

Preliminary Draft: May 24, 2010
Please do not quote or cite without author's consent

CONSULTATION AND LEGITIMACY IN TRANSNATIONAL STANDARD-SETTING

Caroline Bradley*

The recent financial crisis has generated agreement on the need for new transnational standards for financial regulation. When governments work together to develop transnational standards and rules they do so using processes which are not uniform, which often seem to develop in an ad hoc manner, and which do not necessarily reflect any particular conception of good government. Transnational standard setters have responded to critiques of the legitimacy of their role by emphasizing consultation of stakeholders. The article will compare the uses of consultation in the development of policy at the national and supranational levels. It will examine the weaknesses in the construction of transnational consultations which undermine their value as mechanisms of legitimation. For example, transnational consultations lack visibility, they are usually carried out in a limited number of languages, or even only in English. More fundamentally, the article will critique the stakeholder focus of transnational consultations. In practice the identification of stakeholders who are potential respondents to consultations seems to imply that there may be others (non-stakeholders) whose views are less important. As the financial crisis has shown, it is not only those who consider themselves to be stakeholders in financial regulation who are affected by its failures.

* Professor of Law, University of Miami School of Law, PO Box 248087, Coral Gables, FL, 33124, cbradley@law.miami.edu ; <http://blenderlaw.umlaw.net/> . © Caroline Bradley 2010. All rights reserved.

Preliminary Draft: Please do not quote or cite without author's consent

TRANSNATIONAL FINANCIAL STANDARD SETTING

The global financial crisis demonstrated the transnational nature of financial market activity, and persuaded governments to commit to an intensified co-ordination of financial market regulation,¹ including a review of existing harmonized standards,² the introduction of new harmonized regulatory standards,³ and the development of new structures for addressing systemic risks.⁴ At the same time, the crisis meant that financial regulation (often treated as a technocratic sphere) came to be seen as a matter of significant domestic political interest. For example, politicians, regulators and private sector groups recognized that citizen-voters were offended by the fact that bankers, who were seen as having caused the crisis and whose institutions were bailed out by taxpayers, nevertheless had contractual rights to large bonuses while non-bankers suffered increased rates of mortgage foreclosure and unemployment.⁵ Market and

¹ See, e.g., G20, Declaration on Strengthening the Financial System, London (Apr. 2, 2009) at http://www.g20.org/Documents/Fin_Deps_Fin_Reg_Annex_020409_-_1615_final.pdf. Cf. Elliott Posner, Making Rules for Global Finance: Transatlantic Regulatory Cooperation at the Turn of the Millennium, 63 Int'l Org. 665, 669 (2009) (describing an institutionalization of transnational co-operation in financial regulation after 2002).

² See, e.g., BIS, Basel Committee on Banking Supervision, Consultative Document, Proposed Enhancements to the Basel II Framework, 1 (Jan. 2009) available at <http://www.bis.org/publ/bcbs150.pdf> ("The Basel Committee has finalised its proposals for enhancing the Basel II framework in the area of securitisation and more specifically for dealing with resecuritisations. These enhancements are intended to strengthen the framework and respond to lessons learned from the financial crisis.")

³ See, e.g., *id.* at 2 ("once recovery is assured, prudential regulatory standards should be strengthened. Buffers above regulatory minima should be increased and the quality of capital should be enhanced. Guidelines for harmonisation of the definition of capital should be produced by end 2009. The BCBS should review minimum levels of capital and develop recommendations in 2010")

⁴ G20, Declaration on Strengthening the Financial System, *supra* note [1](#), at 1 ("We have agreed that the Financial Stability Forum should be expanded, given a broadened mandate to promote financial stability, and re-established with a stronger institutional basis and enhanced capacity as the Financial Stability Board (FSB).")

⁵ See, e.g., Productivity Commission, Executive Remuneration in Australia, Productivity Commission Inquiry Report No. 49, xv (Dec. 19, 2009) available at

Preliminary Draft: Please do not quote or cite without author's consent

regulatory failures in the financial markets⁶ were acknowledged to have imposed externalities on those outside the financial markets.⁷ These developments led to debates about the extent to which the financial markets provide value to the real economy.⁸

http://www.pc.gov.au/data/assets/pdf_file/0008/93590/executive-remuneration-report.pdf (“A catalyst for this inquiry was concern that executive pay had got out of hand. This perception was fuelled by practices in financial institutions abroad that were seen as a key contributor to the global financial crisis (GFC). Further, while local shareholder value plummeted in 2008 as a result of that imported crisis — with some companies and sectors being propped up by taxpayers — executive pay seemed to emerge unscathed, crystallising a view that executives were being rewarded for failure (after having been rewarded for success).”); FSA, Reforming Remuneration Practices in Financial Services, CP 09/10 (Mar. 2009) at http://www.fsa.gov.uk/pubs/cp/cp09_10.pdf; The Conference Board, The Conference Board Task Force on Executive Compensation (Sep. 2009) at http://www.conference-board.org/pdf_free/ExecCompensation2009.pdf.

⁶ See, e.g., Financial Services Authority, The Turner Review: a Regulatory Response to the Global Banking Crisis, 22 (Mar. 2009) at http://www.fsa.gov.uk/pubs/other/turner_review.pdf (identifying excessive reliance on particular risk management techniques as a factor contributing to the crisis: “Central to many of the techniques was the concept of Value-at-Risk (VAR), enabling inferences about forward-looking risk to be drawn from the observation of past patterns of price movement. This technique, developed in the early 1990s, was not only accepted as standard across the industry, but adopted by regulators as the basis for calculating trading risk and required capital, (being incorporated for instance within the European Capital Adequacy Directive)”).

⁷ See, e.g., Financial Crisis Inquiry Commission, Preliminary Staff Report, Shadow Banking and the Financial Crisis, 41 (May 4, 2010) at <http://www.fcic.gov/reports/pdfs/2010-0505-Shadow-Banking.pdf> (“...many financial firms were crippled, and some only survived with substantial government assistance. Their capital was depleted and many of their revenue channels were extinguished or impaired by the decline in financial activity. This condition severely restricted their capacity to provide funding to consumers, businesses, and governments, reinforcing reductions in real economic activity around the world and magnifying the ensuing recession.”)

