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Neoliberal Diffusion and Regulatory Capture of Financial Rules: Lessons from the 2007-8 Global Financial Crisis*

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Abstract

The 2007-2008 financial crisis that originated from the United States has caused global economic downturns in fear of plunging into a great recession. As situation evolves, regulatory problems of this systematic risk that spread from national to global levels should be detected and analyzed. This paper aims at tracing the origin and diffusion of neoliberal financial governance in the past three decades, which have paved way for today's financial disaster. A perspective that bridges domestic regulatory foundation and international diffusion of rules should be in place to better grasp the nature of current crisis. At domestic side, a perspective of "regulatory capture" in which special interests, regulatory incompetence of public institutions and the dogmatic ideologies all together contributed to this crisis. The regulatory capture further constrains policy options and impacts the following path of financial sector restructuring. In the wake of the U.S. financial meltdown, the Obama administration has made efforts on reforming the financial sector. The latest reform bills signal U.S. government' attempts to tame giant financial institutions and tighten up government regulation. For global implications, the U.S. crisis may jeopardize the credibility of the current global financial norms that have been promoted by advanced countries. The advanced world is now

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divided on how much more regulation should be imposed on new financial activities. It deserves special attention on tracking how a new set of regulatory rules is to be reformulated for years to come.

Key Words: embedded neoliberalism, club standard, regulatory capture of financial rules, moral hazard, systematic risk, the 2007-8 global financial crisis, global financial governance

I. An Overarching Perspective on Global Financial Governance

The 2007-2008 financial crisis that originated from the United States has caused global economic downturns in fear of plunging into a great recession. As situation evolves, the nature of this systematic risk that spread from national to global level, or more specifically stated, from developed to developing countries, should be detected and analyzed. This paper proposes an overarching framework of "embedded neoliberalism" to address how financial liberalization and deregulation has established itself as dominant neoliberal financial order and diffused from advanced to developing world. The neoliberal world order should have rested on compatible domestic foundation of regulation in order to prevent financial instability and crisis from happening. However, since the 1980s, we witness the increasing volume of capital mobility, the corresponding urge for uplifting restrictions on capital-account liberalization, and a series of emerging-market crises, beginning with Mexico in 1994-95, Asia in 1997-98, Russia in 1998, Argentina in 2001-92, Brazil in 2001-02, Turkey in 2000-02 (Goldstein and Xie, 2009: 21), then culminating in the 2008 crisis in the U.S. The trend in the past three decades appear to move toward more financial ventures into the developing countries (or the so-called emerging markets), the proliferation of financial derivatives of different kinds, but less regulations on bank mergers and on the emergence of giant holding financial companies that combine banking, security, and insurance in one. The embedded neoliberalism in the era of globalization, which is supposed to strike a balance between domestic regulation and global expansion, suffers from structural weakness of regulatory governance.

This paper suggests that the risk of "regulatory capture" is especially high once unbridled special interests, regulatory incompetence of public

institutions and the dogmatic neoliberal ideology work together. The proclivity toward capital logic and preference undermines the regulatory foundation of embedded neoliberalism. The regulatory capture further constrains policy options and impacts the following path of financial sector restructuring. How and why the crisis occurred and evolved can shed light on what can be reformed and what cannot be redressed. The U.S. crisis may jeopardize the credibility of global financial norms that have been promoted by advanced countries. Regional responses, especially from East Asia or China in particular, deserve particular attention. It will have important power implications when China put forth with its policy model of “Beijing consensus” in competition with “Washington consensus” in due course.

The first part of this paper is to detect the structural root of the 2007-2008 crisis by focusing on the regulatory capture of the “embedded neoliberalism” in the United States. With the perspective of embedded neoliberalism, I will trace the diffusion mechanisms of norms, rules, and ideology about financial sector restructuring, and explore how policy convergence was adopted in other context, e.g. the 1997 Asian crisis. The second section will explore the nature of global standards and codes of financial regulation, which have been held as orthodox rules by the United States and its European counterparts to endorse capital liberalization. Why did the orthodox regulation not prevent the U.S. financial crisis from happening? The third section of this paper will make an observation and a tentative comment on the current financial regulatory reforms in the United States. Finally, a concluding remark will be put forth with an emphasis on the crisis of neoliberal norms, rules, and ideology on financial regulation.

