Making Rules for Global Finance: Transatlantic Regulatory Cooperation at the Turn of the Millennium

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Abstract This article explains a shift in the way transatlantic authorities managed conflicts over the cross-border regulation of securities markets: from cooperation skewed heavily toward the preferences of U.S. officials and accepted grudgingly by European counterparts; to a Euro-American regulatory condominium characterized by close interactions among decision makers and mutual accommodation. In the final decades of the twentieth century, the asymmetric influence wielded by U.S. securities market authorities had few parallels in other regulatory areas. Why, then, did U.S. officials become more accommodating and European authorities more influential, and why did the turning point occur in 2002 and 2003, an unlikely moment for intensified transatlantic sovereignty sharing? My study shows that institutional change inside the EU recast the North Atlantic balance of regulatory leverage and thereby was the primary factor behind the reshaping of transatlantic cooperation. Internal EU regulatory centralization changed the expectations of U.S. and European firms and authorities and generated new incentives in Washington, D.C., for accommodation and closer transatlantic coordination. My explanation differs from models that, accepting U.S. financial pre-eminence as a given, attribute variance in cross-border regulatory cooperation to factors such as incentives derived from the particularities of issue areas or preferences rooted in domestic politics. While resonating with a well-established theme from the realist branch of IPE, my findings have broad theoretical significance, and open new avenues for dialogue between realists and constructivists about the social, political, and institutional foundations of power in global economic affairs. The transatlantic political process set off by financial transformation in Europe reveals contemporary sources of systemic change and raises questions about what

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the EU's ascendance as a global financial regulator will mean in the aftermath of the late-2000s crisis.

American and European banks, insurance companies, asset managers, and other financial services firms have long competed in multiple jurisdictions with distinct and sometimes incompatible regulatory systems. Beginning in the 1990s, problems sparked by these regulatory differences stood at the center of many often-intense conflicts. This article explains a shift in the way transatlantic authorities managed them: from cooperation skewed heavily toward the preferences of U.S. officials and accepted grudgingly by European counterparts to a Euro-U.S. regulatory condominium characterized by close interactions among decision makers and mutual accommodation.

The transatlantic regulatory relationship is a central node of rulemaking for global economic activity.[1] In financial services before the late-2000s crisis, cross-Atlantic governance tended to set best practice in multilateral and other forums; relations between U.S. and European officials is thus a good measure of global financial rulemaking at the millennium's turn. This focus reflects the renewed scholarly interest in cross-border rules and standards determined outside the World Trade Organization (WTO),[2] but the regulation of finance is important in its own right. Decisions by financial services companies impinge strongly on overall economic growth and have far-reaching political and social implications, both domestically and internationally.[3]

The end-of-the-century turn in transatlantic financial regulatory cooperation presents two compelling empirical puzzles. First, the asymmetric influence wielded by U.S. financial authorities, especially those governing capital markets, had few parallels in other regulatory areas in the period, and the domestic regime they oversaw served as exemplar to the world.[4] Why, then, did U.S. officials become more accommodating and European authorities more influential? Second, transatlantic geopolitical relations were experiencing unusual stress during the run-up to the 2003 war with Iraq, and officials in the Bush administration were unlikely candidates for making compromises in conflicts concerning regulatory sovereignty. The 2002–2003 turning point, moreover, followed a period when U.S. capital markets had grown faster than European ones, contrary to a widely held assumption that market size determines who sets the rules.

To explain this change in transatlantic relations—who got the terms of access they wanted, who made concessions, and when—I compared the management of

1. See Drezner 2007; and Hamilton and Quinlan 2006.
2. See Newman 2008b; Singer 2007; Mattli and Büthe 2003; and Farrell 2003.
3. Zysman 1983.
4. On the creation of independent SEC-like securities agencies outside the United States, see Moran 1991; Sobel 1994; Vogel 1996; Lütz 1998; and Laurence 2001.

six regulatory disputes in the securities market sector[5] between 1990 and 2008.[6] Regulatory cooperation (of which dispute management is an example) varies by the degree to which and the way political authorities give foreign companies and customers access to markets.[7] The change had distributional ramifications for firms and affected the relative influence of authorities. The study uses within-case and cross-case comparisons over time, congruence analysis, and process tracing (examining causal mechanisms and uncovering sequencing effects) to weigh the explanatory power of competing arguments.[8] I develop the historical record from multiple sources: interviews with financiers and market authorities on the two sides of the Atlantic, official transcripts (and personal observations) of public hearings, private and public reports, secondary scholarship, and the financial press.

Institutional change inside the European Union (EU) recast the North Atlantic balance of regulatory leverage and was thereby the primary factor behind the reshaping of transatlantic cooperation. Variance over time in the degree to which EU decision makers centralized regional regulatory arrangements accounts for the timing and pattern of change better than alternative explanations drawn from constructivist, functional institutionalist, and realist theory. While each of the six cases has particular causes unique to the respective subsector, in every instance, the move toward more regionally centralized authority bolstered the Europeans' ability to affect the behavior of U.S. regulators. Efforts to establish Europe-wide rules and Brussels-based rulemaking first changed the expectations of U.S. financial services companies and later the agendas of U.S. officials and European firms and authorities. In spite of widespread skepticism about EU regulatory capacities,[9] perceptions of a new ability to retaliate against U.S. unilateral rulemaking, to increase regulatory costs, and to narrow opportunities for regulatory arbitrage in Europe ultimately generated new incentives in Washington, D.C., for accommodation and closer transatlantic coordination.

By highlighting the effects of internal EU change on the configuration of transatlantic bargaining strength, my explanation differs from models that, accepting U.S. financial pre-eminence as a given, attribute variance in cross-border regulatory coop-

5. The financial services industry is typically divided into banking, insurance, and securities/investment services, which include investment banking, brokering, dealing, managing assets, and providing services for exchanging, clearing, and settling trades.

6. The six cases are the set of major transatlantic regulatory disputes during this period in the securities market sector. I made final observations in September 2008.

