Espaço Discente

LAW AND FINANCIAL MARKETS: THE ROLE OF FINANCIAL STABILITY BOARD TO DESIGN A LEGAL FRAMEWORK FOR THE GOVERNANCE OF THE GLOBAL FINANCIAL SYSTEM[1]

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1. Introduction

The purpose of this work is to develop the theoretical analysis about the law as mechanism of design of markets upon a case study on the international financial regulation, focusing the role of the Financial Stability Board (FSB). In view of such analysis, I will develop two different arguments, one related to its structure and another to its function. Firstly, the institutional design of FSB reflects the changes in balance of powers and consequently the global governance verified in the last decade. The second one is that the effectiveness of FSB's activities is challenged by the tension between its mission towards convergence of legal rules on financial regulation and supervision among several jurisdictions and, on the other side, the recognition of legal differences across the jurisdictions due their specific circumstances.

This work departs from the basic assumption that the law is an essential tool for shaping and provision of stability of markets in a capitalist economic system. Such approach is shared by the most diverse academic movements throughout the ideological spectrum, from the Law and Economics movement to more developmental (interventionist) traditions. The regulation of the financial system is therefore presented as a powerful example of the correctness of this assumption.

The expansion of the global markets and the internationalization of financial markets and the consequent systemic risks created a worldwide space that needs convergence towards macro prudential rules upon

1. I am grateful to my friends Pedro Schilling and Spencer Cooney for early discussions and language review, respectively. All errors are my sole responsibility.

legal reforms in order to avoid possible a race to the bottom by jurisdictions regarding regulatory matters to attract investors. To deal with such problems, the ministries of finance and senior officials of financial and capital markets regulators and supervisors from the major economies met in 2009 for the establishment of FSB.

Regarding the structure of FSB, the first argument to be developed here is that it may represent a new paradigm of global governance on law of markets. Different from FSF, the membership of FSB comprises not only a group regarded as the "developed" capitalist countries such as USA, Japan and EU members, but also a broader group of countries including emerging economies. In other words, this structural change means that the concept of global governance today is different from what it was in the decade of 1990 and the first years of the 2000's when the dominant view was that developed countries (a very narrow and select group – the G7) should lead the establishment of international legal and regulatory standards to be followed by the underdeveloped countries as receipt for growth. It explains why FSB has a more heterogeneous composition than FSF and the emphasis given by FSB in the diversity of institutional arrangements for financial regulation due to very specific regional circumstances instead of the one-size-fits-all model.

The second argument is more concerned with the function of FSB. FSB has the challenging task to reconcile two opposite approaches: it shall provide an international convergence of law (regulation and supervision) in order to avoid systemic risks and to combat regulatory arbitrage at the same time it also needs to deal with different law regimes arisen from specific circumstances of each financial system or region. As already emphasized above, the convergence of regulation is necessary because the interconnectedness of the financial system poses unique systemic risks that, despite the fact that their origin is limited to one country due to regulatory failures, they can spread into other countries, producing catastrophic outcomes for the international economy as a whole.

Apart from these arguments, the role and the circumstances around the creation of FSB also represents a problem to the classic theoretical models by which the law only may be understood as an exclusive product of the will of the sovereign – the state. The efforts of the main economies of the world to build an international legal framework for the financial markets through the convergence of regulatory and supervisory standards to avoid systemic crisis is the recognition of the interdependence of several jurisdictions for the effectiveness of the domestic laws.

This work will structured as follows: (i) an introductory theoretical discussion on the role of law in the design of markets; (ii) the importance of a worldwide governance of the financial system and what is the FSB; (iii) the analysis of the first argument regarding the structure of FSB regarding the new paradigm of global governance facing the needs for a multi-jurisdictional and more inclusive effort to deal with financial systemic risk; and (iv) the analysis of the second argument regarding the function of FSB in the performance, at the same time, of the tasks of legal convergence and the understanding of regional legal divergences (through its Regional Consultative Groups) when performing its role towards soundness, transparency, resilience and development of the financial system worldwide.