II. Institutional Foundation of Embedded Neo-Liberalism: Hegemonic Regulation or Great Powers Concert?

G. John Ruggie (1982) invented the term, “embedded liberalism”, to portray the postwar international order. He emphasized that the maintenance of the liberal world order, which was built upon three pillars, the GATT, the IMF and the World Bank, relied heavily on domestic management of adjustment to cushion external shocks. In other words, international liberal economic order should be embedded in domestic institutions and regulation: Keynesian economic adjustment and compensation from external opening. The demise of embedded liberalism started with Nixson’s termination of dollar’s convertibility to gold in 1971. The collapse of fixed exchange rate regime and the U.S. balance of payment deficit signaled the demise of embedded liberalism; in the process, legitimacy of Keynesian state-centered management declined and monetarist ideology ascended (McNamara, 1998: 144-58). The advent of the neoliberal age beginning in the 1980s is in need of a post-Bretton Woods architecture to provide an international framework for expansion, while domestically the advocacy for a “regulatory capitalism” (Levi-Faur and Jordana, 2005; Levi-Faur, 2005) assigns the state a regulatory role in rapport with market. The tenets of embedded neoliberalism envisage specific domestic institutional configuration, in which the central bank, replacing traditional economic planning agency, assume a leading status for setting monetary targets and exercising monetarist management. Regulatory competence is delegated to independent regulatory agencies in keeping distance from direct political control and partisan intervention. A bulk of empirical works mushroom on investigating how to sustain the new orthodoxy of “central bank independence” and regulatory commitment to credible policy changes (Levy

and Spiller, 1994; Majone, 1997; McNamara, 2002; Keefer and Stasavage, 2003).

Internationally, a rule-based global financial order (Kerwer, 2005) severs as the mainstay to disseminating noliberal ideas and standards, therefore creating a competitive pressure for all countries to adopt. In the policy area of financial governance, if one country fails to follow the neo-liberal trend, financial interests and multinational business would opt for countries with financial markets wide open, liberalized and de-regulated, given financial capital is easily relocated. This triggers “a race to bottom in regulatory standards” (Kerwer, 2005: 619), namely, looser regulatory standards are applied and lesser financial supervision are imposed. The competitive de-regulation pressure eventually swept all over the advanced countries, from the U.S., Britain, Germany, France, to all members of European Community by the end of 1980s (Helleiner, 1994: 146-63).

Neoliberal financial liberalization, replacing Keynesian capital control, became the new orthodoxy under which financial globalization was propagated to bring down national barriers for capital mobility. As far as financial sector regulation is concerned, an array of global standards and codes is proposed by G7 officials, global institutions (IMF, Basel Commission, and other club arrangements), along with private financial actors to govern global finance (Mosley, 2009a; Mosley, 2009b). Neoliberal rules are often imposed either on countries struck by financial crisis via policy conditionality with rescue loans (Finnemore and Sikkink, 1998; Haggard, 2000) or on countries suffered from severe international payment problems via sovereign debt rescheduling (Callaghy, 2003). In short, the club of advanced countries (G7) set standards and task the IMF and World Bank with their global dissemination of the so-called “Washington consensus” (Serra and Stiglitz, 2008). The embedded neoliberalism constitutes the new global order and seeks global diffusion (Slaughter, 1997; Biersteker, 1992).

Critics on and dissidents with the new financial orthodoxy often blame the “American hegemony” for the predominance of Anglo-American ideology and interests. Hegemonic stability theory, coined by Robert Keohane (1984), has been invoked to explain the functioning of the postwar international order under which U.S. “benign” leadership provides international public goods in terms of maintaining an open trade system and a dollar-centered monetary order. Nevertheless, with the collapse of the Bretton Woods system in 1971, neoliberal restructuring and globalization were gradually embraced by advanced countries as a whole. I suggest that, great powers concert, rather than hegemonic regulation, is the underlying architecture of neoliberal global order (Abdelal, 2006; 2007). To outsiders’ surprise, according to Rawi Abdelal’s research, policy shift in the French socialist government was the key to uphold neoliberal orthodoxy and facilitate free capital movements within the Europe (Abdelal, 2007).