7. By contrast, Singer's definition equates cooperation with deliberate efforts to create international standards (Singer 2004 and 2007). I view such efforts, as well as those to otherwise harmonize national rules, as one form of regulatory cooperation. Yet I also include information-sharing and reciprocal agreements to permit foreign firms to operate under various principles, including national treatment/nondiscrimination and mutual recognition.

8. I thus use "intensive testing," designed to see whether a hypothesized explanation does better against the historical record than alternative propositions and conduct a "dynamic comparison," which uses temporal variation to draw causal inferences. See the symposium on Gerring 2007 in *Qualitative Methods* 2007.

9. See Pauly 2008; and Véron 2007.

eration to factors such as incentives and strategies derived from the particularities of issue areas[10] or preferences rooted in domestic politics.[11] My argument also provides a theoretical foundation for what Drezner assumes as a starting point: that the EU has arrived as a global regulation-maker, roughly on par with the United States.[12]

Finally, while resonating with a well-established theme from the realist branch of IPE—that a high level of foreign-firm dependence on a polity's markets is a source of power, leading to external influence[13]—my findings have broader theoretical significance that opens new avenues for dialogue, especially between realists and constructivists. In addition to advancing debates on domestic-international connections[14] and the EU as a global actor,[15] I draw attention to the social foundations of power in global economic affairs. The transatlantic political process set off by transformation in Europe lies at the interface of institutions, power, and ideas, revealing contemporary sources of systemic change[16] and providing clues about what the EU's ascendance in cross-border financial regulation will mean in the aftermath of the late 2000's crisis.

A Pattern of Change in Transatlantic Regulatory Cooperation

During the past fifteen years, Americans and Europeans have been voracious transatlantic consumers of financial securities.[17] Affiliates of U.S. and European banks, brokerage houses, asset managers, stock exchanges, insurers, and other financial services firms have operated extensively in one another's home markets.[18] In the United States, European companies complied with federal and state regulations in part by setting up American entities, occasionally acquiring partial exemptions. Inside the EU, U.S. financial services companies established affiliates regulated by one national regulatory regime (often the UK's), which could at least in principle operate in any other EU national market.

10. Simmons 2001.
11. Singer 2004 and 2007.
12. Drezner 2007.
13. See Hirschman 1980 [1945]; Aggarwal 1985; James and Lake 1989; Krasner 1991; Vogel 1995; Oatley and Nabors 1998; Richards 1999; and Keohane and Nye 2001.
14. See Evans, Jacobson, and Putnam 1993; Risse-Kappen 1995; Raustiala 1997; Mattli and Büthe 2003; Young 2003; Bach and Newman 2007; and Newman 2008b.
15. See Bretherton and Vogler 2006; Meunier 2005; and Ginsberg 2001. On Europe's influence on the international regulation of finance, see Abdelal 2007; and Drezner 2007.
16. Ruggie 1993.
17. For U.S. Treasury statistics on U.S. financial accounts with foreigners, see ⟨www.treasury.gov/tic⟩, accessed 30 June 2009. See also Steil 2002.
18. See Hamilton and Quinlan 2006; and Bureau of Economic Analysis, U.S. Department of Commerce, tables 10 and 11, available at ⟨www.bea.gov⟩. Accessed 30 June 2009. On U.S. affiliates in Europe, see SIFMA statistics, ⟨http://www.sifma.org/research/statistics/global-sector-statistics.shtml⟩, accessed 30 June 2009; and Lackritz 2005. On European affiliates in the U.S., see Bureau of Economic Analysis, tables 6.3, 10, 11; and Nutter 2005.

Given this interpenetration of financial services sectors, it is not surprising that regulatory disputes occurred or that transatlantic market authorities used multiple venues for discussing them.[19] Yet during the past two decades, important changes took place concerning both officials and forums. Throughout the 1980s and 1990s, national central bankers, treasury and finance ministry officials, and securities supervisors had interacted in a web of bilateral connections and multilateral forums such as the Bank for International Settlements (BIS), the International Organization of Securities Commissions (IOSCO), the Financial Action Taskforce of the Organization for Economic Co-operation and Development (OECD), the Joint Forum, and the Financial Stability Forum.[20] Cooperation tended to be fragmented by subsectors.[21]

After 2002, in contrast, transatlantic cooperation was institutionalized. Led and coordinated by the U.S. Treasury and the European Commission, a mesh of ongoing and formalized dialogues not only added a layer to and changed the tenor of the old country-to-country bilateral and multilateral interactions but also shifted attention to EU-U.S. bilateralism. The "EU-U.S. Regulatory Dialogue on Financial Services" introduced in May 2002[22] included negotiations in accordance with the September 2002 Norwalk Agreement, the March 2003 initiated SEC-CESR (Committee of European Securities Regulators)[23] cooperative framework, and the June 2005 CESR-CFTC (Commodity Futures Trading Commission) "Common Work Program to Facilitate Transatlantic Derivatives Business." Whereas in the past U.S. regulators had interacted primarily with their national European counterparts, after 2002 EU member states were also represented by several European-level bodies and, indirectly, by the International Accounting Standards Board (IASB).[24] The European Commission initially played the most important European role, engaging directly in discussions with the U.S. Treasury, Federal Reserve Bank, the SEC, and the Public Company Accounting Oversight Board (PCAOB). Visits by high-level financial authorities from both shores gave the new cooperative relationship stature and publicity. In April 2007, U.S. President George W. Bush, German Chancellor Angela Merkel (acting in her capacity as European Council President), and European Commission President José Manuel Barroso signed the "Framework for Advancing Transatlantic Economic Integration," which featured financial markets as a target area.[25]

19. Coleman and Underhill 1995.

20. See U.S. GAO 2004, 39–41; and Bach 2004.

21. The Financial Stability Forum and Joint Forum are exceptions.

22. The Dialogue was part of the "Positive Economic Agenda" introduced at the U.S.-EU Summit in May 2002.

23. CESR, created in June 2001, is made up of the EU national securities regulators and a representative from the European Commission.