2. Law as the designer of the Markets

Law is an essential tool for the shaping the markets because it defines the basic framework for their very existence: it defines and limits the property rights, freedom of contracting, inheritance rules, and institutions such as courts, police systems for

protection of property and security and so on. In a more specific level, it also can be said that law sets forth the conditions for access to the markets, mandatory form and the of the contracts, what can and what cannot be traded, requisites for enforceability, judicial and extrajudicial restructuring, bankruptcy, dissolution and winding-up of companies and insolvency procedures for individuals.

While prominent market players call for a retreat of the state intervention in the markets, it is necessary that a huge state apparatus set forth by law can provide some correction of market failures in order to provide a good and efficient market structure to stand. This conclusion is supported by Rodrik (2011) when it tested the research originally carried out by the political scientist David Cameron in which the latter concluded that the openness of the international trade was a major contributor for the expansion of the public sector in developed economies in the decades after the World War II.[2]

Rodrik broadened the scope of the Cameron's research including developing economies and several another analytical variables for example, country size, geography, demography, income level, urbanization and drawn same conclusion. The most interesting argument of Rodrik arisen from this empirical research is that the expansion of the governments is necessary to preserve the legitimacy of the markets by protecting people from the risks and insecurities markets bring with them.[3]

It is necessary to point out the Law and Finance movement in the economic literature that became prominent in the last two decades of the 20th century. Upon several empirical researches, the main academics of Law and Finance found a strong correlation between economic development and a legal system sufficiently strong to protect the rights of investors – the common law usually identified as such a "model to be followed" legal system as opposed to civil law.[4]

This literature became so influent that motivated the creation of the project Doing Business of the World Bank in 2003. The quality of the legal system for the financial development then became a major issue for the discussions inside the World Bank for legal reforms of developing countries. An academic discussion about the more or less protection of the investment and consequently the design of markets took concrete consequences when reforms for the improvement of quality of the legal system were transformed as a pre-requisite for concession of financing by the Bretton-Woods organizations, namely the International Monetary Fund and the World Bank.[5]

Although the role of law is recognized across the entire ideological spectrum as essential for the maintenance of the capitalist market economy, the very definition about what is the meaning of "law" remains a matter of heated debates. For example, for the legal positivism movement the law is essentially a product of the state, notwithstanding any moral concerns.[6] On the other side, the

2. Dani Rodrik, *The Globalization Paradox: Democracy and Future of the World Economy*, New York, London, W&W Norton & Company, 2011, pp. 17-19.

3. Idem, ibidem.

4. Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer, Robert W. Vishny, "Legal Determinants of External Finance", *The Journal of Finance*, vol. LII, n. 3, July 1997. Available in *http://scholar.harvard.edu/shleifer/files/legaldeterminants.pdf*. Access on May 31st, 2015.

5. Emerson Fabiani, *Direito e Crédito Bancário no Brasil*, São Paulo, Saraiva, 2011, pp. 53-54. For the evidence of the impact that the Law and Finance movement had in the legal reforms agenda of Brazilian government, see: Brazil, *Reformas Microeconômicas e Crescimento de Longo Prazo*, Brasilia, Ministério da Fazenda, December 2004.

6. For example, Hart understands law as the union of what he calls "primary" and "secondary" rules: "If we stand back and consider the structure which has resulted from the combination of primary rules of obligation with the secondary rules of recognition, change and adjudication, it is plain that we have here not only the heart of a legal system, but a most powerful tool for the analysis

tradition of the natural law, according to Finnis (2011), requires that moral principles and rules as a matter of objective reasonableness should guide the positing of law.[7]

While it is important to emphasize that even the concept of law is a long-standing dispute among the several academic traditions, from the positivism and naturalism to legal anthropology, for the purposes of this article, I use here a functional and more pragmatic approach of the concept of law. "Law" as used here includes written rules issued by competent authorities (from the parliament to the regulatory agencies), judicial decisions and enforceable contracts. All of these rules have direct influence in the pattern of behaviour of the economic agents, in the social and economic development and in the prevention of major political and social disruptions.

The financial regulation provides a powerful example of the influence of the law in the design of the structure of the market. The implications of such rules affect not only the banking or the financial sector but also all other markets, since the financial system, especially the banks, is the main important mechanism to solve problems of information asymmetry between investors and entrepreneurs. In this sense, it is used as a tool for the funding of the productive sectors of the society and therefore the fostering of social and economic development.

