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Global Governance of the World Financial Crisis?[*]

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Abstract

Our contribution evaluates the recent financial crisis in light of the ongoing global governance debate. We contextualize the insights from the interdisciplinary workshop on strategies for solving and preventing global crises and put them within the broader frame of global governance. We analyze solution and prevention mechanisms for global crises phenomena by investigating the reactions to the financial crisis of 2007-9. We provide particular insights into the modes of multi-level-, G20-related, and regional governance mechanisms. Our findings indicate that the dominance of transnational networks and the inherent particularistic interests prevail as regards the reactions to the financial crisis. We discuss whether this outcome can be generalized with regard to the potential implications for other global crises.

A. Introduction

The recent and ongoing crisis in the world financial system along with other global menaces such as climate change, the swine flu pandemic or the spread of weapons of mass destruction have highlighted the susceptibility of a globalized world to equally globalized crises. Yet, at the same time, efforts to establish global regulatory mechanisms are increasing. Setting up a system of "global governance" is portrayed as the answer to global crises. For example, the new President of the EU Council, Herman van Rompuy stated after his election:

> "We are living through exceptionally difficult times: the financial crisis and its dramatic impact on employment and budgets, the climate crisis which threatens our very survival. A period of anxiety, uncertainty and lack of confidence. Yet these problems can be overcome by common efforts in and between our countries. 2009 is also the first year of global governance, with the establishment of the G20 in the middle of the financial crisis. The climate conference in Copenhagen is another step towards the global management of our planet. Our mission is one of hope, supported by acts and action."[1]

[1] Intervention of Herman van Rompuy, 19 November 2009, available at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/111341.pdf (last visited 17 March 2010).

Indeed, the G20 has gained prominence during the world financial crisis and may supersede the G8 as a cardinal means for global economic and financial governance. At the same time, the post-Kyoto Protocol negotiations on greenhouse gas emissions show that classic multilateralism is also a means of global governance in reaction to crises that affect humanity as a whole.

Whether these efforts to establish some form of global governance are a comparatively new development or rather a well-known, evolutionary process may be debatable. However, the change in the fabrics of global governance is a highly dynamic process. New actors, such as China and India are making their influence felt. New issues, such as climate change capture the attention of politicians. Therefore, some authors suggest that the order of global governance is changing rapidly – and that little is known about the current system of global governance, let alone the process of change.[2] At the same time, an abundance of literature analyzing and categorizing the current global order has emerged in a multitude of disciplines, not only in international law, but also in international relations, economics and sociology.[3]

Against this background, in October 2009, young academics from a wide range of disciplines came together at the Georg-August-University to discuss the phenomenon “global crisis”, to analyze it with the methodology of their respective disciplines and to debate about viable solution and prevention strategies for such crises. This issue of the Goettingen Journal of International Law collects their work.

The workshop discussions demonstrated the need to contemplate and investigate global crises phenomena from an interdisciplinary perspective. If global crises are understood as challenges for humanity as a whole, common sense dictates that the whole tool set of all disciplines should be used at the same time to develop concepts for crisis solution, management and prevention. Each discipline will have a different role to play, yet their results have to be brought together for comparison, discussion and evaluation. Interdisciplinarity is thus the means to open up the specific methods, suppositions and theories of economists, legal scholars, political

2 D. Kennedy, ‘The Mystery of Global Governance’ in J. L. Dunhoff & J. P. Trachtman (eds), *Ruling the World* (2009), 37, 38 and 40.

3 For a short overview of some important schools of international law and international relations striving to explain the global order, see Kennedy, *Id.*, 43-54.

scientists and sociologists for each other to sketch a more holistic picture of global crises phenomena.

The articles collected in this issue provide some important findings, yet at the same time highlight that many decisive questions remain unanswered. With our article, we intend to collect some of the workshop's insights in order to integrate them in the wider discussion about global governance.

In the next section, we will outline how the different disciplines may benefit from a cooperative approach towards the research on global crises and give a short overview of the challenges interdisciplinarity has to face. The third part will conceptualize the phenomenon "global crisis" by laying out an analytical framework based on the concept of "global governance". We will then deal with concrete global crisis management and prevention mechanisms and actors. In particular, we will deal with the G20 as a possible new actor in global crises management and prevention. Moreover, we will also look at regional approaches towards global crises. The fourth section will then provide an empirical investigation of the world financial crisis. We conclude by drawing policy implications for facing future global crises.

B. An Interdisciplinary Perspective on Global Crises

In the past two decades, interdisciplinarity has not only become a buzzword for a wide range of loosely coupled scientific journals, research centers, study programs and disciplinary cooperation. Moreover, discourses promoted by federal agencies, private foundations and universities tend to view interdisciplinary research as more transparent and more profitable for political, social and economic development than the traditional, disciplinary bound scientific research based on well-defined and sharply differentiated disciplines.[4]

"Interdisciplinarity" as a term emerged in the arts during the 1920s. Basically, it implies "an integration or synthesis – an interconnection

[4] J. A. Jacobs & S. Frickel, 'Interdisciplinarity. A Critical Assessment', 35 *Annual Review of Sociology* (2009), 45-48 and A. Barry *et al*., 'Logics of Interdisciplinarity', 37 *Economy and Society* (2008) 1, 20-23. This article is based on field research at private institutions in 3 different sectors (environment and climate change research, ethnography in the IT industry, art-science).

between different academic disciplines".[5] During their emergence, modern scientific disciplines have not only led to the formation of distinct notions, methods and theories, but also to a more or less transparent corpus of social and cultural practices that regulate the inclusion and exclusion of members of the academe into the different disciplines, as the following remark emphasizes:

> "Disciplines discipline disciples. A commitment to a discipline is a way of ensuring that certain disciplinary methods and concepts are used rigorously and that undisciplined and undisciplinary objects, methods and concepts are ruled out. By contrast, ideas of interdisciplinarity and transdisciplinarity imply a variety of boundary transgressions, in which the disciplinary and disciplining rules, trainings and subjectivities given by knowledge corpuses are put aside or superseded."[6]

At a general level, the literature differentiates between "multidisciplinarity", which is characterized by a low degree of cooperation between the disciplines, and "transdisciplinarity", which goes beyond disciplinary confines and develops news modes of scientific enquiry often driven by practical demands. Thus, „interdisciplinarity" can be best understood as middle ground between the two and is characterized by " […] cross-disciplinary cooperation feeding back into disciplinary knowledge […]".[7]

Furthermore, contemporary research based on case studies in the privately and publicly funded sector strives to identify existing types or modes of interdisciplinarity.[8] This research shows that the actual mode of interdisciplinary cooperation is defined by the degree of organizational connection between the related disciplines, the degree of cognitive coupling between the participating scientists[9] and that it further entails different

5 D. W. Vick, 'Interdisciplinarity and the Discipline of Law', 31 *Journal of Law and Society* (2004) 2, 164.

6 Barry *et al.*, *supra* note 4, 20-21.

7 M. Lengwiler, 'Between Charisma and Heuristics: Four Styles of Interdisciplinarity', 33 *Science and Public Policy* (2006) 6, 423.

8 *Id.* This survey is based on field research at extra-university research institutions in Germany (3 Max Planck institutes, 3 Leibniz institutes and 1 Helmholtz center). Barry *et al.*, *supra* note 4 is another analysis in point.

