

## Legal aspects of Financial Services Global Liberalisation

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*Globalisation means more than freer movement of goods, services and capital across borders. It entails the faster movement of ideas.*

Joseph Stiglitz

### Introduction

The financial services industry has been profoundly reshaped in the past decades. This has not just been a result of huge information technology advancements, but also due to the de-localisation of economic agents in an increasingly borderless world, fomented by multilateral and regional understandings. Financial markets are today largely integrated and linked on a global basis.

Trade in goods, present in human existence from times immemorial, has been best multilaterally translated into more stable rules since Bretton Woods, under the GATT<sup>2</sup>, and more recently, under WTO<sup>3</sup>. Regulating and adjusting a global approach to financial services liberalisation, however, demands different tools from the ones known today for trade in goods, which did not yet reach an adequate formula.

As noted by Lovett<sup>4</sup>, "international banking has a long history of involvement with foreign trade, shipping and investments. Italian merchant bankers were important in such finance during the Middle Ages and Renaissance and this banking activity gradually spread north to the Netherlands and German towns (...) London took the strong lead as an international banking centre during the 19<sup>th</sup> century, helping to enlarge British trade and industrial development. Britain

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<sup>2</sup> General Agreement on Tariffs and Trade, since 1947.

<sup>3</sup> World Trade Organisation, established after GATT's Uruguay Round, having come to light in 1995.

<sup>4</sup> Lovett, William Anthony. Banking and financial institutions law in a nutshell. 4<sup>th</sup> ed. West Publishing Co, St. Paul, MN, US: 1997, p. 215.

placed a substantial volume of foreign investment in many countries, including the Americas".

The globalisation phenomenon has caused an immense development of the finance industry, this one mainly to serve the global economy<sup>5</sup>. Financial services have also become an end in itself, as securities, banking and insurance products acquired independent spaces, sometimes lacking direct relation to commercial or industrial activities<sup>6</sup>.

Hence, the international financial environment has become more integrated, complex and unstable. In this sense, national laws have proven to be insufficient<sup>7</sup> to treat financial services, introducing an urgency sense towards adequate regulation and supervision. In addition, international finance networks helped build a very efficient crime highway, used for money laundering, easing the financing of drug and arms trafficking, as well as terrorism, demonstrating the need of a multi-nation approach and intense co-operation, on a fully integrated scale.

The community of global nations addresses regulation and supervision of the financial services industry in several fora, creating overlaps and legitimacy erosion problems, not to mention the competition of private unification initiatives. Understanding and regulating such industry clearly demands multidisciplinary<sup>8</sup> information exchange and action.

Market players have almost endless means to create and implement products and strategies, easily overcoming less organised initiatives of nation states, multilateral agencies or international organisations. Understanding some of the positive meeting places between the finance industry, international fora and states, is the objective of this article.

In the nineties, the easily spelled moto was "regulators no longer have sovereignty over the movement of capital across their national boundaries (...) Government policy is now largely influenced and dictated by the free and massive flow of capital

<sup>5</sup> L'économie globale va être de plus en plus dominée par une logique financière qui déborde de son champ d'activité d'origine pour imprégner l'ensemble de l'activité économique. Michalek, Charles-Albert. Les métamorphoses de la mondialisation, une approche économique, in Loquin, Eric et al. La mondialisation du droit. Litec-Credimi, Dijon, 2000, p. 34

<sup>6</sup> Les mouvements de capitaux, qui devaient accompagner le commerce international et les investissements fait à l'extérieur, se sont, en réalité, trouvés multipliés par dix par rapport à ceux-ci. Ils n'avaient donc plus aucun rapport avec l'économie réelle. Auberger, Philippe. La démocratie à l'épreuve des marchés. Economica, Paris, 2003, p. 11.

<sup>7</sup> Si le marché est international, ou plus encore, s'il perd toute localisation, ce droit ne peut plus s'appliquer - Marie-Anne Frison-Roche, Le cadre juridique de la mondialisation des marchés financiers, in Banque et droit, mai-juin 1995, p.46.