24. See below for details.

25. "Framework for Advancing Transatlantic Economic Integration between the United States of America and the European Union," 30 April 2007, available at ⟨http://georgewbush-whitehouse.archives.gov/news/releases/2007/04/20070430-4.html⟩. Accessed 30 June 2009.

The Terms of Financial Regulatory Cooperation

In addition to new faces and forums, the pattern of change in transatlantic regulatory relations featured new terms of cooperation. This shift is a change in the terms of access and competition for foreign firms operating in the transatlantic securities market sector. By the 1990s, relations were generally cooperative, in the sense that laws and rules on both sides of the Atlantic gave foreign firms access to local markets. By mid-decade, however, a number of disagreements emerged over the specific terms of access and were handled in different ways over time. In particular, transatlantic dispute management varied by whose preferred terms of cooperation were adopted, with the outcomes differing by the particular mix of principles. These included national treatment/nondiscrimination of foreign firms, unilateral and mutual recognition of one another's regulation, harmonization of standards or rules, and access on the basis of home-country equivalency.

An Empirical Pattern to be Explained

Between the mid-1990s and 2008, problems set off by regulatory differences stood at the center of six major transatlantic disputes. Conflicts festered at a low level of intensity during the 1990s as the SEC jealously guarded U.S. sovereignty, refused to agree to European demands for mutual recognition, and set the agenda, which began in 1989 to include regulatory in addition to enforcement issues.[26] During a brief two-year span between 2002 and 2003, several disputes became acrimonious. Then Euro-American conflict management entered a period based on mutual accommodation rather than U.S. preferences. U.S. authorities made significant concessions in high-profile transatlantic conflicts. European regulators did not achieve all their goals but did much better than in the past. Figure 1 sketches this empirical pattern.[27]

Dispute Management Reflecting U.S. Preferences

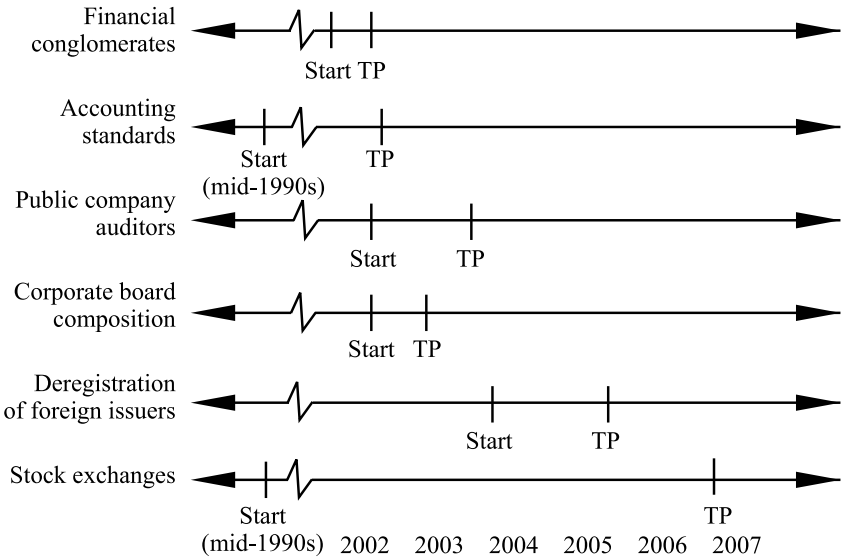
Of the six major disputes (see Figure 1), the two that began in the mid-1990s exemplify the lopsided nature of transatlantic relations. The conflict over accounting standards started when Europeans proposed a mutual recognition regime, whereby EU companies with listings in the United States would use their own national accounting standards and vice versa.[28] U.S. regulators, however, showed little interest in mutual recognition regimes or convergence initiatives. The SEC's view was that the rest of the world would eventually adopt U.S. stan-

26. See Bach 2004; and Securities and Exchange Commission 1997.

27. I coded the cases of dispute management based on the balance of adjustments: either Europe or the United States made adjustments; neither side was willing to make adjustments; or both sides made adjustments through mutual accommodations.

28. European Commission 1995.

dards.[29] U.S. Generally Accepted Accounting Principles (U.S. GAAP) were already accepted by all EU national regulators, and the SEC did not consider European standards and International Accounting Standards (IAS) to be as rigorous.[30]



Notes: Start = Start of dispute. TP = Turning point from cooperation based on U.S. preferences to cooperation based on mutual accomodation.

FIGURE 1. *Transatlantic dispute management over time*

Likewise, the conflict over the rules governing stock exchange competition emerged in the mid-1990s. It began with European demands for a change away from transatlantic competition based on national treatment, to a mutual-recognition regime. European national and EU officials wanted stock exchanges to be able to place screen monitors on traders' desks across the United States and Europe without having to comply with additional host regulatory requirements.[31] The EU exchanges wanted to use their technological advantages to win back trading of European company stocks listed in the United States and gain direct access to

29. See Simmons 2001, 611, fn. 93; Bach 2004, chap. 5, 30; and van Hulle 2004, 6.

30. See Arthur Levitt, "The World According to GAAP," *Financial Times*, 2 May 2001, 21. Also, author's telephone interview with former SEC chief accountant, 8 July 2007.

31. Franke and Potthoff 1997; and author's interview with Federation of European Securities Exchanges (FESE) official, 9 June 2004, Brussels.

American investors.[32] These European entreaties met steadfast U.S. resistance.[33] Emphasizing the dangers to investors of sharing regulatory sovereignty, the SEC argued that mutual recognition might threaten the ability to carry out their primary domestic mandate—protecting shareholders.[34] From the European perspective, however, U.S. politicians and the SEC were coddling the New York Stock Exchange (NYSE) and Nasdaq, fearing that mutual recognition might damage the U.S. financial services industry and cause financial activity to move offshore.