9 Lengwiler, *supra* note 7, 425-426.

forms of logics. It could e.g. lead to the synthesis of a new kind of scientific knowledge beyond disciplinary confines (*integrative-synthesis*), to the dominance of one of the participating disciplines (*subordinate-service mode*) or "[…] be driven by an agonistic or antagonistic relation to existing forms of disciplinary knowledge and practice".[10]

In this regard we are well aware of the limitations inherent in what can only be a short encounter during a workshop. Moreover, interdisciplinarity is no shortcut to scientific progress and valid scientific results.[11] Therefore, our interdisciplinary approach during the workshop aimed at initiating contact and communication between the participating scholars with the goal to elaborate how each discipline can profit from one another and how the connection between them can create a more holistic picture of global crises phenomena. Each participating discipline at our workshop is encouraged to learn from the results of the others where they suspect their own disciplinary weaknesses and where a more holistic view leads to a better and practical useful insight toward the prevention of global crises. Furthermore, in this contribution we synthesize the workshop's links between the participating disciplines to a more comprehensive framing of global crises phenomena. To this end, we apply the concept of global governance, which is able to connect the respective research in a viable way.[12]

C. Framing Perspectives on Global Crises

What determines a crisis – the "peak of a dangerous development" – and in particular, what determines a *global* crisis? A recent economic contribution discusses ten major challenges of global magnitude and, analyses (not explicitly) two kinds of crises.[13] Several dangerous developments are national or local crises which have no direct global (or international) development at its core, but receive their so-called global character from the fact that the crises exist in several countries and are publicly discussed as a big issue of mankind. An example would be

10 Barry *et al*., *supra* note 4, 28-29 (cited text is from 29).

11 Ongoing interdisciplinary research reacts to such difficulties and reflects these in developing epistemological and methodological frameworks. See R. Frodeman *et al*. (eds), *Oxford Handbook of Interdisciplinarity* (forthcoming 2010), Chapters 3 and 7.

12 G. F. Schuppert, Governance im Spiegel der Wissenschaftsdisziplinen, in G. F. Schuppert (ed.), *Governance-Forschung. Vergewisserung über Stand und Entwicklungslinien* (2005), 371-469, especially, 373-374.

13 B. Lomborg (ed.), *Global Crises, Global Solutions*, 2nd ed. (2009).

malnutrition in many developing countries that does not incur direct repercussions on other countries. The second kind of crises is the one of actual global character, as its causes are stemming from several national sources or even an international source, and culminate in effects that affect several locations at the same time and are not controllable by local/national authorities.[14] The latter depicts what we refer to by the phrase *global crises phenomena*, and from our viewpoint it is this kind of 'peak of a dangerous development' that has undergone significant change within the last decades.

I. Global Crises Phenomena

Giving a historical review on global crises is outside the scope of this contribution. Instead we argue for a particular vantage point of what made crises truly global within the last fifty years. The argument here is that our societies were able to reduce transaction costs of global exchange tremendously, thereby generating a pronounced boost in international exchange relationships.[15] Yet this development also cleared the way for increased externalities, which could not be borne by legitimized authorities – the externalities outgrew the authorities.

Consequently, a crisis' global character is derived from its creation of international externalities, which cannot be controlled by traditional (especially nation-based) authoritative institutions. One blurry feature remains, namely whether a strategic choice of national autarky is a valid option in order to circumvent the external effects on a nation: There are crises where these exclusionary strategies are at least a theoretical option, even if highly improbable;[16] there are, however, also phenomena of such kind that make it simply impossible to exclude a territory from its external spill-overs, which is particularly true for natural disasters. In this light, we see the challenge of controlling, or internalizing, external effects from intensified international exchange as central concept at the core of global crises phenomena, and accordingly as decisive for prevention and solution mechanisms.

On the question how to internalize international externalities, one can take several vantage points. In the vein of the workshop contributions and discussion we focus particularly on institutional and efficiency-related

[14] This is mainly due to external effects, climate change being the popular example.
[15] R. Gilpin, *Global Political Economy* (2001), 5-13.
[16] One might think of national exclusion from international capital markets by prohibiting foreign investments.

questions of valid strategies, structuring potential mechanisms along three dimensions: The first dimension is the *level of governance*, ranging from global/transnational over regional, national, to local. The second dimension is the possible *form of codification* between the extremes of hard law and soft law[17] and also implies the categorization of formal – informal rules. Finally, the third dimension is the question about the *mode of governance*: along the public – private, as well as the inclusive – exclusive[18] spectrum.

Manifold governance issues arose along these vantage points throughout the workshop sessions, but cascaded into three pivotal topics, namely the viability and legitimacy of multi-level-governance solutions, secondly G20-related structural fissures in the global governance regime, and finally regionalism as a possibly underestimated alternative or supplement. In the following parts, we will frame these concepts and offer critical insights in relation to the connected factual challenges.

II. Conceptualizing Multi-Level-Governance

As demonstrated previously, countering the global crises is a social enterprise that concerns humanity as a whole. Although not all solutions may necessarily be international in nature, it is a truism that the actors of the international system will have to deal with global crises and their solution. This system is characterized by the interaction of a multitude of actors at a multitude of layers dealing with a multitude of issue areas. However, measures taken on several levels by multiple actors within the context of diverse policy fields may contradict each other. It is by no means uncontested who should take the lead and what methods to employ when dealing with a particular crisis. We currently see several strategies at work: For example, in relation to climate change, the attempt to reach a global

17 We are also including loose cooperation agreements into account, even though these do not constitute codifications in the strict judicial sense.

18 The inclusion – exclusion dimension draws upon political economy literature analyzing, whether political economy mechanisms and decisions are rather of a nature including affected groups into the decision making process as well as in the resulting economic system (see e.g. P. Mooslechner *et al*., 'Financial Market Regulation and the Dynamics of Inclusion and Exclusion', in P. Mooslechner *et al*. (eds), *The Political Economy of Financial Market Regulation. The Dynamics of Inclusion and Exclusion*, (2006); this distinction mirrors the democratic legitimacy deficit stemming from non-democratic club model approaches to governance as opposed to legitimate democratic processes, see e.g. D. Drezner, *All Politics is Global: Explaining International Regulatory Regimes* (2008).

consensus in form of a treaty through multilateral negations (yet accompanied by action on a regional[19] and domestic level[20]) is dominant. In relation to the current financial crisis, the G20 attempt to take the lead (thus leaving many states on the sidelines), while at the same time the focus seems to be less on creating multilateral treaty law but rather on better coordination and possibly the building of institutions.

The impression of the current global system is that of a system undergoing rapid change.[21] Global crisis contribute to these changes and may serve as catalyst for them in various ways: First, they may lead to the establishment of new institutions and orders. For example, one early outcome of the current financial crisis is the replacement of the Financial Stability Forum with the new Financial Stability Board. We may also see the G20 emerge as a powerful actor in the wake of the financial crisis. Secondly, global crises may also challenge existing regulatory mechanisms, possibly causing them to collapse. Lastly, the collapse of a subsystem of international law in itself may constitute or trigger a crisis – for example, a complete breakdown of the Nuclear Non-Proliferation Treaty may be seen as a crisis in its own right.[22] In sum, global crises are closely connected to the state of the current system of global governance. Studying this system is thus crucial for understanding the dynamics behind global crises.

The term "global governance" was coined in the discipline of international relations. As an analytical concept, it came to prominence with the publication by James N. Rosenau and Ernst-Otto Czempiel "Governance without Government"[23] in 1992. They reacted to ongoing debates about the dynamics and structure of international politics in a time of rapid transformation through globalization processes. In their thinking, the concept of global governance denoted all types of control in transnational politics at all levels of social interaction if related to transnational

[19] E.g. the EU Emissions Trading System based on Directive 2003/87/EC.

[20] E.g. national subsidies for the green energy sector.

[21] D. Kennedy, *supra* note 2, 37, 38-42 and 68.