<sup>8</sup> La reconnaissance de la spécificité du phénomène de la mondialisation requiert, au contraire, une vision intégrée. Cette exigence est rendue d'autant difficile que les concepts économiques ont été définis dans une optique de cloisonnement des disciplines conçues comme autant de champs spécialisés du savoir. Michalek, Charles-Albert. Les métamorphoses de la mondialisation, une approche économique in La mondialisation du Droit, Paris, Litec : 2000, P. 14. European Systems have started to adopt the 'economic analysis of law' approach, which is typically associated with American law as well as an 'interdisciplinary' approach. (...) Legal systems are at different stages of development and when they converge it is because the less developed system is catching up with the more mature one. De Cruz, Peter. Comparative Law in a changing world. Cavendish Publishing Limited, London, 1995, p. 481.

worldwide. Those countries with an open market approach to regulation and harmonised rules are more likely to prosper in the global economy as capital (both human and financial) increasingly ignores national boundaries<sup>9</sup>.

Today, economic and social facts lead to a more different and broader approach. Plain and simple de-regulation has been overcome by near-to-fit instruments (including re-regulation) and methods of addressing the financial services liberalisation phenomenon. The way globalisation has been seen has clearly changed in recent times.

As mentioned by Waltz, "we are therefore inclined to see what we are looking for, to find what our sense of the causes of things leads us to believe significant"<sup>10</sup>, and it seems that minds are much more opened than they were, ten years ago.

### Democracy matters

Permeability of markets has caused a multiplication of decision centres. Today it is not clear, as it was some years ago, where financial decisions are taken, affecting millions of persons. Financial services regulation differs enormously from country to country, as national regulation is one of the main barriers to free trade in services<sup>11</sup>. As Christos Hadjemannil well put it, regulators do not operate in a political vacuum<sup>12</sup>.

Industrialised countries generally have monetary and banking authorities with strong political and accountability independence, having chosen a more technocratic approach to market discipline, if compared to less developed countries<sup>13</sup>. Such delegation of democratic powers is a reflection of each country's political model and economic choices. Transplanting models from one state to another shall take into account an immense variety of issues, with no guaranteed success.

Financial services liberalisation, either through multilateral agreements, soft law or voluntary adhesion to convergent regulatory formulas, when correctly addressed, cannot be kept away from the legitimacy test of democratic choice based in transparency.

Democracies do not evolve in the same rhythm as the market. They may be

<sup>9</sup> Walker, Gordon. *International regulation in the information age: the political dimensions of globalisation*. IJBL 11, 1995, p. 463.

<sup>10</sup> Waltz, Kenneth. *Theory of International Politics*. First Edition. McGraw-Hill, US, 1979, p. 12.

<sup>11</sup> Il paraît que les mouvements sur les marchés financiers, en particulier les mouvements sur les monnaies, ont une incidence qui dépasse, de loin, le seul domaine financier: ils ont des incidences économiques, en particulier sur l'activité et l'emploi, des incidences sociales et, par voie de conséquence, dans les pays les plus vulnérables, également des incidences politiques. Aubergier, Philippe. *La démocratie à l'épreuve des marchés*. Economica, Paris, 2003, p. 119.

<sup>12</sup> Academic sessions at QMUL, 1997.

<sup>13</sup> Where neither technocracy, nor democracy, may be practised, but plutocracy instead.

<sup>14</sup> Dillon, Sarah. *International Trade and Economic Law and the European Union*. Hart Publishing, Portland, Oregon, US, 2002, p. 281.

<sup>15</sup> Op cit. p. 11.

squeezed by market forces, and if no public participation exists in defining paths and rules, globalisation naturally becomes a synonym of old and well known dictatorships, which less developed countries frequently experienced in the past being much used to strong political regimes and ruthless statesmen.

The fact that the market squeeze may have been happening results on the widely accepted thesis on Seattle's battles, at the 1999 WTO summit. Those radical protests inspired different forms of clarification on the globalisation process piloted by industrialised countries, having, in a certain way, helped to re-orientate multilateral trade discussions and decisions.

Uncertainty about the scope of the discussions on trade liberalisation, as well as with regards to the actors involved, dimming democratic control. As noted by Dillon, "it is the very open-endedness and unpredictability of the Services Agreement that has called forth such an extreme reaction from the WTO's critics, and such a spirited defence by the WTO itself"<sup>14</sup>.

As Auberger<sup>15</sup> correctly put, there is no public democratic global space, as a shared political culture is purely absent. It may have been thought that some unification of services and their rules would perfect democracy, however this is not happening, mainly because democracies are founded in nation-state concepts. Without a global nation, nor a feeling of its existence or inclusiveness, global democracy is a chimera.

