When the financial crisis erupted, international financial regulators proved of little help in averting its spread. Outside the United States, the bankruptcy of Lehman Brothers “was a mess,” explains Richard Herring, Jacob Safra Professor of International Banking and Professor of Finance at the Wharton School. Like many companies, Lehman Brothers would sweep all its cash into its holding company’s coffers at the end of each business day, squeezing out the most interest income possible by investing the money overnight in bulk. Every morning, it would distribute cash to its subsidiaries.

So, when Lehman Brothers filed for bankruptcy on the morning of September 15, 2008, it did not send money out, forcing its subsidiaries into immediate, disorderly bankruptcy—and foreign regulators into emergency planning. The haste of the bankruptcy proceedings in the United States and United Kingdom made it difficult...
for regulators in both countries to figure out who owed what to whom. And, because the money remained in the holding company’s accounts, subsidiaries in other countries could not access it to wind down their claims. This predicament is often a side effect when multinational companies fail since, according to Herring, regulators “tend to ringfence now and negotiate later.”

Lehman Brothers’ failure, of course, played a role in triggering a global financial crisis. Banks and other financial institutions stopped lending to each other, some went bankrupt, and many countries fell into deep recessions. Part of the blame fell upon regulators. The standards they had put in place before the crisis and the mechanisms they had for international coordination had plainly failed to stem the crisis.

In fact, some of the actions the international regulators took may actually have made things worse. As Mario Giovanoli, Professor Emeritus at the University of Lausanne, wrote in a paper evaluating regulators’ response to the financial crisis, “The impressive corpus of [international financial standards] established over the last thirty-five years, aimed precisely at eliminating systemic risk, failed to do so.” Indeed, he noted, some of the standards adopted by governments across the world had “unintended side-effects” of increasing the riskiness of banks and making it difficult to right banks that fell into trouble.

Regulators are working to do better next time. In these efforts, they are relying on connections they have established over the past forty years with regulators in other countries. Responding to the growth of global financial markets beginning in the 1970s, regulators developed groups to coordinate policy across borders outside of the ambit of formal treaties. These include the Basel Committee on Banking Supervision (“Basel Committee”), which has promulgated widely-implemented standards for bank regulation, and the more recently developed Group of Twenty (“G-20”), which provides a forum for heads of state, finance ministers, and central bank governors to discuss the workings and regulation of the international financial system. Through these institutions, regulators hope to put in place a regulatory structure that will address many of the issues that the 2008 crisis revealed, and provide the international community with the tools to better manage future crises.

II. A NEW REGULATOR EMERGES

An essential component of this new regulatory structure seemed to be a body that could coordinate the work of regulators, both across subject areas and countries, and highlight potential problems and gaps in regulation. The G-20 established the Financial Stability Board (“FSB”) to do just this, placing it near the top of what Herring describes as the “new pecking order” among international financial regulators.
By forming the FSB, the G-20 deepened connections between the technocratic world of international financial regulators such as the Basel Committee and the political world of the finance ministers of countries that are members of the G-20. The FSB should now have the tools to effectively coordinate cross-border issues and rules while taking into account the political will of its members. The actions that the FSB is taking today will shape the future of financial institutions across the world.

The FSB’s origins lie in the Financial Stability Forum (“FSF”), an organization that the Group of Seven (“G-7”) formed in 1999 as a response to two threats to the stability of the financial system: the Asian financial crisis and the failure of a large hedge fund, Long-Term Capital Management. The FSF sought to improve cooperation between national and international financial regulators in order to improve stability in the international financial system. However, the FSF was a passive organization, with a vague mandate, limited membership, and little ability to encourage compliance, explains Chris Brummer, Professor of Law at Georgetown University Law Center.

After the disasters of 2008, “there was a new impetus to chuck the FSF and create a more active coordinating body that would report to the G-20,” says David Zaring, Assistant Professor at the Wharton School. While, in the wake of the 2008 crisis, the FSF produced a report about what had gone wrong, the consensus among the G-20 members was that international regulators needed to be able to do more than produce reports. This meant adding a political body to the web of international regulators, explains Stavros Gadinis, Assistant Professor of Law at the University of California, Berkeley.

