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The President and International Financial Regulation

David Zaring

THE PRESIDENT AND INTERNATIONAL FINANCIAL REGULATION

David Zaring[*]

The president's powers in foreign relations have long been touted as strong, but for international financial regulation, they are at their lowest ebb. Congress does not defer in it. The domestic agencies involved, in particular the Federal Reserve, are independent, and in this way less easy for the president to influence. And the international process, featuring technocratic collaboration by bureaucrats, is also not amenable to dispositive presidential supervision. The good news for the president, however, is that the perceived need for political oversight of international financial regulation has led to a new role for the G-20, of which he is an influential member. It is not authoritative command, but it may afford him more of a role in a process that, until the financial crisis, proceeded without much presidential input.

The president's role in setting foreign policy is usually regarded as commanding, but in international economic law presidential authority is, if anything, at its lowest ebb.[1] Rather than enjoying the authority to act alone presumed by cases such as *United States v. Curtiss-Wright Export Corp.*,[2] the president's power-sharing role in economic relations is constitutionally constrained, as well as structurally encouraged. This short essay explains the reasons for the reduced executive role and identifies one route to more influence that is developing in the field—increased oversight of international financial regulation by the G-20, an informal grouping of heads of state of which the president is a member.

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1. Justice Jackson defined the "lowest ebb" as "[w]hen the President takes measures incompatible with the expressed or implied will of Congress . . . for then he can rely only upon his own constitutional powers minus any constitutional powers of Congress over the matter." Youngstown Sheet & Tube Co. v. Sawyer, 343 U.S. 579, 637 (1952) (Jackson, J., concurring).

2. *See* United States v. Curtiss-Wright Export Corp., 299 U.S. 304, 320 (1936) ("[I]f, in the maintenance of our international relations, embarrassment . . . is to be avoided and success for our aims achieved, congressional legislation . . . must often accord to the President a degree of discretion and freedom . . . which would not be admissible were domestic affairs alone involved.").

While often the Constitution has been used to justify broad, almost plenary authority in foreign affairs, it does not afford the president as much comfort in any kind of economic regulation. Instead, the Constitution gives Congress the express power "to regulate Commerce with foreign Nations."[3] In international economic law, Congress has used that power vigorously, passing laws establishing tariff rates, implementing trade agreements, and even creating some barriers to trade, such as the trade in "critical infrastructure" that implicates national security.[4] When Congress has delegated some of its authority to set trade policy to the president, it has often limited its delegations through regular use of the sunset clause.[5]

In the critical arena of finance, and the supervision of it, the president's power is even more limited, even though, as the last financial crisis has made clear, finance is critical to the country's prosperity (and also to the president's job prospects). The legal limitations requiring the president to share economic lawmaking power are paired with a number of structural impediments to the exercise of any additional power by him.

One such impediment lies in the president's authority over his own financial bureaucracy. American policy in international financial regulation has traditionally been set not by the President and his delegates in the State Department, but largely by independent agencies, including the Federal Reserve (perhaps the most independent of all government agencies), the Securities and Exchange Commission, and the Commodity Futures Trading Commission.[6] These agencies are led by multi-member boards, whose members are subject to Senate confirmation, and, once confirmed, cannot be

3. U.S. CONST. art. 1, § 8, cl.3.

4. *See generally* David Zaring, *CFIUS as a Congressional Notification Service*, 83 S. CAL. L. REV. 81 (2009) (explaining how Congress has inserted itself into foreign policy through extensive oversight of the Committee on Foreign Investment in the United States, an executive branch organization).

5. For discussions of the merits of sunset clauses, see Roberta Romano, *Regulating in the Dark* 14–25 (Yale Law Sch., Nat'l Bureau of Econ. Research & Eur. Corp. Governance Inst., Paper No. 442, 2011), *available at* http://ssrn.com/abstract=1974148. For a critique, see John C. Coffee, Jr., *The Political Economy of Dodd-Frank: Why Financial Reform Tends to Be Frustrated and Systemic Risk Perpetuated*, 97 CORNELL L. REV. 1019, 1033–37 (2012).

6. The Treasury Department, which certainly does enjoy presidential oversight, also plays a critical role. *See* David Zaring, *Administration by Treasury*, 95 MINN. L. REV. 187, 187 (2010) ("The Treasury Department pulled out all the stops during the beginning and middle of the financial crisis, and toward the end, when Congress got involved, its efforts got even more dramatic.").

removed by the president without cause.[7] They do not report to the Office of Management and Budget, and therefore do not have to coordinate their regulatory agendas with White House priorities.[8]

It is also difficult for the executive branch, even apart from these domestic impediments, to affect the increasingly international process that now characterizes the most important portions of financial regulation. The amount of capital banks must hold in reserve to deal with emergencies or shocks, for example, is not set by the president or even by the independent agencies that, if not under his supervision, are at least located in his jurisdiction.[9] Instead, capital adequacy requirements have been set through an increasingly international process in which American agencies participate, but do not control. It is the so-called Basel Committee on Banking Supervision (Basel Committee) making those rules, rather than the Federal Reserve and the Treasury Department.[10] American regulators, including the presidentially responsive Treasury Department, can affect the rules as participants in the Basel Committee process.[11] But the president far from controls it, as he does not control the Federal Reserve or the Securities and Exchange Commission, let alone their interactions with foreign financial regulators, out of which the Basel rules are forged. The Basel Committee has come up with three iterations of its capital adequacy rules;[12] the first two were never endorsed by the president.