Even with the great powers concert in place (Helleiner, 1999: 144), which evolved from G7, G8 to G10 as a response to structural changes in world power, how to come up with international agreements on financial standards to foster capital liberalization still involves “redistributive” politics of rule-setting among great powers (Oatley and Nabors, 1998). Taking the instance of Basel capital adequacy standard setting, the Basel Committee of Banking Supervisors, acommittee of supervisory authorities from the advanced industrial countries that meets regularly at the Bank for International Settlements in Basel, gathered in 1987, in December the G10 signed the Basel Accord on the International Convergence of Capital Measures and Capital Standards (Basel Accord). The far-reaching standard on global financial regulation sought to apply the same minimal capital requirements to all commercial banks. The genesis of the universal rule for all commercial banks actually started as the U.S. response to cope with the 1982 Latin American debt crisis, in which the excessive lending of American Commercial Banks to Latin American countries forced the U.S. government into bail-out. Yet, to

alleviate public and Congressional objection to pouring money to rescue private banks, the U.S. government shifted attention from tightening domestic regulation to push forward an international agreement in raising capital requirement for all commercial banks around the globe. The efforts not only mitigated against banks' repercussion for the decrease of lending profits, but also dragged the European and Japanese banks into the regulatory game, thus leveling the playing field for all the market participants (Oatley and Nabors, 1998: 42-46). With the intention of redistribution of wealth veiled behind the rule-setting negotiation, American regulatory authority eschewed more strict discipline on banking sector and demonstrated how agenda-setting and rule-making power generates redistributive consequences. The Basel Accord has been held as an internationally accepted standard for best supervisory practice.

As illuminated from the case of Basel Accord, the regulatory foundation of embedded neoliberalism espoused by great powers concert has tipped toward market-based measures. As financial liberalization and globalization proceed, the financial sector is no longer predominantly composed of traditional commercial and industrial banks. Private banking, institutional investors (such as investment bank, insurance companies, mutual fund, pension funds and managed-futures funds), together with highly leveraged institutions (such as hedge funds) are, instead, influential players at home and in emerging markets. The capitalization of large offshore hedge fund can sometimes outnumber the reserves of most emerging-market central banks (Eichengreen, 2003). The overlapping networks of different financial intermediaries await clearing up regulatory ambiguity, such as responsibilities among central bank, security commission, financial supervisory commission and finance ministry, and how they are coordinated to cope with the systemic risk of financial crisis (Germain, 1997: 152).

The original Basel standards defined minimum capital ratios for different classes of financial assets, The revision of the Basel Capital Adequacy Standards for International Banks (Basel II) allows banks to estimate their own

capital requirements by using their own model of portfolio risk (Eichengreen, 2003: 194). The resort to "self-evaluation approach" veiled by the euphemism of "private sector risk management" reveals the intractability of new financial practices. As Barry Eichengreen puts, "Advances in computing have made it easier for financial engineers to concoct and price derivative financial securities, in turn encouraging the development of liquid secondary markets in these assets. This has made it easier for portfolio managers to arbitrage regulatory requirements--to securitize assets--and shift them off of the balance sheet without altering overall portfolio risk" (Eichengreen, 2003: 194-5)

While developing countries fend themselves with national regulation or capital control, the advanced countries often favor market discipline as the self-regulating mechanism. Club organizations, such as the Basel Committee of Banking Supervisors and the Financial Stability Forum (FSF), which was established in early 1999, both are to provide a venue for discussion and agenda-setting. Global economic governance organizations, such like the IMF and World Bank, then put these neoliberal standards into implementation (Eichengreen, 2003: 185-6). As Table 1 clear shows, the nature of the rules for global financial regulation thus far is the so-called "club standard," which entails low conflicts among great powers, but possesses high conflicts and divergent interests between club members and other developing countries. Table 2 also summarizes how different types of regulation are linked with specific type of politics. With its specific payoff matrix, standard setting and risk monitoring of financial regulation are susceptible to small-group capture. The logical connection between the type of regulatory coordination and the type of regulatory politics can be well exemplified by the case of financial regulation. The neoliberal financial rules were generated by great power concert. The nature of financial regulation of this type is the "club standard," on which the extent of interest divergence and conflict among great powers is low, whereas the extent of interest divergence and conflict is high between

great powers and other international actors. The example can be provided and demonstrated by how advanced financial powers imposed dominant rules on Japan. The diffusion of neoliberal club standards thus gives rise to dynamics of client politics. Provided that the dispersion of benefits by accepting a club standard is concentrated on the small club of great powers, other financially less developed countries would have had no incentive to comply. However, the costs of resisting dominant rules can be overwhelming for these countries. Resisting the adoption of the same financial standards would damage the country's investment rating by international financial community, and more specifically, by credit rating agencies. In this sense, the dispersion of non-compliance costs is also narrow. Choosing to be a client would reduce potential costs and induce favorable evaluation from the patrons. This is why the "small group capture" emerges in global financial governance.

