerging markets, are the two principal committees through which policies or recommendations are proposed.

38. IOSCO resolutions *available at* <http://www.iosco.org>.

39. For a list of IOSCO MoUs, see the IOSCO website at <http://www.iosco.org>. *See also* Hendrick Jordaan, *IOSCO's Contributions to MoUs with Emerging Market Countries: An Analysis in Light of SEC Experiences,* 2 Y.B. INT'L FIN & ECON. L. 339–67 (1999).

dination, and information-sharing processes. The financial sector reform within developing, emerging, and transitioning economies should reflect the continuing efforts of these two informal international financial organizations.

The conclusion from analyses of both the recent Barings and Daiwa episodes, and the various supervisory initiatives that followed, is that there needs to be improved coordination and cooperation among banking supervisors and securities regulators. This coordination may soon be achieved by a new panel of world financial regulators called the Joint Forum, comprised of officials from the Basle Committee, IOSCO and the International Association of Insurance Supervisors (IAIS), that has agreed to convene, on a regular basis, to address more definitively issues related to the supervision of international financial conglomerates.[40]

In sum, the degree of international regulatory coordination and cooperation is intensifying through the Basle Committee, IOSCO, IAIS, the Joint Forum, and the most recently formed Financial Stability Forum—processes in response to the globalization of financial markets. The international coordination and cooperative information-sharing initiatives have been led primarily by supervisory authorities, and the private sector companies will need to accommodate these initiatives while ensuring the preservation of confidential information given to the regulators. The supervisory initiatives have been bilateral, regional, and broadly multilateral, and the geographic and institutional coverage has varied from specific rules to broadly drawn recommendations. This process is encouraging and needs to continue to develop.

2. *The Global Principles*

Based on the need to establish prescriptive requirements for the sort of safe and efficient financial system that is essential for the functioning of any economy, the G-7 at their Lyon Summit in 1996, in the wake of the Mexican Peso Crisis of 1994 and 1995, directed the international financial institutions and organizations, especially the IMF, the World Bank, and the Basle Committee on Banking Supervision, to develop standards for financial regulation to be implemented in both developed and developing countries, as well as to develop solutions for domestic crises with international implications, such as the Mexican Crisis.[41]

a. Banking Regulation

In the area of banking regulation and supervision, the Basle Committee on Banking Supervision, composed of the G-10 central bank governors, developed *Core Principles for Effective Banking Supervision and Regulation*.[42] In the *Core Principles*, the Basle Committee, in conjunction with regulators from sixteen other jurisdictions, including transition and emerging economies, has produced twenty-five basic principles that should underlie the banking supervisory policies and structures, present the basic outline for effective banking supervision, and serve as a basic reference for supervisory and other public authorities in all countries and internationally. Detailed guidance in the implementation of the *Core Principles* is in turn provided through the Basle Committee's compilation of its ongoing pronouncements over the years.[43]

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40. *See* Joint Forum, *supra* note 36.
41. *See* Group of Ten, *supra* note 30, at 49.
42. Basle Committee on Banking Supervision, *supra* note 31.
43. Basle Committee on Banking Supervision, *Compendium of Documents Produced by the Basle Committee on Banking Supervision* (Apr. 1997), *available at* <http://www.bis.org>.

b. Capital Market Regulation

In the area of capital market regulation, IOSCO has taken the lead with its recent publication and adoption of *Objectives and Principles of Securities Regulation.*[44] In addition, it has developed a framework for minimum content of public offer prospectuses.[45] Finally, IOSCO, along with the International Accounting Standards Committee (IASC), is in the process of developing internationally acceptable accounting standards, with the hope of uniting the international financial system with a single language.[46] These latter documents are intended to set a basic framework for international offering documents that are acceptable to regulators and stock exchanges around the world.

c. Insurance Supervision

As with securities regulation, insurance supervision has historically not received the attention given to that of banking. With the growth of financial conglomerates and the consequent spread of potential systemic risks throughout the financial system, and with the development of significant insurance company assets available for investment, insurance regulation is an area of increased concern for regulators.

The IAIS has published *Insurance Supervisory Principles* to serve as guidelines for the regulation and supervision of insurance markets and is in the process of developing guidelines or standards in the areas of licensing, use of derivatives, on-site inspections, solvency, reinsurance, market conduct, and investment policies.[47] The IAIS has enunciated general principles that identify subject areas that should be addressed in the laws of each jurisdiction, with further guidance tailored specifically to the needs of emerging markets.[48]

d. Corporate Governance

While the area of corporate governance has yet to produce a single set of international principles, the European Bank for Reconstruction and Development (EBRD) published *Sound Business Standards and Corporate Practices* on October 15, 1997, to help companies in the region understand some of the broader concerns that lenders and investors have when considering a potential loan or investment opportunity in the region.[49] These standards delineate guidelines for businesses to consider in their dealings with customers, shareholders, lenders, employees, suppliers, communities in which they operate, and government and local authorities. Such relationships build upon the basic requirements for success of a company having a sound strategy, competent management, valuable assets, and a promising market. In addition, the G-7 has recently mandated the Organization for Economic Cooperation and Development (OECD) to develop a comprehensive set of corporate governance principles to serve as the primary guidance in this area—a currently ongoing project.[50]

44. IOSCO, *Objectives and Principles of Securities Regulation* (Sept. 1998), *available at* <http://www.iosco.org>.

45. IOSCO, *International Disclosure Standards for Cross-border Offerings and Initial Listings by Foreign Issuers* (May 1998), *available at* <http://www.iosco.org>.

46. *See* IOSCO ANNUAL REPORT 1996. *See also* the IASC website at <http://www.iasc.org.uk>.

47. IAIS, Insurance Supervisory Principles (Basle: Sept. 1997).

48. IAIS, Guidance on Insurance Regulation and Supervision for Emerging Market Economies (Basle: Sept. 1997).

49. EBRD, *Sound Business Standards and Corporate Practices: A Set of Guidelines* (Oct. 1997), *available at* <http://www.ebrd.org>.

50. For details, see the OECD website at <http://www.oecd.org>.

e. Financial Conglomerates

Financial conglomerates, now common throughout the world, present special concerns due to their conjunction of banking, securities, and insurance activities and the differing regulatory rationales for each. The Joint Forum on Financial Conglomerates, in which the Basle Committee, IOSCO, and IAIS participate, has now presented a framework for the supervision of financial conglomerates and for the exchange of supervisory information,[51] and the new Financial Stability Forum has been tasked with this issue of conglomerates.

f. Payment, Settlement, and Custody Mechanisms

Ineffective payment, settlement, and custody arrangements undermine the proper functioning of financial markets. In the area of payments and settlements, two organizations have been active. The first, the Committee on Payment and Settlement Systems, which operates under the aegis of the G-10 central bank governors at the BIS, is seeking to develop practices fostering efficient and viable payment and settlement systems.[52] The second, IOSCOs Emerging Markets Committee, in which regulators from sixty-four emerging market countries participate, has released a report proposing the basis for the development of a legal framework for clearance and settlement in emerging markets.[53] The report highlights the main legal concerns that must be addressed in order to achieve an efficient clearance and settlement system for securities in emerging markets.

g. Pension Funds and Collective Investment Schemes

The regulation of international institutional investors, such as pension funds, is of increasing global significance.[54] IOSCO has been the primary actor in developing standards for the regulation of pension funds and collective investment schemes. In 1997, the IOSCO Technical Committee published *Principles for the Supervision of Operators of Collective Investment Schemes*.[55] IOSCO issued further guidance on the regulation and supervision of CIS operators to address fundamental principles presented in the 1997 Report.[56]

h. Accounting and Auditing Standards

In regard to international accounting standards, IOSCO and the IASC committed to the development of international accounting standards for securities firms and companies by July 1998.[57] IASC has now presented its completed program of forty standards for IOSCO's consideration. This development will be of massive importance to all countries wishing to participate in international capital markets. The development of such standards will mark the creation of a truly international language of finance and investment, allowing direct comparisons between investments in different markets.[58]

51. *See* Joint Forum, *supra* note 36.

52. For information on papers, see the BIS website at <http://www.bis.org>.

53. IOSCO, *Towards a Legal Framework for Clearing and Settlement in Emerging Markets, Report of the Emerging Markets Committee* (Nov. 1997), *available at* <http://www.iosco.org>.

54. *See* Joseph J. Norton, *Privatization of Public Pension Systems in Developing Nations: A Call for International Standards*, 64 BROOK. L. REV. 817–66 (1999).

55. IOSCO, *Principles for the Regulation of Collective Investment Schemes, Report of the Technical Committee* (July 1995), *available at* <http://www.iosco.org>.

56. *IOSCO Principles for the Supervision of Operators of Collective Investment Schemes, Report of the Technical Committee* (Sept. 1997).

57. *See* IOSCO, ANN. REP. 1996. *See also* the IASC website at <http://www.iasc.org.uk>.

58. *See* Marc Steinberg et al., *The Development of Internationally Acceptable Accounting Standards: A Universal Language for Finance in the 21st Century?*, SMU L. REV. (forthcoming 1999).