For example, a rule issued by the financial regulator or the monetary authority on compulsory reserve requirements for banks may affect the amount of money they can lend and consequently the interest rates. With a higher interest rate, the willingness of entrepreneurs to finance expansion of facilities, investments in innovation or the access to a new market (in both special and product dimensions) will disappear or be postponed. Several rules on the banking sector and capital markets provide incentives for housing, industrial and infrastructure financing.

Additionally to these indirect impacts, it is part of the purpose of the financial regulation to address concerns about the stability of the financial economic system and the overall macroeconomic policy since it has a significant influence in the size of the monetary availability in the society. Rules on minimum capitalization, limits on leverage and concentration of risks per borrower, foreign capital, requirements for provision of charters (nationalization, prior approval of amendment to by-laws and elections of directors), conservatorship, receivership and contributions for the systems of deposit insurance, are measures that not only aim to avoid big social disruptions due to a systemic failure of the financial system but also constitutes barriers to entrance of new players in the financial markets.

The complexity of financial regulation and the limits to the access due to concerns of stability may result in a highly concentrated market. Otherwise, the lax of such requirements is often used by the financial authority for specific purposes of public policies and may result in an increase of available funds to provide stimuli for the economic activity,

of much that has puzzled both the jurist and the political theorist" (Herbert L. A. Hart, *The Concept of Law*, 2nd ed., Oxford, Oxford University Press, 1961, p. 98).

7. "Rather, the concern of the tradition, as of this chapter, has been to show that the act of 'positing' law (whether judicially or legislatively or otherwise) is an act which can and should be guided by 'moral' principles and rules; that those moral norms are a matter of objective reasonableness, not of whim, convention, or mere 'decision'; and that those same moral norms justify (a) the very institution of positive law, (b) the main institutions, techniques, and modalities within that institution (*e.g.* separation of powers), and (c) the main institutions regulated and sustained by law (*e.g.* government, contract, property, marriage, and criminal liability). What truly characterizes the tradition is that it is not content merely to observe the historical or sociological fact that 'morality' thus affects 'law', but instead seeks to determine what the requirements of practical reasonableness really are, so as to afford a rational basis for the activities of legislators, judges, and citizens" (John Finnis, *Natural Law and Natural Rights*, Oxford, Oxford University Press, 2011, p. 290).

notwithstanding the risks it may bring.[8] It is therefore evident that the theoretical assumption presented in the beginning of this part, that the law plays an essential role in the design of the markets has been proved true, especially in the case of financial regulation.[9]

3. The Role of Financial Stability Board

In the last three decades, the interconnectedness of the financial systems at the global level became more and more intensive. The progress in information's technologies, financial innovations, deregulation of the financial markets and the openness of the global markets upon legal reforms promoted after the end of the Cold war that fostered trade and investment, may be appointed as essential factors that contributed for such changes.

These factors did not only increased the trade and the access to resources by private and companies across the world for consumption and investment but also created a potential for the spread of financial crisis to several countries. Although several downturns have shaken the world's economy along the last centuries, the recognition of the need of joint-efforts by multiple jurisdictions to design an international legal framework for the soundness, transparency and resilience of the financial activities is a recent phenomenon.

The financial crisis of 2008-2009 arose in a very specific and geographic-limited background: the real estate market in the United States. Several factors contributed to the so-called "subprime crisis", many of them requiring a huge legislative work. For example, the liberalization of the over-the counter derivatives markets by the Commodities Futures Modernization Act in 2000 and the progressive dismantle of the Glass-Steagall Act, a law enacted after the Great Depression of 1929, which provided the mandatory separation of activities of investment from commercial banking, reaching its peak with the enactment of the Gramm-Leach-Bliley Act in 1999.

The sophisticated mechanisms of risk transfer of subprime credits from lenders to investors around the world by securitization and derivatives trading resulted in the deterioration of balance sheets of several major institutional investors, failures of a big number and companies and spending of huge amount of taxpayers' resources to rescue too-big-to-fail institutions.