⁸ See, e.g., Adair Turner, What Do Banks Do, What Should They Do and What Public Policies Are Needed to Ensure Best Results for the Real Economy? Speech, CASS Business School (Mar. 17, 2010) at http://www.fsa.gov.uk/pubs/speeches/at_17mar10.pdf. Cf. SOMO, EU Financial Reforms Newsletter (April 2010) at http://somo.nl/dossiers-en/sectors/financial/eu-financial-reforms/newsletter-finance/april_2010/vieu (“The financial sector has the potential to serve the real economy, to improve sustainability and to help people in need, for instance, through credit and investments. However, recent financial crises have shown that the financial industry primarily serves itself. The financial sector has become so powerful that some say we “live in financial times”. It is therefore important to seize the momentum of the ongoing financial reforms to truly transform the financial sector so it serves the real economy, the environment and the interests of the most vulnerable within Europe and especially within developing countries. “)

Preliminary Draft: Please do not quote or cite without author's consent

Before the crisis a number of transnational organizations developed standards for financial regulation:⁹ at the international level, the International Organisation of Securities Commissions (IOSCO),¹⁰ the Basel Committee on Banking Supervision (Basel Committee),¹¹ and the International Association of Insurance Supervisors (IAIS)¹² have all published harmonized principles of financial regulation. The European Union (EU) has promulgated harmonized rules of financial regulation which are binding on its members.

Supranational standards and rules often require implementation within domestic legal systems in order to be effective. EU harmonization measures which are binding on the Member States are often¹³ structured as directives, which require Member State legislation for implementation, and standards developed by bodies such as the Basel Committee and IOSCO are not formally binding, leaving some discretion to states which implement them.¹⁴ The IMF and the World Bank

⁹ Note on terminology: this paper refers to the products of the Basel Committee and IOSCO as standards rather than rules because of their formally non-binding character. However, IOSCO and the Basel Committee often refer to what they produce as principles, rather than as standards. And their principles are principles which should be reflected in domestic regulatory schemes, rather than standards to be met by the suppliers of financial services, which would be more analogous to the products of other standards processes.

¹⁰ For a discussion of IOSCO's Principles of Securities Regulation see, e.g., K. Pistor, *The Standardization of Law and Its Effect on Developing Economies*, 50 AM. J. COMP. L. 97, 116-120 (2002).

¹¹ See, e.g., J. Braithwaite and P. Drahos, *Global Business Regulation*, 104 (2000) (describing how central bank governors established what is now the Basle Committee on Banking Supervision in response to the failures of the Herstaat Bank and Franklin National Bank in 1974).

¹² See, e.g., Pistor, *supra* note [10](#) at 120-1.

¹³ Although not always. See, e.g., Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on Credit Rating Agencies, O.J. No. L 302/1 (Nov. 17, 2009) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0001:0031:EN:PDF>.

¹⁴ See, e.g., D. E. Alford, *Core Principles for Effective Banking Supervision: an Enforceable International Financial Standard?*, 28 B. C. INT'L & COMP. L. REV. 237, 286 (2005) ("because the agreements are not legally enforceable, nations can vary in their own interpretation and implementation of the standards.")

Preliminary Draft: Please do not quote or cite without author's consent

monitor implementation of standards by their members.¹⁵ Weaker states will tend to have less discretion in implementation than more powerful states, but even more powerful states notice the results of reviews by the international financial institutions.¹⁶

Where discretion in implementation of transnational standards is limited, formally as is often the case in the EU, or because of the need to pacify international financial institutions (IFIs) or perhaps because of public commitments such as those made in the G20's crisis-related declarations,¹⁷ the processes whereby the transnational standards are agreed become more significant.

Before the crisis, and in response to critiques of the transparency and inclusiveness of transnational standard-setting,¹⁸ supranational standard-setters

¹⁵ See, e.g., The World Bank, Reports on the Observance of Standards and Codes (ROSC), Overview of the ROSC Accounting and Auditing Program (Jan. 2004) at http://www.worldbank.org/ifa/rosc_aa_overview.pdf.

¹⁶ See, e.g., IMF, Financial Sector Assessment Program, United States of America, The IOSCO Objectives and Principles of Securities Regulation: Detailed Assessment of Implementation, 26 (May 2010) at <http://www.imf.org/external/pubs/ft/scr/2010/cr10125.pdf> (“The overall ratings in the Report, however, do not reflect the CFTC’s and SEC’s regulatory successes and, in some cases, suggest a misunderstanding of the U.S. regulatory system. Thus, the Commissions strongly disagree with many of the ratings in the Report. By way of example, while the IOSCO Principles recognize that regulators may use different approaches to accomplish the same objectives, the Report’s rating on market intermediaries is based on the assumption that every intermediary must be regulated the same way. That is, they must undergo an extensive review prior to registration. This requirement, however, cannot be found in the Principles or the assessment Methodology. The Report rejects a legitimate risk-based approach to a registration requirement and oversight of futures and securities intermediaries without evidence that the approach is ineffective. The Report also states that capital requirements for futures and securities firms do not fully address risk, yet provides no evidence that the CFTC’s and SEC’s current requirements do not already exceed recognized international best practice as reflected in the Principles.”)

¹⁷ And see, e.g., IMF, The G-20 Mutual Assessment Process and the Role of the Fund (Dec. 2, 2009) at <http://www.imf.org/external/np/pp/eng/2009/120209a.pdf>; Financial Stability Board, FSB Framework for Strengthening Adherence to International Standards (Jan. 9, 2010) at http://www.financialstabilityboard.org/publications/r_100109a.pdf.