Further, the president, and all participants in the emerging world of international financial law are increasingly constrained by some

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7. *See* Humphrey's Executor v. United States, 295 U.S. 602, 621 (1935) (preventing presidents from removing the heads of independent agencies without a showing of cause).

8. As Josh Wright has observed, "[p]residents have traditionally declined to exercise authority, through the OMB, over independent agencies." Joshua D. Wright, *The Antitrust/Consumer Protection Paradox: Two Policies at War with Each Other*, 121 YALE L.J. 2216, 2268 n.195 (2012).

9. *See* David Zaring, *Finding Legal Principle in Global Financial Regulation*, 52 VA. J. INT'L L. 683, 696–97 (2012) (discussing the development of the Basel Capital Accord, which is designed to ensure banks are adequately capitalized) [hereinafter Zaring, *Finding Legal Principle in Global Financial Regulation*]; David Zaring, *Rulemaking and Adjudication in International Law,* 46 COLUM. J. TRANSNAT'L L. 563, 580–85 (2008) (analyzing the Basel Accord as a strong example of international rulemaking); *see generally International Regulatory Framework for Banks (Basel III)*, BANK FOR INT'L SETTLEMENTS, http://www.bis.org/bcbs/basel3.htm (last visited Dec. 18, 2012).

10. *See* Zaring, *Finding Legal Principle in Global Financial Regulation*, *supra* note 9, at 686–87.

11. *See id.* at 697 (noting regulators may comment on Basel Committee rules and that the Committee is responsive to such comments).

12. *Id.* at 696.

developing bedrock principles that underpin the legal process. All of the important global regulatory bodies involved with finance operate on principles of consensus, for example.[13] Consensus creates the potential for hold-outs, thus empowering the relative minnows that participate at the expense of the sorts of superpowers led by American presidents.

Other principles require conduct by financial regulators that leave presidents with very little discretion to act. A national treatment paradigm, for example, animates much of the work done in financial regulation. National treatment provides that regulators will not treat their own banks, insurance companies, or broker deals better or differently than the way they treat foreign banks, insurance companies, or broker deals.[14] In financial regulation, it has been paired with a most favored nation principle.[15] Every member of the Basel Committee—there are now 20 members, comprising most of the sophisticated economies of the world—is accordingly committed to, and gets the benefit from, the deal that every other member gets.[16] In short, the regulations to be imposed on the banks of Britain by the United States are the same regulations that will be imposed on the banks of every other member of the Basel Committee.

These sorts of principles have also diminished presidential control in other international economic unions. The president's authority over trade policy was limited by the institutionalization of the World Trade Organization, with its own national treatment and most favored nation paradigms that prevent presidents from playing favorites in economic regulation.[17] The European Union, like the financial regulators, believes in subsidiarity—the delegation of policymaking to the lowest possible level—a level frequently below the European executive's close reach.[18]

13. *See* Zaring, *Finding Legal Principle in Global Financial Regulation*, *supra* note 9, at 706.

14. *See* PRICEWATERHOUSECOOPERS, REGULATORY GUIDE FOR FOREIGN BANKS IN THE UNITED STATES 17 (2005) (noting that foreign banks will be afforded the same powers and subjected to the same limitation as national banks under the "national treatment" policy).

15. *See* Zaring, *Finding Legal Principle in Global Financial Regulation*, *supra* note 9, at 706 (describing the most favored nation principle in the financial regulation context).

16. *See id.* at 706–07.

17. *See* David E. Sanger, *A Blink from the Bush Administration*, N.Y. TIMES, Dec. 5, 2003, at A28; Elizabeth Becker, *U.S. Tariffs on Steel Are Illegal, World Trade Organization Says*, N.Y. TIMES, Nov. 11, 2003, at A1.

18. *See Subsidiarity*, EUROFOUND, http://www.eurofound.europa.eu/areas/industrialrelations/dictionary/definitions/SUBSIDIARITY.htm

But there is more to these principles than the difficulties posed by those of them that delegate power away from any single head of state (or in Europe's case, a commission). The developing welter of rules and the increasing systemization of international financial law also constrain presidents. To the extent that the rules on global finance look less like negotiations and more like a legal system from which derogation is impermissible and amendment difficult, then the president's power—not to mention that of the American delegates more intimately involved in the process—to affect the terms will be increasingly handicapped.

But the news for enthusiasts for presidential power is not entirely bad. In the wake of the financial crisis the G-20, which is comprised of the heads of states of the twenty most important market economies, has become a real and substantial overseer of the process of international financial regulation.[19] The G-20, a purely political organization that might be likened to a Concert of Europe for the modern era, consists of heads of state that meet annually and finance ministers who meet biannually, to deal with the global economy.[20] The G-20 sets the schedule and issues areas that international financial regulators must address.[21] While the president hardly controls the G-20, he plays a critical part in it.