This spillover of the economic crisis across the world lead the governments of the members of the Group of Twenty (G20) to establish a permanent institution to shape an international legal framework to deal with the global systemic risk posed by the financial system through convergence of internal laws.[10]

8. For example, one measure that may be classified both as macroeconomic measure and tool for stability of financial institution is the requirement of maintenance of deposits of certain amounts of money with an account with the Central Bank. In Brazil, this is called "*depósito compulsório*". Several rules were enacted by the Central Bank in moments of low levels of investment reducing the required levels of *depósito compulsório* by financial institutions in order to foster the economy or specific sectors. For example, *Resolução* n. 4.411, of May 28, 2015 of the National Monetary Council (CMN) and *Circular* n. 3.755, of May 28, 2015 of the Central Bank of Brazil.

9. "It is now clear that the elements of economic life – capital, labor, credit, money, liquidity – are creatures of law. The same can be said for the elements of political life – power and right. Law not only regulates these things, it creates them. The history of political and economic life is therefore also a history of institutions and laws. Law constitutes the actors, places them in structures, and helps set the terms for their interaction". David Kennedy, "Law and the Political Economy of the World", in *Leiden Journal of International Law*, 2013, 26, p. 8.

10. Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, South Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, United Kingdom, United States and European Union comprise G20 membership.

Thus, the Financial Stability Board (FSB) was established on April 2009 not by an international treaty signed by its member nations, but as a non-profit organization incorporated under the laws of Switzerland in accordance with the Articles of Association.

The Article 1 of this Charter provides that the purpose of FSB is to:

> (...) coordinate at the international level the work of national financial authorities and international standard setting bodies (SSBs) in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies. In collaboration with the international financial institutions, the FSB will address vulnerabilities affecting financial systems in the interest of global financial stability.[11]

FSB is the immediate successor of the Financial Stability Forum (FSF), a forum of discussions among high officers of central banks, regulatory and supervisory authorities of the Group of Seven (G-7), which comprised the seven most industrialized countries in the world. According to Arner & Taylor (2009), the FSF was established with a threefold purpose: (i) promote financial stability; (ii) improve the functioning of the markets; and (iii) reduce systemic risk through enhanced information exchange and international cooperation in financial market supervision and exchange.[12]

In order to have a most effective role in the convergence of regulatory standards, the Article 10 of FSB's Charter requires that high-level representation at its most important body of governance, the Plenary. Therefore, representatives only may be accepted if the post they hold is the level of central bank governor or immediate deputy, head or immediate deputy of the main supervisory/regulatory agency, and deputy finance minister or deputy head of finance ministry.

The governance of FSB is not limited to states. The Plenary representatives also shall include the chairs of the main international standard setting bodies and committees of central bank experts, and high-level representatives of IMF, World Bank, Bank for International Settlements (BIS) and the Organization for Economic Co-operation and Development.[13]

4. From FSF to FSB: towards a new paradigm of global governance

The Asian Financial Crisis of 1997-1998 was the milestone for the creation of G20. The most important factor for this crisis was the repeal of the system of fixed exchange rate by Thailand and its replacement for a system of floated exchange rate. The result was a speculative attack on the Thai currency (baht) that then collapsed in June 1997.

11. *Financial Stability Board Charter*. Available in: *http://www.financialstabilityboard.org/wp-content/uploads/FSB-Charter-with-revised-Annex-FINAL.pdf*. Access on May 31st, 2015.

12. Douglas W. Arner, Michael W. Taylor, "The Global Financial Crisis and the Financial Stability Board: Hardening the Soft Law of International Financial Regulation?", in *AIIFL Working Paper* n. 6, June 2009, p. 6.

13. Financial Stability Board Charter, Article 10. Cutler explains the important role performed by standard-setting bodies: "However, new sources of law are emerging which do not emanate from public, state authority, but rather from privatized, non-state authority. Examples include legal norms emerging from the dominant legal practices and the contractual activities of transnational corporations and other professionals engaged in international commerce, including bankers, insurers, tax specialists and the like. Model codes, statements of principle, uniform rules for optional use in commercial contracting and standardized contracts increasingly form the core of transnational business practices. International trade, investment and finance are increasingly regulated by soft, porous, discretionary standards and procedures. This tendency is associated by many analysis with the increasing complexity of commercial transacting and the resulting enhanced significance of expert knowledge of the fields of law, accounting and taxation" (A. Cutler, *Private Power and Global Authority: Transnational Merchant Law in the Global Political Economy*, Cambridge, Cambridge University Press, 2003, pp. 22-23).