A valid initiative example in trying to introduce some public inclusiveness in globalisation is the not-so-successful United Nations Code of Conduct for Transnational Corporations. It laid down a set of guidelines defining the rights and responsibilities of transnational corporations in their international operations. The attempt aimed at introducing concepts of international public order within private cross-border activities. More than convincing nations and market participants on a certain conduct regarding opening national borders, the project searched for inducing a behaviour pattern through voluntary adhesion to a moral conduct in global businesses. The initiative has been applied in setting standards in the fields of human and consumer rights.

An important lesson is drawn from these considerations. Treatises and conventions have been frequently torn apart, model laws have been adopted much less than desired, international public and private agreements have been insistently repudiated. All these incidents invariably have similar source: the absence of voluntary and positive will of the really affected parties, i.e. the populations involved. As in basic contract law theory, no agreement may be protected by law if it is not based in a free manifestation of will is given. Imposing formulas on populations has proven to be counterproductive, and as Rudolf von Ihering put it, laws should serve people, not people should serve laws.

At an industry roundtable hosted in Basel<sup>16</sup>, in November 2003, participants discussed the subject of risk management and regulatory approaches in the banking, securities and insurance sectors. The discussions evidenced how much market practices are converging across the three sectors and whether differences in the regulatory approaches to risk across those sectors reflect actual differences in the underlying risk and risk management practices.

The prevailing view was that better information was needed, and so the need for international debate. A sense of public participation, more than just a place for market participants to discuss, creates hopes that the global society will create means to influence global decision at policy making fora.

Globalisation has several definitions, aspects and forms. Michalet<sup>17</sup> suggests an interesting classification of the economic evolution phenomena in different phases: from international to global economy, going through a multinational economy.

In what Michalet calls "International Economy", strong reference to nation states prevails over international specialisation and economic liberalism. At this stage, nation states are at the heart of the trading system<sup>18</sup>. Theories laid down during this period focused in explaining import and export movements of goods between national economies and, for rule making, in the advantages of international specialisation (still using D. Ricardo's<sup>19</sup> inspiration).

In a "Multinational Economy", indicated by the author as dating from the 1960's, a new dimension is given to direct investment and the mobility of productive activities, placing market players from one to another territory. This resulted in a radical change on how production is performed.<sup>20</sup>

This kind of economic organisation has been a recipe for companies' strong growth, practising forum shopping to find best suited places where to establish activities, without much bothering about corruption, environmental, consumer and labour laws. Regarding financial services, at this same time, desert islands became more important with their tax benefits and some lawlessness, as well as countries attracting foreign industries with immediate benefits, despite long term adverse effects not accounted for.

<sup>16</sup> Hosted by the Basel Committee, having senior representatives from 8 Committee member countries (France, Germany, Italy, Japan, the Netherlands, Spain, the United Kingdom, and the United States), 16 non-G10 supervisory authorities (Argentina, Australia, Brazil, Chile, China, the Czech Republic, Hong Kong, India, Korea, Mexico, Poland, Russia, Saudi Arabia, Singapore, South Africa, and the West African Monetary Union), the European Commission, IMF, World Bank, and the FSF.

<sup>17</sup> Loquin, Eric et al. *La mondialisation du droit*. Litec-Credimi, Dijon, 2000, p. 18.

<sup>18</sup> "les territoires nationaux occupent le cœur du système des échanges". *Op.cit.* P. 17.

<sup>19</sup> Dans l'économie globale, la théorie des avantages comparatifs n'a plus de cours. Loquin, Eric et al. *La mondialisation du droit*. Litec-Credimi, Dijon, 2000, p. 39.

<sup>20</sup> Dans l'économie internationale, seuls les marchés des biens et services dépassaient les limites posées par les frontières nationales ; avec le développement de l'économie multinationale, les systèmes productifs deviennent multinationaux. Loquin, Eric et al. *La mondialisation du droit*. Litec-Credimi, Dijon, 2000, p. 22.

The main characteristics of this stage, of economic re-organisation, has been the penetration of national markets by other means than plain and simple exports. On the other hand, countries have also started organising themselves to create conditions which could draw investors' attention. In this sense, studying economic sectors and their strategies has originated very specific nations' policies<sup>21</sup>, competition no longer lying only on production factors within a national territory.

The early 1980's "Global Economy" is characterised by the predominance of a new financial dimension. The rationale behind the investment and production turned into seeking attractive rates of return, through alternative investments in the financial markets. Speculation soared and also liquidity, resulting in some well documented financial crisis that, due to urgency and carelessness in implementation, caused poverty increase and wealth inequalities, which generated a much more unsafe world.

