PRIVATE GOVERNANCE FOR THE PUBLIC GOOD?
EXPLORING PRIVATE SECTOR PARTICIPATION IN GLOBAL FINANCIAL REGULATION

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In 1971, Robert Keohane and Joseph Nye issued a call for greater attention to the role of "transnational actors" in world politics (Keohane and Nye, 1971). Their introduction to a special issue of *International Organization* maintained that, while transnational actors did not replace states, they were increasingly important to the conduct of international relations. As such, greater attention to the effects of transnational actors on formal international institutions and on the global distribution of wealth and power was necessary, as was the development of an alternative to the state-centric paradigm.[1]

During the nearly 35 years since Keohane and Nye issued their call, a wide variety of scholars has acknowledged and explored the role of such actors, not only in economic realms, but in human rights, the environment, and military operations (see, for instance, Slaughter 2004). At the same time, the intensification of globalization, the rise of "complex interdependence," and the accompanying technological advances (e.g. Keohane and Nye, 2001)[2] have rendered transnational actors – including multinational corporations, institutional investors, banks, and non-governmental organization – increasingly important to the conduct of world politics.

The growth in importance of transnational actors, particularly those from the business sector, has been dramatic in the area of global finance. It is not only that the volume and velocity of global capital flows has increased over the last two decades; it is also that efforts to govern various aspects of global finance have evolved. One of the distinguishing features of financial governance in the contemporary era is its use of public as well as private actors. In many instances, regulatory efforts depend on public (government) agents to set rules, and on a combination of public and private sector enforcement. It is now not only "clubs" of powerful governments, but also groups of private sector

[1] E.g. Keohane and Nye (1971), p. 345.
[2] Keohane (2002) draws a distinction between globalization and "globalism." He defines globalism as a state of the world (akin to interdependence), but globalization as "a trend of increasing transnational flows and increasingly thick networks of interdependence." Globalization is, in this sense, the result of increases in globalism (p. 15)

actors, quasi-governmental agencies, and transgovernmental groups that attempt to create and enforce rules.

Despite the growth in private sector participation in global financial governance, and the implications of this growth for questions of equity and efficiency, recent scholarship in international political economy provides few systematic assessments of the sources of variation in international financial governance, nor to investigate the consequences of this variation,[3] in terms of regulatory efficiency and distributional equity. As a result, many of the questions raised by Keohane and Nye in their 1971 article remain unanswered:

> What are the effects of transnational relations on the allocation of value and specifically on asymmetries or inequalities between states? Who benefits from transnational relations, who loses, who controls transnational networks, and how is this accomplished?...What challenges do transnational relations raise for international organizations as conventionally defined?" (Keohane and Nye, 1971, p. 331)

This paper begins with a discussion of the regulation of global finance, with special attention to the public and private sources of governance, and the evolution of governance over time. I present two hypotheses regarding the impact of private sector participation on regulatory efforts – a distributional hypothesis and an effectiveness hypothesis. I argue that, while private sector participation may increase the effectiveness of international and transnational rule-setting efforts, it also can have distributional consequences. Financial institutions have tended to serve the interests of powerful states, and of powerful constituencies within those states, thereby limiting their progress in equity. The private actors that help develop governance regimes tend to come from the financial sector; as a result, privately-developed regimes are likely to reflect their interests. This presents the global community with a difficult challenge – to broaden the voice of developing countries and non-financial actors in the regulatory process, while maintaining the cooperation of developed nations

[3] Recent exceptions are Mattli and Büthe's work (2003) on the role of the private sector in the development of international product standards and Farrell's (2003) account of the EU-US agreement on internet data privacy.

and financial sector players. The paper concludes with an initial empirical assessment of the effectiveness hypothesis.

I. The Governance of International Finance

Intergovernmental Institutions and Economic Governance. In the post-World War II era, intergovernmental institutions often helped solve the free-rider problem, allowing relevant actors to commit credibly to assist in the provision of public goods in a particular functional area,[4] to reap the rewards (such as efficiency and stability) that flow from public goods, and to avoid negative externalities.[5] As Keohane and others have stressed, international institutions can create specific obligations for each actor, monitor national behavior, enforce sets of rules, and create a "shadow of the future," allowing governments to make credible international economic commitments, despite the relatively anarchic nature of world politics. Moreover, through participation in these institutional frameworks, governments, and their citizens, may come to define their interests differently; this evolution of interests provides a fillip to cooperation on economic issues (Keohane 1988). (e.g. Keohane 1988).

The post-World War II era witnessed the dramatic growth of international institutions, in terms of their membership, their scope, and their influence. States were not the only important participants in these efforts, but they remained the locus of – and the ultimate participants in -- much regulatory activity. While international cooperation prior to the interwar years relied on hegemonic leadership and the confluence of national interests over economic policy, policymakers in the 1940s took a more institutionalized route to governing the global economy. While not all these efforts were immediate successes – for instance, the International Trade Organization floundered in the wake of the US refusal to ratify, and was replaced with a less formalized GATT – they did represent a

[4] On global public goods, see Kaul et al (2003). Kaul et al define public goods broadly, as "goods with benefits that extent to countries, people and generations." (p. 23). They also note that global goods can be more or less public, depending on the ways in which they are governed and provided.
[5] For discussions of global "bads" in international finance, and governments' incentives to avoid these, see Drezner 2003b; Knill and Lehmkuhl 2002, Wyplosz 1999.

significant effort to ensure the supply of economic openness, exchange rate stability, and development funds. The obligations created by these entities were largely "at the border," requiring governments to change the ways in which they treated external actors and flows (e.g. their tariff levels), but not to change their domestic policies or institutions.

Following somewhat steady growth in the 1970s and 1980s, the pace and depth of global regulation increased dramatically in the 1990s. Some institutional frameworks were created or expanded; others became more legalized. In both cases, national governments increasingly agreed to be bound by international commitments. For instance, the European Union broadened its scope to include economic and monetary union, greater oversight of national fiscal policies, and the governance of a larger set of non-economic issues. And the GATT was transformed into the World Trade Organization (WTO), an entity which deals with trade in goods as well as with trade in services and intellectual property rights. The hallmark of the WTO is a more legalized process of dispute settlement, with greater safeguards against political interference and expanded enforcement possibilities.

Institutionalization has occurred unevenly, however. Some areas of the global economy are now governed by very clear sets of multilateral rules (for instance, trade, via the WTO or the EU), whereas other areas continue to be governed by bilateral treaties and private sector initiatives (for instance, many facets of international capital flows, particularly foreign direct investment).[6] One explanation for these differences are the preferences of key actors: where the major states have been able to agree and to act as leaders in the process (e.g. Simmons 2001), a more legalized set of rules – making explicit rights, responsibilities, and dispute-settlement procedures – has prevailed. Where major states have not had such consensus, the development of rules has remained more ad-hoc, or has focused more on the private sector.

[6] Keohane and Van Doorn Ooms discussed the lack of a global regime for foreign direct investment in a 1975 article; efforts since to create a comprehensive intergovernmental framework to govern FDI have failed.

More generally, the increase in international governance is both a cause and an effect of economic openness (e.g. Keohane 2002; Slaughter 2004). As trade and financial linkages among nations expand, so does the extent to which national actions and policies generate regional or global externalities. Economic globalization intensifies the functional demand for public and private actors to have clear and credible property rights, dispute settlement mechanisms, and crisis resolution mechanisms. Moreover, some of the national deregulation undertaken in the 1980s created a vacuum, particularly with the increased salience of "behind the border" issues (Helleiner 2002, Kaul et al 2003), which demanded not only changes in governments' policies vis-à-vis external actors, but also revisions in domestic policies, such as taxation, banking regulation, and subsidies. As Keohane and Nye describe it,

> More and more issues are up for grabs internationally, including regulations and practices – ranging from pharmaceutical testing to accounting to product standards to banking regulation – that were formerly regarded as the prerogatives of national governments. (Keohane and Nye, 2001, p. 246)

Hence, "re-regulation" has emerged at the international level (Kapstein 1992, Ronit and Schneider 2000, Vogel 1996), and the contemporary era has witnessed a shift in the subjects of public international law, from only states to states plus individuals and firms, as well as a trend away from "soft law" and norms and toward "hard law" and treaties (e.g. Goldstein et al 2000).

The functional need to govern various aspects of contemporary globalization presents challenges both to our current system of international institutions and to our understandings of international governance. First, as Karl Polanyi pointed out in 1944, and as Dani Rodrik (1997) and others have noted more recently, economic openness is sustainable only as long as there is public support for it. When publics doubt the legitimacy of intergovernmental economic institutions, and economic openness more generally, the continued trend toward economic globalization may be endangered. Hence, finding effective means of governing globalization is central to sustaining globalization (e.g. Keohane 2002, p. 193), and to reaping its economic benefits.

Many of the contemporary challenges to the legitimacy of international institutions are based on the often great disparities in the influences of states on regulatory regimes. The international institutions that provide solutions to functional problems may take a variety of forms. The particular regulatory system that emerges is likely to benefit some actors (states or private actors) more than others, and these benefits have distributional consequences, both internationally and within societies (Krasner 1991; Mattli and Büthe 2003; Rosenbluth and Schaap 2003).[7] For instance, while developed and developing nations tend to have very different preferences over regulatory issues (e.g. Eichengreen 2003), the views of developed nations often hold sway.

When powerful states have great influence on regulatory regimes, the club model of governance has tended to prevail; rules will bear close resemblance to the preferences of large nations. Although these clubs[8] were successful in governing many parts of the global economy during the latter part of the twentieth century, they tended to operate in secret, and they offer very little democratic accountability (Keohane and Nye 2003). Such multilateral institutions have been an important source of regulatory governance, but often as a vehicle for dominant countries to realize their preferred outcomes (Drezner 2003b; Simmons 2001). As a variety of citizens, NGOs and developing nations has begun to worry about the legitimacy of global governance, the club model – and its reliance on like-thinking major powers as the source of international rules – has come under threat (Keohane and Nye 2001; Slaughter 2004).

Second, the recent attention to "behind the border" issues has been accompanied by an increase in the importance and participation of private sector actors, or "transnational actors." In the modern era, states have been they key actors in the development of global rules. But many other

[7] Such an argument focuses on games of cooperation, rather than on games of pure coordination, in which actors are indifferent among outcomes, provided each chooses the same outcome.