[22] For a study of the relevance of the nuclear non-proliferation regime see A. L. Paulus & J. Müller, 'Survival Through Law: Is there a Law Against Nuclear Proliferation?', 18 *Finnish Yearbook of International Law* (2007), 83.

[23] J. N. Rosenau & E.-O. Czempiel (eds), *Governance without Government: Order and Change in World Politics* (1992). For a detailed account of the scientific and political background of the emergence of the concept of global governance see D. Messner & F. Nuscheler, Das Konzept Global Governance – Stand und Perspektiven, in Stiftung Entwicklung und Frieden (ed.), *Global Governance für Entwicklung und Frieden. Perspektiven nach einem Jahrzehnt* (2006), 18-81.

repercussions.[24] Other authors have highlighted that there has not only been a diversification of actors, but also a “disaggregation” of the state, which is thus no longer necessarily a unitary actor in international relations.

As an analytical concept, global governance refers to different levels of societal interaction (global, regional, national, local) and therefore stands for the understanding of world politics as a complex multilayered system. Recently, studies in regional governance, especially on the European Union, have become an important topic of governance studies.[25] At the same time, the concept differentiates between various types of social regulation. Beyond the typical steering mode of political authority and market coordination, it includes further modes such as scientific expertise, legal regulation as well as the regulatory role of solidarity.[26]

However, the term has also been used as a normative or political concept. When used in this context, global governance stands for the political will to regain control of globalized politico-legal and economic structures of the world market. As a matter of fact, international organizations like the UN or the G20 too are political reactions to globalization.[27] In this vein, some proponents of the concept express hope that international organizations may fill the regulatory gap that was left after the end of the Cold War.[28]

It is not always possible to distinguish between the various competing understandings of global governance, since academics have used the concept to combine both analytical and political or normative elements.[29] Politicians have also taken up the concept eagerly. For example, in 1995 the Commission on Global Governance published a report, detailing its concept of a reformed order of global governance. [30] The commission comprised active and former high-ranking politicians. One of its key suggestions was a profound reform of the United Nations. Yet in its

24 K. Dingwerth & P. Pattberg, ‘Global Governance as a Perspective on World Politics’, 12 *Global Governance* (2006) 2, 189-190.

25 For an overview see B. Kohler-Koch & R. Eissing (eds), *The Transformation of Governance in the European Union* (2005) and Schuppert, *supra* note 12.

26 H. Willke, *Global Governance* (2006), 42-73.

27 Dingwerth & Pattberg, *supra* note 24, 193-196 point at criticism of this concept, since it is seen as disguising negative aspects of globalization in favor of the highly industrialized states.

28 E.-O. Czempiel, *Weltpolitik im Umbruch: Das internationale System nach dem Ende des Ost-West-Konflikts* (1991), 82-85.

29 Dingwerth & Pattberg, *supra* note 24, 195.

30 Commission on Global Governance (ed.), *Our Global Neighbourhood* (1995).

definition of governance, formal institutions play an important, but no exclusive role:

> "Governance is the sum of the many ways individuals and institutions, public and private, manage their common affairs. It is a continuing process through which conflicting or diverse interests may be accommodated and co-operative action may be taken. It includes formal institutions and regimes empowered to enforce compliance, as well as informal arrangements that people and institutions either have agreed to or perceive to be in their interest."[31]

The concept is thus open for complex and diverse forms of governance beyond the classic forms of intergovernmental cooperation through diplomacy and international organizations. In particular, the diversification of actors is taken into account. However, while global governance as a purely analytical tool may tell us a lot about how the global system actually works, it tells us little about how things *should* work – despite the efforts made at understanding global governance as a normative concept. The question how and from where any form of governance may obtain its legitimacy remains largely unanswered.[32]

International lawyers have taken up the question. The whole debate about the fragmentation or constitutionalization of international law may be seen as part of an ongoing effort to understand global governance and the role norms play within that system.[33] Nevertheless, the legal structure of the emerging new system of global governance is by no means clear. Some authors speak of a fragmentation of international law. [34] According to this

31 Commission on Global Governance, *Id.*, 2.

32 A. L Paulus, *Die internationale Gemeinschaft im Völkerrecht* (2001), 114.

33 J. L. Dunoff & J. P. Trachtman, 'A Functional Approach to International Constitutionalization' in J. L. Dunoff & J. P. Trachtman (eds), *supra* note 2, 3, 4.

34 G. Teubner & A. Fischer-Lescano, Regime-Collisions: The Vain Search for Legal Unity in the Fragmentation of Global Law, 25 *Michigan Journal of International Law* (2004) 4, 999; for a general assessment of the impact of fragmentation on international law see the Report of the Study Group of the International Law Commission, ILC Report A/61/10, 2006, XII, paras 237-251; cf. B. Simma & D. Pulkowski, 'Of Planets and the Universe: Self-Contained Regimes in International Law', 17 *European Journal of International Law* (2006) 3, 483; for an assessment of the impact of fragmentation on a concrete global crisis, see H. van Asselt, F. Sindico and

view, international law will fray out into various legal systems that are governed by their own principles and rules. These systems are not necessarily connected to each other and the principles governing them may have little to nothing in common. If this is true, it would at least be highly questionable if international law may be the central tool for countering global crises, since global crises frequently have an impact that is felt beyond a single issue area.

However, numerous authors have striven to identify common overarching principles in international law – usually discussed as the idea of constitutionalism in international law.[35] Some authors have focused on the UN Charter and tried to describe it as the constitution of the international community.[36] Whether this approach may be warranted or not, at least in the context of global crises focusing exclusively on the UN Charter would be far too narrow, given the broad range of issue areas and the law governing them that are touched upon by global crises.

Other authors try to harness constitutionalist ideas in a broader way. Martti Koskenniemi calls for "constitutionalism as mindset".[37] Andreas Paulus asks for a "constitutional reading of the international legal foundations on which today's fragmentation of international legal rules rests."[38] In a similar vein, Jeffrey L. Dunoff and Joel P. Trachtman propose a functional approach, advocating a "check list" which will enable the academic to identify norms that serve a constitutional purpose.[39] This rather cautious, functional approach may also be of relevance when analyzing the role of law in global crises situations. In the domestic sphere, constitutional norms are designed as fundamental norms able to withstand any crisis not amounting to outright revolution. Norms of this kind are also needed in

M. A. Mehling, 'Global Climate Change and the Fragmentation of International Law', 30 *Law & Policy* (2008) 4, 423-449.

35 For recent contributions to the debate, see J. L. Dunoff & J. P Trachtman (eds),*supra* note 33; J. Klabbers, A. Peters & G. Ulfstein, *The Constitutionalization of International Law* (2009), V. Jackson, *Constitutional Engagement in a Transnational Era* (2009). Other disciplines have also dealt with the question, cf. e.g. J. Habermas, *Der gespaltene Westen* (2004), 113-193.

36 B. Simma, 'From Bilateralism to Community Interest in International Law', 250 *Recueil des Cours* (1994 VI), 258-283; B. Fassbender, *The United Nations Charter as the Constitution of the International Community* (2009); cf. M. W. Doyle, 'The UN Charter – A Global Constitution?' in J. L. Dunoff & J. P. Trachtman (eds), *supra* note 2, 113-132.

37 M. Koskenniemi, 'Constitutionalism as Mindset: Reflections on Kantian Themes about International Law and Globalization', 8 *Theoretical Inquiries in Law* (2007), 9.

38 Paulus, *supra* note 32, 69, 71.

39 Dunoff & Trachtman, *supra* note 33, 3, 9.

international crises management and prevention. They may constitute a "backbone" structure of international law, holding together the different subsystems of the international legal system.