In search of protection the regionalist trend increased, with the creation of free trade zones and other kind of associations for economic convergence, in competition of a GATT, and later WTO, multilateral economic relation of nations.

In today's unified cyberspace market, competition among countries for investment and hosting financial services activities has soared. A balance between regulation and competitiveness is being constantly searched.

Cities and countries are in constant fight for hosting the fast-growing financial services industry and attracting investments. A physical allocation arbitrage is constantly made and nations are looking at ways to avoid destructive forum shopping. As noted by Fontaine<sup>22</sup>, billions of dollars are daily re-allocated in search of almost insignificant different rates of return on investment, easiness in communication allowing that at a simple finger touch. Nations are constantly searching for a balance between attractiveness and internal security, thus the need for financial services global coordination.

### Unification or harmonisation?

Globalisation has become a test field for the theory of natural convergence. The idea that legal systems of societies will tend to become more alike, as the societies become more like each other, oversimplifies the complexities of making different cultures converge.

<sup>21</sup> The Asian Tigers saga being the best example.

<sup>22</sup> "...l'arbitrage entre les marchés financiers dans le monde entraîne des mouvements de capitaux importants. Ainsi, des milliards de dollars se déplacent pour profiter d'un arbitrage d'un huitième de pour cent sur les taux d'intérêt. Les mouvements de capitaux sont tels qu'il n'est plus possible à un État, et même à l'ensemble des États industrialisés, de les contrôler. Les marchés financiers internationaux échappent à toute réglementation étatique, et pour que les marchés nationaux ne soient pas en retard, la plupart des États ont procédé à leur déréglementation ; ce qui permet entre autres que les taux d'intérêt et de change reflètent le mieux possible les conditions économiques et les anticipations des agents économiques. Fontaine, Patrice et Joanne Hamet. *Les marchés financiers internationaux*. PUF, Paris, 2003, p. 3.

Unification of laws has been part of the human civilisation, and the Middle Ages Glossators mastered very effective methods in this sense, creating conditions for the market economy to flourish.

They introduced secular, not ecclesiastical, education, influencing legal practice and ways of administration. As noted by Robison<sup>23</sup>, such researchers were not poets or alienated philosophers. As he mentions, "it is false to suggest that the glossators had no interest in law in practice; Imerinus himself acted as judicial assessor, and also as an envoy to the Emperor Henry V on the death of Countess Matilda, while in 1118 he was in Rome taking a prominent part in the election of an anti-pope in the imperial interest".

Noting the importance of the Glossator's inspiration on today's unification and harmonisation practice, it is recognised that they "founded a science of law, in the sense of a framework of judicial concepts which made it possible to provide rational legal solutions to conflicts of interests in society in place of solutions based on custom or mere force. The offered law as a self-conscious structure, an ordering instrument for society, and this on a European scale"<sup>24</sup>.

As reminded by Arnaud<sup>25</sup>, in times of deep changes and economic reorganisation, the importance of the legal masters was extreme. They were assigned the power of keeping knowledge and tradition. Based in ancient texts, written in much different times, these scholars commented and adapted documented laws, word by word, to a new era. This has been notably done in relation to property holding and trade, originating fundamental concepts of the law merchant and simplifying formulas, providing certainty and uniformity of interpretation for the movement of goods, until they reach their final destination.

Today we face a quite similar process, performed by unexpected hands. The process of contractualisation of international trade law is a fact experienced by the worldwide adoption of standardised contracts, imposed for entering certain types of transactions. Codes of conduct and market practices are well accepted sources of international trade law, and they have been the basis of the new financial services liberalisation architecture.

Contracts have become law within the global arena<sup>26</sup>. Legal unification under

<sup>23</sup> Robison, OF et al. *European Legal History*, Third Edition: Butterworths, London: 2000, p. 43.

<sup>24</sup> Robison, OF. *Op. Cit.* p. 44.