Dispute Management by Mutual Accommodation

The year 2002 marked a discernable turning point, after which making mutual adjustments became a routine part of managing conflicts. While access to U.S. markets based on national treatment and nondiscrimination still characterized much of the new regime at the midpoint of 2008, the SEC had agreed to recognize non-U.S. regulation in one subsector (accounting standards) and was exploring its adoption in others (stock exchanges, brokerages, and auditing firms). Also novel was the growing frequency and importance of exemptions and exceptions, as both sides made adjustments to new and old legislation and rules to accommodate each other's respective laws. Though occurring at different moments over a five-year period, the shift is observable in all six cases.[35]

The resolution of a conflict over the 2002 EC Financial Conglomerates Directive (FCD)[36] came after months of hostility and suspicion. The FCD requires that the holding company of non-EU financial companies be subject to consolidated supervision—that a single regulator must oversee all parts of large financial conglomerates, including the domestic and foreign banking, insurance, and securities operations. A home-regulator can be the supervisor under the new directive so long as its regulatory system meets EU equivalency standards.[37] U.S. financial-services firms, especially investment banks operating in Europe, complained loudly.[38] At the time, U.S. supervision would not have met the new EU standards. An EU finding of nonequivalency might have been extremely harmful to U.S.-based investment banks because of costly and unwanted changes that included accepting an EU authority (rather than the more lenient SEC) as its global consolidated regulator.[39] In early 2002, the conflict crested with American suspicions that EU officials wanted to "'push back' on the U.S. apparent 'hegemony' of financial market regulation … and impose 'EU' supervisory rules on banks," in the words of one Washington official, who noted, "some U.S. super-

32. See Steil 1996 and 2002; and Coleman and Underhill 1995.
33. Author's interview with European Commission official (Internal Market), 9 June 2004, Brussels.
34. As Steil 2002 points out, the SEC's arguments are far from airtight.
35. Campos 2003.
36. Directive 2002/87/EC of the EP and of the Council of the EU.
37. Tafara 2004.
38. See below.
39. See Singer 2007 on the advantages of U.S. regulations for investment banks.

visors expressed surprise and consternation that the EU and its member state supervisors would presume to 'pass judgment' on U.S. rules and supervision."[40] Others in the United States suspected the Europeans were reneging on a 1989 agreement that allowed U.S. banks to continue to operate in the EU under the national treatment principle, rather than comply with new requirements.[41]

By mid-2002, however, U.S. and EU officials did come to a common understanding. The SEC created a new vehicle for consolidated supervision, which is an alternative to the traditional American net capital rule.[42] Like its EU counterparts, the SEC could then (at least in principle) compare a firm's risk exposure to its entire capital.[43] These new SEC rules, which Europeans accepted as meeting their equivalency requirements, represented a major adjustment. The commission's prior requirements for broker-dealers reflected a history of sharp divisions between lending and securities businesses.[44] Moreover, the new holding company rules challenged the balance of power among U.S. financial regulators and set in motion a series of Washington efforts to make the Basel II Capital Accord responsive to the needs of investment banks.[45]

Three transatlantic disputes arising from the passage of the U.S. Sarbanes-Oxley Act of 2002 were also eventually managed through a process of mutual accommodation. Washington's rapid reaction to the Worldcom, Enron, Adelphia, and other corporate scandals paid little or no attention to the legislation's international effects. Two regulatory issues brought immediate and angry European complaints. Once the costs of the new law were apparent, a third followed. After initial resistance, U.S. regulators accommodated European concerns in all three.

The first involved provisions that required foreign auditors of U.S.-listed firms and of foreign affiliates of American companies to register with a new body, PCAOB, and be subject to inspections, investigations, and disciplinary proceedings.[46] Of the three Sarbanes-Oxley conflicts, the international reach of the U.S. auditing regime generated the sharpest EU response, which included a terse statement from the region's economic and finance ministers and a threat to retaliate.[47] The acrimony did not subside until late 2003.

40. Former U.S. Treasury official's correspondence with author, 31 May 2006.

41. Author's interview with senior staff official, U.S. House of Representatives, 6 May 2004, Washington, D.C. See also Underhill 1997, 117.

42. The SEC created the supervised investment bank holding company (SIBHC) and then the consolidated supervised entity (CSE), but the large U.S. investment banks chose the latter. *Federal Register*, Vol. 69, No. 118, 21 June 2004, Rules and Regulations, 34472 [Release No. 34-49831, File No. S7-22-03] and 34478 [Release No. 34-49830, File No. S7-21-03]. See Alix 2004, 3, fn. 8.

43. On how the EU directive affected U.S. regulation, see Cox 2008.

44. See Coleman and Underhill 1995; and Singer 2007.

45. See Callcott 2003; Alix 2004; and U.S. GAO 2004, 88.

46. Ross 2004. Under the previous regime, foreign firms complied with U.S. public company auditing rules on a national treatment/nondiscrimination basis.

47. See *Financial Times*, 12 June 2003, 8 and 23 April 2004, 9; and European Council, [9822/03 (Presse 149), 16], 3 June 2003. Also, author's interview with European Commission official, Brussels, 9 June 2004.

At the time, 333 European companies were publicly listed in the United States and were audited by fifty-eight EU-based auditors.[48] Those foreign firms complying with U.S. measures not only faced duplicative oversight but also regulatory differences that put them in violation of home-country laws. The initial U.S. position of making modest accommodations gave way to greater flexibility in implementing the act.[49] First, the United States extended the registration deadline twice.[50] Second, in cases where disclosure violated home-country law, the PCAOB started allowing foreign auditors to omit information required of U.S.-based auditors.[51] Finally, it developed a creative cooperative framework with EU and other foreign regulators on a "sliding scale."[52] Meanwhile, Europeans made concessions of their own to assist the PCAOB and to coordinate auditing committee composition with the new U.S. rules.[53] By June 2008, the PCAOB's proposed mutual-recognition policy (whereby the board would accept inspections by some non-U.S. counterparts) had gone through a commentary period and a roundtable discussion.[54]

The second Sarbanes-Oxley spillover concerned new requirements for corporate board and audit committee independence, putting some European companies with U.S. listings, especially German firms, in an untenable bind.[55] If not modified, these companies would have had to choose between complying with U.S. rules or continuing to follow home-country laws and thus forgoing direct access to U.S. investors.[56] This issue was resolved more quickly than the first, as the SEC made concessions to affected European firms in April 2003.[57] The U.S. securities authority allowed for a broad interpretation of compliance and made exceptions about who could serve on auditing committees and who would count as an audit committee financial expert.