It made evident that even most advanced emerging markets could face problems due to vulnerability related to inflows and outflows of foreign investment.

The undermined trust in the robustness of emerging economies lead the world to a global crisis since it made difficult for several developing countries which at that time were undertaking legal reforms for the protection of investors (many of them unpopular) and sought the international lenders (debt issuance in foreign capital markets and rescue packages from international financial institutions) in order to adjust their fiscal situation.

Martinez-Diaz (2007) argues that one of major issues for the Asian Financial Crisis was the weak bank sectors of developing countries and risky private-sector borrowing practices. The domestics vulnerabilities could magnify and propagate the impact of financial crisis so that the rigid requirements for financial institutions set forth in the laws and regulations of developed countries would not be sufficient if the developing countries were still subject to a lax or weak regulatory framework or supervision.

The same author explains that:

> In a June 1999 report to their heads of state, the G-7 finance ministers explicitly rejected the creation of new international organizations and instead endorsed efforts 'to widen the ongoing dialogue on the international financial system to a broader range of countries'. Proposals for an Asian Monetary Fund were famously buried by strong US Treasury opposition.[14]

G20 was established on September 1999. While G7 still exists as a strong and powerful group that aims to voice the concerns of the developed countries, it was recognized that due to the dimension of the emerging economies such as China, India, Brazil and Russia would necessary to have them at the board to discuss and promote overall financial stability. The creation of G20 was directly the first step for the establishment of FSB as a more inclusive and institutionalized arrangement of transnational governance.[15]

It is necessary to point out that FSB was conceived not just as a forum of discussions or a center of study of the international financial stability but also as a tool for legal reform and convergence even though it was incorporated as a non-profit organization under the laws of Switzerland and not by a binding treaty signed by the member-states, which resulted in a more flexibility for the issuance and change of rules and guidelines.

Backer has drawn a similar conclusion regarding the role of FSB as model of the governance of the 21th century, even though he departs from a different analytical perspective regarding participation non-state actors.[16] Notwithstanding the important

14. Leonardo Martinez-Diaz, "The 20 after Eight Years: How Effective a Vehicle for Developing Country Influence?", in *Global Economy and Development Working Paper* n. 12, October 2007, p. 6.

15. FSB membership includes G20 plus Hong Kong SAR, the Netherlands, Singapore, Spain and Switzerland.

16. "Taken together, the emerging FSB construct suggests a new and curious form of transnational governance. It is hierarchical – designed to privilege the role of the state in its operation. This is particularly apparent in its emphasis on devising methods of taming autonomous private global economic actors through state-based or supranational regulation. But the governance apparatus is not controlled exclusively by states, nor directed solely at public governance. At its core, the FSB framework is cooperative, public, and supranational: states and non-state regulatory actors play a critical but secondary role. The FSB structure acknowledges the regulatory role of private transnational actors, mostly in the form of SSBs, yet also acknowledges the power of large private entities to act autonomously. Indeed, the focus on the disruptive power of the largest of these enterprises (at least in terms of global economic governance) suggests both an acknowledgement of their autonomy and an effort to subordinate them to public governance structures beyond the state" (p. 141). In the same perspective, According to Cutler: "However, new sources of law are emerging which do not emanate from public, state authority, but rather from privatized, nonstate authority. Examples include the legal norms emerging from the dominant legal practices and the contractual activities of transnational corporations and other professionals engaged in international commerce, including bankers, insurers, tax specialists, and the like. Model codes, statements of

participation of international financial institutions and standard setting bodies in providing technical expertise for dealing with regulatory matters, since the law enacting is mostly activity of the states for excellence, the argument developed here that a more inclusive global governance is the model for the future is strengthened by the fact that the major emerging countries like the Brazil and China have a big share of their economies held by the state sector.[17]

Considering that FSB has as an express aim to promote global reforms upon the closing of regulatory gaps – especially by political pressure in off-shore jurisdictions – and seeks for more tight prudential and systemic requirements for financial markets worldwide, it goes beyond the mere political discussion space and become an effective institution of global governance, provided that the law and the possibility of its enforcement may be regarded as one of the most important characteristics of the state power.