¹⁸ For a critique of the global legal harmonization phenomenon generally, see, e.g., IUC Global Legal Standards Research Group, IUC Independent Policy Report: At the End of the End of History - Global Legal Standards: Part of the Solution or Part of the Problem?, 9:3 Global Jurist

Preliminary Draft: Please do not quote or cite without author's consent

began to formalize their procedures, developing practices for consulting on proposed standards, and even establishing consultation policies.¹⁹ These developments have led some commentators to argue that the multi-level features of transnational standard-setting may in fact enhance accountability and legitimacy.²⁰ However, the different organizations approach consultation and the reporting of the results of consultation differently.²¹ Moreover, although transnational standard-setters have improved the transparency and openness of their processes, their role and activities are fundamentally different from those of many domestic regulators. Transnational standard setters engage in consultation as a concession rather than as a matter of obligation: they are not required by any binding rules to carry out consultations at all or in any particular way. As a corollary of this lack of obligation, stakeholders do not have meaningful rights to be consulted. Even the EU is concerned to ensure that its interests are taken into account in the transnational standard-setting process.²²

(2009).

¹⁹ See, e.g., IOSCO, Executive Committee, *IOSCO Consultation Policy And Procedure*, (Apr. 2005) at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD197.pdf>.

²⁰ See, e.g., Michael S. Barr & Geoffrey P. Miller, *Global Administrative Law: The View from Basel*, 17 EUR. J. INT'L L. 15, 17 (2006) (“While far from ideal, the Basel process has come a long way from the purely closed ‘club’ model of its origins, and demonstrates the possibility for enhanced accountability and legitimacy in international regulation. At the international level, the Basel committee has recently engaged in a relatively open process akin to a notice and comment rule-making in developing international capital standards, and has improved its transparency. At the domestic level, central banks and national bank regulators have enmeshed the Basel standards in the domestic notice and comment rule-making process, enhancing the legitimacy of the international process through local procedural protections. Moreover, international regulatory processes, including Basel, can in some instances help to reinforce, rather than undermine, domestic norms of accountability and legitimacy, particularly in countries where inside elites block reforms and prevent transparent domestic regulatory processes from occurring.”)

²¹ See generally, e.g., Caroline Bradley, *Private International Law-Making for the Financial Markets*, 29 FORDHAM INT'L L. J. 127, 140-154 (2005).

²² See, e.g., Decision of the European Parliament and of the Council Establishing a Community Programme to Support Specific Activities in the Field of Financial Services, Financial Reporting and Auditing, O J No. L 253/8 (Sep. 25, 2009) at

Preliminary Draft: Please do not quote or cite without author’s consent

There are still few possibilities for challenging transnational standards,²³ and so far no harmonized supranational administrative law.²⁴ Governmental agencies are subject to court challenges to their domestic rule-making activities,²⁵ and to formal review by legislatures and other governmental agencies.²⁶ Transnational standard-setters are not subject to the same type of formal monitoring.

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:253:0008:0016:EN:PDF>.

Recital number 3 states: “In a global economy, there is also a need to converge standards between jurisdictions and develop international standards under a transparent and democratically accountable process. It is therefore important that the Community play a role in the international standardsetting process for financial markets. To ensure that the interests of the Community are respected and that global standards are of high quality and compatible with Community law, it is essential that the interests of the Community are adequately represented in that international standard-setting process.”

²³ Although note that the EU courts have stated that EU and Member State authorities which implement Security Council resolutions must ensure that EU fundamental rights are respected. See *Yassin Abdullah Kadi and Al Barakaat International Foundation v Council and Commission*, Joined Cases C-402/05 P and C-415/05 P 3 C.M.L.R. 41 (2008).

²⁴ See, e.g., B. Kingsbury, N. Krisch, and R. B. Stewart, *The Emergence of Global Administrative Law*, 68 L. & CONTEMP. PROB. 15, 16 (2005) (noting “an accountability deficit in the growing exercise of transnational regulatory power.”)

²⁵ See, e.g., *Chamber of Commerce v SEC*, 443 F.3d 890 (DC Cir. 2006). Cf. HM Government, *The Coalition: Our Programme for Government*, 10 (May 2010) at http://www.cabinetoffice.gov.uk/media/409088/pfg_coalition.pdf (“ We will give the public the opportunity to challenge the worst regulations.”)

²⁶ See, e.g., GAO, *OCC Preemption Rulemaking: Opportunities Existed to Enhance the Consultative Efforts and Better Document the Rulemaking Process*, 5 (Oct. 17, 2005) at <http://www.gao.gov/new.items/d068.pdf> (“OCC does not have written guidance, policies, or procedures detailing the rulemaking process. Instead, OCC uses a “rulemaking checklist” that serves as a guide for completing the required reviews and the routing of documents. According to internal control standards for the federal government, agencies should follow written procedures in making important decisions. Without such documentation, it may not be clear—to agency management, auditors, or oversight committees—that an agency followed applicable requirements.”) .

Preliminary Draft: Please do not quote or cite without author's consent

CONSULTATION IN THE DEVELOPMENT OF POLICY AT THE NATIONAL AND SUPRANATIONAL LEVELS

Domestic conceptions of good government and of how governments should relate to their citizens vary.²⁷ Consultation, which is frequently an aspect of domestic policy-making, performs a number of different functions and often has mixed motives. Although consultation seems to reflect a governmental commitment to transparency as well as to engagement with citizens,²⁸ consultation documents typically frame questions and invite responses to those questions, thus attempting to influence how consultees engage with government.

Consultation processes may be designed to collect information,²⁹ either factual information about the context for which policy is to be developed or specific technical feedback on the details or drafting of proposed changes.

²⁷ Cf. House of Commons Public Administration Select Committee, *Good Government*, Eighth Report of Session 2008–09, HC 97-1 (Jun. 18, 2009) (“Good government is the professed aim of all governments. But while everyone can agree that it is a desirable thing, it is much harder to define what good government actually is and how to achieve it.”).

²⁸ See, e.g., Cary Coglianese, *The Transparency President? The Obama Administration and Open Government*, 22 *GOVERNANCE* 529, 535 (2009) (“transparency can affirmatively improve governmental decision making by helping inform the public about the problems governmental officials seek to solve and the options they are considering. By making more information available, the public can then participate more thoughtfully in the governmental process.”).