The increasing costs of maintaining a listing on U.S. stock exchanges under the Sarbanes-Oxley regime triggered a third transatlantic dispute in February 2004.[58] It concerned decades-old reporting and registration obligations, which made it nearly impossible for a foreign company with a U.S. listing to escape the SEC's reach,

48. Ross 2004.
49. Ibid., 11–2.
50. See *Wall Street Journal*, 23 July 2003, C1 and 29, October 2003, 1.
51. PCAOB Rule 2105 and PCAOB Release No. 2004–005 (9 June 2004, PCAOB Rulemaking Docket Matter No. 013). Available at ⟨www.pcaobus.org⟩, accessed 30 June 2009.
52. See Ross 2004, and *Wall Street Journal*, 10 June 2004, C5.
53. *Wall Street Journal*, 26 March 2004, B2. See the 8th Company Law Directive (2006/43/EC of the EP and the Council).
54. See "PCAOB to Consider Proposal to Enhance International Cooperation in Inspections," 26 November 2007; "All Comments to Date on Guidance Regarding the Implementation of PCAOB Rule 4012," 27 March 2008; and "Roundtable on Proposed Policy Statement Regarding PCAOB Rule 4012," 25 June 2008. Available at ⟨www.pcaobus.org⟩.
55. Tafara 2004.
56. See Steil 2002, 11; and Vitols and Kenyon 2004, 31–34.
57. See Campos 2003; and SEC Release Nos. 33-8220, 34-47654, IC-26001, File No. S7-02-03, 25 April 2003, available at ⟨www.sec.gov⟩, accessed 30 June 2009.
58. U.S. GAO 2006.

even after a delisting. Taking a conciliatory tone, the SEC adopted new rules in the face of pressure from European firms and regulators.[59]

As for the accounting standards dispute, simmering since the 1990s, the SEC began to make concessions to the EU in 2002 by embracing a transatlantic convergence project. The Norwalk Agreement of that September committed IASB, the new EU standard setter,[60] and Financial Accounting Standards Board (FASB), the U.S. standard setter, to making existing International Financial Reporting Standards (IFRS) and U.S. GAAP fully compatible.[61] Because compatibility lies as much in implementation and enforcement as in the similarity of principles, the SEC also worked closely with the European Commission to prepare for an eventual mutual recognition regime, and the SEC and CESR launched a joint work plan.[62] In November 2007, the U.S. regulator's turnabout had produced a new rule that eliminated the requirement of U.S. GAAP reconciliation for foreign issuers using IFRS as published by IASB.[63] While European authorities had pushed to no avail for the inclusion of EU versions of IFRS,[64] with the SEC decision they had achieved their major aim. Even if, as some commentators claim, the acceptance of IFRS marked an SEC victory (in the sense that the U.S. commission considers foreign standards to have converged sufficiently to U.S. ones so that lifting reconciliation requirements would not weaken domestic regulation), the adoption of the new rule still represented a major turning point. The rule based cooperation on mutual recognition—a form of shared sovereignty that allows the acceptance of implementation and enforcement by non-U.S. authorities. The SEC's action, moreover, led directly to plans for shifting U.S. accounting standards from U.S. GAAP to IFRS.[65]

Lastly, the position of U.S. officials on the rules governing stock exchange competition began to change in early 2007. Until then, the SEC had avoided making accommodations, despite the greater frequency and intensity of EU complaints in 2003.[66] In early 2007, however, public pronouncements by SEC authorities sug-

59. See "European Responses to SEC Proposed Rule," Release No. 34-53020, 23 December 2005, available at ⟨www.sec.gov⟩, accessed 30 June 2009; Campos 2006; *New York Times*, 7 December 2006, C6; SEC Final Rule, Release No. 34-55540, 27 March 2007.

60. EU legislation mandates that IASB's standards used by European companies be endorsed by the European Commission.

61. The text of The Norwalk Agreement is available at ⟨www.sec.gov⟩, accessed 30 June 2009. IFRS is the new label for IAS.

62. See Tafara 2004; and SEC Press Release, 2006-130, 2 August 2006, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

63. See SEC Final Rule Release No. 33-8879, 21 December 2007, and Press Release 2005-62, 21 April 2005, available at ⟨www.sec.gov⟩, accessed 30 June 2009; Cox 2007; Nicolaisen 2004; and Securities and Exchange Commission 2004.

64. See Jörgen Holmquist, Comment on Proposed Rule (26 September 2007), Release No. 33-8818, 2 July 2007, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

65. See SEC Press Release 2008-184, 27 August 2008; and *Wall Street Journal*, 28 August 2008, A1.

66. See Frits Bolkestein, "EU-US Regulatory Cooperation on Financial Markets: A Matter of Necessity?" Washington, D.C., 24 February 2003, available at ⟨http://www.eurunion.org/eu/index.php?

gested that the stock exchange conflict was following a similar pattern to the others. SEC Director of the Office of International Affairs, Ethiopis Tafara, published a plan for a mutual recognition regime.[67] Moreover, in August 2007, the SEC solicited comments from the Federation of European Securities Exchanges (FESE) on the transatlantic extension of mutual recognition to the sector.[68] In February 2008, the SEC signed a joint statement with the European Commission endorsing mutual recognition as a governing principle for transatlantic securities markets.[69] In June, the U.S. agency proposed a rule change that would expand exemptions from registration for certain types of foreign securities firms—a rule change that would meet some, though not all, EU demands.[70]

The management of these six conflicts thus followed a two-part pattern. First, the terms of transatlantic regulatory cooperation changed, as U.S. regulators became as likely to make adjustments as their European counterparts. Second, the timing of change in the various disputes occurred at different moments between 2002 and 2008.