[8] Drezner (2003b) points out that economically powerful states make choices between modes of interstate cooperation or regulation, creating intergovernmental bodies (IGOs) that are "clubs, neighborhoods or universes." Sometimes, regulatory public goods are provided by clubs, but their real constituencies are universes. Universes have broad membership, generating greater legitimacy but less decision-making efficacy. Neighborhoods rely on geographical distinctions (e.g. "Europe") to establish membership. Drezner borrows this typology from Michael Walzer (1983).

actors – banks and investment houses, multinational corporations (MNCs), and civil society groups (NGOs) – are important to the provision of information and the implementation of rules. Some international regulatory regimes have begun to include these groups – or least the business and financial components – explicitly; others consult private sector actors informally. The result is a shifting in some realms from governance via multilateral cooperation to governance via "transnational and transgovernmental cooperation" (Keohane and Nye 2001, p. 259). As Slaughter (2004) demonstrates, one element of this is the rise of networks of government officials (transgovernmental networks) as important participants, alongside traditional IGOs, in contemporary global governance. The other element, though, is the participation of nongovernmental actors in many of the same governance processes.

The rise of private actors reflects not only their increased importance in global exchange, but also another shortcoming in traditional modes of intergovernmental regulation – the problem of compliance. Regulatory regimes at the international level have little impact unless states comply with their provisions; compliance, in turn, requires an appropriate mixture of incentive and enforcement mechanisms.[9] Where intergovernmental institutions are concerned, compliance hinges on the ability and willingness of governments to implement rules domestically; and where transgovernmental networks are concerned, commitments are not legally binding, and formal enforcement mechanisms are rare (Slaughter 2004). Therefore, the involvement of private sector actors, particularly at the enforcement stage, can enhance the incentives for states, or for non-state actors in the national polity, to comply.

Governance in the Financial Realm. Mirroring the general trend identified above, international and transnational efforts at financial regulation have increased dramatically in recent

[9] On issues of compliance with international law, see Downs, Rocke and Barsoon 1995, Mitchell 1994, and Simmons 2000.

years (Armijo 2002; Council on Foreign Relations 1999; Eichengreen 1999; Goldstein 1998).[10] Regulatory regimes in international finance can serve two broad – and not necessarily opposing -- purposes: to improve global levels of efficiency, and to facilitate a more equitable distribution of financial resources among societies.[11] Within the broad concept of efficiency, three specific, and sometimes overlapping, elements are important: (a) allocation of investment in a generally efficient manner, ensuring that capital is put to its most productive uses; (b) stability of international financial flows, thereby avoiding the costs generated by financial crises and volatility; and (c) the lowest possible transaction costs, further facilitating the movements of resources across international borders. Equity could encompass the distribution of resources at the international level (among developing nations, or between developed and developing countries), as well as the distribution of resources within countries (among different economic groups, for instance).[12]

First, improvements in the allocation of capital can help ensure that investment is put to productive use, particularly in capital-poor regions. In the longer run, this can – although this is by no means guaranteed – also lead to a more equitable distribution of resources. For example, by requiring its members to implement current account convertibility (see Simmons 2000) and by encouraging its members to reduce restrictions on the capital account, the International Monetary Fund (IMF) can serve to encourage allocative efficiency. Additionally, if the IMF succeeds in acting as a "seal of approval" for nations with economic difficulties, it can encourage the movement of private capital to nations with great capital needs, but with attenuated capacity to attract capital.[13] Moreover, efficiency

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[10] Drezner (2003b) notes that "*none* of the financial standards now considered to be important by the IFIs existed prior to 1996." (p. 19). Simmons (2001) points out, however, that governance efforts in international finance have been less comprehensive and less legalized that in international trade.
[11] International regulation, of course, also may aid in the achievement of other sorts of public goods, such as the protection of environmental resources and the prevention of terrorist activities.
[12] See Magnoli (2002) for a discussions of the potential relationships between equity and efficiency, as well as the various types of efficiency (in production, coordination, or allocation) and equity (in access, capabilities, and results).
[13] Recent research (e.g. Stone 2002, Vreeland 2003), as well as longer-standing concerns about moral hazard, however, suggest that the IMF's role as a catalyst to private finance may be problematic.

could also be improved with common sets of accounting and disclosure standards among actors and across countries (e.g. Crouzet and Véron 2002).[14]

Second, international financial regulation can provide stability and prevent financial crises or contagion. This benefits a variety of actors, including nations that are spared from crises, nations with financial institutions involved in crises, and private agents that are shielded from extreme volatility of interest and exchange rates. For instance, rules on capital adequacy (e.g. the Basel Accords) could help prevent banking collapses – and the spread of banking sector weaknesses -- in the face of local or regional financial difficulties (Simmons 2001). Additionally, financial governance regimes could encourage prudential behavior by governments, preventing them from accumulating large current account or government budget deficits. While the IMF's structural adjustment lending attempts to do this for countries in crises, the IMF's regular surveillance and its standard for transparent economic policymaking attempt this more generally. And the EU's Stability and Growth Pact attempts to do this for euro-zone members. There also are private sector efforts on this front; credit ratings agencies, via their effects on investment allocation, may encourage fiscal probity. More generally, and less formally, private capital markets could encourage governments – via interest rate penalties – to avoid profligate policies.[15] Other means of promoting global financial stability include providing some sort of lender of last resort function and encouraging the provision of information, as the IMF has done since the late 1990s.[16] And international rules also could assist with the resolution of crises once they occur; for instance, procedures for the orderly workout of

[14] Simmons (2001) notes that there are strong incentives for countries to emulate the accounting standards of the most powerful economy; she points out that, dating to an era in which most stock trading occurred within the same or nearby time zones, there has been a regional pattern of accounting standards. For instance, Canada's standards resemble US standards, and Scandinavian standards resemble German standards (p. 609).

[15] For a discussion of the extent to which these sort of financial market pressures vary across groups of countries, see Mosley (2003a).

[16] See Council on Foreign Relations 1999. On market participants' incentives to collect and employ information, see Mosley 2003a, Willett 2000.

sovereign debt would facilitate borrowers' returns to global capital markets and reduce the extent of contagion to other nations (Eichengreen 1999, Herman 2003).

Third, and related to the first two efficiency-oriented tasks, reduction of transaction costs in international capital markets also improves market efficiency. Some regulations can reduce private agents' uncertainty, standardize behaviors across countries, and generate network externalities. For instance, capital owners may worry about the extent to which their investments are safe from expropriation, or about the extent to which host country legal systems will facilitate the settlement of disputes. On the host country side, there may be concerns about the behavior of foreign multinationals, in terms of activities like the respect for collective labor rights or the repatriation of profits. In response, governments of home and host countries can sign bilateral investment treaties (Simmons and Elkins 2004, UNCTAD 2003), which specify the rights and responsibilities of foreign direct investors, as well as other practices (such as tax treatment). Alternatively, governments and private actors could work to establish international regulatory regimes.[17] These regimes might include a multilateral treaty on the treatment of investment by host countries (embodied, for instance, in the failed Multilateral Agreement on Investment); a legalized process for the settlement of investment disputes (either at the global level, or as part of a regional free trade agreement like NAFTA); or a private-public consortium to identify "best practices" in corporate social responsibility (akin to the United Nations' Global Compact).

Table 1 lists several actual and proposed financial regulatory regimes, the functional problems to which these regimes are addressed, and the actors involved in these regulations. This list is by no means exhaustive, but it illustrates the varied set of arrangements that falls under the rubric of "international financial regulation." Some, for instance, encourage transparency and disclosure by national governments and firms, while others govern the regulation and design of economic systems (see Sundararajan et al 2001). Their forms include global intergovernmental institutions (IMF,

[17] Drezner 2003b, Keohane 1984, Koremenos et al 2001.

Table 1: Rules for Global Finance

Issue or Functional Problem	**Actual or Proposed International Regulation**	Rule-setting Actor
Accounting Standards	International Accounting Standards	International Accounting Standards Board
Balance of Payments Adjustment	Stand-by Arrangements and Conditionality; Structural Adjustment Loans	International Monetary Fund
Banking Codes of Behavior	Basel Accords	Basel Committee on Banking Supervision
Behavior of MNCs	• Corporate Codes of Conduct • Global Compact	• MNCs or MNCs & NGOs • United Nations, NGOs, MNCs
Crisis Prevention and Management	• Systemic oversight and monitoring. • Regulation of international banking practices.	• IMF, Financial Stability Forum (FSF) • Basel Accords
Debt Relief	• Highly Indebted Poor Countries Initiative (HIPC) • Debt Forgiveness	• IMF/World Bank • G-7 governments, Paris Club
Debt Renegotiation and Orderly Workouts	• Ad-hoc renegotiation of debts to public and private actors. • Proposed measures for debt workouts	• Paris Club and London Club • IMF (Sovereign Debt Restructuring Mechanism) and others.
Default Risk Assessment	Sovereign Credit Ratings	Credit Ratings Agencies (e.g. Standard and Poor's, Moody's)
Development Assistance	• Development and Project-Specific Loans	• World Bank • Regional Development Banks
Insurance Codes of Behavior	Insurance Core Principles	International Association of Insurance Supervisors (IAIS)
Investment Disputes and Property Rights for Foreign Investors	• Arbitration based on agreements between governments and private actors. • Global rules for host country behavior. • Bilateral rules for host country behavior. • Regional rules for host country behavior and dispute settlement.	• International Center for the Settlement of Investment Disputes • Multilateral Agreement on Investment (Failed) • Bilateral investment treaties • Regional trade bodies and agreements (e.g. NAFTA, Ch. 11)
Limit Government Budget Deficits	• Stability and Growth Pact, Maastricht Treaty • Private capital market pressures	• European Union • Government bond market
Money Laundering and Terrorist Financing	Anti-money laundering and "know thy customer" rules	Financial Action Task Force (FATF)
Provision of Information	• Special Data Dissemination Standard (SDDS) • Joint data on public debt.	• IMF • Joint IMF/World Bank/BIS
Securities Market Regulation	• Objectives and Principles of Securities Regulation • Regional market rules.	• International Organization of Securities Commissions (IOSCO) • Regional trade bodies (e.g. EU)
Transparency of Public Policies	• Code of Good Practices on Transparency in Monetary and Financial Policies; Code of Good Practices on Fiscal Transparency. • Corruption assessments.	• IMF • Transparency International and other private agencies.

World Bank), regional intergovernmental bodies (EU), transnational regulatory groups (IOSCO), and private sector entities (credit ratings agencies, the Paris Club). As such, regulatory regimes may be rooted in the public sector (via intergovernmental institutions, or state-to-state cooperation), in the private sector (through institutionalized coalitions of investors, or through concerted efforts toward “corporate social responsibility”), or at some public-private sector intersection.