Table 1 A Typology of Regulatory Coordination

		Divergence of interests between great powers and other international actors	
		High conflicts	Low conflicts
Divergence of interests among great powers	High conflict	Sham standards	Rival standards
	Low conflict	Club standards	Harmonized standards

Source: Drezner, 2007: 72.

Table 2 Typology of Regulatory Politics

Dispersion Costs	Dispersion Benefits	Type of Politics	Example
Wide	Wide	Majoritarian politics	Tax policy
Narrow	Narrow	Interest-group politics	Industrial subsidies
Narrow	Wide	Entrepreneurial politics	Environment
Narrow	Narrow	Client politics (small-group capture)	Financial regulation

Source: Laurence, 2001: 38.

According to the study of Daniel Drezner (2007: 136-7), half of the financial codes and standards emanated from club-like international governmental organizations or private orders. The Financial Stability Forum (FSF) was regarded as "a club of clubs," heavily representing G7 interests. Only one of the agreed-upon standards took the different stages of development into consideration. In other words, these standards may well constitute a ratcheting up of stringency for the developing countries.

Elkins and Simmons (2005) propose that policy diffusion usually occurred on waves and clusters. A wave of neoliberal rule-semination has emerged in the wake of the 1997 Asian financial crisis, since crisis situation serves as the best catalyst for the promotion of ideation and institutional changes in developing world. The IMF report after the Asian crisis suggested the disclosure of information on trades, positions, and detailed portfolio reporting; these approaches preferred information-based discipline over direct regulation (Eichengreen, 2003). The World Bank and the IMF systematized "eleven areas where standards are important for the institutional underpinning of macroeconomic and financial stability," including international standards on

“data dissemination, fiscal practices, monetary and financial policy transparency, banking supervision, insurance supervision, securities market regulation, payment systems, corporate governance, accounting, auditing, insolvency regimes, and creditor rights” (Soederberg, 2003: 8). These standards and rules aim at harmonizing different national regulatory practices and facilitating global expansion of financial capital. Ostensibly, global regulatory standards seem softer than legal rules by giving sovereign states more regulatory autonomy (Kerwer, 2005). Yet the harmonization of regulatory standards is conducive to eradicating national differential treatments on and barriers to globally mobile capital. The Asian financial crisis sprang up the proliferation of so-called “good governance practices” that attempts to establish comprehensive webs of surveillance in the interest of western institutional investors (Soederberg, 2003: 9).

Some third world countries have questioned that why should the South accept and comply with these club standards that did not address the reckless and unstable nature of transnational financial capital. In this category, Malaysia government refused the IMF financing schemes and turned to its own capital control measures. South Korea, on the other extreme, capitulated to IMF pressures and went through sweeping financial and corporate sector restructurings in which business-government relations were questioned, chaebol was reconfigured, good corporate governance measures were introduced to protect shareholders' rights, restrictions on foreign banking investments were uplifted, and the competitiveness law was installed (Haggard, Lim and Kim, 2003).

The post-Bretton Woods era dwells on the rule-based global order. The trend breeds on literatures on legalization and policy diffusion in international political economy. The legalization school (Goldstein and Steinberg, 2009: 211-241) traces the prominent development in the WTO on harmonizing trade-related rules and establishing dispute settlement mechanism. As the Agreement on Technical Barriers to Trade of the World Trade Organization states, “where technical regulations are required and relevant international standards exist—

Members shall use them—as a basis for their technical regulation." Failure to do so may constitute an obstacle to trade and thus a violation of WTO law (Mattli and Buthe, 2003: 2). The harmonized international standards increasingly serve as instruments of trade liberalization to overcome national barriers of other countries. In the area of finance, internationally accepted frameworks of prudential banking supervision, such as the Basel I and Basel II Accords, and international agreed-upon standards on securities, accounting and insurance have an penchant for "voluntary information disclosure" and self-evaluation approach to govern mobile and volatile financial capital.