Alternative Explanations

My focus on varying patterns of cooperation across subsectors and time belongs to a broad literature about why and how rules governing global economic activity originate and change.[71] One set of explanations for global financial governance embraces the constructivist emphasis on the effects of social context on perceptions, interests, and identities of policymakers and regulators.[72] For example, some scholars attribute cooperation and conflict to shared or clashing normative frameworks.[73] A pattern of change in the terms of cooperation by this logic would depend on the degree to which European and U.S. officials, working under the auspices of international financial forums, developed a shared regulatory culture—that is, a set of

option=com_content&task=view&id=2273&Itemid=131⟩, accessed 30 June 2009; and "The Transatlantic Relationship in Financial Services," Washington, D.C., 14 October 2003, available at ⟨http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/03/461&format=PDF&aged=1&language=EN&guiLanguage=en⟩, accessed 30 June 2009. Also, author's interview with European Commission official (Internal Market), Brussels, 9 June 2004.

67. See Tafara and Peterson 2007; and *New York Times*, 9 February 2007, C1.

68. See Jukka Ruuska, Letter to Christopher Cox, 17 August 2007, available at ⟨www.fese.be⟩, accessed 30 June 2009; and *Financial Times*, 3 January 2008, 11.

69. SEC press release 2008-9, 1 February 2008, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

70. SEC Proposed Rule, Release No. 34-58047, 27 June 2008.

71. On international regimes, see Keohane and Nye 2001; and Krasner 1983. On global economic governance, see Hall and Biersteker 2002; Kahler and Lake 2003; and Barnett and Duvall 2005. On dispute management in the transatlantic sphere, see Farrell 2003; and Young 2003. For work specifically concerned with cross-border regulatory cooperation in financial areas, see Coleman and Underhill 1995; Kapstein 1989; Simmons 2001; Abdelal 2007; and Singer 2007.

72. Examples of constructivist arguments include Sinclair 2005; Jabko 2006; and Abdelal 2007.

73. McNamara 2002 and 1998. On the difference between norm-governed and norm-transforming change with respect to international regimes, see Ruggie 1983.

principles and norms for governing competition and setting standards within and across borders (see Table 1, "Competing Explanation" or CE1a). Yet in five of the six cases, the common normative framework was more or less a constant throughout the period under study and therefore cannot explain change in transatlantic regulatory cooperation. Until the financial crisis of the late-2000s, little in the positions of European national or EU officials indicated a distinctive approach to securities markets akin to what Abdelal finds in the liberalization of capital.[74] European authorities challenged the existing normative framework for regulating securities markets only along the edges,[75] instead demanding better terms of cooperation—without disputing basic principles set under U.S. leadership. They sought a more consistent application of these principles, calling for liberalization by easing access to U.S. markets for firms based in Europe. If a distinctive European approach to securities regulation had existed and clashing normative frameworks made sovereignty sharing more difficult, transatlantic regulatory cooperation would have displayed less mutual accommodation after 2002, not more.

TABLE 1. *Competing explanations*

		Expectation	*Critique*
CE1	Constructivist	a. Cooperation patterns reflect degree of normative consensus. b. Deliberation leads to persuasion, trust, and cooperation.	a. Conflicts emerged and management varied, despite a common normative framework. b. Deliberation was an outcome, not a root cause.
CE2	Domestic dilemmas	Cooperation patterns reflect domestically derived preferences of large countries.	Bargaining dynamics vary over time, even when preferences remain the same.
CE3	Hegemony	Continued U.S. dominance.	Assumes constant distribution of bargaining power.
CE4	Issue areas	Cooperation patterns reflect inherent qualities of issues areas.	Bargaining dynamics vary over time in the same issue areas.
CE5	Market power	European markets expand relative to U.S. markets.	The opposite occurred.

74. Abdelal 2007. On the European doctrine of managed globalization, see Meunier 2007.

75. The EU's Financial Conglomerates Directive, for example, called into question the lenient U.S. regulation of investment banks. However, the SEC arguably had no trouble circumventing the spirit of the FCD, while still winning the EU stamp of equivalence for US-regulated firms. See *New York Times*, 3 October 2008, 1.

Another constructivist explanation emphasizes communication and argument in fostering cooperation.[76] Yet in the transatlantic regulatory relationship, deliberative processes were initially outcomes, not original sources of change. Frequent consultations between transatlantic officials fostered dialogue that led to mutual learning, a better understanding of one another's positions, trust, and mutual accommodation (see CE1b in Table 1). Indeed, repeated interactions among regulatory authorities even set off far-reaching feedback loops. Nevertheless, rather than an initial cause, the sequence of events shows that deliberation was endogenous to a changed configuration of bargaining leverage, a variable given little weight in constructivist accounts.

In the area of securities regulation, many leading explanations, borrowing from realists' insights, engage directly with bargaining leverage and other forms of material power. In assuming continued U.S. dominance in global financial regulatory developments, however, few scholars contemplate the possibility of change.[77] For example, despite a focus on states with large markets and an explicit acknowledgement of the importance of power, Singer[78] holds power configurations constant and instead attributes preferences and, by extension, patterns of cooperation to variance in domestic dilemmas facing national regulators (CE2 in Table 1). In perhaps the most frequently cited explanation for cross-border financial regulatory interactions, Simmons sees "financial power" as the source of U.S. dominance.[79] As a financial power, she maintains, the United States (sometimes in tandem with the UK) does not need to adjust its policies in response to external pressures. Simmons's model (CE3 in Table 1) uses variation in issue area incentives to explain whether the United States will expend resources to achieve its goals or wait for market forces to pressure others to adjust.[80] The premise, deeply rooted in functional institutionalist analysis, is that inherent qualities of issue areas give rise to certain bargaining dynamics and patterns of cooperation.[81] Conflicts in the same issue areas would therefore be expected to result in similar management solutions over time (CE4 in Table 1).

Simmons's and Singer's approaches account fairly well for regulatory relations across subsectors from the 1980s and 1990s. Yet neither helps to predict the impact on regulatory cooperation for subsequent years, when the distribution of financial power changed.