II. The Role of the Private Sector

The Nature of Financial Regulation. Table 1 indicates that much of the current “action” in global financial regulation occurs outside intergovernmental frameworks. The development of an overarching global financial authority, endowed with rule-setting and enforcement capabilities across a range of issues,[18] is politically unfeasible. Rather, the current situation accords with Keohane and Nye’s (2001) observation that there are many ways to govern globalization, ranging from unilateral actions by states (which may then be followed by others), to multilateral state efforts, to transnational and transgovernmental cooperation (which may involve components of states, or only non-state actors) (p. 259-261).[19] This fact raises important research and policy questions. First, how does the type of financial governance matter to regulatory outcomes (efficiency and equity)? Second, and more specifically, how does variation in the degree and type of involvement of private actors influence outcomes? Regulatory efforts affect not only the overall amount of financial flows (often succeeding in enhancing resource transfers); they also affect the location of these financial flows, and the distribution across societies of efficiency gains. This is true even of rules that at first glance might seem very technical, such as transnational merchant law and the provision of financial data (Crouzet and Véron 2002, Cutler 2003, Mosley 2003b).

[18] Eatwell and Taylor (2002) argue that such a World Financial Authority would undertake five functions: “(1) authorization or licensure of private sector financial actors; (2) provision of comprehensive information, thus enhancing transparency; (3) surveillance of market players; (4) enforcement against any breaches of regulations that they may commit; and (5) development of policy” (p. 5).

[19] Along similar lines, functionalist reasoning makes a case as to why cooperation is desirable, but it does not predict the specific form of governance that emerges (Kahler and Lake 2003). On transgovernmental networks, see Slaughter 2004.

The first, and broader, question, intersects with an established literature linking state power with characteristics of intergovernmental institutions. International cooperation involves selecting a specific point along the Pareto frontier (Krasner 1991), and this process has distributional consequences (e.g. Conçeicao 2003; Koremenos, Lipson, and Snidal 2001; Oatley and Nabors 1998).[20] A global lender of last resort, for instance, should improve allocative efficiency, but that lender could be structured in myriad ways (as the US-UK debates of the early 1940s illustrate; also see Kenen 2001). Along these lines, intergovernmental efforts in global finance depend heavily on the major developed nations, especially the US (e.g. Drezner 2003b, Simmons 2001).[21] Developing nations have had little ownership of or influence over most international financial rules (Griffith-Jones 2003a, Griffith-Jones and Cailloux 1999, Griffith-Jones and Ocampo 2003). And these club-based arrangements tend to privilege efficiency over equity and to provide greater benefits to wealthy nations.

Decision-making and quota patterns in the IMF are perhaps the most obvious example: current quota patterns mean not only that large, wealthy nations have the greatest voting power, but also that small developed nations have more voting power than intermediate-sized developing countries. Although their economies and populations are larger, Brazil, Mexico and Korea have much smaller quotas that Belgium, the Netherlands and Switzerland (Buria 2003). Similarly, the development of the 1988 Basel Accord on bank capital adequacy largely reflected a bilateral deal between the U.S. and the U.K., onto which the remaining G-10 nations signed (Kapstein 1992). Given the size of its capital market, U.S. regulators had incentives to set standards unilaterally, disregarding divergence by other governments. The scope of the agreement's influence expanded

[20] Such an argument focuses on games of cooperation, rather than on games of pure coordination, in which actors are indifferent among outcomes, provided each chooses the same outcome.
[21] For instance, in her account of regulatory harmonization processes, Simmons (2001) argues that the majority of international regulatory harmonization in the 1980s and 1990s was driven not by "mutual adjustment" (cooperation among states), but by "unilateral decisions imposed by the dominant financial centers on other jurisdictions." (p. 591).

further with time, as many countries that were not participants in the G-10 forum nonetheless adopted the Accord's main directives, such as the eight percent capital standard and rules on providing information about derivatives trading (Simmons 2001). In the Basel case, national states were the source of the regulation, but only a small set of states was involved in the design of the rules. And, while banking supervision has evolved since the 1980s, the Basel Committee's orientation toward practices in major financial centers has remained (Eatwell and Taylor 2002, Griffith-Jones and Ocampo 2003, Oatley and Nabors 1998).[22]

Another example of this general pattern is the Financial Stability Forum (FSF), which was established in the late 1990s and has promulgated a set of twelve key financial codes and standards (Drezner 2003b, Eichengreen 2003).[23] Developing nations had little input into the design of the FSF's standards (Griffith-Jones and Ocampo 2003, Vojta and Uzan 2003), but they now are -- through IMF as well as private capital market pressures -- bound by such standards.[24] In a different area, the success of efforts to reduce money laundering in the early part of this decade likely was driven as much by direct political pressures from the United States as by national governments' and private banks' desire to maintain a reputation for doing legitimate banking business; Helleiner 2002).

This provides a parsimonious explanation, then, for the fact that international financial regimes have made some progress in achieving efficiency-oriented goals, but less in achieving equity-oriented aims (see Section IV below). But even if we are content to focus on states as the main source of financial regulation, we must explain how states aggregate interests over regulation.

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[22] For instance, how to measure banks' capital, and how to weight the risk of bank capital, was widely disputed in the run-up to Basel II.

[23] In the Financial Stability Forum, each G-7 nation has three seats, for a finance ministry official, a central bank official, and a financial regulatory authority; another sixteen (of 41) seats are held by representatives from the IMF, World Bank, the Bank for International Settlements and related entities; and five seats are held among Australia, Hong Kong, the Netherlands, and Singapore. Slaughter describes it as a "network of networks" (2004, p. 135). The FSF's twelve standards, discussed below, relate to financial sector operations (banking, securities); market integrity (accounting, money laundering); and transparency (data and policymaking).

[24] Also see Eichengreen's (2003) account of how different regulatory bodies dealt with the "hedge fund problem" in the wake of the 1998 Long Term Capital Management collapse. As a "club," the FSF was primarily concerned about global financial stability, but not about market manipulations by private actors or allocative efficiency.

To argue that states are the primary actors in some international regulatory efforts says little about states' preferences over rules. Presumably, these desires are rooted in domestic politics, as well as in state calculations' about its strategic position vis-à-vis other states. One plausible assertion is that state interests tend to reflect the demands of the domestic financial sector, particularly when regulatory issues are highly technical.[25] As a result, states' positions on financial regulatory issues may reflect the demands of a narrow group of private sector ("transnational") actors, as well as those of national regulatory authorities ("transgovernmental" actors).

The issue of state interests points to the second question above -- *how does variation in the degree and type of involvement of private actors influence outcomes?* – as well as to Keohane and Nye's transnational (and transgovernmental) actors.[26] These non-states actors are drawn from the business sphere (e.g. corporations), civil society (e.g. non-governmental organizations, NGOs), "epistemic communities" of experts on a particular topic, or a combination of the three. While private actors may work through national governments (or their agencies) to influence international financial regulation, they may instead work alongside governments in institutional design (Keohane and Nye 2001; Koremenos, Lipson, Snidal 2001), as well as in institutional implementation (Farrell 2003, IMF 2003, Knill and Lehmkuhl 2002). Contemporary financial governance often is a joint public-private effort, relying on private sector actors for rule-setting, rule enforcement, or both. Private actors' involvement in international financial governance has increased markedly in the last decade (Armijo 2002, Council on Foreign Relations 1999, Eichengreen 1999, 2003, Goldstein et al 2000, Koremenos, Lipson, Snidal 2001, Ronit and Schneider 2000, Sandholtz and Gray 2003).

State interests on global issues (for instance, environmental and labor standards) often are diffuse, creating space for private actors to develop their own set of standards, or for private actors to

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[25] Rosenbluth and Schaap (2003), however, suggest that domestic banking regulation may depend on societal interests, and particularly on electoral institutions.

[26] Keohane and Nye (1975) define transnational relations as those involving private sector actors and transgovernmental relations as those involving branches of national governments. Contemporary global financial regulation often involves both types.

play key roles in which standards are ultimately selected.[27] Some accounts of private sector involvement view it as a deliberate choice by governments (Drezner 2003a, Farrell 2003, Pauly 2002), while others treat it as the unintended consequence of capital market openness and technological complexity (Helleiner 1994, Porter 1999, Strange 1996, Underhill 2000).[28]

The participation of private sector actors in global governance is not entirely new, of course. The law merchants of early modern Europe facilitated the functioning of long-distance exchange by collecting and supplying information (Milgrom et al 1990; also see Cutler 2003), not unlike credit ratings agencies of the contemporary era. The Corporation for Foreign Bondholders acted, in pre-World War I London, as a repository of information about sovereign borrowers, as well as the chief representative for investors' in cases of sovereign default (Eichengreen 1999, Mosley 2003a). In that same era, several very wealthy families (e.g. the Morgans, Rockefellers, and Rothschilds) conducted great amounts of multinational lending, information sharing, and government financing (Ronit and Schneider 2000). And, as Kahler (2004) reports, "much of the interwar era was dominated by private governance (oil) or public private networks (finance) in which formal intergovernmental organizations played a negligible role" (p. 14).

Types of Private Sector Participation. In the realm of global finance, what qualifies as "private sector involvement?" I classify private (non-governmental) actors as either commercial or non-commercial. Private commercial actors include financial institutions (such as banks and investment funds), corporations (national or multinational), industry and professional associations, and individual (particularly very wealthy) investors. Non-commercial private actors include non-governmental organizations with interests in human rights, labor rights, and economic development;

[27] Drezner (2003a) argues that, when different groups of states prefer different sets of standards ("rival standards"), NGOs have the greatest opportunity to advance their preferred outcomes.
[28] Among international relations scholars, Strange (1996) was perhaps the strongest proponent of market actors as important players in global governance.

experts not involved on the side of financial institutions; and various other forms of transnational advocacy (e.g. Keck and Sikkink 1998; Reinicke 1999).

Private non-commercial actors also can play a role, particularly in terms of the governance of longer-term foreign direct investment. For instance, rights-oriented organizations often serve as monitors of existing rules, pushing MNCs to meet established standards for working conditions and environmental protection. And NGOs can assist in the development of – or retard the development of, as in the Multilateral Agreement on Investment (MAI) negotiations – rules governing corporate behavior (Haufler 2000, Smythe 2000).[29] In discussing private sector participation in financial regulation, however, I focus on private commercial actors.

Private commercial actors (hereafter, "private actors") could be involved in the development of systems of financial governance, in the enforcement of rules developed by other authorities, or in both processes. There are, then, three main types of private involvement – as autonomous authorities (developing ***and*** enforcing rules); as joint sources of rules (developing rules in concert with governmental authorities); and as enforcers of standards (applying rules developed by other authorities). Each type implies a process that goes beyond state-centric intergovernmental financial institutions.

When private actors serve as autonomous authorities, they both create and enforce rules; states and IGOs delegate – or lose – part or all of their rule-making authority. Mattli's (2003) study of product standards offers an example of partial delegation. He describes a horizontal movement in standard-setting, from the "transnational public" to the "transnational private" sphere.[30] While

[29] For instance, the U.S.-based Fair Labor Association works in conjunction with MNCs to promote certain standards for working conditions in developing countries, particularly in the apparel sector. There has, however, been a good deal of controversy regarding the extent to which the FLA serves the rights of workers or the interests of corporations. An alternative entity, the Workers' Rights Consortium (WRC), founded by United Students Against Sweatshops in 2000, also has garnered support; it has positioned itself as more pro-labor and human rights. Gereffi et al (2001) argue, that such voluntary agreements may help corporations more than they help workers and the environment.