D. Convergence and Impact on Global Public Financial Law

International standard-setting is but one instrument of a broader process of financial market and financial law convergence that is underway globally. The process of convergence is also evolving through the concept of functional regulation (i.e., the provision of similar regulatory and supervisory standards for similar activities that international banks and securities firms currently engage in on an increasingly cross-border basis). This concept, a response to the rapidly changing financial marketplace, is guiding banking supervisors and securities regulators to begin coordinating joint efforts in order to better understand the banking and securities businesses, the corporate structures and attendant risks involved in each business, and the increasing complexities of non-traditional cross-border activities.[59]

1. *The New Global "Soft-Law-Making" Institutions*

Within the banking and securities industries, much of the international consultation among bank supervisors in recent years has been effectively handled through the Basle Committee. For capital market concerns, IOSCO has offered a similar international forum.[60] For the insurance area, there is emerging the IAIS[61] and for the accounting industry, the IASC.[62] What is even more significant is the growing cooperation among these various international bodies as to international standards-setting. Of particular note is the work of the Joint Forum on Financial Conglomerates.[63] In addition, as mentioned in Chairman Sheng's article in this Symposium, a new coordinating body for Bank for International Settlements (BIS), IMF, Basle Committee, IOSCO, IAIS, and the OECD has been formed to help assess the fragilities of global markets, to oversee responses thereto, and otherwise to improve institutional coordination and exchange of information—i.e., the Financial Stability Forum.

The international convergence of *minimum* standards and perspectives of the Basle Committee and IOSCO has successfully produced a number of guiding principles in financial market regulation. This has occurred in direct response to the increasing realization that international banks and securities firms have the expertise and technological ability to engage in the full spectrum of financial activities and services anywhere in the world. Advances in telecommunications and computer technology provide banks and securities firms with new and more efficient opportunities to expand regionally, nationally, and globally in search of new financial activities, markets, and profits. In this respect, the combined utilization of human expertise and technological innovation is resulting in intense international competition. This competition directs such institutions to seek out non-traditional risks in each respective business in pursuit of increased profits. Thus, the demarcation between banking and securities industries is becoming forever blurred, perhaps to the point where fundamental distinctions will no longer exist in some operational areas.[64]

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59. *Cf.* Joseph J. Norton, *Structuring the Banking Regulators and Supervisors: Developed Country Experiences and their Possible Implications for Latin America and the Developing Countries*, 4 NAFTA: L. & Bus. Rev. Am., Summer 1998, at 15–29.

60. For further information, see the IOSCO website at <http://wwn.iosoc.org>.

61. It is hoped that in the near future further information will be available at the Bank of International Settlements website at <http://www.bis.org>, where IASC is now physically located.

62. Further information is available from the IASC website at <http://www.iasc.org>.

63. The three associations of bank, securities, and insurance supervisors collaborate through a "Joint Forum" with respect to issues arising from the rise of international conglomerate financial institutions.

64. *E.g.*, on recent U.S. experiences, see Joseph J. Norton, *The Glass-Steagall Act and Related Bank Legislative Reform in the United States*, 14 Banking & Fin. L. Rev. 11–42 (1998).

2. *Addressing Non-traditional Systemic Risks*

Public financial law also should take into account the new risks within the financial system, as law can be a means for identifying and managing such risks. While financial innovations have provided new opportunities to operate efficiently and to manage and control risks, they also created the potential for financial institutions to accumulate enormous losses in a short period of time. The recent failure of Barings Bank due to rapidly accumulated trading losses in exchange-traded derivatives is one most notable example of such intragroup contagion.[65] In addition, these innovations may increase the possibility for non-traditional systemic risks that should be addressed jointly by financial institutions and regulators. These non-traditional systemic risks arise because enhanced linkages across national and international financial markets increase the volatility of capital flows and the potential for concentrated disturbances to be transmitted more broadly across institutional groups or markets. The increased linkages across markets and volatility in capital flows may precipitate or trigger rapid intermarket contagion, and thus, systemic difficulties. The international ramifications from the Mexican liquidity crisis beginning in December 1994 and lasting through February 1995, and the more recent East Asian Financial Crises of 1997 and 1998, are glaring illustrations of this phenomenon.[66]

There are four principal non-traditional areas of potential systemic risk present in the international financial system today that need to be addressed by bank regulators. Though the full analysis of these risks is outside the scope of this section, it is useful to address each in turn. These risks can only be addressed appropriately by financial institutions and international regulators working together in quasi-symbiotic partnerships.

First, there is the threat that a second sovereign debt crisis will arise because of developing country default on securitized debt obligations. These concerns are exacerbated by the widely dispersed holdings of these obligations among institutional investors and by the fact that the terms and conditions on instruments such as Brady Bonds are not conducive to sovereign debt reschedulings or restructurings.[67]

Second, there is the dramatically increased exposure to foreign exchange payment and settlement risk, otherwise known as Herstatt Risk, underlined by the BIS in its March 1996 report.[68] The fact that the multi-currency clearing systems currently in existence are not subject to regulatory oversight intensifies concerns of such risks.

Third, there is the potentially destabilizing effect of money laundering by criminal syndicates on the international financial system. Money laundering contagion could arise as a systemic risk if financial institutions or financial communities, such as those in certain Latin American countries, Russia and Eastern Europe, or in China, are overcome with criminal

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65. For a more detailed analysis of the failure of Barings plc and its ramifications on international regulatory convergence, see Joseph J. Norton & Christopher D. Olive, *The Globalization of Financial Risks and International Supervision of Banks and Securities Firms: Lessons From the Barings Debacle*, 30 INT'L LAW. 305, 305–23 (1996).

66. *See* Joseph J. Norton, *The Mexican Peso Crisis and the Future of Financial Integration in the Americas*, ch. 12, *in The Changing World of International Law in the Twenty-First Century: A Tribute to the Late Kenneth R. Simmonds* (Joseph J. Norton et al., eds. 1998).

67. *See, inter alia*, Philip J. Power, *Sovereign Debt: The Rise of the Secondary Market and Its Implications for Future Restructurings*, 64 FORDHAM L. REV. 2701 (1996).

68. *See Settlement Risk in Foreign Exchange Transactions, Bank for International Settlements, Committee on Payment and Settlement Systems* (CPSS) (Mar. 1996).

influence and saturated with laundered funds. In short, the interests of international criminal syndicates may not exactly promote the preservation of the stability of the international financial system. If the influence of these groups permeates financial institutions or communities, any aspect of the international financial system could be at risk if financial obligations are ignored or institutions and governments become corrupted.[69]

Fourth, there is non-sovereign-related "cross-border financial crises contagion risk," as most recently evidenced by the East Asian Financial Crises. Addressing this fundamental problem, it has become clear that the new financial architecture will need to be heavily law-based.[70]

Notwithstanding these potential systemic risks, continued legislative or regulatory attempts to maintain segmented regulation between international banks and securities firms will only serve to shift activities to more favorable jurisdictions within the global financial community. In effect, the process of international regulatory convergence in banking supervision and securities regulation is not an attempt to restrict expansion into new activities or competition among financial institutions. Rather, the process is being driven internationally so that regulators may catch up with modern international financial market developments, which are coming about with an almost unnerving speed as a result of the accelerated rate of technological innovation.[71]

Thus, technologically driven market reforms are precipitating revolutionary changes within the banking and securities industries on an international basis. In turn, changes in the methods by which international financial institutions should be supervised and/or regulated are being engendered. These changes are already happening to some degree on the international spectrum. This technological dimension is also something of key importance that will have to be factored into any future efforts in addressing economic and financial law crises.[72]

The process of international convergence, however, has occurred, up to now, largely in a piecemeal and disorganized manner. Nonetheless, the convergence process assuredly marks the transition from fragmented, nationally-based regulatory arrangements in the banking and securities industries towards a system of international principles and standards. These principles will be applied in a functionally integrated global financial services industry that will encompass both banking and securities businesses, and will have to be assimilated into any rethinking of public financial law—perhaps as a species or subset of economic law.

IV. Thematic Strands to the New Global Financial Law

A number of thematic strands underlie the developing framework of the new global public financial law: "coherence," "sequencing," "evaluation," "interconnection," "accounting stan-

69. *Cf., generally*, BANKS: FRAUD AND CRIME (Joseph J. Norton & Gerald N. Olson eds., 2d. ed. forthcoming 2000).

70. *See generally* Group of Twenty-Two Systemically Significant Countries, Reports on the International Financial Architecture (Oct. 1998).

71. *See* CROSS-BORDER ELECTRONIC BANKING: CHALLENGES AND OPPORTUNITIES (Joseph J. Norton & Chris Reed eds., 1994).

72. *See* Jane K. Winn, *The Impact of the Internet on U.S. Regulation of Securities Markets*, 2 Y.B. INT'L FIN. & ECON. L. 409–24 (1999).

dards as quasi-legal rules," "transparency," "governance and the Rule of Law," "ongoing fight against corruption and global financial criminality," and "a viable legal infrastructure."[73]

A. Coherence

According to many writers, a country may *not* need to adopt one total system, but often should pick and choose, as it appears to be best in defined situations. Such an amalgam, however, should be a mosaic, which implies coordination and coherence. Uncoordinated, piecemeal adaptations may, in the long-term, be counterproductive.

It is within the timeframe where exchange controls are to be eliminated and the system fully opened to the international financial system that crises seem most common and potentially damaging. While nations around the world are at different stages of capital liberalization, these issues are of much significance, given the recent experiences in developing and transition countries worldwide. For these reasons, it is important that reform and liberalization are not done in piecemeal fashion, but according to a broader picture of the eventual goal. It is in this respect that the need for careful analysis of any potential underlying problems remaining must be done and these problems attended to before they are exposed to the waves of the international financial system.

B. Sequencing

The European Union model is based on this concept. However, sequencing is not a mechanical process, but should be customized and fine-tuned on a country-by-country basis. The need is to approach law reform from a made-to-order and *not* from a ready-made perspective. As has been demonstrated, improper sequencing (i.e., liberalization preceding strengthening) of financial reforms has been a critical underlying factor in many financial crises. In light of the need for coherence, proper sequencing must also be carefully structured. This is especially true in the case of financial harmonization and liberalization.