Although some authors have been raising doubts about if G20 is succeeding in promoting the interests of developing countries,[18] the inclusion of its members which are developing countries in a global governance body of the financial system with a strong character of law producer is very relevant because it represents a space where political struggles concerning the law on banking and financial regulation on the countries may be foreseen, debated and solved before a potential political and economic crisis.

In addition, the institutional learning that can be shared by a broader number of countries with their specific circumstances and crisis may be a powerful contribution for a most efficient management system of the financial system in domestic level of the fellow countries, which may result in the improvement of the law upon a better macro-prudential legal, regulatory and supervisory framework. This claim is strengthened due to the fact that the 2008 global financial crisis has shown that the borders between domestic and international global markets are indeed blurred.

5. Convergence in Divergence: the functional contradiction of FSB

The promotion of the global stability financial requires a joint effort and a strong commitment for all jurisdictions across the world to avoid regulatory gaps that may increase the vulnerability of overall economy. The so-called "regulatory arbitrage" may be used for some states to attract inflows of capital upon the lax of prudential and systemic requirements for financial institutions.

One of purposes of the FSB is to promote assessment of vulnerabilities and to produce regulatory standards to deal with such problems. For example, several reports have been issued by FSB related to the: shadow banking system – the activity of financial intermediation outside the ordinary banking system and therefore not subject tight regulation; credit rating agencies; systemically important banks, many of them with branches and subsidiaries in several countries – the lack of liquidity available in

principle, uniform rules for optional use in commercial contracting and standardized contracts increasingly form the core of transnational business practices" (Larry Catá Backer, "Private Actors and Public Governance Beyond the State: the Multinational Corporation, the Financial Stability Board and the Global Governance Order", in *Indiana Journal of Global Legal Studies*, vol. 17, 2011, pp. 22-23).

17. China state owned companies represent a huge portion of the country's GDP and in Brazil, the state-owned companies correspond to 25.1% of the average daily traded volume in the Sao Paulo Stock Exchange. *O Estado de S. Paulo*, "BM&F Bovespa quer governança mais rígida para estatais", April 2nd, 2015, Available in: *http://economia.estadao.com.br/noticias/geral,bmefbovespa-quer-governanca-mais-rigida-para-estatais,1662884*. Access on May 31st, 2015.

18. This argument is found in: Leonardo Martinez-Diaz, "The 20 after Eight Years: how Effective a Vehicle for Developing Country Influence?", in *Global Economy and Development Working Paper* n. 12, October 2007.

one country may be harmful for the funding of its subsidiaries or branches in another countries; more precise; resolution regimes for banks; supervision of OTC derivatives markets; and so on.

In this regard, the inclusion of the Bank of International Settlements (BIS) in FSB's structure may provide it with the necessary technical support to recommend legal reforms to deal with such matters. FSB receive funding and services support from BIS under an agreement entered into by both associations in 2013.[19] BIS has a long-standing experience regarding creation of prudential standards for the stability of the domestic financial systems, and the Basel Agreements are the foremost example in this sense.

There are four Standing Committees of FSB: (i) Assessment of Vulnerabilities; (ii) Supervisory and Regulatory Cooperation; (iii) Standards Implementation; and (iv) Budget and Resources. The first three Standing Committees are directly related to the purpose of FSB. In short, the Committee on Assessment of Vulnerabilities identifies the issues, the Committee on Supervisory and Regulatory Cooperation undertakes supervisory analysis and frames the regulatory and supervisory response to the issues, and the Committee on Standards Implementations monitors the implementation of agreed FSB's policy initiatives.

It is necessary to emphasize that the Standing Committees are just advisory bodies in the FSB's structure. The decision-making process is taken by the Plenary by consensus according to the Articles 4 and 6 of the Articles of Association of FSB. Notwithstanding this limited role, the Standing Committees have a strong power because they are responsible for the issuance of reports and supply of information for the decision-making process by the Plenary.

Although the importance of international convergence of regulatory standards is required for the global financial stability, it is not an easy task the law reforms towards a uniform framework for banking and other financial activities, such as insurance and capital markets. The specific structure of the financial market of each country due to historic reasons, public policy concerns, especially the participation of the state through state-owned banks, all of them have a strong influence in how it the regulation and the supervision of the financial system takes place.