²⁹ Governments adopt other strategies for developing policy, including Commissions and Committees which are tasked with reviewing or developing the law to achieve particular objectives. See, e.g., Australian Financial Centre Forum, *Australia as a Financial Centre: Building on our Strengths*, 5 (Nov. 2009) at http://www.treasury.gov.au/afcf/content/reference_papers/downloads/AFCF_Building_on_Our_Strengths_%20Report.pdf (“On 26 September 2008, the then Assistant Treasurer and Minister for Competition Policy and Consumer Affairs, the Hon Chris Bowen MP, announced the establishment of the Australian Financial Centre Forum, designed to position Australia as a leading financial services centre. The Minister stated that the focus of the initiative was on ensuring that Australia’s policy settings allowed the financial sector to take full advantage of business opportunities in the region.... The Minister announced the appointment of Mr Mark Johnson, retired Deputy Chairman of Macquarie Bank, to lead the work of the Forum, along with the establishment of a small group of senior financial sector executives to form a Panel of Experts... The Forum was further supported by the establishment of a Reference Group of representative industry bodies.”)

Preliminary Draft: Please do not quote or cite without author's consent

Consultations may also solicit or manipulate opinions about proposed legislation or regulation. Often, consultations combine data-gathering and opinion forming functions. In times of emergency governments may limit their consultations in the interests of speedy rule-making.³⁰

At the domestic level, consultations may be structured differently at different stages in the policy-development process. Consultation exercises may be presented as preliminary, for example being denominated as discussions rather than consultations.³¹ Governments may set up groups of experts to provide advice in particular policy areas.³² Data gathering consultations may be carried out by congressional or parliamentary committees at an early stage before the consideration of proposed legislation, or in the context of specific legislative proposals. When governments publish documents setting out their proposals for new legislation they may seek data from the public about the likely impact of the proposals.³³ Pre-legislative consultations carried out by the executive allow

³⁰ Cf. House of Lords Select Committee on the Constitution, *Fast-Track Legislation: Constitutional Implications and Safeguards*, Vol. 1- Report, 39, HL Paper 116-I (Jul. 7, 2009) at <http://www.publications.parliament.uk/pa/ld200809/ldselect/ldconst/116/116.pdf> (“We .. urge the Government to put mechanisms in place to ensure that relevant parliamentary committees and stakeholders are consulted about and given the opportunity to respond to proposed fast-track legislation ahead of Second Reading in the House in which the bill is introduced. This should be possible in all but the most extreme circumstances.”)

³¹ See, e.g., HM Treasury, *Discussion Paper on Developing Non-bank Lending Channels for UK Businesses* (Jan. 12, 2010) at http://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/non_bank_lending_discussionpaper.pdf.

³² See, e.g., Department for Business, Innovation and Skills Press Release, *Business Secretary Vince Cable today announced the creation of a new group of experts to advise him on business and economic policy* (May 18, 2010) at <http://nds.coi.gov.uk/content/Detail.aspx?ReleaseID=413396&NewsAreaID=2>.

³³ See, e.g., The Insolvency Service, *Encouraging Company Rescue*, 8 (Jun. 15, 2009) (“Rescue Consultation”) at http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/con_doc_register/ (“A1. Do you agree that it would be helpful for medium and large-sized companies to be allowed to benefit from the option of a moratorium from creditor action for up to 28 days? A2. How useful do you think this would be? Do you think it would encourage medium and large-sized companies to utilise the CVA procedure? (If you can give figures, or comment on those in the initial Impact Assessment,

Preliminary Draft: Please do not quote or cite without author’s consent

governments to communicate with voters about their proposals to change the law in order to maintain confidence that they are addressing perceived problems or keeping campaign commitments. In a sense, therefore, some, particularly pre-legislative, consultations are designed to improve a government’s relations with its public.³⁴

Pre-legislative consultations may raise broad issues of principle for discussion. However, pre-legislative consultations on measures to implement supranational rules or standards are often limited in comparison to other pre-legislative consultations. Such consultations will reflect any limits on their discretion with respect to implementation inherent in the supranational rules or standards.³⁵ They may come to resemble domestic regulatory consultations which, reflecting the limited rule-making powers of the regulatory agency, concentrate on relatively narrow, more technical questions.

When governments work together in different fora to generate agreements about standards and rules that should operate transnationally, they do so using processes which are not uniform, which often seem to develop in an ad hoc manner, and which do not necessarily reflect any particular conception of good government. A growing literature on global administrative law seeks to address

that would be helpful.”)

³⁴ See, e.g., Rescue Consultation, *supra* note 33, at para. 2 (“The UK has a long established and well developed insolvency legislative framework, which is highly regarded worldwide, with a reputation for fairness and for striking the right balance between the interests of debtors and creditors. We want to ensure that the insolvency regime remains world class and fit for purpose and this consultation is part of that ongoing process.”)

³⁵ See, e.g., HM Treasury, Public Consultation: Draft Terrorist Asset-freezing Bill, Cm 7852 4 (Mar. 2010) at http://www.hm-treasury.gov.uk/d/consult_terrorist_assetfreezing_bill.pdf (“The Government is committed to ensuring that there is full and effective scrutiny of its draft asset freezing legislation. As such, it is launching this public consultation exercise to seek the views of interested parties and the general public on our proposed approach to terrorist asset freezing. In particular, the Government is interested in responses to the following questions:• does the draft Bill set out the most effective way of meeting our UN obligations and protecting national security whilst also ensuring sufficient safeguards in respect of human rights?...”)

Preliminary Draft: Please do not quote or cite without author’s consent

deficiencies in rule-making and standard-setting at the supranational level.³⁶ This literature tends to take as a given that supranational standard-setting is analogous to regulation rather than legislation at the domestic level. However, although supranational standard-setting may seem to take on the form of administrative processes, it also operates at a more fundamental policy-setting level.³⁷ And even where supranational standard-setters develop highly technical standards, those standards may embed policy assumptions, and they may have significant impacts on the lives of citizen-voters around the world. The generation of supranational standards may be intended to prevent national governments from making policy choices which diverge from the standards, and may in fact preclude such divergent choices.³⁸ For example, the 1988 Basel Capital Adequacy Accord required states to impose capital adequacy requirements on international banks, even if those states addressed risks to financial stability in other ways. The Accord was agreed after the US and the UK announced they would apply stringent capital

³⁶ See, e.g., Benedict Kingsbury, Nico Krisch, & Richard B. Stewart, *The Emergence of Global Administrative Law*, 68: 3&4 L. & CONTEMP. PROBS. 15, 17 (2005) (defining “global administrative law as comprising the mechanisms, principles, practices, and supporting social understandings that promote or otherwise affect the accountability of global administrative bodies, in particular by ensuring they meet adequate standards of transparency, participation, reasoned decision, and legality, and by providing effective review of the rules and decisions they make.”)