C. Evaluation

Clearly, economic law reform efforts to date have been largely unscientific processes, with little or no built-in procedures to ensure accountability, monitoring and reevaluation. The need for appropriate and ongoing monitoring and evaluation mechanisms is perhaps the ultimate challenge for IFOs, IFIs and concerned emerging economies. As can be seen, temporary success is not sufficient evaluation. Domestic efforts must focus on determining potential problems before they are exposed by the market and treating them decisively and effectively. As noted before, small- and medium-sized, open economies do not have the luxuries that large economies do in this respect.

D. Interconnection

Today, various areas of law reform are inextricably interconnected, e.g., banking with securities law reform. The need for interconnection of related and interlinked areas of law reform cannot be understated, although it is sometimes neglected, even in the developed world. Once again, underlying problems such as those described in the context of corporate

73. Portions of this section have been derived from recent articles by the author on financial sector law reform in London at the University of London and in Hamburg at the Max Planck Institute. *See, e.g.*, Norton, *supra* note 34.

governance need to be addressed before they impact some seemingly unrelated, and potentially economically significant, variable or vulnerability.[74]

With these thoughts in mind, individual nations may need to adopt solutions corresponding to their different levels of development and their different needs, especially in relation to the financial sector; however, this must be done carefully, thoughtfully, and rationally—not simply at the behest of foreign investors or the IMF or even out of desire to appease the World Trade Organization (WTO).

E. Accounting Standards as Quasi-Legal Rules

Accounting standards clarify relationships and encourage investment, both domestic and foreign, because they provide an understandable common language for businessmen to communicate about their businesses and finances.[75] In addition, internationally accepted accounting standards encourage investment because they provide transparency and comprehensibility. For these reasons, consistent accounting standards are absolutely essential for the success of continued financial stability and development in any emerging market economy. With the accounting profession applying internationally accepted accounting standards that should not be compromised, companies will gain greater experience and confidence with accounting systems and practices, thereby increasing their own role in the international financial system. Perhaps more importantly, business people in emerging markets will find that clear systems of accounting are not only good for encouraging foreign investment, but also for their own internal management purposes and maintenance of profitability in the long-term.

Consistent accounting standards are absolutely essential for the success of enterprise reform in any country. Accounting standards clarify relationships and encourage investment, both domestic and foreign. Further, accounting standards are the basis of the operational fiction that in many cases allows financial institutions to continue to exist in the face of probable technical insolvency. While accounting standards must eventually be internationalized in order to provide transparency for both domestic and international investors, this process can be gradual as internal problems are eliminated, currencies move towards convertibility, and markets open to international capital. For that reason, all countries, including the United States, would do well to consider the developments in this area and to work to use and facilitate the use of such international standards.

In particular, a country's ongoing involvement in the IASC and assimilation of its efforts should be encouraged. Also, the role of regulatory authorities in fostering and in shaping appropriate accounting rules and practices for domestic financial and business institutions should not be underestimated.

F. Transparency

Transparency is necessary so that all the various players understand the rules of the game, and the game can continue successfully.[76] As the recent experiences of Thailand, South

74. Some suggest that this may be a problem in South Africa. *See* Jabulani Sikhakhane, *Open Season: Some Are More Equal Than Others*, Fin. Mail, Apr. 10, 1998, at 42.

75. *See, e.g.*, D. Mercado, *Evolving Accounting Standards in the International Markets*, Practicing Law Institute, Corporate Law and Practice Course Handbook Series, No. B4-7166 (Oct. 1996).

76. *See, e.g.*, Louis Lowenstein, *Essay: Financial Transparency and Corporate Governance: You Manage What You Measure*, 96 Colum. L. Rev. 1335 (June 1996) (discussing the importance of transparency in the U.S. financial system).

Korea, and Japan have shown, legal and financial transparency are of utmost importance in the long-term successful development of an effective financial system.[77] The emerging international consensus on the requirements for financial stability is built on the principle of transparency, and for this reason, the financial and legal infrastructure of any emerging market must be transparent. Moreover, the advantages of transparency are a baseline for financial and legal development, and resulting financial stability and economic success.

Transparency is necessary not only for international investors, but also for domestic investors. Transparency is necessary to whatever solution a government chooses to resolve banking problems, because without it, investors, companies, banks, and markets will not understand and will not have confidence in the process chosen. It is necessary in accounting so that investors can determine values for productive and non-productive assets and make decisions accordingly. It is necessary for banks in order to lengthen loan horizons and evaluate borrowing and lending decisions. It also is necessary for capital markets in order for investors to understand the nature and risks of investing in securities and thereby prevent the potentially disastrous rise and collapse of stock market bubbles. Furthermore, it is necessary for international investors to make comparisons and to make secure and well-thought-out business decisions, which will benefit not only themselves, but also companies making choices that encourage investment and eventual success in the market.

Both the Mexican and the East Asian crises were triggered and exacerbated partly when investors found out that reserves were smaller than they had thought and that short-term debt was higher.[78] One of the many lessons drawn from Mexico and East Asia is that the extent of the crisis was worsened by the poor quality of information supplied to both the official sector, including the IMF, and the markets—and perhaps even by well-meaning government suppression or distortions of critical information in the hope of buying more time for the reform processes to set in. The East Asian crises reinforce the argument for better and more timely provision of information, including information on central bank forward operations.

There are two arguments in this regard: (i) better informed markets are likely to make better decisions, and in both Mexico and Asia, this would have meant that markets withdrew funds sooner than they did, thereby hastening adjustment; and (ii) the obligation to publish information on certain interventions would affect the extent and nature of those interventions, helping to prevent some unwise decisions. In this regard, at the moment, the IMF is only seeking to further strengthen its Special Data Dissemination Standard (SDDS); however, it is quite possible that stronger measures are forthcoming.

According to Alan Greenspan, the primary protection from adverse financial disturbances is effective counterparty surveillance and hence, government regulation and supervision should seek to produce an environment in which counterparties can most effectively oversee the credit risks of potential transactions.[79] In this respect, a major improvement in transparency, including both accounting and public disclosure, is essential. However, given the financial crises earlier in the decade in Norway, Sweden, and Finland—countries with highly transparent economic systems and advanced institutional frameworks—more transparency is probably not sufficient in and of itself.[80] Yet in this author's view, the long-term

77. *See, e.g.*, Sandra Sugawara, *Market Troubles Felt Far and Wide*, INT'L HER. TRIB., Nov. 8, 1997, at 1.

78. *See* Joseph E. Stiglitz, *Boats, Planes and Capital Flows*, FIN. TIMES, Mar. 25, 1998, at 32.

79. *See Implications of Asian Financial Crisis*, *supra* note 2.

80. *See* Stiglitz, *supra* note 7. It may be argued, however, that in the context of these countries, problems were exacerbated by the existence of implicit government guarantees and explicit currency pegs similar to those that finally in fact led to the crises in Asia and Mexico.

benefits of enhanced disclosure and surveillance need to come, principally on a regional or sub-regional and on a per country basis, with closer communications exchanges with reputable private, local market analysts, and not from undue reliance on the surveillance mechanism of the international monetary and financial institutes.

G. Governance and the Rule of Law

The emerging international consensus is that a transparent, predictable, and enforceable legal regime underlies successful economic development.[81] It is important for investors and businesses to feel that their investments are safe and can be protected in order to provide the necessary confidence in the financial system.

The "Rule of Law" as to economic or other societal regulation is of little practical value unless fair and effective enforcement can be attained and sustained. As such, regulatory authorities require adequate personnel and technological capabilities to ensure *effective enforcement*. The enforcement must also be *fair*, both substantively and procedurally; this will require transparent and judicially reviewable administrative processes. Also, administrative enforcement cannot be entirely fair and effective without an independent, well-educated, and non-corrupt judiciary.

H. Ongoing Fight Against Corruption and Global Criminality

Corruption can undermine the reform process by reducing public confidence.[82] As corruption increases, confidence in the fairness and openness of the financial system decreases, causing investment to decrease and move to other shores. While corruption in some countries such as China, Russia, and certain countries of Latin America is of international concern, it nonetheless must always be a concern in any country. From the standpoint of general financial stability, if corruption is too pervasive, confidence in the financial system will weaken and investment and stability will decrease. From the standpoint of banking, if corruption palpably exists, banks may be weakened by insider lending practices, such as has been the case in Thailand, Indonesia, and Korea—these are the moral hazard problems discussed earlier and commonly referred to as "crony capitalism." Finally, from the standpoint of capital markets, corruption can cause wariness to invest due to perceptions of a "rigged" market or can in fact shake confidence to such an extent that the market collapses. Corruption in fact can be seen as the primary cause of the collapse of the UK stock market at the time of the South Sea Bubble in the early 1700s.[83]

Corruption, however, does not necessarily equate with the absolute requirement of arm's length business transactions. In some cultures, such a solution is obviously impossible; however, a few requirements are probably in order: maximum lending limits to a single borrower in line with international standards, prohibition and punishment of market manipulation, and the punishment of self-dealing, perhaps through the development of corporate fiduciary

81. *See* Group of Ten, *supra* note 30.

82. For detailed information on the impact of corruption and international efforts to combat it, see the homepage of Transparency International, an organization formed to monitor and encourage international efforts against corruption, at *Transparency International* (last modified June 21, 1999) <http://www.transparency.de>.