The literature on policy diffusion (Simmons, Dobbin, and Garrett, 2006, 2008; Simmons and Elkins, 2003), on the other hand, examines various mechanisms for disseminating mainstream policy "consensus." Among the items on the list, competition, emulation, coercion and learning are routs to policy diffusion and ultimate policy convergence. Although encountered with the repulsion from the "varieties of capitalism" (VOC) thesis, which insists that particular institutional combinations of national capitalism cannot easily be swept aside by globalization, there is no gainsaying that neoliberal ideas, norms and rules have permeated into national practices, and gradually accepted as technically rational policy options to "link with globalization." Then, an embarrassing question emerges, if the dominant neoliberal financial rules and standards are primarily promoted and practiced by the U.S.-centered authority, how come the U.S. became the epicenter of the 2008 financial meltdown? The following session turns to the U.S. case.

III. Regulatory Capture of the U.S. Financial Governance

Few would have ever imagined that a suprime mortgage bubble burst in the summer 2007 kindled a series of financial institutions crisis. From Bear Stearns, Fannie Mae and Freddie Mac, Lehman Brothers, Merrill Lynch, AIG, to Citigroup, the horrendous crisis hit the United States and damaged global economies. So far, only a limited consensus is reached on the causes of the 2007-08 crisis (Davies, 2010), not to mention what lessons are to be drawn from this economic and financial crisis. Senior economists generally pay attention to the following broad issue areas, which may, in combination, cause the crisis: The first category focuses on macroeconomic policy failures. The former chairman of Federal Reserve Board, Mr. Greenspan, was blamed for his monetary policies mistakes; his too low interest rates and too loose credit policy spurred housing booms and stepped up bubble economy (Johnson, 2009a). His overall policies had encouraged borrowing in the first instance, and in turn encouraged excessive leverage among secondary market participants (Noland, 2009: 182).

The second category concerns failures of financial-sector supervision and regulation. The credit ratings agencies and regulators were scorned “asleep at the switch” and U.S financial regulation system being regarded “fragmented and inadequate.” In conjunction with abundant liquidity and regulatory lassitude, a grand scale of frauds added to the systemic crisis (Noland, 2009: 182). This paper basically follows this line of reasoning by tracing the roots of ill-regulated financial liberalization: Neoliberalism in financial sector has been embedded in an inadequate and fragmented regulatory structure in the United States. Unfortunately, this set of regulatory rules and beliefs had been the mainstream in financial governance.

The third category pays heed to the poorly understood, and thus poorly regulated, financial engineering. The Wall Street financial engineers designed derivatives and securitizations of multiple forms, from interest-rate options to more intricate credit-default swamps and collaterized debt obligations (The Economist, July 18th 2009). Risks of financial ventures have been wrapped as "financial products" for trading; risks were born by consumers all over the world. Arguments from this perspective hold the Wall Street, including financial engineers and speculators, as suspects.

The fourth category cares about the excessive risk taking on the part of large financial institutions in their global business (Truman, 2009). Decades of financial liberalization and integration have given rise to vertical and horizontal concentration of financial capital. Financial giants and securities firms have operated on the global reach. According to Simon Johnson's testimony to the U.S. Congress, the handling of problematic giant financial institutions, conducted by the Treasury Department and the Federal Reserve, did not act on any coherent principle or legislation. Instead, regulators served as a "broker" mediating among troubled debtors and potential market buyers via government guaranteed capital injection. Given the nexus of Treasury and Wall Streets, U.S. government acted carefully not to upset the interests of big finance, thus the terms of restructuring were apparently favorable to the banks (Johnson, 2009b). To salvage these giants easily falls into victim of the "too big to fall" principle of financial restructuring.

The above mentioned policy mistakes and regulatory failures seem predicated on "wrong policies" taken by individual decision-makers, or innocent ignorance on new forms of financial engineering. Mainstream arguments thus far eschew identification of structural causes involved in the ideas and practices of embedded neoliberalism. I maintain that "regulatory capture" by established financial interests has undermined the domestic foundation of embedded neoliberalism. Ten years ago, Randall D. Germain (1997) foresaw the structural imbalance between public authority and private financial intermediaries, in

which public authority surrendered regulatory powers to private financial capital (market forces). Scholars warn that the global regulatory responsibility has been “privatized” and been handed over to new global rulers as national authorities are in retreat (Buthe and Mattli, 2011). The so-called “transnational financial network” or “international financial community” gradually coalesced around converged consensus and exercised great competitive and emulative pressures for other countries to follow. The distinction between “Anglo-American” and “Rhenish” models of finance has been blurred as the latter category of countries embraced transaction-oriented capital markets. Worse still, governments with piling national debts become increasingly dependent on the willingness of private financial actors to purchase and hold public bonds and securities. The reliance on private markets to fund government debt has further deepened the dilemma of regulatory capture.