<sup>25</sup> Arnaud, André-Jean. *O Direito entre Modernidade e Globalização*. Renovar, Rio de Janeiro: 1999, p. 63.  
 Cette extension de la normalisation contractuelle trouve sa cause dans le phénomène de la déréglementation des marchés et dans l'impuissance des États à réglementer des marchés immatériels. Comme l'écrit Mme Delmas-Marty, « loin de réduire la part du droit, la déréglementation marque seulement l'apparition d'un nouveau processus d'engendrement des normes fondé sur l'affaiblissement du principe hiérarchique. C'est cet affaiblissement qui entraîne le recul de l'État au profit d'un marché sans frontières, dont il semble que le véritable pilier soit le contrat ». Ainsi, se profile l'émergence « d'une société de contrats au lieu et place d'une société réglementée ». Loquin, Eric et al. *La volonté des opérateurs vecteur d'un droit mondialisé*, in Loquin, Eric et al. *La mondialisation du droit*. Litec-Credimi, Dijon, 2000, p. 93.

this scheme avoids conflicts of laws, praising the freedom of contract in search of absence of public intervention within private conventions.

The financial markets are already unified, by means of contractual instruments and products. As noted by Lalive<sup>27</sup>, scientific and technical development, easy communication, demand for quick decisions, all this generates a demand for new formulas. These ones are transformed in professional usage at specific activities, in type- or model-agreements, before being codified by some trade association or public bodies.

The lex mercatoria phenomenon has been exacerbated by the deregulation wave of the 1990's, with profound effects within the financial services industry. During such time, liquidity has sharply risen due to the creation of modern financial schemes like swaps and derivatives, which increased the distance between the real economy and the imaginative artificial – or synthetic – economy, composed of indexes and futures.

The International Swaps and Derivatives Association (ISDA) is a good example of a lex mercatoria originator, with regards to the financial services industry. ISDA represents participants in the privately negotiated derivatives industry, being the largest global financial trade association, by number of member firms<sup>28</sup>. Having introduced new methods of trading, the derivatives came to light for over the counter transactions, an imaginative way to escape, at its creation time, some regulatory constraints for banks, primarily in OECD countries. Such creativity demanded public oversight and, although privately traded, derivatives soon came to supervisors' attention, causing extensive regulation<sup>29</sup> to be introduced, with full cooperation with ISDA and financial markets players.

Bond issues (international debt instruments) and global bank facilities (loans), including those generated in multilateral institutions, such as the World Bank, follow the same contractualist rationale, not giving much room of manoeuvre to borrowers. Despite national regulation, freedom of contract and mandatory waiver of immunity clauses in contract terms, by repetition, are turned into effective law, shaping the financial services sector.

When re-regulation of the markets turned to be urgent and necessary, due to

<sup>27</sup> Apud Loquin, Eric et al. *La volonté des opérateurs vecteur d'un droit mondialisé en La mondialisation du droit*. Litec-Credimi, Dijon, 2000, p. 92.

<sup>28</sup> <http://www.isda.org>

<sup>29</sup> After Bering's failure, regulatory agencies from 16 countries responsible for supervising futures markets draw on the consequences for regulation regarding increase in traded volumes especially derivatives, more and more inter-dependents, having decided to: (i) establish cooperation between market authorities for information exchange on most important players, their risk exposure and market presence; (ii) position protection (margins) and client receivables becoming more coherent between different markets and countries limiting losses of order givers if an intermediary fails, (iii) intermediary failure, especially sound conducts for handling positions, rapid information exchange between regulators in case of failure and isolation of problem within failed member country, (iv) practical cooperation methods in case of urgencies (contingency plans).



the late perception of high exposures to risks demonstrated in bank crisis<sup>30</sup> and bankrupt nations, a set of rules was already in place. The industry prevented politicians, central bankers and regulatory bodies from having the burden of drafting some new market architecture, differently from the 1930's. Using consecrated formulas as basic inspiration for regulating financial services, within national borders and in the international arena, has been a normal and effective practice.

Private initiatives like the Core Principles for Effective Banking Supervision formulated by the Basel Committee<sup>31</sup> for Banking Supervision, the Objectives and Principles of Securities Regulation formulated by the International Organization of Securities Commissions (IOSCO), and standards developed by the Committee on Payment and Settlement Systems (CPSS), the International Association of Insurance Supervisors (IAIS), and the International Accounting Standards Committee (IASC), are examples of market agents that act closely, influencing governments in a decisive manner.

Considerations on the unification of financial practices and market regulation aiming at restructuring this industry necessarily leads to the International Monetary Fund's (IMF) raison d'être. The IMF, as well as the World Bank, has played a substantial role in helping regulation converge and enhancing market discipline, especially in less developed countries. This work has not prevented the IMF from suffering harsh criticism regarding ready formulas and biased political choices, being accused of fostering moral hazard<sup>32</sup>. OECD's influence in the world's financial liberalisation architecture<sup>33</sup> has also been extremely relevant, serving as an inspiration for multilateral bodies<sup>34</sup>.