83. *See generally* John Carswell, The South Sea Bubble (1960).

duties. Obviously, such requirements protect ownership interests, as well as enhance general confidence in the financial system, and should be strongly implemented.

Given the historical situation and the strong domestic perceptions of corruption and "crony capitalism" in many developing and transition countries, efforts in this respect are of great significance.[84] Most importantly, these problems undermine domestic confidence in capital markets, the financial system, the judicial system, and individual perceptions of potential for development and success. Efforts to update laws on monopolies and insider lending and dealing, along with appropriate enforcement of these sorts of provisions, would help to reduce perceptions of a rigged financial and judicial system and increase domestic, as well as international, participation.

In this latter context, recent efforts of regulatory authorities to emphasize enforcement needs in most of the countries worst affected by recent crises are to be applauded. Certainly these financial regulators need to be in a period of consolidation, revaluation, monitoring, and enforcement. Enforcement practices need to be fair, open, rule-based, reviewable, and balanced; however, overly aggressive enforcement should not be used as a substitute for effective government supervisory practices, as this could lead to an unwarranted "chill" on legitimate business and financial activities (e.g., as occurred in the United States during the 1989 to 1992 period).

Related to the need to crack down on corruption is the ongoing fight against using financial institutions for illicit, money laundering purposes. This problem goes to the core of the integrity of financial institutions and their management and touches such institutions and financial systems in both emerging and developed countries.[85]

I. Viable Legal Infrastructure

Based on experiences gained in recent international financial crises and the extensive literature on the topic, one can identify core areas of the legal infrastructure that are necessary for the development of functioning decentralized financial markets and the creation of a sound business environment. While it is also a priority for countries in the region to develop stable macroeconomic frameworks and policies, these policies must be strengthened and supported by the development of an environment of effective laws and institutions. Indeed, in the context of potentially very lucrative investments, e.g., in the energy sector, the legal and institutional environment can in fact be as, if not more, important than the existence of a stable macroeconomic framework.[86]

While the following list is by no means exhaustive, these core areas are of great importance and, when combined with an appropriate second level of financial regulation and supervision, which was discussed in the previous section, create the necessary environment for the development of viable financial markets:

- Clear and defined property rights. The creation of property rights is of course a cornerstone of the development and transition process. In many ways, without the creation of property rights, development or transition is not possible.

84. *See, e.g.*, Traisorat, *supra* note 5.

85. *See, inter alia*, BANKS: FRAUD AND CRIME, *supra* note 69; and Cologne Report, *supra* note 3, paras. 28 and 29.

86. *See* discussion in Norton, *supra* note 34; *see also* KATHARINA PISTOR & PHILIP A. WELLONS, THE ROLE OF LAW AND LEGAL INSTITUTIONS IN ASIAN ECONOMIC DEVELOPMENT, 1960–1995 (1998).

- A regime supporting binding and enforceable contracts. Investment is predicated on binding and enforceable contracts, without which parties cannot effectively structure their transactions.
- Adequate company law incorporating principles of good corporate governance. Prospective investors, both domestic and foreign, need to be assured that the legislative and contractual frameworks within which corporate entities operate provide adequate protection of their legitimate interests and expectations. The importance of effective corporate governance has been underlined by the G-10 and recent international financial crises. In addition, its impact can be seen directly in the context of investors' decisions not to invest in companies, and sometimes even countries, that are viewed as problematic in this respect.
- Adequate lending infrastructure, including secured transactions law. The role of an adequate lending infrastructure is at the heart of recent problems in East Asia and Mexico. A proper legal framework for lending encourages extended loan duration and improved currency matches and enhances the development of domestic financial markets.
- Clear rules governing foreign investment and public-private partnerships (concession law). Without clear rules on foreign investment, foreign capital will not enter a market. Clear rules discourage corruption and enhance respect for the Rule of Law as well as aiding in the transfer of funds and technology necessary to transition and development. Public-private partnership arrangements require a legal infrastructure that recognizes the legitimate needs and expectations of the parties.
- Effective bankruptcy provisions, including for financial institutions. Once again, East Asia has underlined the significance of bankruptcy procedures, not only for economic renewal, but also for adequate protection of investor rights in the context of a business failure.
- Fair and reasonably predictable tax laws. Fair and reasonably predictable tax laws are an absolute necessity both for the adequate functioning of domestic governments and for the encouragement of investment and growth. The negative impact of Russia's unclear and ineffective tax system on financial development is generally recognized.

While no international consensus has evolved in respect of underlying legal infrastructure, the concentration of bilateral and multilateral legal assistance in these core areas illustrates consensus around the critical role these core areas play in transition and economic development.

V. The Unfinished Agenda

Unfortunately, despite best efforts, the domestic, regional, and international authorities do not seem as yet able to present any comprehensive solution to the problems of financial law reform in emerging markets. While the emerging international consensus is very important and useful in terms of general standard-setting and detailing of policy options, no one choice is always appropriate, but rather should be tailored individually in each case. In this regard, it is obviously important to emerging economies to look to learn any lessons that it can from the experiences of Mexico and its other East Asian neighbors in order not only to avoid these sorts of crises occurring again, but also to enhance its own national path of sustainable development.

A. Lingering Problems

Looking specifically at the overall problems likely to continue to affect the financial systems in many emerging markets for the near future, the following come to mind: the weakness of banking institutions, the prevalence of corruption and "crony capitalism," the lack of effective and consistent regulatory enforcement, the lack of sophisticated and efficient judicial mechanisms for the resolution of financial disputes, the inexperience of market participants, and the shortage of domestic savings.

At a more fundamental level, the inefficiencies of general corporate law and of investment firm regulation, and in particular the absence of appropriate solutions to questions of conflicts of interests and insider dominance in corporate governance and securities activities, are likely to impede the smooth and rapid maturation of financial systems. While the financial systems of the affected East Asian economies are maturing, these sorts of problems are likely to be of major importance in the near future, given these countries' need to develop confidence and broaden participation in its financial system and the range of financial instruments (including suitable debt and derivative products).

These are all problems without easy, quick, or necessarily direct solutions. In the final analysis, however, maybe one can agree on a few points. First, the international standard-setting process is encouraging in that in the past little attention was paid directly to this very important issue and little was done directly to address these fundamental problems. Second, the role of the intergovernmental organizations, whether on a worldwide, regional, or subregional level, and of internationally oriented domestic institutions in weaving together the strands for sustainable financial and economic development in transitioning and emerging economies, cannot be underestimated, yet they cannot be overestimated. This role can be viewed as largely directive, in a general sense, and supportive of a particular country's national commitment to true market, legal, political, and social reform.

B. Short-Term Capital Flows

Some are now arguing that short-term capital flows such as those that triggered the recent financial crises in Mexico and East Asia do not bring ancillary benefits, but instead only increase the vulnerability of an economy, especially in situations such as East Asia where high domestic savings rates existed and resulted in misallocation of marginal investment.[87] Even the editors of the *Financial Times* (London) agree that the case for early and complete freedom for international capital flows has been damaged and that the question is how to maximize the benefits of capital flows to developing countries, while minimizing both the number of panics and the damage they cause.[88] The question, and it is a complex one that no one knows the answer to, is how to do this. Joseph Stiglitz, Senior Vice President and Chief Economist of the World Bank, first suggests that at the domestic level, tax, regulatory, and policy distortions that may have stimulated such flows and encouraged short-term foreign borrowing, such as the Bangkok International Banking Facilities, need to be eliminated. Second, capital inflow inhibitions, such as those in Chile (essentially a tax on short-

87. *See* Stiglitz, *supra* note 78.

88. *Regulating Capital Flows*, Fin. Times, Mar. 25, 1998, at 33; *see also* P.B. Rana, Surges and Volatility of Private Capital Flows to Asian Developing Countries: Implications for Multi-lateral Development Banks; IMF Occasional Paper No. 19 (Dec. 1998).

maturity loans), may be appropriate. The suggestion being that these, together with solid fundamentals and a sound financial system, may be the reason that Chile has been relatively unaffected by recent crises. In the future, however, because the East Asian and other emerging economies will continue to need international capital for development, it would do well to focus on mechanisms such as lending infrastructure and domestic currency markets to encourage longer-term, domestic currency lending, while at the same time increasing and protecting its international reserves.

C. Regional Responses to Financial Crises

In terms of East Asia we are not speaking of only domestic reform, but about developing realistic, viable, and workable mechanisms for pursuing this reform process on an appropriate regional or subregional basis.

The globalization of financial markets has increased the complexity of the international financial system and the volume and size of international capital flows. These complexities present new challenges and opportunities to international trade arrangements, law reform, and economic development. In the 1996 Lyon Summit *Economic Communiqué* the G-7 nations asserted that, in calling for the strengthening of economic and monetary cooperation, their respective economic policies would continue to be coordinated towards sustaining non-inflationary growth and that its finance ministers would continue to cooperate closely on economic policy and in the foreign exchange markets.[89] The G-7 declared that strong and mutually beneficial growth in trade and investment "will be sustainable and therefore most beneficial to all if conducted within a strong multilateral framework of rules," thus reaffirming the central role of the WTO and the preeminence of multilateral rules to serve as the framework for regional initiatives.[90]

The recent crises have highlighted the potential role of regional organizations. Because of the different levels of development and openness to the international financial system in the region, it is extremely important to take into account in the drafting process the tension between liberalization, safety and soundness and the potential for financial crises discussed earlier.