Thus, the G-20 broadened the FSF’s membership to include a longer list of countries (see Appendix II) and conferred upon it responsibility for identifying threats to the viability of the international financial system. Under this new mandate, the FSB collaborates with international organizations such as the International Monetary Fund (“IMF”) and the World Bank, and oversees and coordinates the work of international standard-setting bodies, including the Basel Committee, the International Organization of Securities Commissions (“IOSCO”), and the International Association of Insurance Supervisors (“IAIS”). The FSB also has a mandate to coordinate activity among these bodies and monitor the implementation of standards by national financial authorities in banking and securities regulation.

While the FSB is not the only entity that plays a role in the coordination of international financial regulation, it is uniquely positioned to act in cases where other regulators cannot. Other organizations that might be said to coordinate financial regulation include the IMF, which monitors countries’ compliance with regulatory standards and best practices, and the Joint Forum, which aids coordination between three international bodies that set standards in, respectively, the areas of securities, banking, and insurance—IOSCO, the Basel Committee, and IAIS. The IMF
supervises real economic indicators and macroeconomic issues, while the FSB is in charge of pinpointing problems in the financial system and financial regulation.

But what makes the FSB unique, explains Gadinis, is its close relationship with the G-20, a political body that directly oversees the FSB. Because the FSB's membership includes institutions headed by what are generally cabinet-level ministers with political ties to their home states, the organization can bring political will to bear at the international level. Partly for this reason, explains Gadinis, the FSB has taken the lead on developing best practices around cross-border resolution—in most countries, rules for cross-border resolution require input and support from members of the government in addition to regulators.

III. STANDARDS, REPORTS, AND PEER REVIEWS

Despite its activity on cross-border resolution, the FSB does not usually establish its own standards. Instead, it espouses standards developed by other international regulators. However, the FSB is, according to Gadinis, a proactive organization that makes suggestions for additional efforts and areas of focus, based both on requests from the G-20 and on its own judgment. For instance, writes Gadinis in a recent paper, in 2009 the G-20 directed the FSB to encourage the Basel Committee to adopt a leverage ratio, in addition to risk-based capital requirements, which the Basel Committee did. Another key area of collaboration between the FSB and other international organizations is around setting up methods for the peer review processes that these organizations use to measure the progress that countries have made in putting standards in place.

Substantively, the FSB has taken an active role in a number of areas of regulation—perhaps too many, some suggest. Its work on how to resolve large, bankrupt financial institutions may be most important. In October 2011, the group published a report on best practices entitled Key Attributes of Effective Resolution Regimes for Financial Institutions. The report encourages FSB members to establish national resolution authorities and enter into institution-specific cooperation agreements, among other prescriptions. Other areas of recent focus include mortgage underwriting practices, how to reduce reliance on credit-agency ratings, and executive compensation. The FSB has also played a key role in compiling a list of twenty-eight globally systemically important financial institutions, explains Michael Taylor, a member of the FSB Secretariat, and is now grappling with the issues presented by two key components of the global economy that proved treacherous during the financial crisis: the shadow-banking system—that is, the issuing of credit outside of banking institutions—and the over-the-counter derivatives market—the market for derivatives outside of organized, regulated exchanges.

Finally, the FSB is working with international and national regulators to establish standards for risk governance and uniform accounting principles for financial
institutions, as well as governance for financial benchmarks such as the London Interbank Overnight Rate, or LIBOR.

Apart from developing standards, the FSB is starting to expend more resources monitoring compliance with the best practices standards that it has developed, and has released peer reviews of countries’ implementation of best practices, as well as “thematic” reviews on issues for which it has been compiling standards, as mentioned above. In this vein, it has developed a framework for monitoring the implementation of financial reforms adopted by the FSB and approved by the G-20.