Although it is by no means clear that domestic constitutional principles will serve the same function in the international sphere, this nevertheless seems to be at least a good assumption to start off with. After all, the principles identified have been developed in hundreds of years of constitutional practice and thus stood the test of time on the domestic level.[40] In contrast, the genuinely international principle of state sovereignty is neither able to guide the solution of international conflicts, nor is it helpful when allocating scarce resources.[41] Moreover, although some of the principles are clearly not neutral formal principles, but rather rooted in the western democratic tradition,[42] in the absence of any competing constitutional models that have proven to be more successful it seems to be a plausible assumption to operate with these concepts.

Consequently, these functional approaches may help to identify norms that are likely to stand the test of global crises. Norms of a constitutional character are less likely to fall prey to a state-of-the-exception rhetoric aimed at shaking off all legal bonds. However, this is exactly what some authors (and probably some politicians) seem to prefer, when declaring that in times of crisis, (international) law has to remain silent. This idea is not only dangerous, but in effect contrary to the whole idea of international law as a set of rules making behavior predictable and manageable even and especially in times of crisis. On the contrary, times of crises are times of law. This is why the study conducted by Maria Agius is such a timely contribution to the debate.[43] She outlines that law may indeed exert influence on the actors in times of crisis, despite the constant temptation to

40 Paulus, *supra* note 32, 90.

41 For an overview of the problems associated with the classic concept of sovereignty cf. J. H. Jackson, 'Sovereignty-Modern: A New Approach to an Outdated Concept', 97 *American Journal of International Law* (2003) 4, 782; see also G. Nolte, 'Sovereignty as Responsibility?', *Proceedings of the 99th Annual Meeting of the American Society of International Law* (2005), 389-39. An Hertogen suggests that the current definition of monetary sovereignty is outdated and that a reframing of the principle is warranted, 'An Unusual Suspect? Monetary Sovereignty and Financial Instability', 2 *Goettingen Journal of International* Law (2010) 1, 243-266.

42 B. Fassbender, 'Rediscovering a Forgotten Constitution' in Dunoff & Trachtman, *supra* note 2, 133, 139-140.

43 M. Agius, 'Dying a Thousand Deaths: Recurring Crises and Exceptional Measures in International Law', 2 *Goettingen Journal of International Law* (2010) 1, 219-242.

revert to a claim of a state of emergency. However, she also points to the fact that law, to be effective in times of crisis, has to provide a necessary degree of flexibility in order to allow for the accommodation of extraordinary interests in exceptional situations.

In sum, we are connecting to the ongoing debate about and the continuing development of the concept of global governance in three aspects:

1. An understanding of the global system as a complex multi-layered structure containing different types of social regulation, which go beyond the scope of state-based authority and market-based coordination.
2. Understanding the concept of governance as a bridging-concept capable of bringing together scientific results of various disciplines by focusing on the importance of institutions for the implementation of governance mechanisms, by looking at governance from a structural perspective and viewing it as a theory of regulation.
3. Stressing the need to connect the discussion about global governance to the debate about the fragmentation or constitutionalization of international law, with a particular focus on studying principles that enable norms to guide behavior even in times of crisis.

Not only is a better understanding of global governance in times of crisis needed, but also a better understanding of how norms operate in these situations and how they should be designed so as to remain operable even under intense pressure. Research presented at the workshop demonstrates that both aspects may be successfully pursued. In particular, two layers of the current global order were studied during the workshop, namely global actors with a focus on the G20 and regional initiatives. Consequently, we will turn to these actors in greater detail in the following parts.

III. The Developing Role of the G20

The 1970s were a challenging decade for the industrial countries due to the oil price shock of 1973, the first repercussions of economic and financial globalization following the abolition of the Bretton Woods system and the first appearances of recession. In 1978 German Chancellor Helmut Schmidt and French President Giscard d’Estaing initiated the formation of the Group of Seven (G7), consisting of the then major world economies United States, Japan, Germany, France, United Kingdom, Italy and Canada.[44] Its aim was to strengthen global economic governance through regular meetings of the member's finance ministers and heads of state. Furthermore, the G7 was devoted "[…] to diffuse globally its core principles of 'open democracy, individual liberty and social advancement.' "[45] In the 1990s the G7 was expanded to the G8 by the inclusion of Russia.

Due to the rapid economic development of countries in South America, the Middle East and Asia and their ever growing integration into the international financial system, it became necessary to broaden the membership of the G8. In 1999, after testing summits like the G22 or the G33, the G20 emerged, in part also as an answer to the Asian financial crisis in 1998-99. The first meeting was held in Berlin on December 15-16 under the chair of the Canadian and German finance ministers.[46] The aim of the creation of the G20 was to take account of the changing distribution of international economic importance and widening its scope beyond the strong Anglo-American influence on agenda- and norm setting. In this regard, it was expected by some scholars that "[t]he focus of the new G-20 forum would be on global economic governance broadly constructed to include trade, finance, health, environment, education, human security, poverty reduction, and conflict resolution, thereby extending beyond the realm of ministers of finance."[47] After its creation the activity of the G20 was based on regular meetings where the agenda was increasingly set by members outside the G8. The G20 became more open to ideas from its new members. Despite open organizational issues concerning a possible

[44] C. Bradford Jr. & J. F. Linn, *Global Economic Governance at a Crossroads: Replacing the G-7 with the G-20*, The Brooking Institution Policy Brief # 131 (April 2004), 1, available at http://www.brookings.edu/~/media/Files/rc/papers/2004/04globaleconomics_colin%20i%20%20bradford%20%20jr/pb131.pdf (last visited 29 January 2010).

[45] J. Kirton, *From G7 to G20: Capacity, Leadership and Normative Diffusion in Global Financial Governance* (2005), 1, available at: http://www.g7.utoronto.ca/scholar/kirton2005/kirton_isa2005.pdf (last visited 28 January 2010).

[46] See the G20 Homepage http://www.g20.org/about_what_is_g20.aspx (last visited 29 January 2010) as well as Bradford & Linn, *supra* note 44, 2-6.

[47] *Id*., 6.

permanent secretariat or an annual head of state meeting,[48] it became an important enhancement of the G8.[49]

However, the financial crisis of 2007-9 sheds new light on the aim, membership, organizational structure and policy scope of the G20. Is the G20 able to become an institution that reflects and incorporates the ongoing transformation of the global system and the changing shift of economic and political power?[50] The expectations were high, as experts referred to Bretton Woods[51] to articulate the importance of the G20 meetings during the peak of the financial crisis 2007-9 and to evaluate their outcomes. The logic behind these expectations seems to be that a financial crisis of such an enormous scale has to be followed by the institutionalization of more effective and better enforceable global norms for the financial markets. A review of the literature on the financial regulation by the G20 demonstrates some contours of what seems necessary and possible.[52]

First of all, the G20 remains in narrow contact to technocratic international bodies of the world finance architecture and remains in most cases reliant on their expertise and infrastructure to pass declarations. A very important institution in this regard remains the Financial Stability Forum (FSF, established 1999, now FSB),[53] which in the wake of the financial crisis made about 60 recommendations concerning global financial regulation. In its final declaration the "G20 Leader Summit on Financial Markets and the World Economy" in Pittsburgh 2008 heavily relied on these recommendations made by the FSF.[54]. This is emphasized by Régis Bismuth's contribution to this volume where he outlines the technocratic power of international bodies such as the International Organization of Securities Commissions (IOSCO) or the Basel Committee on Banking

48 *Id*., 7.

49 Kirton, *supra* note 45, 20.

50 In his contribution to this special issue of the GoJIL Luca Schicho points at the important role of Sovereign Wealth Funds (SWFs); an issue that until now has not been included into the scope of the G20 'Pride and Prejudice: How the Financial Crisis Made Us Reconsider SWFs', 2 *Goettingen Journal of International Law* (2010) 1, 63-92.