The nexus of public-private collaboration in financial governance has been euphemized as “network governance” of a new regulatory shift (Mosley, 2009b). The problem is that public authority subsides with the rise of transnational alliance of private financial interests, and the financial game turns too complicated for prudential supervision impossible. The private financial sector has been active in the formulation of universalized standards within various club organizations and in collaboration with IMF and World Bank. The U.S.-based credit-rating agencies, notable known Moody’s, and Standard and Poor’s (S and P), have immense powers on rating for soundness of sovereign states and private institutions (Sinclair, 1994). The complex structured financial products depend on risk weighting that is tied to credit ratings. If credit ratings agencies get it wrong, the self-regulated risk weights for the liquidity requirements are miscalculated. Ironically, some of the troubled financial institutions in this crisis have been rated inaccurately, which fundamentally undermined the credibility of the current regulation.

This is why the 2007-08 financial crisis, with its epicenter in the U.S., is believed to cast a devastating blow not merely to the credibility of financial

institutions of all types, but also to credibility of U.S. risk management and distribution. It is outrageous for government regulators to rely on "value-at-risk" (VAR) models used by institutional investors to calculate how much capital they should set aside as insurance against losses on risky assets, according to the Basel II Accord (Tarullo, 2008; The Economist, 2009). Indulging rapacious financial interests for self-governance illustrates how regulatory capture by the network of private financial institutions could be a catastrophe. The consequences may be summarized as "socialization of risks, privatization of benefits."

The moral hazard problem is sequentially ushered in the process of financial restructuring. Particularly constrained by the faith in neoliberal capitalism, U.S. government pours into huge public money, gauges cost distribution between shareholders, bank creditors and taxpayers, but refuses to nationalize those giant financial institutions. With insistence on market-type incentives, U.S. government gives up on the golden window of opportunity to clean up problematic financial institutions and render bankers an effective veto power over financial policy (Johnson, 2009b). Only with the ideological disenchantment from neoliberal capitalism could the state-market imbalance be remedied and the global financial architecture be overhauled.

To sum up, my analysis that links neoliberal diffusion and regulatory capture of financial rules has been well illustrated by the case of U.S. Subprime Crisis. The origin of the neoliberal regulatory rules began with the sweeping advocacy of financial liberalization and globalization, which had paved way for U.S. financial industry for global expansion. The neoliberal rules were consolidated by changing the Basel I to the Basel II, which removed strict requirements of capital adequacy and opted for market self-discipline, soft regulation, and inner risk evaluation by financial sector. Domestically, U.S. financial regulatory acts had gone through corresponding liberalization revisions. Great power concert and the club of financial community help propagate and disseminate the new financial tenets. The

process of neoliberal embeddedness espouses market discipline with the retreat of state regulatory authority. Owing to the predominance of market ideology and the lack of transparency on risk calculation and supervision, the subprime mortgages was securitized as priced financial products and traded in the financial value-chain. Thereby, the default and the credit crunch in a marginal segment of the U.S. financial industry had spread to large financial institutions (e.g. Citibank), investment banks (e.g. Lehman Brothers and Merrill Lynch), hedge funds, pension funds, mutual funds, and to insurance industry (the AIG) via the dense network of financial interconnections (Moschella, 2010: 128-132).

IV. U.S. Regulatory Reform in the Wake of Crisis

The crisis of this scale quietly alters the power structure of global economic governance. The club-like international organizations (G7, IMF and FSF) acknowledge their credibility and legitimacy crises, thus incorporate more participation from developing countries. In the wake of the crisis, the ascendance of G20, the reallocation of IMF quota shares and voting shares (U.S. lost its veto status along with China's quota increase), and the transformation of Financial Stability Forum (FSF) into Financial Stability Board (FSB) to include China, India, Korea and Indonesia all illuminate the underlying power shifts. It is worth observing whether the power shifts affect the existing neoliberal global governance. U.S. hegemony has been in further decline as the financial bail-outs and economic stimulation pushed fiscal deficit to new high. The great power concert between the U.S. and the EU, which is often called "transatlantic convergence," on neoliberal financial governance is now in disarray. Although G-20 in 2008 and 2009 proposed a set of reform consensus in a very broad term, such as setting up Financial