[30] Also see Mattli and Büthe (2003). Cutler (2003) describes a similar phenomenon in the realm of transnational commercial law, as does Farrell (2003) regarding internet privacy standards.

governments remain the ultimate backers of standard-setting, they have delegated substantial authority to private-sector entities, which have greater resources and higher levels of technical expertise.[31] Such efforts also occur domestically; for example, in 1996, in response to concerns about weak national disclosure requirements, the privately owned German stock exchange (Deutsche Börse) created a separate market segment (the Neuer Markt). Companies listed on the Neuer Markt were required to comply with the more stringent International Accounting Standards (IAS). This change increased investor confidence and market size, thereby contributing to efficiency gains (World Bank 2001).[32]

In other cases, the loss or delegation of authority to private actors is greater, and these actors operate independently of public authorities. Accounts of financial globalization that focus on the power of private markets to influence national policies (e.g. "bond market vigilantes") are a key example, although these accounts are sometimes overstated (see Mosley 2003). To take another example, private credit ratings agencies (e.g. Moody's, Standard and Poor's) are in the business of providing assessments of a range of bonds, issued by governments and corporations. Other financial firms purchase these ratings, treating them as authoritative sources[33] of information regarding credit risk. By virtue of their direct influence on the allocation of institutional investment, as well as their indirect influence via use in various domestic and international rules, credit ratings agencies serve as sources of rules (what sort of economic policies and outcomes are appropriate?) and enforcers of rules (what is the market penalty or reward for various economic policies?) regarding creditworthiness.

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[31] Underhill and Zhang (2003), however, point out that technical expertise could work against public regulatory purposes: if only private sector actors have the proprietary knowledge necessary to set rules for financial governance, the ability of public sector agents to monitor the enforcement and the content of these rules will be greatly diminished.

[32] Glaum and Street (2003), however, find that Neuer Markt-listed firms using IAS principles have lower levels of compliance than those using US GAAP principles.

[33] For an argument about why credit ratings agencies should not be treated as authoritative sources, see King and Sinclair (2003).

Similarly, MNCs sometimes act independently to establish rules of behavior; in the face of pressure from consumers and NGOs, a movement toward "corporate social responsibility" has blossomed (OECD 2001). Under this model, firms create or accede to codes of conduct, which set appropriate standards of behavior (and, sometimes, independent mechanisms for measuring attainment of these standards) in areas including collective labor rights, working conditions, and environmental impacts. These codes of conduct offer firms material benefits, in terms of improved reputation in the consumer marketplace (Haufler, 2000), as well as the avoidance of public-sector regulatory efforts. The marketplace benefits are particularly important for firms that produce branded, clearly identifiable products (Bair et al 2002; Haufler 2003).[34]

Joint governance, on the other hand, involves the participation of private agents in concert with governmental authorities.[35] In some instances, private actors take part in the establishment of rules. For instance, private regulators (such as the International Account Standards Board representative) participate alongside governments in the Financial Stability Forum. In other cases, public authorities create rules, but private actors bear primary responsibility for enforcement (Farrell 2003).

Lastly, private actors can serve as enforcers – but not as creators -- of publicly-developed rules. Private actors could be the primary enforcers of rules, or they could provide supplemental enforcement, in addition to that provided by public bodies. The latter is more common, but it also allows for rules to be used in unanticipated ways. For instance, in the EU, the criteria for pre-EMU economic policies (the Maastricht convergence criteria) and post-EMU fiscal policies (the Stability and Growth Pact, SGP) represent yet another combination of public and private sector involvement

[34] Fox et al (2002) argue that the public sector ought to play a greater role in the development of corporate social responsibility-oriented standards but that, thus far, MNCs, consumers, and investors have played the biggest roles in the development of global rules. The set of codes of corporate conduct recently reviewed by the OECD (2001) was comprised mainly of codes from companies (48%) and from associations (37%), with the remainder of codes based in "partnerships of stakeholders" (13%) and IGOs (2%).

[35] On joint – or "hybrid" -- governance, see Cutler 2003, Farrell 2003, Mattli 2003 and Underhill 2000. Underhill describes a situation in which "state authority and the socioeconomic structures of the market are fused in a pattern of global governance which cuts across domestic and international levels of analysis." (p. 22).

in rule-setting and enforcement. Both sets of rules were set by public authorities; again, however, they shared enforcement duties with the private sector. While EU governments could decide to exclude Maastricht violators from membership in EMU, and they may decide collectively to fine violators of the SGP, they also have assumed that private market actors will implement the rules. That is, governments that violate either set of rules (by running large government budget deficits) will be charged higher rates of interest in the government bond market (Mosley 2004).

The degree and type of private sector participation, as described briefly here, is a key determinant of, and an understudied influence on, both the success and the distributional implications of global regulatory efforts. This phenomenon is one that Keohane and Nye acknowledge in the third edition of *Power and Interdependence.* In Chapter 10, they point out that governments and intergovernmental organizations do not have a monopoly on governance; it is undertaken by firms, groups of firms, and NGOs, sometimes acting in concert with governments, and sometimes acting independently of governments (p. 202). Indeed, Keohane and Nye briefly offer a matrix for contemporary global governance, suggesting three levels of authority (supranational, national and subnational) and three genres of authorities (private, governmental, third sector). But, while Keohane and Nye argue for the importance of understanding "new agents in networks," such as transnational corporate associations and NGOs; and while they note the rise of "trisectoral partnerships," involving intergovernmental institutions, private firms, and civil society groups, they do little to explore the effects of these different forms of governance on outcomes (Keohane and Nye 2001, p. 210-213).[36] Moreover, while those in the policy community have examined the need to involve private sector actors in the resolution of crises (e.g. Eichengreen 1999, Kenen 2001), they have paid less attention to the role of private actors in financial regulation generally.

[36] Among international relations scholars, Susan Strange (1996) was perhaps the strongest proponent of market actors as important players in global governance. Farrell (2003) explores the impact of private sector actors on the origins – but not on the impact – of the EU-US agreement regarding internet privacy. Also see Porter 1999, Underhill 2000.

III. The Impact of Private Sector Participation: Two Hypotheses

In recent years, scholarship on the politics of regulation has begun to explore the impact of private sector agents on financial governance. This work often employs a principal-agent framework, focusing on the interaction among legislatures, national regulators, and private interests (e.g. Singer 2004); or on the existence of multiple principals, some private and some public (e.g. Mattli and Büthe 2004). While these approaches hint at the impact of private sector participation on broader regulatory outcomes, they do not explore it fully.

Similarly, literature that explores the accountability of global governance also touches on the role of private agents. If private agents become a more important locus of authority, the legitimacy of global rules may suffer. Keohane notes that, as part of the general rise of a world polity with "disarticulated and fragmented institutions,"[37] private actions can replace public legislation:

> when Nike and Mattel create codes of conduct governing their subcontractors in less developed countries, they may be imposing codes that would not have passed the legislatures of Honduras or India (and which those governments would have opposed at the WTO)." (2002, p. 211).

In this example, MNCs are implementing a set of rules different than those that would have resulted from other processes; these rules are likely to serve the interest of MNCs rather than a broader public interest.

What, then, are the specific implications of private sector involvement for global financial regulation? Does private sector participation have distributional and efficiency consequences and, if so, under what conditions? I posit, first, that global regulations will reflect the self-interest of regulatory decision-makers. And, where private sector actors have greater involvement in the design of financial governance, those systems will reflect more closely the interests of organized finance, as well as of developed nations (e.g. Crouzet and Véron 2002; Simmons 2001):[38]

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[37] Keohane (2002), p. 15
[38] Of course, other private sector actors (such as rights- and development-oriented NGOs) sometimes are involved in creating international rules. For instance, corporate codes of conduct and "corporate social responsibility" efforts

> ***Where private sector actors have greater influence on the design of international regulatory institutions, the institutions will more closely reflect the interests of organized finance, as well as of developed nation (versus developing country) members.* [Hypothesis 1]**

Private sector participation at the design stage should increase the success of regulatory efforts (as in Hypothesis 2 below), but it also will alter the nature of international governance. The linkages between who makes the rules and the character of the rules will influence both equity (in terms of who wins and loses) and efficiency (in terms of how smoothly global capital markets operate). Slaughter (2004) puts this more starkly: "the problem [with private global policy networks], however, is ensuring that these actors uphold the public trust" (p. 9).

If this hypothesis is correct, it presents a conundrum for the international community. Given that private sector actors control a great deal of financial resources, and given that compliance with rules depends on their behavior, it is important to "bail in" these entities (Eichengreen 1999, Knill and Lehmkuhl 2002, Underhill and Zhang 2003). But these actors may have very different views from other affected parties, such as developing countries. Private financial actors often will not act on the basis of public interest, and they are even less accountable to domestic publics than are indirectly-democratic IGOs (Eatwell and Taylor 2002; Underhill and Zhang 2003, Vojta and Uzan 2003). And they will be loathe to sign off on rules that do not serve their interests, as King and Sinclair (2003) suggest has happened with the attempted revisions of the Basel Accords.[39]

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reflect NGO influence (Haufler 2000, OECD 2001). The role of such actors in financial regulation, though, is much less than that of private investors, credit ratings agencies, and MNCs. Slaughter (2004) suggests that transgovernmental networks, which are comprised of national officials with domestic accountability, could be a solution to the problem of unaccountable private actors.

[39] King and Sinclair (2003) argue that private actors do not like the proposed Basel II Accords, because they seem to promise only higher costs and increased competition. Griffith-Jones (2003b) makes a different argument: by not acknowledging the benefits of international portfolio diversification, the accords may "institutionalize the unwillingness of banks to lend to developing countries because it is going to use banks' own risk models to determine the level of capital requirements….As developing countries are perceived as high risk, they will have to pay more." (p. 270). She also argues that the new Basel Accords would amplify the pro-cyclical nature of international capital flows.

Second, global rules often depend on private sector actors for implementation (Eichengreen 1999, Vojta and Uzan 2003) ,[40] and the prospects for private enforcement are linked inextricably to the rule-making process. Where private sector involvement in rule design is greater, we can expect more successful private sector adoption and enforcement of those international rules. I predict that

> ***Implementation and enforcement of international regulatory frameworks will be more successful, all else equal, where private sector involvement in institutional design is greater*** **(Hypothesis 2).**

In other words, when global rules require private enforcement, they also benefit from private involvement in their development (e.g. IMF 2003). The more consistent rules are with private actors' interests and beliefs, the more likely they are to help enforce such rules (Mosley 2003b). Moreover, private actors' technical expertise can be used to improve the sophistication of public regulatory authorities (Knill and Lehmkuhl 2002, Mattli 2003).