A recent letter by the FSB to the G-20, dated February 12, 2013, accompanied by reports on the effects of reform efforts on the availability of long-term finance and on convergence of accounting standards (the latter written jointly by the International Accounting Standards Board and the Financial Accounting Standards Board, and presented by the FSB), evaluated progress in regulatory implementation in several of these areas. Evaluating the G-20’s post-crisis financial reform program, which included the development of new capital requirements for banks and over-the-counter derivatives regulation, the FSB concluded that the program has improved confidence in the system, but so far has had little impact on long-term financing, an unsurprising outcome given that the program is still at a relatively early stage of development. Typifying its position as a regulatory coordinator, the FSB also castigated the slow pace of convergence between American and international accounting standards boards, and recommended that the G-20 become more actively involved in promoting the convergence of accounting standards on a worldwide basis. Finally, the letter discussed the extent to which other regulatory reforms have been implemented, and emphasized four of the FSB’s main priorities: the development of greater regulatory certainty, better oversight of shadow banking, development of stronger banks and financial institutions, and ending the “too big to fail” phenomenon.

This is an ambitious program for the FSB, particularly since it has only twenty-four full-time staff members, according to Taylor. Indeed, some worry that it has taken on too much, and for the wrong reasons. Howell Jackson, James S. Reid, Jr. Professor of Law at Harvard Law School, notes that the FSB “has developed an ambitious agenda that goes beyond the core elements of the financial crisis where international collaboration is most likely to be useful and they are arguably overcommitting given the size of their staff.” In part, their agenda follows politics, he added: “they seem to be going where the politics take them, and may be turning into a vehicle for somewhat unrelated regulatory projects.”

However, the FSB’s central focus has undeniably been on the regulation of banks—and, indeed, it has been criticized for being overly bank-focused. “Some people feel that it is overly weighted to banking,” says Hal Scott, Nomura Professor and Director of the Program on International Financial Systems and Co-Chairman of the Council on Global Financial Regulation (“CGFR”), an independent oversight group that
provides recommendations to the G-20, financial regulators, and international regulatory bodies. On the other hand, “there is a reason why it is bank-centric—this is where there has historically been the most systemic risk,” explains Brummer. “Some trade lawyers wonder why they are not also included, but how broad do you want the FSB to be?”

In addition, despite continued concerns about the FSB’s emphasis on bank regulation, its membership also includes regulators from the U.S. Securities and Exchange Commission (“SEC”), IOSCO, and other securities regulators, and these members appear to be very active within the FSB. According to Eric Pan, Associate Director of the Office of International Affairs of the SEC who works with both the FSB and IOSCO, the SEC spends a significant amount of staff time and resources working with their FSB counterparts.

But there are challenges around the integration of different perspectives on risk that bank and market regulators bring to the table. According to Pan, “bank regulators tend to focus on the minimization or elimination of risk to ensure safety and soundness, while market regulators tend to focus on the disclosure and pricing of risk to ensure a healthy environment for risk-taking.” Since, Pan notes, “most of the FSB members come from a pure bank regulatory perspective,” it is important that “these FSB members are careful not to overlook other perspectives.”

The upside is that these differences in perspective can lead to productive debates on regulatory approaches, which, Pan says, is “really important when you have multilateral discussions.” According to Pan, “the FSB and IOSCO have been successful in taking their different approaches and learning from each other.”

IV. SHERIFF OR TRAFFIC COP?

What does it take to monitor the global economy? For now, the international community is betting that this small, informal body producing peer reviews and reports and consulting with other regulators is enough. The FSB currently has no formal status in international law; indeed, it only established itself as a legal entity on January 28 of this year. Now it has the ability to rent its own office space and pay employees under its own name, explains Pan. But, though this change has provided the FSB with greater autonomy, under its new Articles of Association, the FSB’s funding still comes from the Bank of International Settlements (“BIS”), its host in Switzerland. The BIS is a bank organized by international treaty to provide services to

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2 SEC Commissioner Elisse B. Walter sits on the FSB Steering Committee, alongside Federal Reserve Governor Daniel K. Tarullo and Treasury Department Under Secretary for International Affairs Lael Brainard, the other two U.S. regulator representatives on these committees.
Central Banks and takes deposits from central banks across the world; it also houses the Basel Committee.