³⁷ For example, The Basel Committee on Banking Supervision develops technical standards for capital adequacy but has also set out what it regards as the core necessary elements of banking regulation. See BIS, Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision* (Oct. 2006) available at <http://www.bis.org/publ/bcbs129.pdf> and BIS, Basel Committee on Banking Supervision, *Basel II: International Convergence of Capital Measurement and Capital Standards: A Revised Framework - Comprehensive Version* (Jun. 2006) available at <http://www.bis.org/publ/bcbs128.pdf>.

³⁸ Cf. Liesbet Hooghe & Gary Marks, *A Postfunctionalist Theory of European Integration: From Permissive Consensus to Constraining Dissensus*, 39 BRIT. J. POL. SCI. 1-23, 2 (2009) (“Governance is a means to achieve collective benefits by co-ordinating human activity. Given the variety of public goods and their varying externalities, efficient governance will be multi-level. But governance is also an expression of community. Citizens care – passionately – about who exercises authority over them. The challenge for a theory of multi-level governance is that the functional need for human co-operation rarely coincides with the territorial scope of community.”)

Preliminary Draft: Please do not quote or cite without author's consent

adequacy requirements to foreign banks doing business in their jurisdictions.³⁹

Although supranational standards and rules may reduce the discretion of national governments, and thus would seem to imply a more general, principle-focused consultation, transnational consultations tend to resemble domestic regulatory, rather than pre-legislative, consultations. In this context the EU, with parliamentary representation of citizens as an aspect of the policy development process, is more like a domestic government than more technocratic bodies such as the Basel Committee and IOSCO. The EU's policy development process includes the publication of Green Papers, White Papers, Communications,⁴⁰ and other pre-legislative consultative documents which solicit comments on general policy issues.⁴¹ Other supranational and transnational organizations may respond to the EU's consultations.⁴²

Transnational standard-setters such as the Basel Committee and IOSCO

³⁹ See, e.g., Stavros Gadinis, *The Politics of Competition in International Financial Regulation*, 49 HARV. INT'L L. J. 447, 500-503 (2008).

⁴⁰ See, e.g., Communication from the Commission, Reinforcing Economic Policy Coordination, COM (2010) 250 (May 12, 2010) at http://ec.europa.eu/economy_finance/articles/euro/documents/2010-05-12-com%282010%29250_final.pdf.

⁴¹ Cf. Mario Monti, A New Strategy for the Single Market. Report to the President of the European Commission, José Manuel Barroso, 17 (May 9, 2010) at http://ec.europa.eu/bepa/pdf/monti_report_final_10_05_2010_en.pdf ("Before launching the single market project with the 1985 White Paper, Jacques Delors had prepared the initiative through a "tour des capitales" of the then 10 Member States, plus Spain and Portugal who were soon to join. Today the European Union is not only larger and more diverse, with its 27 Member States, but also more complex in its articulation, with a much broader involvement of stakeholders and civil society.")

⁴² See, e.g., IMF, *Regional Economic Outlook: Europe, Fostering Sustainability*, 21 (fn. 4) (May 2010) at <http://www.imf.org/external/pubs/ft/reo/2010/EUR/eng/ereo0510.pdf> ("The consultation documents, including the IMF's staff contributions, are available on DG Markt's website: ec.europa.eu/internal_market/bank/crisis_management/index_en.htm#consultation; and ec.europa.eu/internal_market/consultations/2009/deposit_guarantee_schemes_en.htm .")

Preliminary Draft: Please do not quote or cite without author’s consent

are structured as groupings or networks of domestic regulators.⁴³ Thus the standards-development process they are engaged in is qualitatively different from that of a legislative or governmental body. But it may also be different from that of a domestic regulatory body engaged in domestic rule-making. Regulators may not have formal rule-making powers as a matter of domestic law,⁴⁴ but their limited domestic responsibilities may not effectively limit their ability to participate in transnational standard-setting.⁴⁵ More generally, even where domestic regulators have rule-making powers, these powers are constrained by statute. Regulators may not feel themselves to be constrained in the same way when they participate in transnational standard-setting.

In normal times, and to the extent that transnational standard-setting is really a process of identifying best practices based on what national regulatory systems prescribe, such that regulators with limited domestic functions do no more than represent the characteristics of their domestic systems in the transnational processes, the idea of constrained domestic regulators functioning as the articulators of transnational standards seems relatively unproblematic. If, on the other hand, constrained domestic regulators see their role in the context of

⁴³ On governance networks, *see, e.g.*, Carolyn M. Hendriks, *The Democratic Soup: Mixed Meanings of Political Representation in Governance Networks*, 22 *Governance* 689 (2009). Hendriks examines the enactment of representation in a governance network around energy reform in the Netherlands in terms of dramaturgy and rhetoric. *Id.* at 693-4.

⁴⁴ *See, e.g.*, Julia Black & Stéphane Jacobzone (2009), *Tools for Regulatory Quality and Financial Sector Regulation: A Cross-Country Perspective*, OECD Working Papers on Public Governance, No. 16, OECD Publishing, © OECD. doi:10.1787/218772641848 at <http://www.oecd.org/dataoecd/40/53/44306704.pdf> p. 9 (“The greatest variation is with respect to rule making powers, where OSFI and ASIC lack powers to make binding rules, yet in contrast the FSA, the Securities and Exchange Commission (SEC) and the Commodities and Futures Trading Commission (CFTC), for example, have extensive rule making powers exercised independently of the executive.”) Although ASIC does not have the power to make regulations it does have the power to issue regulatory guidance and regulatory relief. *See, e.g.*, ASIC: A Guide to Our Regulatory Documents, 5 (June 2007) at [http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/ASIC_Guide_to_regulatory_docs.pdf/\\$file/ASIC_Guide_to_regulatory_docs.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/ASIC_Guide_to_regulatory_docs.pdf/$file/ASIC_Guide_to_regulatory_docs.pdf).