Decentralized enforcement via private market activity gives "bite" to international regulatory efforts (e.g. Council on Foreign Relations, 1999). In turn, governments' willingness to subscribe to and comply with such rules depends on the rules' perceived costs and benefits. Benefits of standards flow directly from private markets, as compliant governments receive better treatment than non-compliant ones. Hence, widespread government adoption of the standard requires that market actors respond to the standard, and that governments care about these market reactions. Institutional effectiveness is closely tied to the nature of the standard, and to the subsequent behavior of private market actors (Germain 2001).

At the same time, though, market-based discipline in not always an effective means of enforcement. Where private sector enforcement is aimed at governments, market-based discipline assumes that private markets are efficient, in terms of responses that correspond quite closely to violations. Recent booms and busts in global capital markets suggest otherwise, as does the lack of

[40] On issues of compliance with international law, see Downs, Rocke and Barsoon 1995, Mitchell 1994, and Simmons 2000.

market-based enforcement of the EU's Stability and Growth Pact (Mosley 2004). This problem provides another reason for pause about the Basel II Accords: in some instances, private credit ratings will be used to judge the adequacy of banks' capital reserves. But credit ratings can be pro-cyclical, and ratings are more likely to exist for developed (than for developing) nations, increasing the stringency of regulations on developing country banks. And it is quite possible for governments and banks to "forum shop" in an effort to obtain higher ratings (King and Sinclair 2003).

Moreover, private sector enforcement that involves self-regulation (e.g. national auditing associations following internationally agreed-upon standards), assumes that self-regulation is effective. But recent corporate scandals in the United States and Europe – and subsequent regulatory changes, like Sarbanes-Oxley -- remind us that private actors often have marked incentives to defect from self-regulatory commitments. Moreover, the concentration of technical expertise in the hands of private actors could make it difficult for public sector agents to monitor independently the enforcement of international rules (Underhill and Zhang 2003). Therefore, while there is an argument to be made about the contribution of private actors to compliance and enforcement, there also are reasons to worry that this will not hold in all cases. I return to this issue in the final section of the paper.

Taken together, these hypotheses highlight the effect of the form of governance on distributional outcomes, as well as on their success in implementation (compliance). Table 2 summarizes these hypotheses, as well as the relationships they imply between dependent and independent variables. These conjectures suggest that private sector participation at the design stage should increase the success of regulatory efforts, but it also will alter the distributional nature of the regulatory institution. While the regulation of international finance can provide the public good of global financial stability, it also can provide private benefits to specific groups – for instance, to private commercial actors rather than to national publics, or to developed rather than to developing nations. As such, private sector involvement *could* reinforce, rather than rectify, problems currently

Table 2: Hypotheses

Hypothesis	Independent Variable	Dependent Variable
1 (Distributional hypothesis)	Degree of private sector involvement in rule-making.	• Changes over time in distributional outcomes (across nations) with rule implementation. • Variation (within or between country) in distributional outcomes across rules. • Variation in distributional outcomes between participating and non-participating countries.
2 (Effectiveness hypothesis)	Degree of private sector involvement in rule-making and rule enforcement.	• Level of compliance with or implementation of a given global regulation. • Success of a given regulation in promoting financial stability (controlling for other relevant factors)

associated with providing efficient and equitable global regulation. This is the tri-lemma identified in discussions of contemporary global governance: "we need global rules without centralized power but with government actors who can be held to account…" (Slaughter 2004, p. 10).

IV. Initial Evidence

Evaluating these hypotheses requires the collection of systematic data across a variety of global rules and financial issue areas – for instance, on insurance, banking regulation, and fiscal transparency. Additionally, assessing the distributional effects of regimes (Hypothesis 1) requires either a comparison of effects on developing countries across regulatory sectors (that is, identifying outcomes that are affected by a specific set of rules, but not by other rules), or the comparison of countries that adopt a given set of rules with those that do not. Such evidence would allow us to confirm what we likely expect to be true: private sector actors tend to serve private interests (e.g. Slaughter 2004). These empirical tasks, however, are left for future research. This section reviews briefly broader literature on the success of current financial governance arrangements, and then offers a first-cut empirical assessment of the second hypothesis. I assess Hypothesis 2 using the correlation between global regulatory performance in specific issue areas and the degree of private sector involvement in standard-setting.

Current financial governance and developing nations. Robert Keohane's recent work reflects a concern with the equity implications of globalization: who wins and loses, and what does this imply for globalization's political sustainability? In particular, he points out that there remain great disparities both within and between societies; while these are due to a variety of factors, economic globalism plays a role. Borrowing from Thomas Freidman, Keohane and Nye (2001) observe "the problem is that, in many countries, some citizens get more of the gold while others feel more of the [straight]jacket" (p. 255).[41] Keohane's older work also hints at this issue: for instance, Bergsten, Keohane and Nye (1975) discuss various economic criteria – including efficiency and income distribution within and among societies -- by which to judge international economic systems. In doing so, they hint that tradeoffs may be unavoidable: "It will become apparent both that it may be difficult to achieve any of these objectives and that there may be sharp conflicts between them." (p. 26).

Other studies of the performance of developing nations within the international financial system highlight problems with equity, as well as with efficiency. While these problems often have domestic roots, they also are related to the current governance of international finance. Although none of these studies examine variation in governance *across* financial issues (as a proper assessment of Hypothesis 1 would do), they do suggest financial regulation often falls short. Successful governance of international capital markets should allow capital flows to variety of low- and middle-income nations (at risk-adjusted rates of return),[42] as well as a medium to long-run stability of these

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[41] Econometric analyses of trends in world income inequality reach varied conclusions. In a medium-term perspective, there has been a divergence across countries in income per capita during the last four decades. But over the longer term (from 1820), world inequality among individuals peaked in the mid-twentieth century; world income distribution today is similar to that in 1950. See Bourguignon and Morrison (2002).
[42] The argument is not that developing nations should expect large capital flows at low rates of interest; rather, developing nations should receive a meaningful portion of global investment, at risk-adjusted interest rates.

flows. These capital flows could offer a variety of benefits, including higher rates of growth, poverty alleviation, intertemporal consumption smoothing, greater macroeconomic policy discipline,[43] and stronger domestic financial systems (e.g. Eatwell 1996, Griffith-Jones 2003a, World Bank 2001).

But international financial regulation to date has a mixed record, with some – but far from complete – success in efficiency goals, and little success in equity goals. Various international measures could enhance equity globally (for instance, procedures for orderly workouts of sovereign default, as in Eichengreen 1999; or sharing the costs of crises more evenly between borrowers and lenders), but these mostly remain under discussion. And capital market openness, especially to shorter-term instruments, brings risks, including increased volatility and the abrupt reversals of flows, and well as banking crises (World Bank 2001). These risks stem partly from domestic policy mistakes, but also stem from the general instability of contemporary capital markets (Agenor 2001). There are continued costs, as well as benefits, for financial openness in developing nations.

In terms of benefits, studies of the relationship between capital flows and growth offer a mixed and complicated picture, sometimes finding small or even non-existent effects on growth in developing nations.[44] Global capital flows also are limited in their scope. Foreign investment in developing nations is concentrated in a narrow set of middle-income recipients; many lower-income developing nations continue to receive less capital than an efficient (and risk adjusted) global allocation suggests. In a recent survey, the *Economist* (2003) reported that, at the end of 2001, less than 8 percent of the worldwide stock of cross-border bank loans ($9 trillion total) were directed to developing country borrowers; and developing countries accounting for only $600 billion of the $12

[43] Greater policy discipline may be seen in a negative (restricting autonomy) or a positive (precluding overly-expansionary policies) light. See Mosley 2003a for a review.
[44] For instance, Agenor (2001) reports that portfolio flows have little effect on growth. Durham (2002) finds that stock market development has a positive impact on growth, but that this effect is most pronounced in nations with higher incomes, lower country risk, and greater legal development. In the latter case, capital flows are associated positively with growth where appropriate domestic regulatory structures are in place (also see Griffith-Jones and Cailloux 1999). The mixed pattern also is due to the varying effects of different types of capital flows. Studies that distinguish among portfolio flows, bank lending, and direct investment find that FDI has the greatest positive impact on growth (Agenor 2001; Dobson and Hufbauer 2001; Griffith-Jones and Cailloux 1999).

trillion in global cross-border securities investment. Similarly, during the 1989-2002 period, the top eight recipients of portfolio equity investment accounted for 84 percent of total flows; and the top ten recipients of FDI comprised 70% of developing country direct investment in 2002 (World Bank 2003). While the latter is an improvement (from 79% in 2000), the general pattern persists: China, Mexico, Brazil, South Africa and other middle-income nations may do well at attracting capital, but smaller, poorer nations have much less success.

Capital flows also distributed unevenly on a temporal basis: investment, especially on the shorter-term end, surges when the global economy booms and contracts when global recession looms. Reduced barriers to capital flows mean not only that foreign investors can come and go, but also that domestic capital owners in developing countries also are free to take their assets elsewhere. Investors' views of developing nations often alternate between manias, in which all developing nations are able to attract large amounts of investment, and panics, in which even the most stable developing nation has difficult accessing global capital markets (e.g. Griffith-Jones and Cailloux 1999, IIF 2004, Mosley 2003a). While some of the movements of investment in and out of developing nations are pro-cyclical responses to local conditions ("pull factors;" e.g. Agenor 2001), many others are the result of global economic trends and market sentiment ("push factors"), which are far beyond the control of emerging economies.

The volatility that characterizes international capital markets reduces the benefits of liberalization. While financial globalization offers developing countries greater access to resources and higher levels of growth, it also brings with it a higher likelihood of crisis. Conceição (2003) reports that between 1975 and 1998, there were 116 currency crises, 42 banking crises, and 26 twin (banking and currency) crises in emerging market countries. These crises were associated with cumulative output losses between 5 and 19 percent of annual GDP. Similarly, Dobson and Hufbauer (2001) estimate that banking and financial crisis cost Latin America 2.2% of annual GDP during the 1980s, and cost East Asia 1.4% of annual GDP during the 1990s. More generally, several recent studies hint at a strong, negative relationship between financial volatility and economic growth (Griffith-Jones 2003b). And, as the East Asian crisis demonstrated, it is the poor – who lack social safety nets and personal savings – who often bear the brunt of financial crises and post-crisis contractions.[45] Furthermore, the benefits of capital flows likely are distributed unevenly within societies, just as they are distributed unevenly at the global level.