51 E. Helleiner & S. Pagliari, 'Towards a New Bretton Woods? The First G20 Leaders Summit and the Regulation of Global Finance', 14 *New Political Economy* (2009) 2, 275-287.

52 A thorough evaluation will be provided in our empirical section D.

53 The FSF has been transformed into the Financial Stability Board (FSB) after the G20 meeting of 2 April 2009.

54 Helleiner & Pagliari, *supra* note 51, 276-277.

Supervision (BCBS) in creating internationally recognized standards for international finance without being subjected to democratic legislative processes.[55]

Secondly, the ongoing transformation of the global system has been accelerated by the financial crisis with fierce repercussions on the fiscal stability of Western governments[56] and left countries at the fringe of bankruptcy. These states, therefore, might lose their central power position in the system of global governance, which in the past was backed by their economic performance and the dominance of their models of financial and economic regulation. It is not yet clear if the G20 will be able to include ideas and policy concepts of members like Brazil, India and China to connect those regions more efficiently into the global economic and financial system and step in where the Anglo-American concept of international finance lost its integrative function in the system of global governance. The trend toward regional fragmentation in the governance of economic and financial issues grows stronger and as a consequence it might become ever more complicated to regulate those issues on a global scale.[57] Therefore, and despite its outstanding position in the system of global governance and its ability to transmit decisions regarding the global economic and financial system into international organizations like the World Trade Organization (WTO) or the International Monetary Fund (IMF), the G20 faces serious challenges created by the financial crisis 2007-9 and the power shift in the global system. At the same time, it remains to be seen if the G20 will strengthen or undermine the United Nations and the legal order centered on the UN. Moreover, the G20 will also have to face serious questions as to its representativeness and consequently also to its legitimacy.

55 R. Bismuth, 'Institutional Issues in International Financial Governance: The International Activity of Independent Financial Regulatory Authorities', 2 *Goettingen Journal of International Law* (2010) 1, 93-110.

56 R. C. Altman, 'The Great Crash, 2008. A Geopolitical Setback for the West', 88 *Foreign Affairs* (2009) 1, 2-14.

57 E. Helleiner, 'Reregulation and Fragmentation in International Financial Governance', 15 *Global Governance* (2009) 1, 16-22 and M. Beeson & S. Bell, 'The G-20 and International Economic Governance: Hegemony, Collectivism, or Both?', 15 *Global Governance* (2009) 1, 67-86.

IV. Aspects of Regionalism

Even though emerging countries like Brazil or Indonesia are now members of the G20, developing countries like Cambodia, Ecuador or Senegal are not represented. Developing countries are internationally less integrated and have only little influence on other international institutions, like the World Bank, IMF and WTO. In addition, the impact of global crises is felt differently in developing countries. Thus, it can be expected that solution strategies proposed by the G20 do not consider comprehensively their special problems. Therefore the question has to be asked how they may successfully deal with global crises.

The present financial crisis affects developing countries even though they are only weakly connected to the international financial market. They are not fully detracted from the breakdown of the American subprime market but rather influenced by the side-effects of the financial disturbances. The transmission channels are the decrease of remittances, the decline of capital flow as well as the impact on trade and international prices of primary products.[58] Remittances decline due to a worse labor market in the industrialized countries. Capital flows decrease because international investors have a strong need for capital. Therefore, they absorb the losses caused by the subprime market crash rather than invest in new projects in developing countries. Uncertainty and increased capital costs reduce consumption and investment. Consequently, international trade declines and the prices for primary products, which are mainly exported by developing countries, decrease. Overall, the financial crisis reduces private income and GDP growth, which in turn may lead to an increase of social tensions. In other types of crises, such as pandemics or climate change, developing countries are affected worse, simply because they lack the necessary financial and technological means to deal with the effects of these crises. Consequently, it is crucial to examine how to reduce the vulnerability to occurrences of global crises and how to respond, if a global crisis starts to affect their domestic economy and society.

There are relevant arguments that regional cooperation of countries makes local economies more robust in respect to external shock like global

[58] S. Griffith-Jones, J. A. Ocampo, 'The Financial Crisis and its Impact on Developing Countries', 53 *International Policy Centre for Inclusive Growth Working Paper* (2009) and W. Naudé, 'The Financial Crisis of 2008 and the Developing Countries', 2009/01 *UNU-WIDER Discussion Paper*, (2009).

crises. Moreover, such cooperation supports sustainable development.[59] A free trade and free capital flow area increases the market size for companies, which only have operated in their home country before. Thus, companies can better make use of economies of scale and increase sales volume. Capital can be used where it is more productive. Moreover, the level of competition increases, since foreign companies enter the domestic market. All mechanisms force companies to produce more efficiently. In addition, harmonized standards, less trade barriers as well as less capital controls reduce bureaucracy related transaction costs. Overall, a plus of efficiency increases the per capita income of the local population.

However, changes of the economical environment might be accompanied by harmful adjustment processes for at least part of the society.[60] Some sectors may fail to face growing competition with the result of job losses and others may unreasonably take profit of new chances of economic development.

A country with low economic power has no influence on the conditions of the global world market. Therefore, a quick integration in the global economy might go hand in hand with uneven economic development.[61] The advantage of regional coordination is that thereby even states with a small economy are able to influence the rules of transition in dealing with its regional partners. Consequently, painful adjustment processes can be stretched over a longer period of time, which allows companies to improve productivity and people to adapt to new economic environments.

Nevertheless, game theory proposes that negotiation may fail, if countries profit differently from regional cooperation treaties. If this happens, there are incentives for countries to take into account only their own advantage in the negotiation process. Hence, negotiations fail or the

[59] A. L. Booth, *The Economics of the Trade Union*, (1995) and J. Agnew 'From the Political Economy of Regions to Regional Political Economy', 24 *Progress in Human Geography* (2000) 1, 101–110 and H. Dieter & R. Higgott 'Exploring Alternative Theories of Economic Regionalism: From Trade to Finance in Asian Co-operation', 89 *CSGR Working Paper* (2002), available at http://www2.warwick.ac.uk/fac/soc/csgr/research/workingpapers/2002/wp10702.pdf (last visited 14 March 2010).

[60] P. G. Cerny, 'Restructuring the Political Arena: Globalization and the Paradoxes of the Competition State', in R. D. Germain (ed.), *Globalization and Its Critics: Perspectives from Political Economy* (2000).

[61] G. Esping-Andersen, 'Positive-Sum Solutions in a World of Trade-Offs?' in G. Esping-Andersen (ed.), *Welfare States in Transition: National Adaptations in Global Economies* (1996).

overall outcome of regional cooperation is less than optimal. Franziska Müller concludes that in the case of the Southern Africa Development Community only a small part of the potential of regional co-operation is exploited.[62] This is due to the diversity of the participating states, which leads to differing state interests. However, new international institutions like the African Development Bank start to play the promising role of an external adviser, bringing countries together in order to find overall efficient strategies.

An important precondition for regional cooperation is that the local institutions are able and have the power to effectively enforce agreements on a local basis.[63] In addition, local regulatory institutions need to keep pace with companies increasingly challenged by competition. It is probable that market deficiencies are exploited to a greater extent if every amount of return is potentially crucial for the continuance of business activities. Thus, especially markets with sensitivity to market failures need to be soundly regulated in a competitive environment. This is particularly the case for financial markets because of their addiction to information asymmetries, moral hazard, non-fundamental speculation and excessive risk-taking.[64] Laurissa Mühlich analyses cases of regional monetary cooperation in South East Asia, South Africa as well as Central and South America.[65] Regional monetary cooperation may lead to deeper financial markets which ease credit taking and reduce financial volatility. However, for success a role model seems to be crucial that offers sound regulation practices other countries can easily rely on.