In addition to global standards and risk protection, a complementary regional response is also warranted, primarily because contagion effects have tended to be strongest within the region of the country immediately affected. Further, regional and subregional neighbors may be better poised both for cost-effective surveillance and for effective peer monitoring. Possible mechanisms include funding, surveillance, and technical cooperation.

Beyond the high-profile efforts of the European Union, other regional organizations are beginning to venture into the financial sphere. Of most recent note, of course, are the initiatives being taken in Southeast Asia, through the Association of South East Asian Nations (ASEAN). Beyond Southeast Asia, the North American Free Trade Agreement (NAFTA) and Mercosur are both increasingly influential in the sphere of financial regulation and supervision within their respective member countries, and should become even more so if the preliminary international work currently underway following the April 1998 Second Summit of the Americas held in Santiago, Chile, is any indication of the future.

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89. *See, e.g.*, *Making a Success of Globalization for the Benefit of All*, *in* Economic Communiqué (G-7 Summit, Lyon, France) (June 28, 1996), *reprinted in* 13 BNA Int'l Trade Rep. no. 27, at 70 (1996).

90. *Id.*

In looking at regional integration, a "bottom-up," "building block" strategy also is perhaps best. Under this approach, the first stage is focused on laying an appropriate foundation in the form of an effective institutional framework for the financial system in each country, including an independent central bank and private institutions and markets. Following this initial program, by no means an insignificant accomplishment, the goal is to look at issues of market access and potential harmonization and integration. If a similar coherent and sequenced approach had been followed in respect to East Asia's entry into the international financial system, the crises there might have been avoided.

It should be noted, however, that the East Asian and other emerging economy countries face numerous challenges in addressing these sorts of integration issues. The region's nations span a wide range of economic, political, and social development. For that reason, a political choice to focus first on cooperation, then coordination, followed by possible eventual harmonization may be a wise and pragmatic one indeed. Not only does such a "road map" reflect the *realpolitick* of differences in development and sensitivities to sovereign "pressure points," it also reflects the real underlying needs of the constituent nations: development, not political integration. These efforts can be further complicated by the existence of IMF and other self-imposed structural adjustment programs in numerous nations throughout the region. These pre-existing requirements must be taken into account and internalized within any integration process.

In all of these things, however, the role of law and the threat of law-based failures creating potentially self-fulfilling vulnerabilities cannot be ignored. As such, legal efforts must be aimed first at preventive and developmental measures in the immediate time frame, with harmonization and integration as secondary goals over a longer horizon.

D. Reform of the IFIs

For well over two decades, the traditional IFIs (i.e., the IMF, the World Bank, and the Regional Development Banks) have been struggling to identify and redefine their core missions. Institutionally, these organizations have been adrift, reacting more to the rapidly changing, and often volatile and unpredicted, economic, financial, monetary, technological, and political environment(s) impacting our global society. Severe criticism and suggestions for reform, and even for elimination or consolidation, of various organizations have been awash in recent years.[91]

What tends to be forgotten is the historical significance and bureaucratic composition of these IFIs. Each was a key part of a supplement to the ingenious and largely successful Bretton Woods System that brought the Western World economies back on their feet and set a foundation for broader economic development within the Third World. In reality, the broad goals remain the same: (i) promotion of an efficient international training system, (ii) assurance of a stable international monetary and financial sphere, and (iii) allowance of an "equitable, socially acceptable distribution of income and wealth."[92] The economic, political, and funding environment within which these institutions operate today, however, are fundamentally different from those of the 1950s and 1960s.[93]

91. *See, e.g.*, Jeffrey D. Sachs, *Power unto Self*, FIN. TIMES, Dec. 11, 1997, at 21.
92. Alexander Swoboda, *Reforming the International Financial Architecture*, 35 FIN. & DEV., No. 3 (1999).
93. *Cf.* Martin S. Feldstein, *Refocusing the IMF*, 77 FOREIGN AFF., No. 2, at 20 (1998).

Further, the historical bureaucratic composition and focus of these institutions reflect inherent limitations on expanding or substantially changing functions of the IFIs. For example, the IMF has traditionally focused on macroeconomic issues affecting monetary arrangements and stability. Now they are being asked to take on responsibilities for financial sector and corporate structural reforms in emerging and developing economies, for technical assistance on these various microeconomic issues, for financial crisis prevention, and for monitoring (i.e., through surveillance) the global financial environment. Based upon expertise, adequate staffing, and budgetary capacity, the IMF is simply not well-suited or prepared, at the moment, for the enormous tasks that are being thrust upon it.[94]

Certainly, the set of principles that the Cologne Report proposes as a guide for strengthening and reforming the IFIs are desirable but are incomplete: for instance, increasing transparency within and collaboration among the IMF and World Bank and its constitutional member countries, effecting internal institutional reform such as transforming the IMF's Interim Committee into a permanent council, and fostering economic development in the Third World on economically productive, yet socially and equitably acceptable bases. The dilemma, however, is that the nature, scope, and dynamics of the international trading system, of our international monetary financial environment, of the fragmented developmental dynamics of the Third World concluding emerging and transitioning economies, and of our dramatically reconfigured global political environment have made it virtually impossible for the IFIs to arrive at a clear, longer-term, and meaningful review of their respective organizational missions.[95]

In addition, it needs to be kept in mind that the IFIs are essentially international bureaucracies comprised mainly of well-trained technocrats, who are primarily economists. As such, these institutions are, to a large extent, transmitters or implementors of the changing, and at times conflicting, objectives of their key member states and are subject to increasing restrictive budgetary constraints to the extent their budgets may depend on member state funding. Though designed as largely depoliticized institutions, in times of major crises and global uncertainty, the institutions appear to be influenced substantially, albeit indirectly, by the prevailing political and economic views of their key member states. The recent Mexican, East Asian, and Russian financial crises and the dominating influence of the U.S. Treasury are cases in point. Revamping available financing facilities, increasing technical assistance, and enhancing institutional surveillance functions of IFIs and Regional Development Banks cannot be argued against. Yet, no major government seems to wish a general and collective rethinking of these institutions' roles. Until this happens, the IFI's role will be largely ad hoc and reactive, with prospects for the long-term institutional success severely limited.[96]

E. Interaction of International Standards of Public: The WTO/GATS Financial Law and Process

Countries, both developed and otherwise, must consider the implications of financial

94. *See generally* D. Folkerts-Landau & Garber, *The New Financial Architecture: A Threat to the Markets?*, Deutsche Bank (Apr. 1999).

95. *See* Cologne Report, *supra* note 3, paras. 10–15.

96. *Cf.* Karen Lessakers, The IMF and the Asian Crises—A View from the Executive Board, Presentation Made at University of London (May 1999).

crises on the efforts of the WTO[97] and, more directly, the General Agreement on Trade in Services (GATS) and its component negotiations on financial services concluded on December 12, 1997.[98] In the present extensive debate taking place regarding the role of the "architecture of the international financial system"[99] in both preventing and responding to financial crises, one component that is not addressed is the interplay of the Bretton Woods institutions (the IMF and World Bank Group) with their long-lost sister, the WTO.

In developing financial stability and the requisite legal infrastructure, four issues seem to be paramount: (i) a robust financial system, including an independent central bank;[100] (ii) corporate governance and the creation of an effective incentive and monitoring structure for corporate performance;[101] (iii) a strengthening and expansion of domestic capital markets;[102] and (iv) the need for an effective insolvency regime combined with the creation of a suitable social safety net in order to resolve business and financial institution failures and to prevent political and social instability.[103] These must all be undertaken and largely successful prior to full integration with the international financial system. Although not a predicate to trade liberalization, such development underpins the growth of successful trade finance, which is necessary for trade growth. Defining this nexus between trade liberalization and "safety and soundness" concerns for financial markets and institutions becomes a major, cooperative challenge for trade and financial services officials and financial authorities, on the multilateral, regional and domestic levels.[104]

The new requirements of international financial law need to be increasingly taken into account in the processes of traditional international economic law such as the WTO. At present, the road forward is not clear, but as implementation and expansion of the membership of the GATS and the financial services protocol[105] continues to attempt to further liberalize trade in financial services worldwide, countries must necessarily address their own domestic financial system weaknesses as a precursor to increased openness.

F. An Educational Infrastructure

The unfolding of the NIFA indicates a more coordinated study of banking and securities and other relevant areas of financial law: the broad umbrella is really one of financial in-

97. *See generally* John Howard Jackson, The World Trade Organization: Constitution and Jurisprudence (1998); *idem.*, World Trade and the Law of GATT (A Legal Analysis of the General Agreement on Tariffs and Trade) (1969).

98. For details, content and signatories, see the WTO website at <http://www.wto.org>.

99. *See, e.g.*, Camdessus, *supra* note 3.

100. *See generally* Rosa Marie Lastra, Central Banking and Banking Regulation (1996). *See also, inter alia*, E.P. Davis, Debt, Financial Fragility and Systemic Risk (1992); and Patrick Honohan, *Banking System Failures in Developing and Transition Countries: Diagnosis and Predictions*, 1997 BIS Working Paper no. 39 (1997).

101. For development of this thesis in the context of the United States, see Mark J. Roe, Strong Managers, Weak Owners: The Political Roots of American Corporate Finance (1994). Also, generally note the recent OECD project on corporate governance, at *OECD Principles of Corporate Governance* (last modified June 22, 1999) <http://www.oecd.org/daf/governance/principles.htm>.

102. *See* IMF, *supra* note 8. This well might include also the development of securitized instruments. *See* B. Barbour, J. Norton & T. Slover, *Securitization in Emerging Markets, in* 2 Y.B. Int'l Fin. L. 1997 281–316 (1999).