Despite many sad stories, it is highly positive that "the unification of law is sought to be achieved through the use of international institutions specifically intended to promote the unification of law. Programs of international organisations

<sup>30</sup> In response to BCCI's collapse, the Basel Committee on Banking Supervision (G-12) established stronger Minimum Standards: (i) All international banks should be capably supervised by a home country authority with consolidated accounting; (ii) Host countries should impose restrictive measures on unsound operations in their territories that are not well supervised. Thus, home and host countries should make effective arrangements to prevent other failures like BCCI. In this way prudential practices can be improved for banking in the global marketplace.

<sup>31</sup> Members are Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Spain, Sweden, Switzerland, United Kingdom and the United States of America.

<sup>32</sup> In standard market economies, if a lender makes a bad loan, he bears the consequence. The borrower may well go into bankruptcy, and countries have laws on how such bankruptcies should be worked out. This is the way market economies are supposed to work. Instead, repeatedly, the IMF programs provide funds for governments to bail out Western creditors. The creditors, anticipating an IMF bailout, have weakened incentives to ensure that the borrowers will be able to repay. This is the infamous moral hazard problem well known in the insurance industry and, now, in economics. Insurance reduces your incentive to take care, to be prudent. A bailout in the event of a crisis is like "free" insurance. Stiglitz, Joseph E. Globalization and its discontents. W.W. Norton & Company, New York, 2003, p. 201.

<sup>33</sup> Les bases de la libéralisation du commerce des services sont posées dans certains codes de l'OCDE (le Code de la libération des opérations invisibles courantes, le Code de la libération des mouvements de capitaux) ou encore dans l'instrument relatif au traitement national. Ciabrin, Sylvie. Les services dans le commerce international. Presses Universitaires de France, Paris, 1996, p. 9.

with broader objectives also frequently seek to generalise or standardise legal rules and practices, for example, in the European Community<sup>35</sup>. Although democratic deficits still persist in some multilateral and regional arenas, convergence programs have largely succeeded in enhancing regulatory standards and savings protection.

Financial regulation has experienced cyclic and successive phases, from protection, de-regulation (thus creating conditions for a freer market, disintermediation and transaction cost reduction, increase in investment banking activity), competition increase, re-regulation (mainly in prudential and supervisory areas), excess capacity (high communication costs) to consolidation.

When too much market freedom proved to weaken a brand new global financial arena - at the sake of several economic set-backs, which caused fears of a possible re-edition of 1929's economic crisis - discussions on multilateral liberalisation of financial services within the WTO and the need to establish new supervisory rules in high levelled fora, once again, searched for market inspiration.

Hence, two financial services regulation levels have become evident. One related to a set of transactions (international private law) and another related to international and domestic public order (international and domestic public law). Revolving doors policy, enabling professionals to switch from public to private practice, has also - when bad faith was absent - enabled better and market tuned regulation.

Today's scenario is composed of products offered within the financial services industry which are most standardised. Banks, securities and insurance firms adopt very similar product structures, with almost imperceptible variations, backed by commercial laws and in the principle of freedom of contract. Such products are sold worldwide, this contractualisation of the sectors serving as a safety net, ensuring a real unification of rules, turning them into stone. These become sources of international financial law (via a *lex mercatoria* rationale), and although they present some variations in different countries, economies of scale are securely achieved and, most of the time, shared with customers, by means of the reduction of transaction costs.

Self-regulation has been the moto of financial services for a long period of time, and until very recently the industry regulated and supervised itself. As increasing savings remains the principal goal in our economy society (as true *homos economicus*), as they finance not only consumption, but also investments, research and welfare, public intervention in times of high powered money and

<sup>34</sup> A very interesting discussion on this topic was launched in March 2000's Alan Meltzer's report for the US Congress International Financial Institution Advisory Commission. The work aimed at reporting on the future role and responsibilities of international institutions, including the IMF, World Bank, the African, Asian and Inter-American Development Banks, the European Bank for Reconstruction and Development, the Bank for International Settlements and the World Trade Organisation. The report has been formally republished by the US Department of the Treasury.

<sup>35</sup> De Cruz, Peter. Op. Cit. P. 485.

global transactions cannot be neglected.