In the middle of a crisis, regional cooperation may lead to information sharing and a pooling of resources for concentrated action. Partners can profit on the mutual experience of solution strategies. Again it must be avoided that countries take into account their own advantage only and apply

62 F. Müller, 'Storming, Norming, Performing: Implications of the Financial Crisis in the Southern African Development Community', 2 *Goettingen Journal of International Law* (2010) 1, 167-190.

63 D. C. North, *Institutions, Institutional Change, and Economic Performance*, 16th ed. (2004).

64 J. E. Stiglitz, 'Markets, Market Failures, and Development', 79 *The American Economic Review* (1989) 2, 197-203.

65 L. Mühlich,' Regional Monetary South-South Cooperation', 2 *Goettingen Journal of International Law* (2010) 1, 135-166.

"beggar thy neighbor" strategies.[66] International actors with local ties like regional development banks might coordinate proceedings to reach overall efficient arrangements.

In the context of the global governance architecture regional cooperation is a promising tool to avoid and fight against negative impacts of global crises. The more willing countries are to cooperate and the better local institutions are able to conduct negotiated decisions, the more effective it is. Role models and "neutral" mediators help to exploit the whole potential. For developing countries, it is one important tool for sustainable development. And having the success story of the EU in mind, which is now by itself a member of the G20, regional cooperation may be an approach to take over a part of global economic as well as political significance in the future.

D. The Global Financial Crisis 2007-9 as a paradigm

Taking the workshop results into account, we encounter several questions regarding the mechanisms apt to control global crises. Multi-level-governance, as well as G20-related and regional solutions are on the table. Turning to our paradigmatic case, namely the financial crisis of 2007-9, it manifested as a clearly global phenomenon in our above definition. Recent studies have highlighted that causes as well as effects had undeniable national variations, but also that the turmoil as such clearly exhibits that spill-over effects such as the US-American sub-prime crisis have spread throughout the world in hours.[67]

As prerequisite of an evaluation of the levels of solution mechanisms, it is mandatory to distinguish what the truly global facets of the crisis are and what we consider as constituting an international, a transnational, regional, national or local solution/prevention mechanism. While we will discuss the global magnitude of the causes of the crisis within the analysis, we want to clarify at this point that we consider a mechanism or instrument

66 J. E. Stiglitz, 'Beggar-Thyself versus Beggar-Thy-Neighbor Policies: The Dangers of Intellectual Incoherence in Addressing the Global Financial Crisis', 66 *Southern Economic Journal* (1999) 1, 2-38.

67 B. Eichengreen *et al.*, 'How the Subprime Crisis went Global: Evidence from Bank Credit Default Swap Spreads', NBER Working Papers (2009), 14904, available at http://www.nber.org/papers/w14904 (last visited 13 March 2010); S. Shirai. 'The Impact of the US Subprime Mortgage Crisis on the World and East Asia', Munich Personal RePEc Archive Papers (2009), 14722, available at http://mpra.ub.uni-muenchen.de/14722/1/MPRA_paper_14722.pdf (last visited 14 March 2010).

as international, when it is an agreement on the level of national governments of states from at least three continents that inherits at least a minimal set of binding arrangements targeted to or at least open to all states.[68] Regional mechanisms differ in that they encompass only a regionally coherent group of countries that belong to one or two continents and have some common institutional or societal background. National solution and prevention is characterized by single actions of national authorities, while transnational activities are such that incorporate decision makers which are clearly separate from their national governments, but that negotiate somehow for their nations.

Our central aim is to infer from responses targeted at the current financial crisis to global crises solutions and prevention mechanisms in general. For this purpose, we build upon a secondary analysis of several investigations into the roots of the turmoil, and devise a three-dimensional categorization of the causes. Subsequently, the resulting structure can be applied to embed the reactions to the crisis witnessed so far (December 2009). In this regard, we turn to mechanisms aimed at preventing future crises as well as solutions to curbing the present one. The advantage is a clearly traceable and tractable analysis.

Reviewing the economic and political economy literature on the causes of the financial havoc,[69] and deriving a bird's-eye perspective, we sketch the crisis as one *enabled* by *macro-imbalances* stemming from a mixture of historical accident and political failure in the reaction to it, then *initiated* by *financial market failures* due to excessive risk taking and opaqueness, and finally *deepened and widened* through *regulatory failures* in supervising and preventing the havoc.[70]

[68] When referring to the term 'binding', we also include mechanisms of political and social peer-pressure, as well as market or competition-induced pressure, not only legally binding contracts.

[69] See e.g. V. Acharya & M. Richardson (eds), *Restoring Financial Stability: How to Repair a failed system* (2009), and C. Goodhart, 'The Background to the 2007 Financial Crisis', 4 *International Economics and Economic Policy* (2008) 4, 331; furthermore M. Hellwig, 'Systemic Risk in the Financial Sector. An Analysis of the Subprime-Mortgage Financial Crisis', *Reprints of the Max Planck Institute for Research on Public Goods* (2008) 43, as well as J. Taylor, 'The Financial Crisis and the Policy Responses: An Empirical Analysis of What Went Wrong', *NBER Working Paper* (2009) 14631, available at http://www.nber.org/papers/w14631 (last visited 14 March 2010).

[70] Actually, we identify seven broad categories, but refrain from going into too much detail here, since the evaluation of the crisis' causes is not our aim. For the derivation of the causes, consult the quoted contributions. The seven factors are: central bank

Turning to the prevention of future crises, as outlined above, we see *macroeconomic imbalances* at the root of the subprime crisis, as these enabled the huge asset bubbles, which burst during the turmoil, to evolve. We argue that historically relevant events and political reactions to these events enabled financial markets to grow beyond reasonable market size: In reaction to the Asian financial crisis in 1997-8, as well as to the dot.com-crisis and to the terrorist attacks of 9/11 central banks around the globe, but particularly the US Federal Reserve Bank (Fed), reacted with the injection of increased liquidity into financial markets in order to prevent severe economic downturns.[71] This central bank capture resulted eventually in the origination of excess liquidity.[72] The evolving credit bubble in the US and other developed economies was furthermore fuelled by global accounts of payment imbalances.[73] Bluntly put, the emerging economies in East Asia, Eastern Europe and elsewhere with their high saving rates and their transfer through the international capital markets have fed the systems of those states with highly developed financial services industries.[74] The global dimension of these capital-driven roots is obvious, as the problems only arose because of the free exchange possible within global financial markets. Even though the central bank driven liquidity could also arise in an autarky, in a global capital market it almost inevitably results in international spill-overs.

Yet, were the solutions and ideas for future prevention mechanisms comparably global? Yes and no.[75] While the central bank and macroeconomic policies remain clearly within unrestricted national

driven excess liquidity, global payment imbalances, sub-optimal exorbitant risk-taking of investors, opaqueness within financial firms and the system as a whole, principal-agent-related problematic of rating agencies, regulatory supervision failure; adding a further component, we see principles of financial regulation allowing the risky strategies, opaqueness, and rating-agency influence, i.e. transnational regulatory failure; the last determinant, however, is a perspective not shared by most economic analyses, but rather stems from political economy evaluations.

71 V. Acharya, *et al*., ‘Prologue: A Bird’s-Eye View. The Financial Crisis of 2007-2009: Causes and Remedies’, in V. Acharya & M. Richardson (eds), *Restoring Financial Stability: How to Repair a Failed System* (2009), 1.

72 See e.g. Goodhart, *supra* note 69, 332-3, as well as Taylor, *supra* note 69, 2-3.

73 A. Kern & C. Fahrholz, ‘Global Imbalances and a Trade-Finance-Nexus’, *Journal of Financial Economic Policy* (2010, forthcoming).