Like the Basel Committee, the FSB has no power to enforce its recommendations. Instead, it relies on its peer review process, “naming and shaming” states that do not comply with its suggestions, Herring explains. FSB member states are expected to lead by example, according to the FSB’s website. For example, they must publish IMF and World Bank reviews of their implementation of best practices, even though non-FSB countries need not make these reports on their compliance public. One of the main goals of the FSB’s monitoring activity is to facilitate transparency through this public process, according to Gadinis. Even with these requirements, though, Herring cautions that “a lot of countries will agree to everything and enforce nothing.” Gadinis is also leery—while he praises the FSB’s transparency, he notes that “when we have another crisis, we will see how the systems we have put in place actually operate.”

V. ROOM FOR IMPROVEMENT?

As the FSB matures, its members will have to think critically about its future. Already, there are critiques, especially surrounding the Board’s decisionmaking process and treatment of problems in developing countries.

For one thing, how the FSB works is a “black box,” notes Domenico Lombardi, Senior Fellow at the Brookings Institution. This “black box” might be familiar to followers of central banking—the Basel Committee and many central banks have historically employed opaque decisionmaking processes. But this opacity comes at the cost of transparency. The FSB “is not as accountable as it should be,” says Daniel Bradlow, Professor of Law at Washington College of Law and a collaborator of Lombardi’s on a paper providing recommendations to the FSB, who suggests that the group should increase the number of regulatory bodies and countries that decide its agenda.

Another significant problem that Bradlow and Lombardi point to is the lack of attention that the FSB pays to problems faced by developing countries. Yet, says Bradlow, the failure of a large financial institution can adversely affect financial institutions and the financial system in developing countries. It can also mean that small and medium size enterprises and households in these countries have difficulty accessing finance. This, in turn, can have substantial negative economic consequences for both the global real economy and the international financial system. While the FSB’s expanded membership includes China, India, and Brazil, most developing countries are not well represented in the organization’s membership and thus to a great extent are excluded from participation in the FSB’s agenda setting. However, the FSB is aware of these concerns and recently released a report on the effects of regulatory reforms on developing countries.
To address the problem of representation, the FSB has created six regional consultative groups (RCGs) with representation from the national financial authorities of countries in the Americas, Asia, Europe, the Middle East and North Africa, Sub-Saharan Africa, and the Commonwealth of Independent States. The RCGs, which are co-chaired by representatives from both an FSB-member and a non-FSB-member institution, appear to be a formalized version of the FSF regional meetings that occurred before the formation of the FSB and that also involved participation from both FSF members and non-member countries. Although this is progress, says Lombardi, it is not clear what the criteria are for membership in these groups. Going forward, the RCGs “could be pro forma or could be an effective forum.”

Still, not all are convinced that the FSB is the appropriate place to have discussions about the problems of developing countries. According to Scott, “the needs and problems of developing countries are so different from those of developed financial systems that it would be a big mistake for the FSB to try to formulate policy that would be applicable to them.”

The potential for expansion of participants is not limited to developing countries. Bradlow argues that private non-state actors—including corporate and civil society groups—should also have some input into agenda setting. “We are all stakeholders in the global financial system,” he explained. And Pan suggests that “it would be a positive move to engage the public, and not just industry,” perhaps through a process similar to the notice-and-comment proceedings used in U.S. administrative rulemaking.

Another area that remains to be developed is how decisions will be made within the group’s membership. Currently, decisions require consensus. Though Scott says that this method has so far been successful, part of the reason for this success is that “there was a lot of political pressure by those who wanted to see action.” In particular, major countries with robust banking and financial sectors put pressure on emerging market countries to agree to certain regulatory changes. Emerging market countries are incentivized to comply since, if they do not, they risk facing changes in the FSB decisionmaking process at the hands of the developed countries.