The G-20 has grown out of the smaller and still extant western head-of-state meetings begun in the 1970s, the G-6 and G-7.[22] These organizations had a reputation as talking shops and were founded in part as get-to-know-you affairs for the important anti-communist world leaders.[23]

In the midst of the financial crisis, however, it was the G-20 that provided much of the leadership for the global response, such as it was. At head-of-state summits in Pittsburgh and London in 2009, the

(last updated Nov. 30, 2010); Gráinne de Búrca, *Reappraising Subsidiarity's Significance After Amsterdam* 17–22 (Harvard Jean Monnet Ctr. for Int'l & Reg'l Econ. Law & Just., Working Paper 7/99, 1999), *available at* http://centers.law.nyu.edu/jeanmonnet/archive/papers/99/990701.html.

19. For an overview of the G-20, see generally John Kirton, *The G20, the G2, the G5 and the Role of Ascending Powers* (G20 Research Grp. & G8 Research Grp., Dec. 27, 2010), *available at* www.g20.utoronto.ca/biblio /kirton-g20-g8-g5.pdf.

20. *See* David Zaring, *International Institutional Performance in Crisis*, 10 Chi. J. Int'l L. 475, 493 (2010). Members may scale the regular meetings back to annual ones, as they grow more confident that the financial crisis is behind them. *Id.* at 496.

21. *See* Zaring, *Finding Legal Principle in Global Financial Regulation*, *supra* note 9, at 692–93.

22. *See* Zaring, *supra* note 20, at 493–94.

23. *Id.* at 494.

G-20 agreed that it would make a priority of the international regulatory coordinative process.[24]

In those meetings, the G-20 mandated the creation of the Financial Stability Board, a network designed to coordinate international financial regulation.[25] It also set an agenda for the Board and the underlying networks regarding reform of the financial regulatory system. The G-20 directed financial regulators to increase the capital requirements for banks, create a more centralized process for the trading of derivatives, explore ways to "resolve" (that is, quickly fail and recapitalize) insolvent banks, and look into the ways that executive compensation at these institutions incentivized risk.[26]

Because of these directives, the G-20 appears to have taken on an important role in setting the agenda for post-crisis financial regulation. The G-20 has followed up on the progress made on its agenda by insisting on progress reports from financial regulators at subsequent meetings; indeed, financial regulatory reforms, in addition to macroeconomic surveillance, global warming, and ire about off-shore tax havens have comprised the bulk of the G-20's stated agenda.[27]

This is quite a change from the way that international financial regulation used to work, and it is a change that gives the president more of a voice in this critical area. Since 1974, when this process got underway, the *weltanschauung* has been technocratic, and politically insulated bureaucratic collaboration. The process of setting global rules for accounting, bank safety, and insurance practices were regulatory affairs in which political involvement appears to be minimized.[28] However, the advent of the G-20's oversight has changed that dynamic.

The result is that financial regulation has a political overseer, and, as the top of the increasingly elaborate post-crisis pyramid of international regulation, it is a unique example of political oversight in international governance. It is also the kind of circumstance that

24. Douglas W. Arner, *Adaptation and Resilience in Global Financial Regulation*, 89 N.C. L. Rev. 1579, 1594 (2011).

25. *See* Douglas W. Arner & Michael W. Taylor, *The Global Financial Crisis and the Financial Stability Board: Hardening the Soft Law of International Financial Regulation*, 32 UNSW L.J. 488, 489–90 (2009) (describing the formation of the Financial Stability Forum, which was later "reconstituted" as the Financial Stability Board).

26. Huw Jones, *G20Task Force Ups Derivatives Reform Pressure*, Reuters (June 15, 2012), http://www.reuters.com/article/2012/06/15/g20-derivatives-idUSL5E8HF2UL20120615 (discussing the timeline and process for introducing such derivatives rules).

27. *See* Arner, *supra* note 24, at 1588–91.

28. *See generally* David Zaring, *What Can International Law Learn from International Financial Regulation?* (Working Paper, 2012).

does not afford the president the sort of absolute power he may enjoy as commander-in-chief of the armed forces[29] or the country's principal agent in managing foreign affairs,[30] but it does give him an important role to play in one of the most interesting developments in international law in the last forty years.

29. Curtis A. Bradley & Jack L. Goldsmith, *Congressional Authorization and the War on Terrorism*, 118 HARV. L. REV. 2047, 2049 (2005) (discussing the commander-in-chief authority).

30. For discussions of the President's strong foreign affairs hand, particularly vis-à-vis Congress, see Harold Hongju Koh, *Why the President (Almost) Always Wins in Foreign Affairs: Lessons of the Iran-Contra Affair*, 97 YALE L.J. 1255, 1257 (1988); Saikrishna B. Prakash & Michael D. Ramsey, *The Executive Power over Foreign Affairs*, 111 YALE L.J. 231, 234 (2001).