103. For a helpful compilation concerning legal and economic issues of international and comparative insolvency, see Jagdeep S. Bhandari & Leonard W. Weiss, Corporate Bankruptcy: Economic and Legal Perspectives (1996).

104. *Cf.* Jackson, *supra* note 26. Mary E. Footer, *GATT and Foreign Banking as a Trade in Services*, ch. 2, *in* International Banking Operations and Practices: Current Developments (Joseph J. Norton et al. eds., 1994).

105. WTO, *Fifth Protocol to the General Agreement on Trade in Services*, S/L/45 (Dec. 3, 1997).

stitutions, financial markets, financial institution and market law, and financial law. In addition, such study will require a comparative law understanding of financial law systems and of other countries, and an international understanding of the Basle Committee on Banking Supervision, the IOSCO and other IFI processes will be required. While much of the subject matter will remain the realm of domestic law or international soft-law, the subject matter as a whole should become an increasingly important dimension for the teaching of international economic law.

A most significant component of financial law in the twenty-first century, whether in Asia, Africa, the Western Hemisphere, or the Wider Europe, will involve, necessarily, an interdisciplinary and international conceptualization of how regulatory and marketplace forces can interconnect compatibly to provide an appropriate legal environment for the eventual melding of a *new working partnership* among the various financial institution regulators themselves and then among these combined and cooperating regulators, the financial institution industries and the major international financial institutions.

In this context, traditional public lawyers need to come to terms with the increasing reality that economic regulation is becoming a significant part of public law: simply, because it is *financial* regulation does not make it any less public law.[106] It is *not* proposed that the traditional relevance of private law aspects of financial law (e.g., regarding the bank-customer relationship and financial instruments) will no longer be important. To the contrary, private financial and commercial law aspects should be of increasing educational and practical importance. What is suggested, however, is that the private law dimension will have to be evaluated in the overall context of an expanding, interconnecting, and converging—nationally, regionally, and internationally—regulatory framework for financial institutions and financial services.[107]

As such, the need to foster further financial stability and to maintain international supervisory and regulatory standards will be even greater. To this end, a greater academic, administrative, and judicial understanding and appreciation of the increasing international regulatory dimensions of financial law will be required. Also, one will need to study carefully the implications of how WTO liberalization of financial services will accommodate legitimate prudential supervisory concerns. Defining this nexus between trade liberalization and "safety and soundness" concerns for financial markets and institutions becomes a major, cooperative challenge for trade and financial services officials and financial authorities, on the multilateral, regional, and domestic levels.[108]

Moreover, an integrated understanding of expanding regional approaches to financial sector development, e.g., with the European Union,[109] Mercosur and

106. *See* Joseph J. Norton & Christopher D. Olive, *The Ongoing Process of International Bank Regulatory and Supervisory Convergence: A New Regulatory Market "Partnership,"* AM. REV. BANKING L. 227 (1997).

107. *Cf.* JOSEPH J. NORTON, INTERNATIONAL BANKING LAW ON THE THRESHOLD OF THE TWENTY-FIRST CENTURY (1996).

108. *Cf.* John Howard Jackson, *Regarding International Economic Behaviours—Reflections on the Broader Settings of International Financial Markets and Institutions*, *in* EMERGING FINANCIAL MARKETS AND THE ROLE OF INTERNATIONAL FINANCIAL ORGANIZATIONS, ch. 2 (Joseph J. Norton & Mads T. Andenas eds., 1996). Mary E. Footer, *GATT and Foreign Banking as a Trade in Services*, *in* INTERNATIONAL BANKING OPERATIONS AND PRACTICES: CURRENT DEVELOPMENTS, ch. 2 (Joseph J. Norton et al. eds., 1994).

109. *See, inter alia*, Michael L. Gruson, *Convergence of Bank Prudential Supervision Standards and Practices*

NAFTA,[110] will be essential; this will have a heavy public international law dimension. In all events, the new economic and political dynamics shaping financial markets and portraying an increasingly globalized environment, the diversity of the underlying cultures and related values, the disparities in legal systems and approaches through the world, and the sheer realities of the enormous changes that are occurring within East Asia, Latin America, Central and Eastern Europe and the Commonwealth of Independent States, and Southern Africa will have a significant impact on the future scope for the study of international economic law, and of financial law in particular. The ongoing need for viable financial sector law reforms and the growing importance of international and regional cooperative efforts, and of the role of international and regional financial and monetary institutions, will also impact these areas.

Albeit, one could categorize a good portion of these developments as soft law; however, this does not diminish the legal significance and relevancy for setting new international rules of the road respecting financial markets and financial institutions, whether private, public, or intergovernmental in nature, in the global environment of the twenty-first century.[111]

Law, domestic or international, is not a static notion restricted by history and traditional notions. Law is indeed a dynamic and evolving concept. While shaped, in part, by history and while rooted in traditional public international law notions, international law for our modern global financial system should be capable of embracing and legally responding to the dramatically changing nature and demands of our international economic, political, and social environments. In this sense, the traditional legal dichotomies of public and private law need to give way to a more fluid and relevant view of the dynamics of modern legal society.

The new global financial law for the twenty-first century will need to be steeped in a rich mesh of private law, commercial law, corporate law, effective private dispute resolution, and related areas; even enhanced accounting principles will have to be part of the package. All of this will need to be within a viable, responsive, yet constitutionally sound, public and administrative law framework, and will require a sound understanding of public and private international (conflicts of law) and of the comparative law methodology.[112]

Yet, still implicit in this search for a viable legal education infrastructure are the traditional dichotomies between public and private law and between public international law and international business and financial law. The reality though, from a global perspective, is a confluence and not a divergence among and within these traditional legal categorizations.

But what is a global legal education infrastructure? In a real sense, it represents the combined and coordinated commitment of the relevant academic and community leaders to integrate the study of global legal issues within and throughout the legal education environment and to create a vibrant forum for the ongoing discussion and critical analyses of key global issues. In effect, global legal education will need to interconnect committed law faculty members with a core of top domestic and international law students and dynamic external elements of the local, regional, and international legal and business communities

Within the European Union, in Essays in International Financial & Economic Law, No. 20 (London Institute of International Banking, Finance and Development Law ed., 1999).

110. *See* NAFTA: A NEW FRONTIER IN INTERNATIONAL TRADE AND INVESTMENT IN THE AMERICAS (Judith H. Bello et al. eds., 1994).

111. On notion of "international soft law," see, inter alia, JOSEPH J. NORTON, DEVISING INTERNATIONAL BANK SUPERVISORY STANDARDS, chs. 5 and 6 (1995).

112. *See* Joseph J. Norton, *Introduction to Reflections on the Future of Banking Law in the New Hong Kong SAR: A 25th Anniversary of the University of Hong Kong Law Faculty*, 1 Y.B. OF INT'L FIN. & ECON. L. 183–202 (1996).

in order to create a synergistic environment for training and retooling lawyers, domestic and international, who will help build the global marketplace in the twenty-first century.[113]

The effectiveness of traditional legal institutions and paradigms increasingly is being challenged, eroded, and transformed by the development of more vigorous transnational, regional, and local institutions, by increasingly intertwined economic and financial markets, and by the exponential, innovative growth of information technology. This emerging global environment will necessitate the development of alternative legal and quasi-legal arrangements, standards, and institutions and fundamental constitutional, economic, and commercial law reform within and among the nation-states of the region and of the world. This will require lawyers capable of shaping and functioning within the new law-based environment, where traditional legal subject-matter categorizations are not controlling, and in many instances, not relevant.

Global legal education is not primarily about conventional international and comparative law teaching or about producing lawyers to work in a select group of international law firms or intergovernmental institutions—although these aspects remain of considerable importance; it is about educating lawyers working in a local-domestic environment to understand and to be responsive to the sundry effects and implications of globalization and about lawyers who can assist in affecting appropriate and meaningful policy, legal, and institutional reforms conducive to sustaining and expanding a global environment. The new global environment significantly will impact most, but not all, areas of traditional legal education, whether private or public: commercial, business, financial, taxation, energy, environmental, intellectual property, information technology, litigation and alternative dispute resolution, healthcare, employment, telecommunications, criminal, administrative, or constitutional.

Thus, the requirement of the new paradigm of globalization represents important challenges for the future legal education. With continuing meaningful sector law reform and its effective implementation, consistent with evolving international standards and best practices supported by a high-quality, globally-orientated education system, countries will bolster their chances for better safeguarding and avoiding, or least minimizing, the adverse impact of future financial crisis.

G. The Social Safety Net Component

One of the non-prioritized, and even forgotten, aspects of financial sector reform and related corporate sector reform has been the provision of an adequate social safety net. It is only more recently that the inextricable linkage between financial and economic reform and social issues have been identifiable by the IFIs and industrialized countries as a major priority.[114]

Recent events in the world economy have underlined the important link between economic and social issues; and that good economics depend both on stable relationships between government and their citizens and strong social cohesion. An efficient social system, by equipping people for change, builds trust, and encourages people to take the risks that are a necessary part of a competitive modern market. This in turn helps to mitigate the risks and spread the benefits of globalization. Effective social policy can, in particular, ease

113. *See, e.g.*, John B. Attanasio, A Global Law School for the Metroplex, SMU Law School Brief (Fall 1999).

114. *See* Cologne Report, *supra* note 3, particularly paras. 53–60 (paragraphs quoted are 53 and 54).

the task of adjustment during times of crises, helping build support for necessary refocus and ensuring that the burden of adjustment does not fall disproportionately on the poorest and most vulnerable groups in society.