76. See Risse 2000; and Farrell 2003.
77. See Sobel 1994; Oatley and Nabors 1998; Simmons 2001; and Singer 2007. Exceptions include Coleman and Underhill 1995; and Cerny 1993.
78. Singer 2007.
79. Simmons 2001.
80. Ibid., 592–601.
81. See Keohane 1984; and Stein 1983.

An Alternative Explanation

In the tradition that treats economic interdependence as a potential source of external influence, market power, and ultimately bargaining strength, stem from foreign reliance.[82] Influence over global rules, by this line of reasoning, derives from the relative concentration of foreigners willing to accept a regulator's decisions to gain access to customers or suppliers. As Simmons and others substantiate, the international influence of U.S. securities regulators in the post–Bretton Woods era emerged largely from the number of foreign firms that depended on U.S. financial markets and therefore complied with SEC rules.

A corollary of this reasoning—that bargaining dynamics should vary with shifts in relative dependencies—can be used to generate causal propositions to explain change in regulatory relations. A relative increase (or decrease) in the concentration of foreigners operating in a given jurisdiction should enhance (or reduce) the bargaining strength of officials representing it. Logic suggests at least two routes by which the numbers of foreign companies under an authority's jurisdiction might change. One is an increase in the size of markets within the same political boundaries (CE5 in Table 1). This tends to be the default hypothesis—as scholars assume that markets and, by extension, foreign firm concentrations grow because of exogenous economic and technological forces. At least in the transatlantic arena, such an argument predicts continued U.S. pre-eminence in the securities market sector. In fact, if such forces had altered the distribution of bargaining strength and affected transatlantic financial regulatory relations, we would expect U.S. officials to have made fewer, not more, adjustments in the years under study. U.S. regulators would have gained bargaining strength relative to their European counterparts because by most measures the size gap between American and European national capital markets and related industries (either individually or aggregated) expanded, not contracted, over the years preceding the 2002 shift in the terms of cooperation. In most areas of the securities industry, the United States maintained or expanded its global position.[83] The U.S.-to-European ratios of equity market capitalization and total value of share trading, for example, increased from approximately 2:1 in 1994 to 2.5:1 in 2003.[84] After peaking in 1998 at 2.7:1, U.S.-to-European ratios of investment banking revenues leveled off at 1.7:1 in 2003, the same ratio as in 1995.[85]

82. See Hirschman 1980 [1945]; Aggarwal 1985; Krasner 1991; and Vogel 1995.

83. Despite the overall pattern, in a few niches, Europe did extend traditional strengths (such as in the asset management for high-net-worth individuals) and narrow the U.S. lead (such as in the turnover of exchange-traded derivatives). See International Financial Services London (IFSL), "Financial Market Trends: Europe vs. U.S.," October 2004; and "Rising Financial Activity in London Points to Increasing Global Influence of London," Press Release, 18 October 2004, ⟨www.ifsl.org.uk⟩, accessed 30 June 2009.

84. World Federation of Exchanges, ⟨www.world-exchanges.org⟩, accessed 30 June 2009. For the United States, I combined figures from the NYSE, Nasdaq, and Amex. For Europe, I added the figures from the LSE, Euronext, and Deutsche Boerse.

85. IFSL, "Rising Financial Activity in London Points to Increasing Global Influence of London."

Between 1998 and 2003, moreover, the U.S. diminished Europe's lead in international bonds, over-the-counter derivatives, and foreign equity trading.[86]

There is, however, a second logic—a political institutional logic—for why the number of foreign firms operating under a jurisdiction might change in a politically fragmented polity: centralizing rulemaking and enforcement.[87] The resulting expansion of the center's regulatory authority is likely to capture a greater number of foreign firms than could even the largest political subunits under a more decentralized arrangement. So long as political frontiers remain more or less static, accounts of bargaining strength built on standard statist assumptions of congruence between regulatory authority and national borders make sense. Yet in contexts characterized by fluid jurisdictional boundaries, such explanations run the risk of missing changed power distributions and their effects.

This reasoning yields the following proposition: under conditions of interdependence, centralizing (or decentralizing) regulatory authority in large polities, all other things being equal, increases (or decreases) the international bargaining power of market officials and thereby enhances (or lessens) their influence over the terms of cross-border cooperation.

Financial Regulatory Centralization

Political centralization is thus the primary causal variable of my explanation. As a social science concept, the term can mean different things in different contexts.[88] Within the European regional polity, political centralization occurs when informal and formal decision-making processes, authority, and rules move from the many national capitals to the EU. Since the mid-1990s, this type of institutional change has taken place in the arrangements for governing financial activity. While not entirely new, regulatory centralization after the euro's introduction (and in the name of creating a "single financial market") rapidly accelerated and qualitatively changed what had until then been a gradual and uncertain shifting of authority to the center of the region.[89] The transfer is far from complete, and the new rulemaking apparatus—comprised of multiple committees and a delicate balance of power among member governments, the European Parliament, and the European Commission—hardly fits classic notions of hierarchical administration.[90] However, at least from the viewpoint of market participants and foreign authorities, single sets of rules increasingly govern firm behavior across the entire continent and are produced and enforced by an EU process.

86. Ibid.

87. There is a third logic, exemplified in the UK after its 1980s "big bang," whereby foreign firms buy local ones.

88. For a slightly different usage of the concept in the politics of finance literature, see Verdier 2003. On financial regulation in federal political systems, see Deeg 1999; and Deeg and Lütz 2000.