74 See Acharya *et al*., *supra* note 71, 13.

75 The following analysis of the crisis’ causes and the remedies taken is based on a thorough evaluation of national, regional and global initiatives between January 2007 and October 2009 and thereby relies on several secondary analyzes as well as official documentation (each as quoted). A protocol of the single assessments in tabular format can be obtained from the authors upon request.

authority, institutional re-arrangements have been undertaken within the field of payment disequilibria. Some coordination of central bank policies has been undertaken, informally, during the hot period of market meltdown, but in the long run no preventive coordination seems to follow, leaving this to national (or in the European case supranational regional) approaches.[76] Regarding the prevention of payment disequilibria, however, some substantial institutional rearrangements are underway, mainly reforming the IMF in terms of funding and voting shares. In particular, the IMF lending facilities have been extended and made substantially more flexible.[77] However, the reform remains limited, as only small voting share rearrangements at the IMF and the World Bank are underway. In sum, what we see is a multi-level regime that relies on independent macroeconomic policies, but with enhanced global emergency mechanisms, seeking to prevent global spill-overs.

These macroeconomic enablers were at the root of the financial crisis but did not initiate it. The latter happened due to *financial market failures*: opaqueness and risk-taking. Global financial markets, as integrated and in some instances weakly restricted as they still are, exhibited what some would call ‘textbook market failures’: market participants took excessive risks, because the negative consequences were not felt by them but rather externalized on the whole economy; furthermore, these actors exploited the increasing opaqueness of financial markets, which originated in complex instruments and risk management mechanisms of the big international financial intermediaries, e.g. investments banks. The short-term profit orientation of financial firms led to *excessive risk taking* (and thereby mis-pricing of risk). They were followed by term transformation strategies, i.e. firms and traders lent long in illiquid markets to gain the high interests and associated profits, but refinanced the necessary capital short term thereby putting heavy reliance on repo markets. Put bluntly, they leveraged their capital extremely and relied on the allegedly low risk levels of high yield assets. This was brought to perfection through high-complexity risk management via a multitude of instruments but also utilizing the

76 H. Zimmermann, ‘Conclusion – Whither Global Financial Regulation?’, in E Helleiner, *et al*. (eds), *Global Finance in Crisis: The Politics of International Regulatory Change* (2010).

77 G20, G20 *Leaders Summit in Pittsburgh: Progress Report on the Actions to Promote Financial Regulatory Reform* (2009), as well as S. Katada, ‘Mission Accomplished, or a Sisyphean Task? Japan’s Regulatory Responses to the Global Financial Crisis’, in E. Helleiner *et al.* (eds), *supra* note 76.

opaqueness or the lack of transparency of increasingly complex instruments and markets, i.e. sub-prime mortgages, securitization instruments, special investments vehicles, as well as the derivatives and further over-the-counter (OTC) instruments. The bankers were supported even more by problematic principal-agent issues (that further worsened opaqueness and risk taking): this encompassed the rating-agencies' missing incentive for evaluating risk appropriately and their support of the originate-to-distribute model of mortgages, which reduced incentives of the originator to monitor creditworthiness of the borrower. Last, but certainly not least, came the short-term profit-oriented compensation schemes of financial firms.

The propagated solutions in reaction to these market failures have so far been highly path-dependent in that they are incremental with strong reference to the existing regime and mainly processed by the transnational policy community of national regulators and other technical experts who created the current regime. This regards the enhancements within banking regulation, in particular the refinement of capital adequacy rules, accounting restrictions regarding securitization, trading book and special investments vehicles, establishment of liquidity risk management, and internal risk governance best practices of financial firms. The G20 forum merely adapted these transnational approaches.[78] Nevertheless, this may already be a relevant step forward, particularly taking into account that all G20 countries pledged to implement the Basel II standards.[79] The few substantial reforms that were not just adjustments came from national players: over-the-counter derivative and hedge fund regulation stemming largely from US and UK initiatives.[80] This has been mirrored by increased regional cooperation within the EU, which has also made its influence as transnational player felt: The EU has implemented a multitude of binding regulations and directives aimed at such fields as credit rating agencies, clearing and settlement of over-the-counter derivatives, accounting standards, alternative investment funds, packaged retail investment products, and remuneration of directors of listed companies and employees of financial service firms.[81] Finally, we experienced the power that was retained by private actors in their fight for

78 Helleiner & Pagliari, *supra* note 51, 275.

79 G20, G20 Leaders Summit in Pittsburgh: Leaders' Statement (2009).

80 Helleiner & Pagliari, 'The End of Self-regulation? Hedge Funds and Derivatives in Global Financial Governance', in Helleiner, *et al*. (eds), *supra* note 76.

81 Posner, 'Is a European Approach to Financial Regulation Emerging from the Crisis?', in Helleiner, *et al*. (eds), *supra* note 76.

self-regulatory freedom. Especially the accounting profession remains largely unrestricted from public political influence.[82]

In sum, we see global dedication to an ideal of better regulated financial markets, but also witness the international institutional restrictions, where no sufficient expertise is outside the transnational bodies. At the same time, the pivotal domestic interests of the most powerful players (states and increasingly the EU) focus on what is most important for their domestically determined interests.

These market failures were permitted and even worsened by *regulatory failure* – on a national as well as on a transnational level. National regulatory regimes induced serious moral hazard through ex- and implicit guarantees for too-big-to-fail and too-interconnected-to-fail institutions,[83] which enabled excessive risk taking while externalizing losses. Too-big/interconnected-to-fail problems can be broadly approached by two strategies. The first is prohibiting institutions becoming too big/interconnected. The second being to provide legal rules, institutions and instruments to resolve an insolvent institute, in order to allow politics let such firms fail without too serious social consequences. On the second issue transnational action has taken place, with adoption by the G20 once again. Working Groups around the FSB are elaborating on international supervision of large, complex financial institutions, as well as the resolution of insolvent international firms. With regard to preventing financial intermediaries from becoming too big or interconnected, strategies to deal with this delicate issue have only in rare circumstances reached official consideration, although this may change due to the recent proposals of restricting the scope of banking business by the current US president Obama and the considerations in further countries, emerging in response to the US proposals. So far states abstained from severely restricting banking business – probably due to the potentially incurred economic losses. Interestingly, this might change due to the US initiative – potentially offering evidence in favor of the remaining hegemonic dominance or market power of the US.[84] Yet, even of higher interest seems to be, if the G20 will once again pick up

82 Even though some minor adjustments had to be undertaken by the International Accounting Standards Board (IASB). See A. Nölke, ‘The Politics of Accounting Regulation: Responses to the Subprime Crisis’, in Helleiner, *et al*. (eds), *supra* note 76.

83 Consider the cases of Bear Stearns, AIG, or the German Hypo Real Estate.

84 For this line of argument, see e.g. D. Singer, *Regulating Capital. Setting Standards for the International Financial System* (2007), 13-35.

these ideas and lead to international cooperation. Furthermore, neither the national nor the transnational regulatory authorities accommodated the systemic risks stemming from transformed global financial markets (i.e. the spread of counterparty risk, large and complex financial institutions, and increasing interconnectedness). The latter argument has received high attention on the international level and led to the creation of the Financial Stability Board, which might be seen as the fourth pillar complementing the IFIs and the WTO as pivotal institutions in the governance of the international political economy. The strengthening of this transnational-based institution was a predominantly G20-led objective.