More urgently, the FSB may need to develop a larger staff with more definite responsibilities. The FSB’s staff of twenty-four mostly comes on secondment from central banks, and high-profile representatives such as finance ministers can only devote a limited amount of time to the FSB. Within the organization, the consistent turnover that results from the secondment process may inhibit the building of institutional memory and the establishment of working relationships with the many

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3 This last group encompasses Russia, Ukraine, Armenia, Belarus, Kazakhstan, Kyrgyz Republic, and Tajikistan. All of the groups have held at least one meeting since their establishment in 2011, according to the FSB’s website.
organizations that the FSB aims to coordinate. This could potentially make it difficult to provide oversight of these agencies, and so the CGFR recommends that the international bodies further clarify delegation of responsibility among themselves so as to avoid any overlap in scope. This may be particularly important since the FSB seems understaffed in light of its weighty and challenging mandate.

VI. ONWARD AND UPWARD

What does the future hold for the FSB? The answer is unclear. Right now, the organization may be on the verge of an expansion in which it “could become the coequal of the IMF. But it could also fail to develop and result in something much less significant,” Bradlow notes. “To a great extent, the result will depend on how it manages issues of participation and accountability.” For his part, Zaring says that the FSB “will become increasingly significant.” In particular, he notes that “it will be interesting to see if the peer-review process will evolve into something formal, because that has clearly been missing.” To be sure, the FSB has a long way to go before it gains the clout and prestige of organizations such as the IMF or WTO, which have far wider memberships and influence, as well as much larger permanent staffs.

Another important question is what will happen to the FSB as the financial crisis recedes. Scott notes that the financial crisis did much to energize consensus building among nations, but he questions whether this momentum will continue as the crisis recedes. Nonetheless, he says, “it is becoming more important every day. The basic fact is that we have a global financial system and there is a lot of support for global regulation, not the least of which comes from banks and financial institutions. They want to see a global, coordinated approach to problems.”

APPENDIX I: STRUCTURE OF THE FSB

The FSB consists of the Plenary; its decisionmaking body, the Steering Committee, which provides operational guidance between Plenary meetings; the Secretariat, a group of full-time staff members led by the Secretary General; and several standing committees and working groups.

The Plenary controls FSB membership, work agenda, and budget; appoints the FSB Chair, the chairs of the Standing Committees, and the Secretary General; and oversees the Standing Committees and working groups.¹ Plenary meetings occur twice a year, and the Chair may invite non-FSB members, including representatives from the

¹ FSB Charter, Art. 9.
private sector, to attend these meetings. Representation in the Plenary is proportional to the “size of the national economy, financial market activity and national financial stability arrangements of the corresponding Member jurisdictions,” and the number of seats assigned to a Member jurisdiction is based on this assessment.

The Steering Committee is influential in guiding the FSB’s work plan between Plenary meetings. According to the Brookings Institution paper on the governance of the FSB, “[a]lthough the Plenary is the formal decisionmaking body, in practice, the Steering Committee plays a very influential role…. [O]rganizational power has increasingly shifted to the committee, which shapes and in effect manages the FSB’s agenda.” According to Pan, the Steering Committee evaluates proposals for projects submitted to the FSB Chair, which are then brought before the Plenary for approval.

The Secretariat is headed by a Secretary General appointed by the Plenary and currently consists of a full-time staff of twenty-four. Though the Secretary General and Secretariat staff members work solely for the FSB during their tenure, many staff members are on temporary reassignment or secondment from member countries or organizations. Apart from the secretary-general and Secretariat, most other committee and working group members participate on a part-time, volunteer-basis.

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5 FSB Charter, Art. 10.
6 FSB Charter, Art. 10.
APPENDIX II: MEMBERSHIP OF THE FSB
Institutions Represented on the FSB