Though the IMF, World Bank, and Regional Development Banks have begun to incorporate social components into their adjustment, financing, and technical assistance programs, creating complementary social systems that work and that are fundable, presents one of the greatest, yet most neglected, challenges for the NIFA.[115]

H. The New Elite Corp of Banking Institutions

While the recent G-7 Cologne Report is viewed as focusing primarily on financial sector reform and emerging markets, what can be overlooked is that this report also directs itself to reform in industrialized countries. In fact, the genesis of NIFA is rooted in the Basle Committee processes, a G-10 concoction, and in the European Community's single financial market efforts of the 1980s and 1990s. In fact, though outside the scope of this article, this author perceives a dual approach to banking system reform under the NIFA: (i) the imposition of minimum internationally accepted supervisory standards and practices for emerging and transitioning economies, and (ii) as to industrialized economies, the making of a new and evolving governance among government, banking authorities, international financial institutions, and international commercial banking institutions and conglomerates in search of grounding a stable, but viable global financial environment.

Expanding and diversifying global banks into even more complex activities and cross-border organizational structures is narrowing the "playing field" of such banks into a fairly small class of elite global banking institutions. These institutions are necessarily engaged in intense competition, on a global scale, in all such activities, and undertake greater and more complex risks to enhance profits.[116] There is little question that the elite global banking institutions generally possess far greater expertise and resources to manage risk exposures, using sophisticated risk measurement and aggregation methodologies, that greatly exceed the sophistication of other banks and banking authorities. Thus, a dominant trend in international bank regulation and supervision over the past several years has been to separate *de facto* elite banks into their own class for purposes of regulation and supervision and subtly shift the regulatory and supervisory framework towards more of a "functional self-regulatory" framework.

This shift has occurred through often opaque maneuvering by the leading domestic and international banking authorities, such as the U.S. Comptroller of the Currency (under the U.S. Treasury), the key Central Bank Supervisors (e.g., the U.S. Federal Reserve Board of Governors), and the Basle Committee on Banking Supervision (Basle Committee) towards "risk-based supervision" schemes for large global complex banking institutions.[117] This

115. *See, e.g.*, James Wolfensohn (President of World Bank Group), Underlying Human, Social and Structural Problems Must Also Be Addressed, Washington Meeting of Trilateral Commission (1999).

116. *See* Federal Reserve Board Governor Laurence H. Meyer, Moving Forward Into the 21st Century, Address at the Conference of State Bank Supervisors, Williamsburg, Virginia (June 3, 1999) (stating that the Fed began "sharpening its focus" on 20 U.S. banks and 10 international banks last year in response to their increasing size and complexity) *available at* <http://www.bog.frb.fed.us/boarddocs/speeches/1999/19990603.htm>.

117. *See, e.g.*, Comptroller of the Currency, *Large Bank Supervision, in* Comptroller's Handbook for Bank Examination and Supervision (Dec. 1995); Jimmy F. Barton, *Supervision By Risk*, in ch. 10, *Current Legal Issues*

"risk-based supervision" framework essentially redirects responsibility and accountability for the design, development, and implementation of risk management and internal control processes to the elite banks themselves, subject to purported oversight and imposition of general parameters and standards set forth by the authorities.

The movement towards functional self-regulation is primarily evident in the recent market risk amendment to the Basle Capital Accord of 1988 introduced in January 1996, and recently implemented at the domestic level.[118] The market risk amendment officially adopted the "internal models" approach for global banks with significant trading operations. The "internal models" approach authorizes such banks to develop and utilize their own risk management measurement and aggregation methodologies from the collection of "value-at-risk" (VAR) approaches, subject only to limited quantitative and qualitative parameters established by the Basle Committee and domestic banking authorities.[119] Thus, the approach essentially provides elite global banks with nearly free reign to determine their market risk capital requirements using individually tailored VAR methodologies.

This development is further augmented in the capital adequacy context by the proposed regime change to the Basle Capital Accord for credit risk capital requirements, released in June 1999.[120] Although the proposed regime changes for credit risk do not explicitly incorporate the "internal models" approach for measuring credit risk requirements, a cautious review indicates an intent to shift responsibility for the design and implementation of credit risk capital requirements to the banks themselves.[121]

The move towards "functional self-regulation" is also predominant in the OTC derivatives context. The international authorities as well as the U.S. banking authorities have conducted various studies and reviews of the OTC derivatives market since 1993, and have encountered numerous market events involving OTC derivatives, which arguably demonstrate that a regulatory and supervisory framework for these activities is desirable.[122]

Affecting Central Banks (explanation of OCC program by the then-Chief National Bank Examiner, OCC); Federal Reserve Board, SR 97-24, *Risk-Focused Framework for Supervision of Large Complex Institutions* (Oct. 27, 1997) (FRB handbook attachment); Joint Forum on Financial Conglomerates, *Supervision of Financial Conglomerates* (Feb. 1998) (consultation documents released by the Basle Committee on Banking Supervision) <http://www.bis.org/publ/bcbs34.htm>.

118. *See* Basle Committee on Banking Supervision, *Amendment to the Capital Accord to Incorporate Market Risks* (Jan. 1996) <http://www.bis.org/publ/bcbs24a.htm>.

119. *See, e.g.*, Darryll Hendricks & Beverly Hirtle, *Bank Capital Requirements for Market Risk: The Internal Models Approach*, FEDERAL RESERVE BANK OF NEW YORK, ECON. POL'Y REV. (Dec. 1997), at 1.

120. *See* Basle Committee on Banking Supervision, *A New Capital Adequacy Framework* (June 1999) <http://www.bis.org/publ/bcbs50.htm>.

121. *See* Federal Reserve Bank of New York, *Consultative Paper on a New Capital Adequacy Framework* (June 3, 1999) <http://www.ny.frb.org/pihome/news/speeches/mcd990603.html>.

122. *See, e.g.*, Commodity Futures Trading Commission, *OTC Derivatives Markets and Their Regulation* (CFTC: Oct. 1993); General Accounting Office, *Financial Derivatives: Actions Needed to Protect the Financial System*, GAO/GGD-94-133 (May 1994); Basle Committee on Banking Supervision, *Framework for Supervisory Information About the Derivatives Activities of Banks and Securities Firms* (May 1995) <http://www.bis.org/publ/bcbs003.htm>; General Accounting Office, *Financial Derivatives: Actions Taken or Proposed Since May 1994*, GAO/GGD/AIMD-97-8 (Nov. 1996); Comptroller of the Currency, *Risk Management of Financial Derivatives*, Comptroller of the Currency Handbook (Jan. 1997); Commodity Futures Trading Commission, *Concept Release: Over-the-Counter Derivatives*, 63 Fed. Reg. 26,114 (May 12, 1998); Basle Committee on Banking Supervision & Technical Committee of the International Organization of Securities Commissions (IOSCO), *Supervisory Information Framework for Derivatives and Trading Activities* (Sept. 1998) <http://www.bis.org/pub/bcbs39.htm>; Bank for International Settlements, *Report on OTC Derivatives: Settlement Procedures and Counterparty Risk Management* (Dec. 1998) <http://www.bis.org/publ/otc_hy9906.htm>; General Accounting Office, *The Commodity*

Nonetheless, the banking institutions and bank authorities have uniformly engaged in considerable efforts to preempt and to stunt any momentum towards adopting any such framework, meaningful accounting standards for these instruments, or even meaningful disclosure and oversight of such activities.[123] This has occurred even as available information strongly suggests that OTC derivatives and the handful of global elite banks acting as OTC derivatives dealers assert a dominating influence over the international exchange-traded financial markets, such as derivatives and equities exchange markets.[124]

The amendments and proposals for the Basle Capital Accord and OTC derivatives postures are supplemented by various other internationally derived guidance in the form of best practices for risk management and internal control processes, developed and issued primarily through the Basle Committee and more importantly in close consultation with the banking industry groups and other groupings of international financial regulators, e.g., IOSCO, Joint Forum, and the Financial Stability Forum.[125]

Exchange Act: Issues Related to the Commodity Futures Trading Commission's Reauthorization, GAO/GGD-99-74 (May 1999).

123. This has occurred most visibly through the battle over adopting and implementing accounting standards for OTC derivatives, and in various regulatory authorities collaborating to stifle the CFTC's attempt to raise and address various unresolved issues pertaining to OTC derivatives in its May 1998 Concept Release. *See, e.g.*, *Greenspan Criticizes FASB Proposal, Urges Use of Fair Value Disclosure*, 29 SEC. REG. & L. REP. (BNA), Aug. 8, 1997, at 1118 (reviewing Greenspan letter urging FASB to drop derivatives accounting rules); *CFTC Release on OTC Derivatives Does Not Go Far Enough, Exchanges Say*, 30 SEC. REG. & L. REP. (BNA), June 12, 1998, at 908 (reviewing preliminary opposition of U.S. regulatory authorities to CFTC Concept Release on OTC derivatives, 63 Fed. Reg. 26,114 (May 12, 1998)). *See also* Basle Committee on Banking Supervision & Technical Committee of the International Organization of Securities Commissions (IOSCO), *Recommendations for the Public Disclosure of Trading and Derivatives Activities of Banks and Securities Firms* (Feb. 1999) (joint consultative paper).

124. *See, e.g.*, Bank for International Settlements, *Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity* (1998) <http://bis.org/publ/r_fx98.htm>; *Cf.* Bank for International Settlements, *Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity* (1995) <http://bis.org/publ/fx96.htm>; David Folkerts-Landau & Alfred Steinherr, *The Wild Beast of Derivatives: To Be Chained Up, Fenced In or Tamed?*, AMEX BANK REVIEW (1995) (on file with author) (OTC derivatives markets rely on exchange-traded derivatives markets for hedging purposes).