Hence, again, we witness inclusionary public trends on a global scale, but so far this has to build upon existent transnational structures. The unanswered question remains, if the future route goes from transnationalism to more inclusive international decision-making. Currently, there is a clear push towards more international cooperation by the inclusion of the G20 countries into the FSB as well as the transnational bodies of the Basel Committee and the International Organization of Securities Commissions and most importantly through the G20 itself as central international body.

Finally, let us investigate the nature of the *solutions* for suppressing the spread of the current turmoil. There have been largely three kinds of reactions identified: First, (very) short-term reactions to secure liquidity in order to prevent market breakdown; second short to medium term guarantee and bail-out actions to prevent illiquid, but solvent as well as systematically relevant firms from drowning and taking the market with them; and third, medium to long term rescue packages to keep the economy running. Evaluation of the actions undertaken by the G20, transnational, as well as regional and national initiatives suggests that the fast reactions to turmoil were almost exclusively national emergency measures, and thereby had a politically exclusive character, as the national executives took action in a relatively autonomous fashion.[85] The acute counter-measures encompassed liquidity provisions and bail-outs as well as further guarantees to stabilize the financial system.[86] This national domination changed only modestly with the succinct rescue packages: national authorities took the actions they deemed appropriate, but there was a global agreement that state action is necessary and that protectionist measures are to be evaded. This was

85 See E. Tsingou, 'Regulatory Reactions to the Credit Crisis. Analyzing a Policy Community Under Stress', in Helleiner, *et al*. (eds), *supra* note 76, 25-28.

86 Admittedly, after the first liquidity provisions, there has been some coordination among G7 central banks.

developed in the context of the April 2008, April 2009, and September 2009 G20 Leaders' Summits. However, there have been large differences which are difficult to resolve between the states on principles, contents, value and implementation. Duration was also controversial, but there was at least some understanding about the minimum duration negotiated at G20 level. The nation-state's dominance is further emphasized by the fact that regional cooperation was mostly seen in Europe, and the size of it was only minimal;[87] furthermore, transnational cooperation has been absent, except some technical committee reports in response to the upheaval initiated by Bear Stearns in March 2008. The swift replies, necessary in such a menacing turmoil, could only be undertaken by national entities, since no appropriate institutional structures were available. The G20 agreements on preventing 1930s style beggar-thy-neighbor policies was the only limited success on a global scale. Nevertheless, within the G20 process, macro-economic coordination and arrangements about sustained public fiscal impulse are steadily evolving.[88]

E. Policy Implications

What are the quintessential insights for solution and prevention strategies to deal with global crises that we can take from the paradigm of the financial crisis? Although only limited conclusions may be drawn at this time, as the crisis and the reactions are still underway, we see four interesting patterns emerging: (1) increased global coordination and possibly the establishment of new legal rules, (2) currently states newly included into the global governance regime merely take over the rules devised by others, (3) transnational domination due to lack of international alternatives, and (4) domestic powers behind substantial change combined with some extended regional cooperation.

The strategies for encountering the ongoing financial crisis as well as the currently debated political measures to prevent such crises in the future demonstrate a particular feature, namely international coordination in combination with pragmatic transnational detailing and implementation work. While the current level of international coordination seems far-reaching in historical dimensions, it also has enlarged the circle of decision-takers by including important emerging countries along the G20 lines. We

[87] *Id*., 25-28.

[88] G20, Leaders' Statement September 2009, *supra* note 79, as well as G20, Progress Report September 2009, *supra* note 77.

see an increased global coordination in order to solve (and prevent) the (future) global financial crisis (crises), but, at the same time, we witness the lasting, and potentially increasing importance of transnational codification and implementation by private and public transnational bodies.[89]

However, multilateral, inclusive governance is currently limited to agreements on basic principles and some loose form of coordination. The example of the three G20 summits in 2008 and 2009 suggests that a rather small group may provide leadership by setting standards and principles and by developing new rules which may then be discussed and agreed upon with other affected actors. [90] At least this crisis has changed the status of several emerging countries to become rule-takers, but whether these countries will have a significant impact in the future and thereby transform prevention and solution strategies to global mechanisms remains to be seen.[91]

This in turn then strengthens, (at least it did within the context of the current crisis), the transnational bodies of international financial regulation like the Basel Committee and the Financial Stability Board. We may be experiencing an intermediate stage of altered global governance reality: On the one hand, a move towards more inclusion on a somehow (more) international scale, while, on the other hand, the structures, actors, and institutions are not ready or even in place yet. This is why other actors and institutions fill the gap of implementing what a new "global club" (the G20) has coordinated in principle. These are national, regional and transnational actors. Furthermore, we see a mixture of private and public players. Maybe this is all we can currently ask for in terms of global solution and prevention strategies given the dense time frame. This is illustrated by an interesting comparison with the Bretton Woods initiative in 1944, when it took two years and a large number of specialists to prepare the conference, compared to the rather short periods before the last G20 Summits.[92] Projecting this insight onto other policy fields, we need to consider carefully how the institutional settings and capacities differ, as this will impact on the global decision-making capabilities.

89 See E. Tsingou, *supra* note 85, 25-28.

90 Confirming this analysis with regard to the first summit in November 2008 are Helleiner & Pagliari, *supra* note 51, 275.

91 Some even see the G20 as a hindrance towards new global regulatory approaches, as it undermines the club model approach of the G10 that characterized financial market regulation throughout the last three decades, and thereby renders international agreement impossible, see e.g. D. Singer, 'Uncertain Leadership: The US Regulatory Response to the Global Financial Crisis', in Helleiner, *et al.* (eds), *supra* note 76.

92 Helleiner & Pagliari, *supra* note 51, 275, 283.

Partially due to the sustained agenda-setting power of the transnational regulatory circles, we only see incremental changes in the technicalities. Yet in substance path-dependencies remain regarding the general principles, as is observable in the negligible adaptations in the accounting field,[93] as well as in the further strengthening of value-at-risk based modeling and risk management.[94] In other words, the existing financial governance system remains uncontested – there is no trend to the establishment of classic hard law instruments such as multi-lateral treaties.

The far reaching reforms underway stem from national or, in the European case, regional initiatives, where domestic or supranational interests are the main driving factors. Moreover, we witnessed that the existent global arrangements are not capable of coping with short-term, sudden global shocks, as the pressure for short-term reactions is too demanding for international or even transnational structures.

In sum, solutions to the global crises will require a complex mixture of global, regional, national and transnational rules. The quint-essence is that global mechanisms are needed but that these can only be viable, if solutions are chosen that rely on national, regional or transnational actors in terms of implementation and the constellations of institutions and the interests of their actors are taken into consideration. In essence, a complex web of governance is pragmatically inevitable. However, the decisive concern is not on what level these decisions are taken, but rather how issues of accountability, transparency and legitimacy are taken into account. Although we have seen a major system failure, our evaluation of the current financial crisis indicates that the processes of financial regulation are still largely determined by the same highly organized particularistic interests.

Finally, if we put these results into a more general framework, we can derive at insights for other global challenges. Financial regulation became an international challenge that was handled by cohesive groups of highly specialized actors.[95] This leads to path-dependencies (as described above) and makes it hardly possible to substantially restructure the system, as it would be dependent on the technical expertise of the system's actors. Thought a step ahead, we ask what we can expect for other policy fields that

93 Nölke, *supra* note 82.

94 T. Porter, 'Risk Models and Transnational Governance in the Global Financial Crisis. The Cases of Basel II and Credit Rating Agencies', in Helleiner, *et al.* (eds), *supra* note 76.

95 D. Drezner, *All Politics is Global: Explaining International Regulatory Regimes*. (2008), 119-148.

are susceptible to global crises, while at the same time increasingly becoming subject to regulation by expert-led networks. In such a scenario it is therefore indispensible to carefully consider, if and what particularistic interests are dominant within the regulation of global issue areas.