Not so well organised as financial services players, and having different goals in time and in scope, nations – representing populations – are demanded to deal with the global services phenomenon in different regulatory levels. Apart from the unification performed as necessary by market agents, states are obliged to respect their very own needs with regards to international inclusion, as well as their internal welfare generation capacity. In this sense, cross-sectoral convergence (banking, securities and insurance sectors) in market practice and in regulatory approaches has been occurring quite naturally<sup>36</sup>.

Harmonisation of rules have become, besides unification implemented by the market, an acceptable answer to address the complex and ever growing financial services industry. As a matter of fact, concentration in the financial services industry, as a result of a globalised economy, has somehow eased the task of regulators, in the same way that Glossators have, in the Guild Age, identified commercial common grounds.

Searching for inspiration at international fora, looking for alternatives in multilateral organisations and private associations, as well as borrowing concepts from other systems, are the most common forms of legal change. De Cruz reminds us, however, that “transplantations may or may not be ‘successful’, depending on a country’s particular conditions for receptivity”<sup>37</sup>.

#### International Financial Services Law

Regulation of financial services relates to the structure, conduct (with impacts on price) and operation (also called prudential). Barriers for financial services liberalisation are regulatory, fiscal, structural and cultural (in the way that states are involved). Usury, gaming and gambling<sup>38</sup> laws severely affect such sector, and also consumer, banking, insurance and tax laws, as well as exchange controls.

Trade in financial services also present different forms<sup>39</sup>, entailing the transfer of information, the movement from supplier towards clients and vice versa, clients moving towards suppliers. Regulation must take into account that information

<sup>36</sup> See the Core Principle Liaison Group report at the Basel Committee on Banking Supervision.

<sup>37</sup> De Cruz, Peter. Op. Cit. p. 486. See also Stiglitz on failed initiatives of regulation transposition, op. Cit.

<sup>38</sup> In the case of derivatives 1916’s Brazilian Civil Code caused derivative transactions to be classified as forbidden non-collectable gambling. The 2001 civil code reform introduced article 816, a result from the industry’s claim for giving legal certainty to this kind of transaction.

<sup>39</sup> GATS defines four ways (or “modes”) of trading services in general: services supplied from one country to another (e.g. international telephone calls), officially known as “cross-border supply” (in WTO jargon, “mode 1”); consumers or firms making use of a service in another country (e.g. tourism), officially “consumption abroad” (“mode 2”); a foreign company setting up subsidiaries or branches to provide services in another country (e.g. foreign banks setting up operations in a country), officially “commercial presence” (“mode 3”), and individuals travelling from their own country to supply services in another (e.g. fashion models or consultants), officially “presence of natural persons” (“mode 4”).

<sup>40</sup> <http://www.imf.org/external/np/mae/mfr/code/index.htm#>

asymmetry is a fact, which affects the nature of the financial business environment. Not all participants have the same quality assessment, which generates quality deterioration, adverse selection, market failure and political constraints.

The IMF has laid down a code on Transparency in Monetary and Financial Policies, which was adopted by the interim committee in Sept 26, 1999<sup>40</sup>. Aiming at strengthening the architecture of the international monetary and financial system, the IMF was called to develop a code of transparency practices for monetary and financial policies, in cooperation with appropriate institutions. The Fund, working together with the Bank for International Settlements, where the Basel Committee on Banking Supervision, and in consultation with a representative group of central banks, financial agencies, other relevant international and regional organizations, and selected academic experts, has developed a Code of Good Practices on Transparency in Monetary and Financial Policies.

The main goal of this unified action was to unify financial services treatment. As stated in the code, “transparency by financial agencies, particularly in clarifying their objectives, should also contribute to policy effectiveness by enabling financial market participants to assess better the context of financial policies, thereby reducing uncertainty in the decision-making of market participants. Moreover, by enabling market participants and the general public to understand and evaluate financial policies, transparency is likely to be conducive to good policy-making”.

The justification for such unified strategy has been helping “to promote financial as well as systemic stability. Transparent descriptions of the policy formulation process provide the public with an understanding of the rules of the game. The release of adequate information to the public on the activities of financial agencies provides an additional mechanism for enhancing the credibility of their actions. There may also be circumstances when public accountability of decisions by financial agencies can reduce the potential for moral hazard.”