**Group of Twenty Member Countries**

- **Argentina**
  - Banco Central de la República Argentina
- **Australia**
  - Reserve Bank of Australia
  - The Treasury of Australia
- **Brazil**
  - Banco Central do Brasil
  - Comissão de Valores Mobiliários
  - Ministério da Fazenda
- **Canada**
  - Bank of Canada
  - Office of the Superintendent of Financial Institutions
  - Department of Finance
- **China**
  - People’s Bank of China
  - China Banking Regulatory Commission
  - Ministry of Finance
- **Germany**
  - Deutsche Bundesbank
  - Bundesanstalt für Finanzdienstleistungsaufsicht
  - Bundesministerium der Finanzen
- **India**
  - Reserve Bank of India
  - Securities and Exchange Board of India
  - Ministry of Finance
- **Indonesia**
  - Bank Indonesia
- **Italy**
  - Banca d’Italia
  - Commissione Nazionale per le Società e la Borsa
  - Ministero dell’Economia e delle Finanze
- **Japan**
  - Bank of Japan
  - Financial Services Agency
  - Ministry of Finance
- **France**
  - Banque de France
  - Autorité des Marchés Financiers
  - Ministry of Economy and Finance
- **Republic of Korea**
  - Bank of Korea
  - Financial Services Commission
- **Mexico**
  - Banco de México
  - Secretaría de Hacienda y Crédito Público de México
- **Russia**
  - Central Bank of the Russian Federation
  - Federal Financial Markets Service
  - Ministry of Finance
- **Saudi Arabia**
  - Saudi Arabian Monetary Agency
- **South Africa**
  - Ministry of Finance
- **Turkey**
  - Central Bank of the Republic of Turkey
- **United Kingdom**
  - Bank of England
  - Financial Services Authority
  - HM Treasury
- **United States of America**
  - Board of Governors of the Federal Reserve System
  - U.S. Securities & Exchange Commission
  - U.S. Department of Treasury
# Institutions Represented on the FSB

## Other Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Institutions Represented</th>
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<tbody>
<tr>
<td>Hong Kong SAR</td>
<td>Hong Kong Monetary Authority</td>
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<tr>
<td>The Netherlands</td>
<td>De Nederlandsche Bank, Ministry of Finance</td>
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<tr>
<td>Singapore</td>
<td>Monetary Authority of Singapore</td>
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<tr>
<td>Spain</td>
<td>Banco de España, Ministerio de Economía y Competitividad</td>
</tr>
<tr>
<td>Switzerland</td>
<td>Swiss National Bank, Swiss Federal Department of Finance</td>
</tr>
</tbody>
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## International Organizations

- Bank for International Settlements (BIS)
- European Central Bank (ECB)
- European Commission (EC)
- International Monetary Fund (IMF)
- Organisation for Economic Co-operation and Development (OECD)
- The World Bank

## International Standard-Setting Bodies

- Basel Committee on Banking Supervision (BCBS)
- Committee on the Global Financial System (CGFS)
- Committee on Payment and Settlement Systems (CPSS)
- International Association of Insurance Supervisors (IAIS)
- International Accounting Standards Board (IASB)
- International Organization of Securities Commissions (IOSCO)
APPENDIX III: RESOURCES


COUNCIL ON GLOBAL FIN. REGULATION, PRACTICAL MEASURES FOR ENHANCING INTERNATIONAL FINANCIAL REGULATORY COORDINATION (2011).


APPENDIX IV: INTERVIEWS

Telephone Interview with Daniel Bradlow, Professor of Law, American University Washington College of Law (Oct. 19, 2012).

Telephone Interview with Chris Brummer, Professor of Law, Georgetown Law (Mar. 13, 2013).

Telephone Interview with Stavros Gadinis, Professor of Law, The University of California, Berkeley (Mar. 28, 2013).
Telephone Interview with Jo Marie Griesgraber, Executive Director, New Rules for Global Finance Coalition (Oct. 9, 2012).

Telephone Interview with Richard Herring, Professor, Wharton School of Business, Finance Department, University of Pennsylvania (Oct. 2, 2012).


Telephone Interview with Eric Pan, Associate Director, Office of International Affairs, U.S. Securities and Exchange Commission (Feb. 28, 2013).


Telephone Interview with Michael Taylor, Member of the Secretariat, Financial Stability Board, Bank of International Settlements (Feb. 28, 2013).

Telephone Interview with David Zaring, Assistant Professor, Wharton School of Business, Legal Studies Department, University of Pennsylvania (Nov. 8, 2012).