125. *See generally* Basle Committee on Banking Supervision, *Operational Risk Management* (Sept. 1998) <http://bis.org/publ/bcbs42.htm>; Basle Committee on Bank Supervision, *Framework for Internal Control Systems in Banking Organisations* (Sept. 1998) <http://bis.org/publ/bcbs40.htm>; Basle Committee on Banking Supervision, *A Framework for the Evaluation of Internal Controls* (Jan. 1998) <http://bis.org/publ/bcbs33.htm>. *See also* Technical Committee of the International Organization of Securities Commissions (IOSCO), *Risk Management and Control Guidance for Securities Firms and Their Supervisors* (May 1998) <http://www.iosco.org/docs-public/1998-risk_management_and_control.htm>; *Basle Committee on Bank Supervision Intra-Group Transactions and Exposures and Risk Concentrations Principles* (July 1999) <http://bis.org/publ/bcbs51.htm>. The work of the Basle Committee on Banking Supervision, IOSCO, and the Joint Forum (formerly known as the Joint Forum on Financial Conglomerates, established in 1996 and consisting of members of the Basle Committee, IOSCO, and the IAIS), are generally well known in the international financial law community. The *Financial Stability Forum* was developed following the G-7 Finance Ministers' meeting in Bonn, Germany, in February 1999, at the suggestion of Deutsche Bundesbank President Hans Tietmeyer. The group is chaired by Mr. Andrew Crockett, General Manager, Bank for International Settlements, and consists of finance officials from both developing and developed nations, regulatory authorities, central bankers, and members of international financial institutions. The group will purportedly focus on three areas designated following the Asian financial crisis: (1) highly leveraged institutions that have a potential for creating financial market instability through trading activities; (2) offshore centers that are "host" to financial transactions that may be unregulated; and (3) short-term capital flows and the steps that nations may take to render themselves less vulnerable to volatile capital flows. The Financial Stability Forum is tasked to report on its endeavors after the next meeting in September 1999.

All this being said, the trend toward functional self-regulation vis-à-vis the major international banking institutions bonds the fate of success to proactive, constructive, and transparent public-private partnership. The ultimate question remains, however, whether the international regulators and international banks are up to the task and whether the creation of an elite group of international banking institutions will prove a wholesome event in the evolvement of a global financial system.

VI. Concluding Observations: Is There a "New International Financial Architecture"?

A. Generally

It has become evident in the wake of recent financial crises that issues of economic and commercial law reform are of primary political and societal concern. The sustainability of economic growth, of enhancement of the quality of life, and of the stability of the economic and financial systems must be a driving imperative for the twenty-first century for all economic systems, whether lesser developed, developing, emerging, transitioning, or industrialized. All of this will require viable, and "safe and sound," financial and commercial law systems of considerable sophistication and of high integrity and transparency.[126]

Moreover, it has become apparent since the breakdown of the Bretton Wood's (International Monetary) System in the early 1970s that financial markets around the world have become and are becoming more and more interconnected and interdependent. As such, many countries, especially developing, emerging, and transitioning economies, are finding themselves in a state of major transformation as to the nature and requirements of their economy and its financial markets. The modern reality is that political and economic power comes, in part, from developing and sustaining viable and substantial economic and financial markets—markets that are becoming increasingly internationalized.[127]

B. Several Preliminary Observations

On the critical importance of the future development of financial law and regulation, and its relationship to the evolving notion of "public financial law," several preliminary observations can be drawn, particularly as to issues that will be subject to considerable external regional and international pressures. The recent financial crises in East Asia, Russia, Brazil, and elsewhere bring this point home.[128]

A first observation is that the relationship of law to financial markets and financial institutions is an evolving and diverse process entailing a rich matrix of *private* and *public* laws, of domestic, regional, and international laws, including "soft law," and a mix of statutes,

See Bank for International Settlements Press Release, *Financial Stability Forum Establishes Working Groups* (May 11, 1999) <http://www.bis.org/press/p990511.htm>.

126. *See, e.g.*, John Howard Jackson, The World Trade Organization: Constitution and Jurisprudence (1998).

127. *See, inter alia*, Joseph J. Norton & Douglas Arner, *International Co-Operative Efforts and Implications for Law Reform*, *in* Bank Failures and Bank Insolvency Law in Economies in Transition (Rosa M. Lastra & Henry N. Schiffman eds., 1999).

128. *See* Joseph J. Norton, *Financial Sector Reform and International Financial Crises: The Legal Challenges*, *in* Int'l Fin. Econ. L., No. 16 (London Institute of International Banking, Finance and Development Law ed., 1998).

administrative regulations, and case law. This unfolding legal framework covers both traditional and segregated notions of particular types of financial institutions and broader, more integrated notions of "financial services" and "financial institutions."[129] As such, "the new financial law," domestic and international, will require a blend of private and public law. In all events, this developing area of law will need to become attuned and receptive to these dramatically and vastly changing notions, to the new legal and economic realities of the individual countries, to the general growing economic interdependence within the East Asia Region, and to the more general international financial market developments.[130]

A second related observation suggests that the future of domestic financial institutions and markets will and should continue to be influenced and shaped, in a significant measure, by external international and regional supervisory developments. These external pressures may well come to provide the strands for a gradual integration and convergence by "small steps" respecting the financial systems and markets of individual sovereign nations, and otherwise should help foster, generally, greater transparency and stability in the financial markets domestically, regionally, and internationally.[131] Yet, all this needs to be effected within a system that embraces a strong "rule of law" and has sound constitutional underpinnings. Again, private and public law are "twinned."

C. A NIFA?

The question remains to be answered, however, as to whether this new web of international standards and principles of financial law constitutes a "new international financial architecture." Whatever the answer, the initial inquiry is of long-term global significance and is one that touches upon a fundamental restructuring of existing international economic and financial institutions; a further evolvement of international "soft law" practices and standards; a reconfiguration of varying regional and subregional arrangements; and, above all, a robust and sustained effort of domestic systems to effect fundamental and long-term legal, economic, political, social, and educational reform processes. In this sense, there will be no one comprehensive and defined "new architecture," but a loose, yet complex construct for seeking long-term domestic, regional, and international stability and equilibrium in financial and other economic markets.[132] Looking at it another way, the NIFA terminology, while vague, serves as a critical code word or point of reference for the ongoing search for coherency, meaning, effectiveness, and some semblance of structure within what essentially has become a highly fragmented, volatile, yet interconnected, network of financial markets and systems (i.e., a non-system). To be flippant, the NIFA is a useful metaphor.

More particularly, the period from 1986 to the present has been one of strengthening of regulation and supervision of financial institutions and markets, with the overriding goal

129. *See* Ross Cranston, Principles of Banking Law (1997).

130. *See* Joseph J. Norton, *The Korean Financial Crises Reform and Positive Transformation: Is a Second "Han River Miracle" Possible?*, 27 Global Econ. Rev. 3-36 (1998).

131. *See, e.g.*, Stanley Fischer, *Reforming World Finance, Lessons from a Crisis*, The Economist, Oct. 3-9, 1998, at 23.

132. *See generally* Cologne Report, *supra* note 3. *See also* Working Paper, June 1999; Basle Committee on Banking Supervision, *Supervisory Lessons to be Drawn from the Asian Crisis* (June 1999) <http://www.bis.org/publ/bcbs_wp2.htm>; U.N. Executive Committee on Economic and Social Affairs, *Towards a New International Financial Architecture* (Final Version, Jan. 21, 1999) <http://www.un.org/esa/coordination/ifa.htm>. *Cf.*, however, a highly critical review of the NIFA by Folkerts-Landau & Garber, *supra* note 94.

of achieving "international standards." Further, in this author's view, the period from 1986 to 1995 was really a period of modernization and search for best practices worldwide. Moreover, the period since the Mexican financial crisis in 1994 and 1995 has seen the beginning of a new period centered on establishing minimum internationally acceptable standards of public financial law through a process centered on the Group of Seven, the Group of Ten, the Basle Committee, IOSCO, IAIS, the Joint Forum, the most recent Financial Stability Forum, and even the largely private IASC—what may be called the new "international financial groupings"—and the traditional "international financial institutions" such as the IMF, World Bank Group, and the regional development banks.

Following the financial crises in East Asia, Russia, and Brazil of the past two years, attention has focused even more on the importance of developing such standards and upon their implementation into domestic legal systems and regulatory and supervisory practices.

Whether all of this, along with the broader global convergence process mentioned above, amounts to a "new international financial architecture" is still an open question.[133] Nonetheless, with the development of this new public financial law comes the need for legal academics to adjust and to train the next generation of lawyers and scholars to understand and to influence the ongoing process of developing and implementing international standards of public financial law, largely through "soft law" initiatives. In doing so, it should be kept in mind that this process intersects with fundamental domestic economic law reform, with varying reconfigurations of regional support frameworks, and with a restructuring of the old Bretton Woods institutions.

133. In a real sense, the "NIFA" is a misnomer, as the process is not "new," nor purely "international," nor solely "financial," nor really about any scientific, concrete "architecture." For further consideration, see Chairman Andrew Sheng's article in this issue, and Joseph J. Norton, Is There Really A New International Financial Architecture?, Presented at the Hong Kong University Global Conference on "The Recent Financial Crises: Lessons for East Asia" (June 3–4, 1999).