⁴⁵ As of May 12, 2010 Tony D'Aloisio, the Chairman of ASIC, was a member of IOSCO’s Presidents’ Committee, Executive Committee and of its Technical Committee.

Preliminary Draft: Please do not quote or cite without author’s consent

transnational standard setting as being the development of standards which differ from those they are charged to administer, this is more problematic.⁴⁶ And in the aftermath of the crisis transnational standard-setters are clearly doing more than just distilling current best practices into transnational standards: they are developing new rules for the transnational financial system.

The idea that the role of transnational standard-setters has evolved from a positive role of describing existing best practices to a normative function of identifying what best practices should be raises new questions about the role of consultation in the transnational context. Supranational standard-setters have turned to consultation to enhance their perceived legitimacy, to inform their work, and to make those affected by their standards more receptive to them.⁴⁷ Some have argued that shifting decision-making to multilateral institutions can improve democracy, rather than undermine it.⁴⁸ But transnational consultations as currently structured suffer from numerous weaknesses which undermine their value as mechanisms of legitimation.

Transnational consultations lack visibility, they are usually carried out in a limited number of languages, or even only in English. They state that they are aimed at stakeholders, which likely reflects their limited visibility and the aim of achieving buy-in by those likely to be most affected by the standards. But this stakeholder emphasis also implies that there may be others (non-stakeholders) whose views are less important. As the financial crisis has shown, it is not only

⁴⁶ Cf. Jonathan R. Macey, *Regulatory Globalization as a Response to Regulatory Competition*, 52 Emory L. J. 1353, 1354 (2003) (suggesting that regulators may engage in “regulatory globalization” to make it difficult for local opponents to block policy changes the regulator favours).

⁴⁷ See, e.g., IOSCO, Executive Committee, *IOSCO Consultation Policy And Procedure*, (Apr. 2005) available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD197.pdf>.

⁴⁸ See, e.g., Robert O. Keohane, Stephen Macedo & Andrew Moravcsik, *Democracy-Enhancing Multilateralism*, 63 INT’L ORG. 1 (2009). The authors state that a “comprehensive analysis of the effects of multilateralism on democracy is beyond the scope of this article, but it is an essential task for future scholarship.” *Id.* at 28.

Preliminary Draft: Please do not quote or cite without author's consent

those who consider themselves to be stakeholders in financial regulation who are affected by its failures.

If one takes the view that what matters in the context of standard-setting is the identification of optimal rules, limited consultation of those with relevant expertise might be appropriate. However, if one takes the view that there are no optimal substantive rules, but perhaps only optimal (or good enough) processes for identifying rules, the structure of consultation is critical. Better Regulation agendas⁴⁹ involve aspects of both of these views: the emphasis on evidence-based policy-making⁵⁰ suggests that the objective of identifying the right rules is key, whereas focusing on transparency and accountability involves a concern for process.⁵¹

WEAKNESSES IN THE CONSTRUCTION OF TRANSNATIONAL CONSULTATIONS

Although transnational standard-setters have increased their emphasis on

⁴⁹ See, e.g., EU Commission, Action Plan : Simplifying and Improving the Regulatory Environment, COM (2002) 278 (Jun. 5, 2002) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2002:0278:FIN:EN:PDF> (Action Plan); EU Commission, Better Regulation for Growth and Jobs in the European Union, COM(2005) 97 (Mar. 2005) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2005:0097:FIN:EN:PDF>. More recently, policy makers have been promoting smart regulation. See, e.g., EU Commission, Stakeholder Consultation on Smart Regulation (Apr. 23, 2010) at http://ec.europa.eu/governance/better_regulation/smart_regulation/docs/smart_regulation_consultation_en.pdf.

⁵⁰ See, e.g., Good Government, *supra* note 27 at 25 (“Processes for preparing and scrutinising policy and legislation should be as thorough and well-informed as possible, in the interests of good government.”) Impact assessment is a component of better regulation. See, e.g., Action Plan, *supra* note 49, at 7.

⁵¹ See, e.g., EU Commission, Consultation Document: Towards a Reinforced Culture of Consultation and Dialogue - Proposal for General Principles and Minimum Standards for Consultation of Interested Parties by the Commission, COM (2002) 277 (Jun. 5, 2002) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2002:0277:FIN:EN:PDF>. The Commission notes that “good consultation serves a double purpose by helping to improve the quality of the policy outcome and at the same time enhancing the involvement of interested parties and the public at large.”. *Id.* at 5.

Preliminary Draft: Please do not quote or cite without author’s consent

consultation as a mechanism of legitimation, consultations carried out by the Basel Committee and IOSCO lack some of the critical characteristics of domestic consultations. Transnational standard-setters work towards agreement on standards within their own networks, rather than on ensuring a broader acceptance of their work. In practice, public participation in consultations by transnational financial standard-setters is limited.⁵² There are a number of reasons for this: transnational consultations on standards are framed in a way that makes the views of non-experts seem irrelevant, and they are not designed to be visible and/or accessible. For example, the Basel Committee/IADI’s “Consultative Document” on Core Principles for Effective Deposit Insurance Systems did not contain requests for comments, or even any indication as to where comments could be sent.⁵³ Transnational standard-setters have not adopted standard practices with respect to publicizing the results of their consultations, and incorporating the results of consultations into announcements of final standards.

The transnational standard-setters could take advantage of some of the work of the EU Commission, which regularly reviews its consultation practices with a view to improving them.⁵⁴ The EU has recently attempted to make some consultations more visible by publishing citizen summaries of consultations

⁵² See, e.g., Barr & Miller, *supra* note 20, at 26 (“The role of the broader public was relatively muted, which reflected in part the technical nature of the Basel Committee’s work and the fact that for most public-interested organizations, the connection between banking standards and broader social concerns was not pronounced.”)

