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Introduction to Cooperative Efforts in International Banking Regulation

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COOPERATIVE EFFORTS IN INTERNATIONAL BANKING REGULATION

The panel convened at 10:00 a.m., April 24, 1982, Cynthia C. Lichtenstein* presiding.

INTRODUCTORY REMARKS BY THE CHAIRWOMAN

The audience is familiar with the issues posed for the international community by the postwar burgeoning of multinational corporations. Perhaps because buying and selling money are invisible, the internationalization of the financial markets, and the role of multinational banks therein, has been less in the public eye, at least until the Iranian assets freeze in 1979. Lately, of course, there has been a good deal in the newspapers on the question of how and when Poland is to repay the 501 banking institutions from which it has borrowed money.

The newspapers for a time carried stories on issues of "default," or calling Poland in "default," but very few stories made clear what the issues were or why it might be a matter of interest to anyone but the banks and Poland. The truth of the matter is that today the public function of the circulation of the world's money is carried on by private actors, not by governments or by public international organizations. If these actors fail in any number—as U.S. banks closed en masse in 1933—it is the global economy that halts.

No country today permits internal "free banking"; all countries today treat dealing in money as a function too integral to the health of their domestic economies to allow unlicensed unsupervised persons to take deposits and relend them. The quantity and quality—and indeed theory—of banking regulation varies enormously from country to country, but all countries regulate to some extent banks' dealing in the domestic economy in the country's own currency. There is the point. Because the purpose of the regulation is to protect the domestic economy, very few countries in the past have concerned themselves much with what their banks do outside the country, particularly if the "off-shore" business is carried on through a subsidiary or joint venture rather than through a branch. Sometimes the domestic regulator did not regulate even onshore banking business if it was not denominated in the country's own currency. There are a number of explanations as to why London grew up as the chief center for international banking business denominated in dollars, but that the United Kingdom did not apply its former stringent system of exchange control to dollar accounts on the books of licensed banks must have helped.

In any event, banks that desired to deal in money on an international scale established branches or subsidiaries in London and began to trade in dollars, eventually carrying out that "recycling" of petrodollars you have heard about—and in the process creating an enormous, largely unregulated market—the Eurocurrency market, where sovereigns and multinationals borrow short and long term and the banks borrow daily from one another. London, of course, is no longer the only Eurocurrency center. As the business grew, so did the number of centers. The multinational banks will move offshore business to any jurisdiction that will remove regulatory impediments and costs: the Cayman Islands, Hong Kong, Singapore, and now New York City with its international banking facilities that are really "free zone" international banking.

Why do these "free zone" international banking centers matter? In the case of

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banks headquartered in the United States—or that come to the United States—there is still a considerable amount of regulatory oversight. But it is difficult for the most stringent authority to regulate its banks' foreign operations without impeding its banks' capacity to compete in these huge markets. So there is some push towards the lowest common denominator of regulation, to be the Delaware of international banking.

Again, this might not matter if banks could be allowed to fail when they were imprudent. But, as our panelists will describe, all the regulators are in the same boat, that of the extreme interdependence of the international and the domestic financial systems. If the separate national regulatory systems fail to work out a system of pulling together to supervise the international business, they may have only ruins of domestic systems to regulate. And they know it. So, quietly—quietly, because they don't want to worry the public by admitting why they must cooperate—the regulators have begun to talk about how they can deal with their common problem.

REMARKS BY PAUL L. LEE*

In the scheme of things I am to present some reflections on cooperative efforts in international banking regulation. As I reviewed the program, I wondered whether our panel would seem as topical as other panels. But I suppose that the Falkland/Malvinas crisis demonstrates anew that the international banking and payments system is particularly vulnerable to the risk of international events. Indeed, it must be clear even to the casual observer that the international banking system is increasingly being used as a conscious tool, a pressure point, a lever in the larger arena of international diplomacy and conflict resolution. I should like to return to these themes a little later. I mention them now only to demonstrate that the problems of regulating and administering the international banking and payments system are very live ones, indeed.

Let me turn to some more mundane questions of the basic infrastructure for the cooperative regulation of international banking; for, at least in part, the strength and flexibility of that infrastructure will tell us something of the capacity of the system to respond to shocks like that delivered by the Iranian freeze or like that which would be delivered by a default by Poland on its international bank borrowings.

I begin with the observation that the infrastructure for cooperation among international bank regulators is relatively rudimentary. The "internationalization" of the capital markets has in some instances outstripped the capacity of the regulators to monitor those markets. This is particularly true in the banking area and somewhat less true in the area of securities markets where, at least in this country, the level of regulation probably has slowed the natural progress of the internationalization of those markets. The growth of the Eurodollar market and the scale of lending to Third World borrowers and other international borrowers are matters beyond the reach of any one national regulator. Yet these are precisely the areas in which international cooperation among national regulators has been most difficult to obtain. The reasons are not difficult to discern. Indeed, for a group like this, seasoned observers of the international legal scene, what follows may seem axiomatic of the difficulties facing international cooperative efforts.

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