As stressed by the working group, transparency in the financial services industry is indicated in order to avoid market disruptions. In this sense, “with regard to informing the public about monetary and financial institutions and their policies, an important issue concerns the modalities that these public disclosures should take. In particular with regard to monetary policy, should transparency practices have a legislative basis in a central bank law, or be based in other legislation or regulation, or be adopted through other means? The Code takes a pragmatic approach to this issue and recognizes that a variety of arrangements can lead to good transparency practices. On matters pertaining to the roles, responsibilities, and objectives of central banks (and for principal financial regulatory agencies), it recommends that key features be specified in the authorizing legislation (e.g., a central bank law). Specifying some of these practices in legislation gives them particular

In a globalised world populations are faced with the dilemma of being global citizens or global consumers<sup>41</sup>. Information technology has imposed flexibility on all societies, forcing them to adapt to a new environment, immaterialised such as in financial services. It is a current say that rigid economies and societies – be it in regulation, negotiating methods, moral habits permeated by religion – may not survive, or may remain *parias*.

Financial services treatment and liberalisation cause worries about managing wealth, making it easily movable. Recent trends confirm the option towards unilateral or bilateral, instead of multilateral, decisions taken mainly by industrialised nations, the US in the forefront.

As Stiglitz<sup>42</sup> has well clarified, “globalisation has meant that there is increasing recognition of arenas where impacts are global. It is in these arenas where global collective action is required – and systems of global governance are essential. (...) The most fundamental change that is required to make globalisation work in the way that it should is a change in governance”.

On the other hand, in a global economy market participants become gradually intolerant to regulatory disparities. Home countries undertake market players’ sides, helping shape policies aimed at attaining only profit-increasing, short-termed, objectives. This generates a strong movement towards maintaining self regulation afoot, in detriment of genuine public intervention for defending public interest.

If the world community cannot escape globalisation – which it should not – it surely can shape it.

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prominence and avoids ad hoc and frequent changes to these important aspects of the operations of central banks and relevant financial agencies. Information about other transparency aspects, such as how policy is formulated and implemented and the provision of information, can be presented in a more flexible manner. However, it is important that such information be readily accessible, so that the public can with reasonable effort obtain and assimilate the information.<sup>43</sup>

Positively put, it is important to clarify the role of transparency, not being “an end in itself”, nor “a substitute for pursuing sound policies; rather, transparency and sound policies are better seen as complements”. Transparency, however, is always a pre-condition in democracies, and is most recommended in services liberalization, working both ways (public to private and vice versa), reducing information asymmetry.

Trade in services is extensively treated in GATS, WTO’s members having endorsed<sup>44</sup> fundamental principles, i.e. the right to regulate and to introduce new regulations on the supply of services in pursuit of national policy objectives; their right to specify which services they wish to open to foreign suppliers and under which conditions; and the overarching principle of flexibility for developing and least-developed countries. In this sense, the guidelines remained sensitive to public policy concerns in important sectors such as health-care, public education and cultural industries, while stressing the importance of liberalization in general, and ensuring foreign service providers have effective access to domestic markets.

The WTO way of inducing regulation however, leads to overcoming national interest. Having recognised that domestic regulations are the most significant means of exercising influence or control over services trade, WTO agreement say governments should regulate services reasonably, objectively and impartially, however when a government makes an administrative decision that affects a service, it should also provide an impartial means for reviewing the decision, e.g. the judiciary.

Despite the de- and re-regulation movements of the past two decades, today it is widely accepted, especially with GATS that commitments to liberalise do not affect governments’ right to set levels of quality, safety, or price, or to introduce regulations to pursue any other policy objective they see fit.

<sup>41</sup> La déclaration ministérielle de Punta del Este insiste sur le fait qu’un cadre multilatéral de principes et de règles pour le commerce des services devra respecter les objectifs politiques des lois et des réglementations nationales applicables aux services. Pour comprendre cette logique, il ne faut pas perdre de vue que les réglementations nationales du secteur des services relèvent du droit souverain des gouvernements, en particulier lorsque celles-ci visent à réalisation d’objectifs de politique nationale. Ciabrini, Sylvie. Les services dans le commerce international. Presses Universitaires de France, Paris, 1996, p. 10

<sup>42</sup> Le comportement de l’électeur semble rapprocher de plus en plus celui du consommateur. Ses choix politiques sont de plus en plus individuels et personnels, de moins en moins dictés par des préoccupations collectives ou d’intérêt général. Auberger, Philippe. La démocratie à l’épreuve des marchés. *Economica*, Paris, 2003, p. 169.

<sup>43</sup> Op. Cit. Pages 223 to 226.