⁵³ See Basel Committee on Banking Supervision & International Association of Deposit Insurers, Consultative Document: Core Principles for Effective Deposit Insurance Systems (Mar. 2009) available at <http://www.bis.org/publ/bcbs151.pdf>. Contrast e.g., IOSCO, Regulatory Implementation of the Statement of Principles Regarding the Activities of Credit Rating Agencies, Consultation Report, 3 (May 2010) at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD319.pdf> (identifying 3 possible means of communicating views on the document).

⁵⁴ See, e.g., Smart Regulation, *supra* note 49, at 3 (“What concrete improvements could the Commission make to ensure that all relevant stakeholders are aware of and able to participate in consultations? Are there particular forms of consultation which you found useful when taking part in the Commission consultations (open internet questionnaires, stakeholder meetings, public hearings)?”)

Preliminary Draft: Please do not quote or cite without author’s consent

(although it is not clear that this has been very effective),⁵⁵ and has even dedicated financial resources to the development of effective stakeholder groups.⁵⁶ The EU’s internal focus on developing effective consultations with stakeholders may effectively pressurize transnational standard-setters to reform their own consultation practices. For example, the Commission has noted that because transnational consultation processes (like domestic consultations) may not effectively reflect the views of all stakeholders, governments may decide that it is their function to represent the public interest.⁵⁷

One major way in which transnational consultations differ from domestic consultations is that the transnational standard setters do not necessarily seek to communicate with stakeholders in the stakeholders’ own languages. Whereas governments of multi-lingual populations communicate with their citizens and residents in their own languages (although probably more frequently with respect

⁵⁵ See, e.g., EU Commission, Communication on an EU Framework for Cross-border Crisis Management in the Banking Sector, COM (2009) 561 (Oct. 20, 2009) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2009:0561:FIN:EN:PDF> (“Crisis Management Consultation”) and Citizens’ Summary, Commission Communication on an EU Framework for Cross-border Crisis Management in the Banking Sector (Oct. 2009) at http://ec.europa.eu/internal_market/bank/docs/crisis-management/091020_citicens_summary_en.pdf. The full consultation document raised some quite technical policy issues and is seventeen pages long. The summary is two pages long, and seems to be designed to persuade citizens that the EU is taking action rather than about trying to solicit meaningful comments from the public.

⁵⁶ This strategy is not uncontroversial. See, e.g., Andrew Reitman, *EU-funded Think Tanks Defend Their Credibility*, euobserver (Jan. 29, 2010) at <http://euobserver.com/9/29368>.

⁵⁷ EU Commission, Communication from the Commission to the European Parliament and the Council, Internet Governance: The Next Steps, 4, COM(2009) 277 final (Jun. 18, 2009) (“Private-sector leadership in the construction and day-to-day management of the Internet that we know today has worked well. As noted before, this **private-sector initiative must be maintained**. But non-governmental stakeholders must recognise that Internet users worldwide — most of whom do not participate and are not otherwise represented in Internet governance fora — have a **legitimate expectation** that their governments will guarantee that any current or future governance arrangements will reflect the **public interest of society as a whole** and will not be subject to capture by narrow commercial or regional interests. **Private-sector leadership and effective public policies are not mutually exclusive.**” (Emphasis in original))

Preliminary Draft: Please do not quote or cite without author’s consent

to the provision of services⁵⁸ than with respect to consultation), transnational consultations on proposed standards are usually conducted in a limited number of languages,⁵⁹ if not only in English. Although the EU makes efforts to communicate with EU citizens in their own languages, such efforts are costly, and even EU institutions publish consultation documents in a limited number of languages.⁶⁰ Commentators on the IMF’s transparency policy urged that the IMF should translate more of its documents into languages other than English.⁶¹

Consultations are targeted at particular groups in a number of different ways. Consultation documents may be sent to particular people, signaling that their responses will be valued, and roundtables and meetings may be set up to encourage particular people and firms to give their feedback. In a less intrusive way, drafters of consultation documents sometimes identify specific categories of potential respondents as stakeholders,⁶² or they may construct different consultation documents or response forms for different groups. These documents may ask different questions of different groups. For example, when the IMF

⁵⁸ And even in the context of service delivery agencies may not provide adequate language assistance services. *See, e.g.*, GAO, Selected Agencies Can Improve Services to Limited English Proficient Persons, 12 GAO-10-91 (Apr. 26, 2010) at <http://www.gao.gov/new.items/d1091.pdf> (“Because SBA provides both business development services as well as disaster-recovery assistance that require different language access services, SBA should use DOJ’s guidance to help it complete its LEP plan and recipient guidance consistent with SBA’s specific requirements.”)

⁵⁹ The BIS publishes some documents in German, Spanish, French and Italian as well as in English. See <http://www.bis.org/>.

⁶⁰ CESR, the Committee of European Securities Regulators, consults in English. See <http://www.cesr-eu.org/>.

⁶¹ Consultation Roundtable on IMF Transparency, Summary of Comments from Civil Society Organizations, at <http://www.imf.org/external/np/pdr/trans/2009/052809.htm>.

⁶² *See, e.g.*, Department for Business, Innovation & Skills, Civil Sanctions Pilot: A Consultation on the pilot Operation of Civil Sanction Powers for Consumer Law Enforcers, 2 (Mar. 2010) at <http://www.bis.gov.uk/assets/biscore/corporate/docs/c/10-706-civil-sanctions-pilot.pdf> (stating that “[t]his consultation is relevant to: consumer representative bodies; businesses; business representative bodies; consumer law enforcers.”)

Preliminary Draft: Please do not quote or cite without author’s consent

sought views about its transparency policy it required commentators to categorize themselves as civil society organizations, financial markets participants or “think tanks, academics and other stakeholders”. The questionnaires were different for the different groups. For example, whereas civil society organizations and think tanks were asked their views about whether IMF transparency should be improved by making reports easier to understand, more timely, more frank, or easier to access, financial markets participants were not asked this question.⁶³

The identification of specific stakeholders in consultation documents may imply that there may be others (non-stakeholders) whose views are less important. So, a consultation document which refers to stakeholders as those who are subject to a regulatory regime, rather than those whom it should benefit, seems to imply that the views of the beneficiaries of the regime are unimportant.⁶⁴

Although much of financial regulation is complex and technical there are aspects of financial regulation which involve combinations of issues which are technical and of little interest to consumers, and issues which are directly relevant to consumers.⁶⁵ Whether transnational standard-setters emphasize the technical aspects or the consumer aspects may have a significant impact on consumers’ interests. Transnational consultations which are framed as technical exercises through a combination of the specific questions which are asked and the

⁶³ See IMF Seeks Views on its Transparency Policy, at <http://www.imf.org/external/np/pdr/trans/2009/index.htm> .