The uneven distribution of international investment, as well as the lack of a strong relationship between financial liberalization and growth, suggests that international regulation has yet to provide fully the public goods of financial stability and market efficiency. Regulatory features are not the only cause of the global capital market deficiencies (e.g. Sundararajan et al 2001), of course, but they do play a role.[46] In some substantive areas, such as FDI, there is simply little global regulation. In other cases, the problem is the structure of current regulatory regimes. For example, while the Bretton Woods financial institutions might promote the efficient allocation of capital, recent studies suggest that their actions often are conditioned by political -- rather than economic -- factors, and that IMF programs are associated – even once selection effects are considered – with lower rates of economic growth (Stone 2002, Vreeland 2003). And in still other cases, the problem is one of compliance with regulatory frameworks. For instance, between the late 1980s and the late 1990s, many nations adopted minimum capital requirements for domestic banks; these often met and sometimes exceeded the 8 percent mandated by the first Basel Accords. But problems with enforcement remained: developing nations could easily announce the existence of a capital adequacy standard, but actual implementation lagged behind (World Bank 2001; also see IMF 2000). It is this phenomenon, perhaps, which gives rise to efforts to introduce a greater private sector monitoring role

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[45] For a stronger view of the costs to developing countries, see Eatwell (1996). He argues that the benefits of financial liberalization generally accrue to developed nations and that borrowers pay higher real interest rates. "None of the five benefits [of liberalization] appear to have been substantially realized, and in many cases the liberalization of international financial markets has been associated with a sharp deterioration in economic performance." (p. 25)

[46] For instance, Sundararajan et al (2001) find little evidence of a direct relationship between compliance with international regulations (the Basel Core Principles) and bank performance in developing nations.

in Basel II; this also hints at the potential relationship – as in Hypothesis 2 – between the private sector and compliance.

Private sector participation and regulatory compliance. One of the implications of Hypothesis 2 is that areas of global financial governance with greater private sector involvement also will demonstrate higher levels of compliance. In this analysis, the independent variable is the degree to which private actors participate in the development and enforcement [or simply in the enforcement] of rules. Table 3 classifies various international financial rules according to their enforcement and establishment. For each dimension, rules are classified into three broad categories -- fully public, to shared public and private, to fully private. The table includes the nine areas used in the empirical assessment below (in bold), plus several others.

The upper left area of the table indicates traditional, state-centric rules, which are both established and enforced by public actors (states and IGOs). For instance, the Financial Action Task Force's (FATF) rules on money laundering were created by states, initially G-7 countries, and now a broader set of members. Although there are some private market pressures for financial centers to "know their lenders," the major impetus for compliance with the FATF's Forty Recommendations comes from powerful states (Simmons 2001). The lower right area, by contrast, highlights the contemporary trend toward private sector involvement, in which various private actors create and implement standards. For instance, corporate codes of conduct are created and enforced by MNCs, with some additional enforcement pressures from labor or environmental NGOs. Similarly, for the anti-sweatshop movement, a majority of rule setting, and almost all of the enforcement, occurs in the private sphere. ILO conventions help to suggest norms of corporate behavior, but these are propagated by rights-oriented NGOs, which sometimes work in partnership with MNCs. Similarly, as discussed above, private credit ratings agencies develop standards regarding appropriate economic policies; by relying on these ratings for asset allocation decisions, private investors serve to enforce these standards.[47]

Table 3: The Public-Private Continuum in International Finance

	Enforcement		
Establishment	**Public**	**Public-Private**	**Private**
Public	**·Money laundering (FATF)** ·Debt Rescheduling (Paris Club)	**·Data Dissemination (IMF SDDS)** ·EMU Convergence Criteria, Stability and Growth Pact	·Bank supervision (Basel II, agreed 2004; implementation in the future)
Public-Private	**·Financial Stability Forum's 12 key standards (Fiscal transparency; monetary transparency; payment and settlement systems; insolvency)**[48] ·ICSID arbitration	**·Bank supervision (Basel Committee capital adequacy rules, 1988-2004)**[49] **·Corporate governance (OECD)** **·Securities regulation (IOSCO)** **·Insurance Supervision (IAIS)** ·Structural adjustment programs (IMF) ·Global anti-corruption movement[50]	·Anti-sweatshop movement
Private	·Financial Reporting Rules in the EU (using IASB rules)	**·Accounting rules (IASB)** **·Auditing rules (IAASB)** ·International Chamber of Commerce	·Credit Ratings ·Corporate codes of conduct

Efforts to develop global accounting and auditing standards also are centered on the private sector, albeit with shared public-private enforcement. The International Accounting Standards Board (IASB) operates independently of governments and is funded through donations from accounting firms, stock exchanges, and underwriters. The IASB sets International Accounting Standards (it has

[47] One also could note that these credit ratings sometimes are used by public actors; for instance, the revised Basel Accords proposed to use them as a guide to the risk profile of banks' assets. Their main use, though, remains within the private sector.
[48] Not all twelve of the FSF's twelve key standards would be classified in this cell, however. For instance, the FATF efforts at money laundering are more public sector-based; and accounting and securities regulations are more private-sector based.
[49] Note the contrast, below, between Basel I (1988) and Basel II (2004).
[50] On the global anti-corruption movement, see Sandholtz and Gray 2003.

promulgated approximately 40 IFRS – formerly known as IAS -- thus far). The IASB's board members are drawn from national accounting boards, the private accounting sector, or accounting consortia in nine nations. In its efforts to bring about the convergence of national accounting standards toward a single model, however, the IASB sometimes relies on public sector actors. Where the IASB and the US Financial Accounting Standards Board have agreed on common standards,[51] for example, the US Securities and Exchange Commission helps to enforce those rules (via its control of access to listing on stock exchanges, and its recognition of FASB standards as authoritative).[52] The IASB standards also have been endorsed by IOSCO, the IMF, and the UN. Similarly, the International Auditing and Assurance Standards Board (IAASB), an arm of the International Federation of Accountants (IFAC) works to develop and promulgate a set of global "best practice" standards for auditing and related matters. IFAC's members are national auditors' associations, and IFAC urges its members to incorporate global standards into their codes of behavior and to pressure national regulators to adopt these global standards. As in the accounting sphere, there are hints of public sector involvement in enforcement, as national regulatory authorities become increasingly interested in auditing practices (witness, for instance, the U.S. Sarbanes-Oxley legislation), and as IFAC seeks to preserve the reputation of the auditing profession in light of recent corporate scandals.[53]

Another example that combines private rule establishment with mixed enforcement mechanisms is the International Chamber of Commerce (ICC). The ICC began to create various systems of international commercial arbitration in the 1920s, filling gaps where public sector

[51] The IASB and the FASB formally agreed, in September 2002, to work toward the convergence of the IASB's IAS and the US Generally Accepted Accounting Procedures. Crouzet and Véron 2002, however, note that many large US firms lobbied against adopting IASB principles, as they worried about declining influence over accounting rules. Similarly, European banking institutions intensely opposed the EU's adoption of IASB rules on the treatment of derivatives ("fair value" accounting), and it is likely that the standards will be applied differently in different member states (*Economist*, October 21, 2004).
[52] On problems of enforcement of accounting standards, see Quinn 2004.
[53] In April 2004, IFAC announced that it was tightening its membership criteria; members would be required to "use their best endeavors" to incorporate global standards into national practice, and to encourage their home governments to do likewise.

regulation was weak or non-existent (Ronit and Schneider 2000). By its own account, the ICC took the lead in establishing worldwide acceptance of arbitration as the best means of solving international commercial disputes. The ICC has administered over 12,000 arbitration cases (involving parties from over 170 states and territories) since its founding, and it continues to create new measures in international trade and business law. For instance, it now sets codes of conduct in the realm of advertising (Cutler 2003). While the ICC's standards are enforced mainly in the private sector, IGOs also have welcomed their standards.[54]

Intermediate areas of Table 3 reflect instances of joint governance; many contemporary instruments of financial governance fall into these cells. To take an example, IMF staff negotiates the terms of structural adjustment programs, and these are approved by the Executive Directors, acting as agents of member governments. By tying the disbursement of funds to the fulfillment of conditionality, the IMF also enforces these programs. But, on both dimensions, the IMF draws significantly from the private sector: the Fund's ideas of appropriate adjustment polices are tied very closely to those of the private financial sector (e.g. Gould 2003). And if the IMF is an effective signal to private investors, non-compliance with IMF programs can result not only in the suspension of IMF financing, but also in the reduction of private capital flows.

The Basel Committee's rules on capital adequacy for banks (banking supervision) also involve a mixture of public and private. The 1988 Accords (Basel I) were created largely in the public sphere, with strong influence from the US and UK, as well as from G-10 central bankers generally (Kapstein 1992). In revising the accords (Basel II, 2004), however, there was greater private sector involvement, including several rounds of consultation with private banks and other financial market participants. The Basel Accords rely primarily on national banking regulators (again, in the public sphere) to enforce the standards;[55] the Accords are strengthened by the fact that

[54] See Ronit and Schneider (2000) for a detailed account of the development and functions of the ICC.
[55] In most cases, national governments give regulators the statutory authority to enforce Basel's provisions.

international financial institutions often consider them as part of their overall assessments of country creditworthiness and performance. On this dimension as well, Basel II relies more heavily on private sector actors (through direct market discipline, or “Pillar 3”) for enforcement.

Securities regulation also reflects a mixture of public and private governance. The International Organization of Securities Commissions (IOSCO), the chief global regulatory body in this area, is comprised primarily of representatives of national financial services regulatory agencies (e.g. the US Securities and Exchange Commission). IOSCO grew out of a US-backed effort at international regulatory cooperation in the Western hemisphere; in 1984, the organization reorganized into a more globally-oriented body. IOSCO has published a set of benchmarks for securities regulation (IOSCO Principles, 1998); encouraged international information sharing (via its 2002 Memorandum of Understanding); and most recently (October 2003) has launched an effort to assess national compliance with its principles. In each of these efforts, IOSCO acts mostly as public sector entity. But IOSCO’s Self-Regulatory Organization Consultative Committee is comprised of private sector securities market and investment associations. Additionally, many scholars have suggested that – given their need for technical expertise and their professional backgrounds – securities regulators are not completely independent of the private financial sector (Underhill 1995).

Moreover, insurance supervision and corporate governance also mix public and private sector involvement. The International Association of Insurance Supervisors is comprised of national supervisory authorities, with insurance professionals, financial institutions, and insurance companies as observers. It has little direct enforcement capacity, but relies on the actions of national regulators, as well as on pressures from private markets and international financial institutions (the IMF). The OECD’s Principles of Corporate Governance were created by developed nation governments (at the OECD), but in consultation with a variety of civil society groups, professional organizations, and private standard-setting bodies. And their enforcement relies less on the direct exercise of power than on the diffusion of corporate governance principles to national (OECD and emerging market) regulatory authorities[56] and international financial institutions, as well as on ideational change, via policymakers' adoption of "best practices."