In order to deal with such problems, the FSB created six regional consultative groups: (for the Americas, Asia, the Commonwealth of Independent States, Europe, the Middle East and North Africa, and Sub-Saharan Africa) to assess the regional vulnerabilities and to propose specific measures addressed at them. It is outside of the scope of this work to analyze in details the reports issued by FSB, especially the characteristics of the regional vulnerabilities. However, the conciliation of the tasks of to promote a uniform law and to recognize the particular situations of every jurisdiction involved remains very problematic.

For example, the main framework of current financial regulation in Brazil was built since the 80's to deal with specific problems faced by the Brazilian banks, for example, the use by state governors of state-owned banks for issuance of money, which resulted in specific insolvency regimes as for example, the RAET – *Regime de Administração Especial Temporária* (a conservatorship regime without suspension of the flow of payments by the banks); the unlimited liability of administrators and controlling shareholders; and incentives for the creation of big conglomerates in order to avoid financial distresses by the banks, even before the dismantle of Glass-Steagal in USA.[20] It explains why when Basel I was

19. Articles of Association of FSB, Article 7.

20. *PROER-Programa de Estímulo à Reestruturação e ao Fortalecimento do Sistema Financeiro Nacional* was a program of the Federal Government to

put in place, the prudential requirements of capital by the banks in Brazil were higher.

This concrete tension related to the transnational legal governance of financial system faced by FSB may illustrated a problem related to the overall international law as a whole. The difficulty of achieve a consensus for the financial regulation in the international level lead the countries of the Group of Twenty to choose a corporate structure for FSB without rigid and binding commitments instead of an international treaty.

Also, although widely recognized that the borders of the financial markets are blurred and due to this fact it is needed an international legal framework to deal with global vulnerabilities, the FSB faces a major difficult due to its own contradictory task of standardization of law and analysis of regional and country-level vulnerabilities that may spread across other jurisdictions. This is just a specific example about problems may be faced by the transnational legal governance in other fields such as international trade, human rights and environment.

6. Conclusion

Law is necessary for the existence and good working of the markets. This assumption has been proven true because law in a broad sense, including court decisions, legislative acts and regulations, defines the structure of the markets, conditions for access, how the companies shall be governed, what kind of products or services can be traded and several other conditions. The financial regulation is the most evident example of how law is decisive for not only the shaping of the markets but also to avoid social disruptions that may be caused by their imperfections.[21]

The financial crisis of 2008 has shown that an international financial market requires an international legal framework. The globalization made blurred the borders of the banking systems so that a domestic financial crisis may become global in a short period due to the interconnectedness of the financial sector, understood as comprising banks, insurance companies and capital markets players.

In view of the above, the major economies of the world established FSB in 2009 recognizing the need for a transnational and international governance of the financial system. Two remarks were developed here regarding the structure and function of FSB, respectively.

Regarding the first argument developed here related, it is important to highlight that FSB is the messiah for the aspirations of the developing countries in the international decision-making, but represents an important step towards a more inclusive structure of legal international governance as opposed to G7 due to the relative increase of the importance of developing countries in the global markets.

The second one is that the FSB illustrates a problem of the global governance because it needs to conciliate two opposite tasks: the uniformization of the law in an international level to deal with international problems at the same time that it needs to deal with regional and country-level vulnerabilities very specific according to the history and policy background of each region. This may represent a problem of effectiveness when it comes to perform its normative (or rule-making) activity.

stimulate mergers and acquisitions in the banking sector motivated by the assumption that may summarized as: "the bigger the stronger". It was transformed into law by the Provisional Measure n. 1.179 of November 3, 1995. The *Resolução* n. 1.524 of September 9, 1998 and the Accounting Plan of the Institutions of the Financial System (COSIF) in the same year permitted the consolidation of the so-called "multiple banks", with authorization to perform investment and commercial banking. Emerson Fabiani, *Direito e Crédito Bancário no Brasil*, São Paulo, Saraiva, 2011, p. 29.

21. For example, deposit insurance systems to avoid the panic caused by bank runs.

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