Stability Board (FSB), strengthening prudential regulation, preventing systematic risk, emphasizing consumer protection, and expanding regulation over credit rating agencies and various new financial products, the most pressing issue for global financial governance is to observe how American authority conducts a regulatory overhaul to tackle the underlying problems in financial industry. And, once the reform is set in motion, how the new regulatory practices in the United States turn into an international agreement? Would the EU have its own reform agenda? What does the divergence of regulatory preferences between the U.S. and EU influence the neoliberal global order? Provided that financial "re-regulation" at national level is still under way, this paper can only examine the U.S. financial reform as the EU lag behind on passing new financial legislations. This is due to the complex decision-making framework under which the initiatives of the European Commission must acquire approval both from the Council of Ministers (under qualified majority rule of 27 member countries) and from the European Parliament (Hooghe and Marks, 2001; Goldstein and Veron, 2011: 11).

The underlying problems of the 2007-2008 financial crisis revealed could be summarized as follows: first, the "too big to fall" problems of large financial (including non-bank) institutions need to be redressed. The large banking and financial holding companies have posed the "moral hazard" problem of "too big to fall." One way to tackle this problem is to place a size cap on it. Another approach under which the U.S. Congress favors is to require these institutions via a higher capital adequacy standard and quantitative minimum holding of liquidity. Second, the "self-regulation" approach of the Basel II should be overhauled with more government intervention. Government re-regulation comes back. The "Volcker rule" that is advocated by former Fed chairman and the current administration's economic advisor, Paul Volcker, set out government restrictions on excessive risky activities and proprietary trading activities, not really done for clients. Third, the conflict of interests for credit rating agencies should be emphasized. New regulations

consider to hold credit rating agencies legally responsible for their credit assessments. Forth, customer protection agency will be set up to stop abuses on financial products.

Simon Johnson, in his testimony before Joint Economic Committee in the U.S. Congress on October 29, 2009, points out: if America wishes to maintain its global political and economic leadership, despite the rise of Asia, it is urgent to revise its policy stance toward the financial sector, which means largest banks to be broken up, “excess risk taking” to be taxed, and nontransparent interconnectedness among financial institutions of all types to be reduced as well (Johnson, 2009a). Fred Bergsten also points out, the “overleveraging finance and under-pricing of risk”-especially in the United States manifest that systemic inadequacy of global financial regulation. An international consensus on the key issues such as capital requirements, liquidity and leverage ratios, resolution authorities, and compensation practices is the most urgent (Bergsten, 2009). These proposals of reforms attest that the structural roots of the 2008 crisis lie on excessive liberalization and securitization of financial capital beyond sound and systemic regulation. The domestic foundation of embedded neoliberalism has been put in jeopardy, not only in the United States, but in some other European counterparts.

The U.S. Senate finalized a new regulatory bill, Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act 2010) in July 2010. This is the most severely tightening act of financial regulation since the 1980s and 1990s. A historical perspective on the regulatory changes in America illustrates how the age of “embedded liberalism” beginning with the 1930s Great Depression transited to the era of “embedded neo-liberalism starting in the 1980s. As Goldstein and Veron (2011) indicate, the U.S. had a tradition of suspicion about large banks. That is why the 1927 McFaddn Act prohibited banks from opening new branches across the States. The 1933 Glass-Steagall Act made a forced separation of investment banking from depository banking activities. These two acts demonstrated how the old model of “embedded