In a slightly different vein, the Financial Stability Forum developed its list of key standards for international finance as a private-public consortium. There is variation across the dozen standards in terms of their classification.[57] Table 3 classifies five of these standards as public-private in establishment, but almost entirely public in enforcement – insolvency; transparency in fiscal and monetary policymaking; and payment and settlement systems, of central banks and in the financial system generally.[58] The transparency standards were developed largely by the IMF; G-10 central banks (the BIS' Committee on Payments and Settlements Systems) created the settlement standards; and the World Bank took the lead on developing insolvency rules. In 2000, these twelve key standards (and only those twelve standards) were, at the urging of the G-7, incorporated the IMF and World Bank's regular member surveillance, providing the main means of enforcement (Drezner 2003b; Sundararajan et al 2001).[59] And in a few recent cases, the IMF has included information from its routine surveillance in standby arrangements. Other organizations also work to implement these standards, including UNCITRAL (a UN entity), the International Bar Association, and the Group of 36 (an association of law and accounting firms) in the insolvency area. To take another example, the arbitration of investment disputes by the International Center for the Settlement of Investment Disputes (ICSID) reflect a similar combination of private-public establishment with public enforcement.[60]

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[56] The OECD's Principles are non-binding: "The legislation needed to enforce these standards is the responsibility of individual governments." ["Frequently Asked Questions about the OECD Principles of Corporate Governance;" http://www.oecd.org/faq/]

[57] Note, however, that some of the other standards discussed in this section, and placed elsewhere in Table 2 (e.g. accounting rules, corporate governance principles) are included in the FSF's set of twelve key standards.

[58] Payment and settlement systems aim to ensure the clearing of markets with respect to financial transactions; these systems are the "plumbing" that facilitates national and international financial transactions.

[59] Schneider (2003) discusses some of the problems with the IMF's Reports on the Observation of Standards and Codes (ROSCs), which are a key part of recent surveillance efforts.

[60] The EU-US Safe Harbor arrangement also would fit, according to Farrell's account, in this cell.

A different combination of private-public governance is represented by recent changes to financial reporting rules in the European Union. A 2000 report from the European Commission, plus subsequent legislation, requires companies domiciled and listed in the EU to prepare their financial statements according to International Accounting Standards, beginning in 2005.[61] The use of single standards should facilitate the creation of a single European financial market, and should help to improve investor protection within the EU. At the same time, however, this represents a reliance on private sector rules.[62] Some European governments have expressed concerns about the decline in influence of public standard-setting bodies;[63] the European Commission has promised to consult regularly with the IASB. The EU's involvement also may help to address potential enforcement problems with accounting standards (Quinn 2004).

The final "mixed" type is that of data dissemination (as well as EU fiscal policy, discussed in Section II above). The IMF's Special Data Dissemination Standard (SDDS), which encourages national governments to provide high-quality economic data in a timely fashion, also was established publicly, but relies partially on the private sector for enforcement. Investors, however, have been slow to embrace the IMF-sponsored data dissemination regime (Mosley 2003b).[64] As a result, the SDDS lacks a credible enforcement mechanism, and many governments have been slow to adopt the standard.

Table 3 provides some sense of the variation in nature of international financial regulation, in terms of the role of private actors. In order to assess Hypothesis 2 -- the implementation of global rules varies with their degree of private sector participation – I measure the dependent variable

[61] Following objections from various European governments and firms, this requirement has been modified; adoption of international accounting standards is mandatory only for listed entities that prepare consolidated financial statements.
[62] Mattli and Büthe (2003) offer a similar account of the establishment of product standards: these rules sometimes (but not always) are adopted by national governments and are often included in trade agreements, but they are set almost entirely by private sector bodies.
[63] This paragraph draws on Deutsche Bank Research 2003.
[64] Schneider (2003) reports similar findings: once economic factors (e.g. growth, public debt, debt service) are controlled for, subscription to the SDDS has little, if any, impact on interest rate spreads.

(effectiveness, or compliance) using data taken E-standards Forum.[65] E-standards Forum is a private sector, subscription-based effort to monitor compliance with various standards, and to provide cross-country data to market participants.[66] E-standards attempts to provide summary indicators of compliance; like any one-dimensional measure, its scores can overlook the complexity of regulatory efforts (e.g. Schneider 2003). But the measures are useful as a means of comparing macro-level performance across financial standards, and as a tool for first-cut analysis.

E-standards Forum currently provides assessments of compliance with thirteen global standards,[67] including many of those listed in Table 3. These data are available for between 35 and 83 nations, depending on the standard. The data are provided on a current, but not historical, basis; data reported here were collected in August 2004. Data are provided for all OECD nations, as well as for some developing and transition (here, "emerging market") nations. The developing and transition economies included are those with some participation in international capital markets – central and eastern Europe, Latin America, and Asia, mostly. E-standards Forum assessments are on a 5 point scale, including "no compliance,", "intent declared," "enacted," "compliance in progress," and "full compliance." I assign ordinal scores to these categories, ranging from zero for no compliance to four for full compliance.

Figure 1 provides information on the average levels of compliance with various global standards, for OECD, emerging market, and all nations. Higher scores represent greater compliance. The charts are arranged with more "public" standards on the left side, and more "private" ones on the right. For this figure, the enforcement and establishment dimensions of Table 3 are collapsed. Governance arrangements are considered mostly public (money laundering, fiscal transparency, monetary transparency, payments and insolvency), mixed public-private (data dissemination,

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[65] Compliance could also be assessed using reports (ROSCs) from the IMF-World Bank Financial Sector Assessment Program, http://www.imf.org/external/np/fsap/fsap.asp#o

[66] See www.estandardsforum.com; for a discussion of other private sector efforts, see IMF 2003, pp. 29-30.

[67] The Financial Stability Forum has 12 key standards; EStandards Forum separates one of these standards – payment systems – into general principles of payments systems and central bank payments systems.

corporate governance, bank supervision, securities regulation, and insurance supervision), and mostly private (accounting and auditing).

Insert Figure 1 here.

As we would expect, compliance levels are highest among OECD countries; these countries are both more involved in rule-making and in possession of greater technical resources. And in most cases, there is greater variation among emerging market than among OECD outcomes.[68] In both the overall and the emerging markets samples, compliance is highest with rules regarding monetary policymaking transparency, money laundering, payment systems (principles), and banking supervision. The average compliance score for these measures ranges from 1.8 (payments in emerging markets) to 2.6 (monetary policy transparency in the entire sample), on a four point scale. Money laundering and monetary transparency were publicly-created rules, and one could argue that the pressure from powerful countries (in the case of the FATF), as well as from the IMF (in the case of monetary policymaking) motivates this compliance. Global banking regulations are based on a combination of public and private sector activity (the latter more for Basel II than for Basel I); as such, relatively high compliance with those rules provides modest support for Hypothesis 2. Interestingly, the difference in average compliance levels between emerging market and developed countries is much smaller for banking supervision (2.5 for OECD nations; 1.95 for emerging markets) than for money laundering (3.18 and 1.72, respectively) and monetary transparency (3.67 and 2.05).

The next set of standards, in terms of compliance outcomes, includes fiscal transparency (overall compliance level of 1.98), data dissemination (1.94 overall), central bank payments systems (1.89), securities regulation (1.82), and insurance supervision (1.86). Again, there is some variation in the extent to which OECD performance exceeds that in emerging markets, with the most

[68] For eight of the thirteen standards, the standard deviation of compliance scores is higher in emerging markets than in OECD nations. For the remaining cases, variance is larger in OECD nations. For banking supervision, OECD variance is markedly greater.

pronounced differences existing for securities regulation and fiscal transparency. What do these outcomes tell us about the impact of private sector participation on regulatory performance? The answer is mixed: fiscal transparency, data dissemination and payments rules were established largely in the public sphere, while securities regulation and insurance supervision reflect a mix of public and private rule-making. Despite these differences, their compliance levels are relatively similar, suggesting (not surprisingly) that other factors are at play. For instance, the fact that emerging markets comply at higher rates with data dissemination and fiscal transparency rules might suggest that IMF and World Bank influence plays an important role.

The weakest standards, in terms of the compliance rates reported in Figure 1, are auditing (1.75 average, overall), corporate governance (1.49), insolvency (1.45) and accounting (0.56). Compliance with corporate governance rules is higher in the OECD (a mean of 1.9), but sits between "intent declared" and "enacted") for the entire set of nations. A similar pattern holds for insolvency, where OECD nations comply at a slightly higher rate (1.71, compared to 1.46 in emerging markets). Insolvency rules were established at the public-private nexus, as were corporate governance rules; corporate governance rules rely more on mixed enforcement. But, in both cases, it may be true – but this is very tentative -- that greater private sector participation could generate greater pressures for compliance.

Auditing and accounting, on the other hand, were established almost entirely in the private sector and rely on mixed (but more private) enforcement. Levels of compliance with auditing rules (1.81 in OECD nations, 1.71 in emerging markets) are comparable to some of the publicly-enforced rules, suggesting that, at the very least, private sector enforcement might not detract from implementation. Levels of compliance with accounting rules, however, are markedly low for both sets of countries. Accounting rules have a compliance level of just 0.56, on average.[69] This directly

[69] Estandards Forum's assessments of international accounting standards were updated in November 2004, to reflect the IASB's recent revisions to International Accounting Standards. The figures included these revisions, which

contradicts Hypothesis 2: here, rule making is entirely based in the private sector, yet compliance is very low.

This suggests that standards that are housed entirely in the private domain (that is, with private establishment and largely private enforcement) may lack regulatory "teeth." While some private sector participation may encourage investors to later use standards as part of their decision-making criteria, a complete reliance on private actors may go too far. For accounting and auditing, private actors engage mostly in self-regulating (enforcing standards on themselves) rather than in regulating others (using market discipline to reward or punish governments). These could be cases in which self-regulation fails to provide appropriate incentives for compliance.

It also could be a case in which, unless standards also are embraced by public sector bodies – for instance, by stock market regulators – there are few incentives for developed or developing nations to expend the resources required for compliance. The results for accounting do, in fact, fit with recent work that questions the extent to which the IASB's rules are enforceable (e.g. Crouzet and Véron 2002, Glaum and Street 2003). In their study of compliance by companies listed on the German Neuer Markt, Glaum and Street find substantially lower levels of compliance with IASB rules than with US GAAP – perhaps reflecting the IASB's lack of regulatory bite. The low levels of compliance also could reflect recent EU-US tensions regarding the delineation of appropriate accounting standards.

Interestingly, the "low compliance" set of standards – corporate governance, accounting, auditing and insolvency – also are those for which the World Bank is charged with overseeing, via the IMF/World Bank Reports on Standards and Codes (ROSCs), which are voluntary (and occasional) assessments of members' policies. The IMF is responsible for surveying the other eight key standards. As of 2003, however, only twelve percent of completed ROSCs concerned the World

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resulted in a lowering of assessments of compliance, from an average level of 1.10 (still the lowest implementation rate among the 13 standards) to an average of 0.56.