⁶⁴ See, e.g., Ministry of Justice, Department of Business, Innovation and Skills & The Insolvency Service, Debt Management Schemes – Delivering Effective and Balanced Solutions for Debtors and Creditors, Consultation Paper CP09/09, 10 (Sep. 18, 2009) available at <http://www.justice.gov.uk/consultations/docs/debt-management-schemes.pdf> (“In developing these proposals, we have listened to the views of a wide range of stakeholders from the credit and advice sectors, current operators from both the not-for-profit and commercial sectors and other Government Departments. This consultation provides the opportunity to comment further.”)

⁶⁵ Some issues are of high salience for consumers. See, e.g., Federal Reserve, Notice of Study and Request for Information, 69 Fed. Reg. 29308, May 21, 2004, and the comments submitted in response to this request for information about debit card fees, which are available at http://www.federalreserve.gov/generalinfo/foia/index.cfm?doc_id=OP%2D1196&doc_ver=1&ShowAll=Yes

Preliminary Draft: Please do not quote or cite without author’s consent

identification of particular groups of relevant stakeholders tend to undermine the legitimacy of the consultation as an element in the production of standards, especially those standards which eliminate discretion in implementation. Consumers and the organizations which represent their interests are more likely than financial firms to be excluded from effective participation in supranational standard-setting due to the combined effects of opaque processes, framing, and lack of resources.

The approaches of transnational standard setters to publicizing the results of consultations vary. Although some Basel Committee publications do not give much information at all about responses to consultations,⁶⁶ the BIS has begun to publish comment letters on its website.⁶⁷ IOSCO prefers to characterize the comments it receives,⁶⁸ although respondents may publish their responses on their own web sites.⁶⁹ In domestic regulatory systems courts may review the record on

⁶⁶ *See, e.g.*, Basel Committee on Banking Supervision & International Association of Deposit Insurers, Core Principles for Effective Deposit Insurance Systems (Jun. 2009) available at <http://www.bis.org/publ/bcbs156.pdf>.

⁶⁷ *See, e.g.*, BIS, Comments Received on the Consultative Documents "Strengthening the Resilience of the Banking Sector" and "International Framework for Liquidity Risk Measurement, Standards and Monitoring" at <http://www.bis.org/publ/bcbs165/cacomments.htm> .

⁶⁸ *See, e.g.*, Technical Committee of the International Organization of Securities Commissions, Hedge Funds Oversight Final Report, 8 (Jun. 2009) available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD293.pdf> (“Having considered the public comments received on the Consultation Report, the IOSCO Technical Committee has developed the six high level principles below which should be applied to the regulation of hedge funds.”) In addition the document has an annex reporting on the results of the consultation. *Id.* At 17-22 and conclusions in light of responses at 23. In some cases the Report refers to the responses of specific entities with attribution. *See, e.g.*, at p 19 “Considering the international dimension of the hedge funds activities, all respondents supported the need for more convergence on the regulation of hedge fund managers in order to minimise the risk of regulatory arbitrage and ensure better level playing field. *See, e.g.*, International Council of Securities Associations’ Public Response to the IOSCO Consultation Report on Hedge Funds Oversight.” But comments are not always attributed to particular respondents. *See e.g.*, at p 20 “One respondent challenged that the wider publication of details on business plan and fees charged could create commercial problems for the managers.”

⁶⁹ The ICSA letter referred to in footnote 66 is available at <http://www.icsa.bz/pdf/ICSA-Letter-IOSCOreHedgeFunds-Apr09.pdf> .

Preliminary Draft: Please do not quote or cite without author’s consent

which regulators act, but this type of review does not exist in the context of transnational standard-setting.

Transnational consultation systems where standard setters voluntarily set their own principles for consultation and for the reporting of the results of consultation with no accountability to voters or through judicial review are problematic, particularly when they produce standards which limit domestic rule-makers’ discretion.

Fixing transnational consultation is not easy. Some techniques which can increase publicity for proposals about regulation at the domestic level may work differently at the transnational level. Open meetings⁷⁰ benefit those with the resources to travel. Taking steps to help consumers and consumer groups to participate in consultations as stakeholders may not in fact enhance the legitimacy of the process if consumers’ views are only sought with respect to issues identified in advance as consumer issues or where the standard setter assumes that consumer stakeholders will be relatively uninformed so that their views can be discounted. And whereas limiting the ways in which stakeholders can respond to consultations makes it easier for standard setters to process responses,⁷¹ it is not the most effective way of legitimating the resulting standards.

⁷⁰ See, e.g., Crisis Management Consultation, *supra* note 55, at 17 (“The Commission plans to organise a public hearing in early 2010 in order to present the results of the consultation and to set out how it intends to proceed. This will feed into the preparation of a roadmap of follow up initiatives in the areas of early intervention, resolution and insolvency in order to build a crisis management framework that would ensure that, in future, all competent authorities effectively coordinate their actions and have the appropriate tools for intervening quickly to manage the failure of a bank.”)

⁷¹ See, e.g., EU Commission, Consultation Document: Review of Directive 2002/87/EC on the Supplementary Supervision of Credit Institutions, Insurance Undertakings and Investment Firms in a Financial Conglomerate, 1 (2009) at http://ec.europa.eu/internal_market/financial-conglomerates/docs/20091106_questionnaire_fcd_review.pdf (“The Commission services would like to ask you to respond to the specific questions that were designed to supplement the responses you may have given to the JCFC's consultation of its draft Advice... In order for your contributions to be timely and properly evaluated, when submitting your replies, please maintain the structure of the questionnaire provided in this document”)