liberalism" was concerned about the necessity of preventive regulation over financial sector expansion. The old regulatory model was replaced with neoliberalism as the wave of financial liberalization and globalization swept the U.S. and the globe. The 1982 Garn-St. Germain Act allowed financial holding institutions to acquire out of State failed banks. The 1994 Riegle-Neal Act lifted restrictions on interstate branching. The 1999 Gramm-Leach-Bliley Act jettisoned much of Glass-Steagall stipulations on merger and removed the legal barriers to the formation of diversified financial conglomerates (Goldstein and Veron, 2011). Tracing the path of regulatory changes and the ascending re-regulation in the wake of 2007-2008 financial crisis, the new financial act attempts to regain national control over the privatized financial self-regulation. The important stipulations of the new act, summarized as follows, demonstrate the day of re-regulation is in order. First, financial holding companies with $50 billion or more in assets will be automatically subject to enhanced standards of prudential regulation. Second, the so-called "Volcker rule" prohibits all banking entity from engaging in proprietary trading or investing in hedge funds and private equity funds. In addition, mergers and assets acquiring for any insured depository institutions are subject to a 10% limit of total consolidated liabilities. Third, large and interconnected banking companies will be required to have extensive, rapid, and orderly resolution plans to be approved by the Federal Reserve and the FDIC. And government reserves powers to take over important financial institutions in case of crisis. Fourth, a comprehensive risk monitoring framework, Financial Stability Regulatory Commission, will be set up, composed of the Federal Reserve, the Treasury, and all other federal agencies in charge with securities and insurances, to provide integrated regulation. The remaining area to be reformed is concerned with new rules to constrain risk-taking by and leverage in the largest global financial institutions (Goldstein and Veron, 2011: 9-10).

It appears that the outrage from the public toward the financial community provided great momentum for substantial reform to move forth.

Economic advisors have also repeated the necessity to turn the domestic reform into a new agreement of financial governance. It is important for the U.S. government to harmonize the new rules among peer countries in order to avoid competitive disadvantage for its own financial industry. How the European Union and other G20 countries react will be of great importance for the future of global financial reform.

V. Concluding Remarks

This study proposes an integrated framework on "embedded neo-liberalism" to bridge domestic regulatory foundation with international diffusion of norms, rules, and ideology. The norms of neo-liberal financial regulation center on market discipline, capital account liberalization, financial integration and globalization. We have witnessed that, complying with the neoliberal norms, U.S. financial rules and regulatory style became policy consensus for financial regulation. The European continent also embarked on their path of financial market integration. This fashion of policy consensus and financial rules, as important components of the so-called "Washington Consensus," has swept all over the world and imposed on crisis-hit economies. The neoliberal policy guidance on solving the Mexican, Russian and Asian financial crises have fortified the neoliberal orthodoxy. The rule changes from the Basel I to the Basel II, along with the emergence of dense network of under-regulated global finance, manifested the heyday of neoliberal ideology. Nevertheless, the most ironic blow on the neoliberal order came from the financial burst-up in the United States, the ultimate source of the dominant norms and rules in finance. The default and credit crisis of a marginal subprime mortgage market proceeded to affect and tear down giant financial, security, insurance, and investment companies via the complicated securitization of risk products. Hit

by the significant magnitude and depth of this systematic crisis, the domestic regulatory foundation of the U.S. has been shaken and restructured. Neoliberal norms encountered severe legitimacy setback and its policy prescriptions were questioned. The swift post-crisis regulatory changes taken in the United States illuminated the structural imbalance between state and market was being recognized and partially redressed. The financial governing institutions, among which the IMF in particular, have called for tightened regulatory standards as new policy consensus. It is still too early to claim the neoliberal demise, at least no other visible ideological alternatives in sight in the near future.

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新自由主義金融規則的擴散與管制擄獲：2007 至 2008 年全球金融危機的教訓

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摘要

2007 年源自美國次貸危機的全球金融海嘯，使得金融體系系統性風險的全球與各國管制問題浮現。本論文回溯過去三十年新自由主義金融治理規則，提出一個新自由主義制度鑲嵌的理論架構，論述當前造成系統性金融危機的起源在於 1980 年代以來的管制擄獲，亦即私人金融資本、大到不能倒的大型銀行、信用評等機構與國際金融治理俱樂部，共同設計出由市場自我規範、風險自行估算的金融管制規則，形同放任被管制者自訂遊戲規則，由國際經濟組織背書，並向開發中國家推展新自由治理規則，擴張金融版圖。各國管制權威的效能不彰其實受制於金融先進國家彼此間的利益競爭，管制越鬆散的國家越能吸引跨國金融資本的高風險槓桿操作，以及名為金融創新，實為風險層層包裝以獲利的衍生性金融遊戲。此次金融危機迫使美國進行再管制，迅速通過新金融法案，歐盟則因決策架構複雜，有待時間推動其管制變革。新自由金融規則的演變仍在進行中。

關鍵詞：新自由主義制度鑲嵌、俱樂部標準、金融規則的管制擄獲、道德風險、系統性風險、2007 至 2008 年全球金融危機、全球金融治理

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