Bank's four standards of interest. Perhaps, then, indirect market pressures – in which private actors respond to public reports on implementation – operate more strongly for IMF-surveyed than for World Bank-monitored standards.

Figure 2 presents the same data, but aligns them according only to the establishment – and not to the enforcement – of the rule. Of the thirteen standards, two are publicly established (money laundering and data dissemination); two are privately established (accounting and auditing); and the remainder are established in some sort of joint process. This figure provides a more direct assessment of Hypothesis 2, although there is little systematic variation across categories. The broad "joint establishment" category, for instance, includes instance of relatively low (insolvency) and relatively higher (monetary transparency, payments principles) compliance. Unpacking the variation within "joint establishment" will be central to future work on the impact of private sector participation on implementation.

Insert Figure 2 here.

This brief empirical analysis is very preliminary, but it raises important issues. First, are private actors appropriate enforcers of standards? Do private investors, for example, prioritize the same substantive areas and promote the same rules that international financial institutions or national governments do? (e.g. Kenen 2001, Mosley 2003b, Schneider 2003). Or, given the potential problems with self-regulation, might hybrid systems (private enforcement, but accompanied or backstopped by public enforcement) be best (see Farrell 2003)? Second, are all forms of private sector participation equal? It may be the case that, while some types of private involvement promote compliance, other types detract from it. As suggested above, it may matter if the private sector engages in self-regulation (enforcing rules on itself) versus in enforcement against other private actors or against national governments.[70]

[70] Cutler et al 1999 differentiate between these two types of private sector involvement.

Third, why are developed nations substantially more compliant than emerging markets (as we might expect) in some cases, but only marginally more compliant than others? If international financial institutions or private investors press governments to comply, these pressures should be greatest on developing countries. At the same time, though, these pressures could vary across substantive issues, and they could be offset by domestic political and technical capacity issues. Furthermore, what are the linkages among various financial standards? Standards may not operate independently of one another. For instance, a country that is responsive to IMF pressure regarding fiscal transparency practices may be more likely also to change its data dissemination procedures. Perhaps, then, there are not many separate standards (as Tables 1 and 3 suggest), but a smaller set of "regime complexes" or "networks of networks" in global finance (Raustiala and Victor 2004, Slaughter 2004).[71]

Finally, how does the "private actor participation" variable interact with other causal influences to produce regulatory outcomes? Recent literature on compliance has identified several important factors, and these should be integrated into future analyses (Simmons 2000). For instance, when international rules mesh with domestic laws and institutions, they are more likely to be effective (Pistor 2000; Underhill and Zhang 2003);[72] but a one-size-fits-all approach that seeks to implement identical global standards in all developing countries is unlikely to succeed. Unfortunately, many recent reforms have been implemented in isolation, or without consideration of sequencing issues (see Sundararajan et al 2001). And particularly in developing nations, successful implementation often requires national capacity-building, which is often missing from contemporary efforts at global governance.

[71] Factor analysis on the E-standards data, however, suggests at least five clusters of standards.
[72] This "capacity" argument suggests that Hypothesis 2 is more likely to hold in developed nations, where technical capacity is greater.

V. Conclusion

The successful governance of international finance could improve the overall allocation of investment, prevent financial crises, lower transaction costs, and promote a more equitable distribution of resources. But financial regulation often falls short. Investment often does not flow to where it is most needed, and financial crises are a recurring feature of the contemporary global economy. Moreover, the rules that exist tend to be biased toward developed nations and private financial actors in terms of their assignments of rights and benefits. I have argued that the forum in which rules are set – public versus private, as well as clubs vs. universes –affects the nature of the rules themselves. I maintain that, while understudied, private sector participation has important implications for the effects, and effectiveness, of global financial rules. Private sector involvement in rule-setting can help to increase compliance with regulations, but that it also will change the distributive nature of global governance. As a result, gains in efficiency could be offset by reductions in equity.

Of course, there are many models of private-public involvement in financial regulation, and each permutation differs in its implications for equity and efficiency. The consequences for global cooperation of new and varied forms of rule-setting may be far-reaching, but our understanding of these consequences is, thus far, limited. The challenge is not only to improve the governance of international finance, but also to determine the most appropriate means of doing so. The paper offers a preliminary empirical assessment of the "effectiveness" component of this argument; the reported evidence, though, is quite weak. There is, however, fruitful empirical ground to be covered, in terms of exploring more systematically the implications of private sector participation for the quality of global governance, and in terms of looking at a wider set of governance regimes in finance – including corporate codes of conduct and sovereign credit ratings -- than those analyze in Section IV.

Exploring the impact of the private sector on financial governance outcomes also returns us to the issue of accountability. How can we involve the private sector in governance (increasing efficiency) without deleterious effects on equity? Are certain forms of private sector involvement compatible with private incentives for compliance, and yet not too skewed toward private interests? Slaughter suggests that transgovernmental policy networks may be, as more accountable counterweights to private networks, the solution to this quandary. They could act "as the spine of broader policy networks, including intergovernmental organizations, NGOs, corporations, and other interested actors, thereby guaranteeing wider participation in government network activities but also retaining an accountable core of government officials" (pp. 28-29). This is an optimistic claim, but one that would fit squarely with Keohane's longstanding focus on transnational actors, and with his more recent concerns about accountability and equity. The empirical challenge, then, is to delve deeper into the causal effect of both private and transgovernmental governance.

Figure 1: Compliance with International Standards

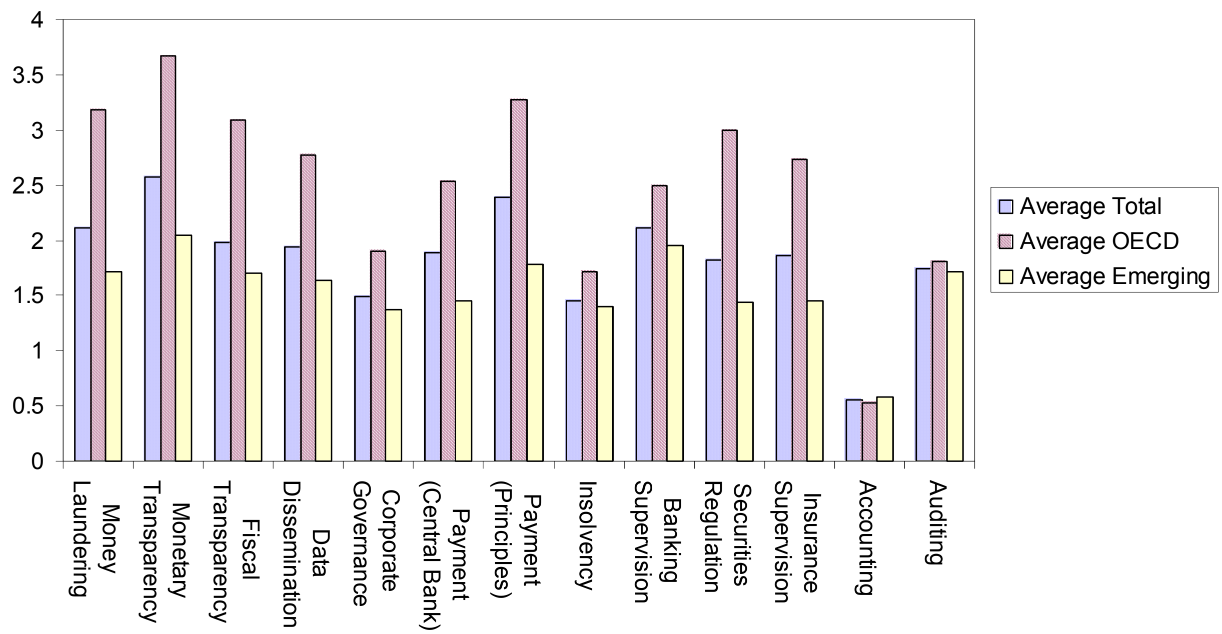
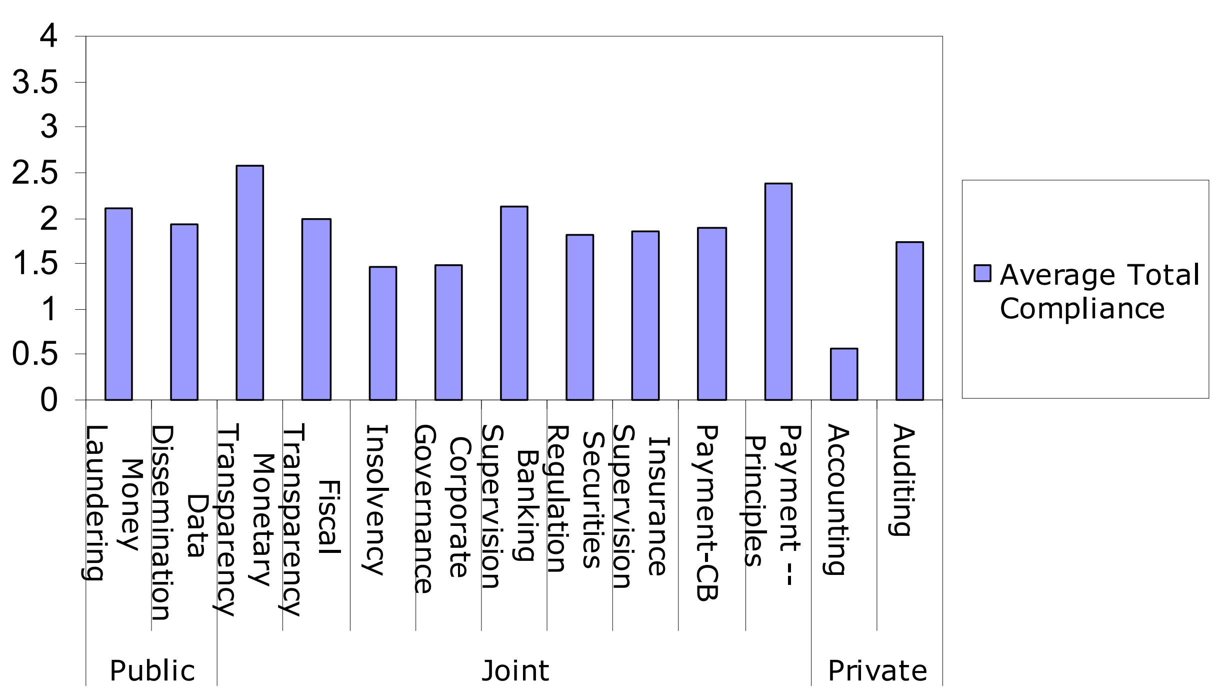


Figure 2: Compliance and Rule Establishment



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