89. See Mügge 2006; Posner 2007; Quaglia 2007; Jabko 2006; Coleman and Underhill 1995; and Underhill 1997.

90. Sabel and Zeitlin 2008.

In particular, the EU effort to harmonize rules and centralize rulemaking led directly to two intertwined, internal projects. The Financial Services Action Plan (FSAP) of March 2000 provided the content: the proposed legislation deemed necessary to integrate European national financial services industries.[91] The new laws centralized regulatory authority by harmonizing national rules to a much greater extent than in the past, often requiring a single set of EU standards and regulations with equivalency clauses for foreign firms overseen by home regulators. The second EU project, the Lamfalussy process, altered rulemaking procedures for financial services legislation and supervision[92] by delegating the creation of detailed rules to the Brussels bureaucracy and using new bodies, comprised of national regulatory authorities, to advise and to coordinate transposition, implementation, and enforcement. The Lamfalussy process marks a historic turn away from an arrangement that was primarily the sum of multiple and idiosyncratic national decision-making regimes to Brussels-based procedures. Most rules now originate from these new arrangements, and while national agencies are responsible for on-the-ground implementation, interpretation, and supervision, EU mechanisms increasingly constrain their actions. To a much greater extent, the application of centralized legislation in EU member countries no longer results in differing rules on the ground.

To evaluate the effects on transatlantic regulatory relations of this massive, two-pronged project, I focus on the timing of new pieces of legislation and the degree to which they centralize regulatory authority. Centralization did not occur all at once. The forty-some pieces of separate legislation were enacted over a decade. In addition, European policymakers did not introduce the same combination of reform principles in every subsector. Specifically, the adoption of single sets of EU standards or rules represents a high degree of centralization. The narrowing of national differences in standards and rules, in combination with mutual recognition, by contrast, represent a lower degree of centralization—though not nearly as low as 1980s and early 1990s legislation that combined minimal levels of regulatory harmonization with the principle of mutual recognition.

Empirical Expectations

Such variance in regulatory centralization lends itself to a few simple empirical expectations about transatlantic dispute management. When Europeans rely heavily on principles such as complete standardization, mandating a single set of rules with which local and American firms must comply, we would expect an increase in EU relative bargaining strength and more accommodative behavior on the part of U.S. regulators. This is because EU policymakers would be setting access and

91. European Commission 1999 and 2006.

92. Lamfalussy 2001. Originally, the Lamfalussy process only included the securities industry but was expanded to banking and insurance in 2003.

competition rules for a greater number of U.S. firms or their affiliates operating in Europe. EU officials could thus credibly threaten to use their authority in ways that might damage the businesses of a larger number of U.S. firms or affiliates than was the case before the change. In such a scenario, European authorities would gain the same potential to harm foreign businesses and retaliate against foreign government measures that U.S. authorities have long possessed. The EU would become a rulemaker, rather than a rule-taker. Such "highly centralized regulation" characterizes several subsectors covered by the FSAP.

By contrast, looser forms of regulatory integration, such as the principle of mutual recognition when accompanied by only minimal levels of harmonization, do not create a single set of rules for companies operating in the EU, and we would not therefore expect a change in Europe's bargaining power with the Untied States or more accommodative behavior on the part of U.S. officials. Such "minimally centralized regulation" typified efforts before the FSAP and the Lamfalussy Process. I summarize these empirical expectations of my regulatory centralization explanation in Table 2.

TABLE 2. *Empirical expectations of regulatory centralization explanation*

	(t_2) Expectations for management of EU–U.S. conflicts
(t_1) EU chooses regulatory principles	
Highly centralized	United States inclined to make adjustments. Terms of cooperation reflect mutual accommodation.
Minimally centralized	No change in U.S. behavior. United States reluctant to make adjustments. Terms of cooperation reflect U.S. preferences.

The argument, then, is that variance in internal EU institutional reforms alters transatlantic market dependencies, changes the balance of leverage among regulators and thereby serves as an important determinant of dispute management patterns, a type of regulatory cooperation. Market dependencies create structural power, a probabilistic causal variable.[93] I therefore expect any particular case to have multiple causes but for EU institutional reforms to appear prominently among them. Consistent with these empirical expectations should be a general trend across cases corresponding to the observed pattern of EU-U.S. cooperation. If the explanation accounts well for the pattern of change, variance in the way EU decision makers reformed the subsectors of the securities market sector would capture the timing and direction of shifts in transatlantic regulatory cooperation.

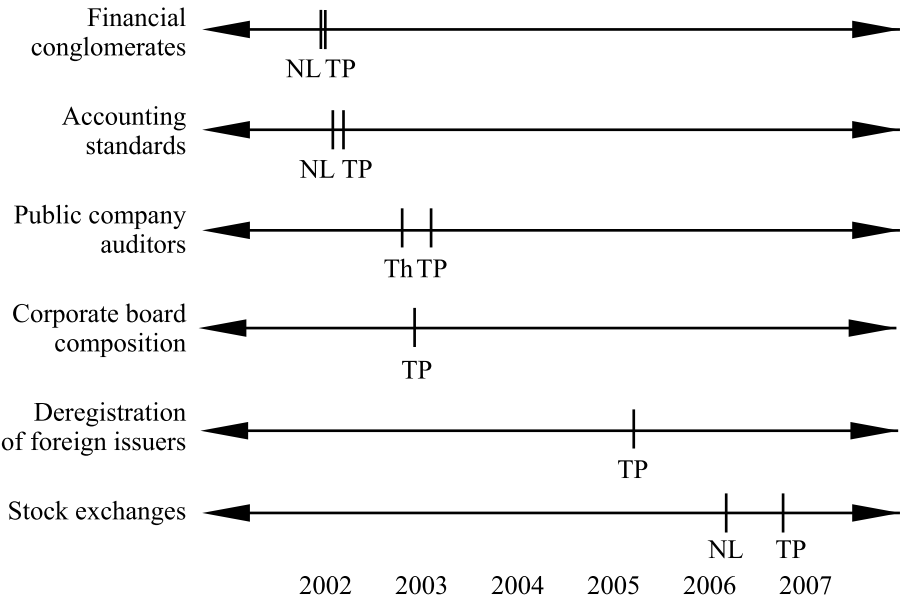
93. Keohane and Nye 2001, 9–17. See also Strange 1994.

An Empirical Investigation

My small-*n* investigation into the causes behind the pattern of change documented earlier begins with congruence analysis and then uses follow-up tests designed to uncover the actual causal mechanisms at work and to understand two outlier cases.

Congruence Analysis

The congruence analysis, summarized in Figure 2, suggests that my empirical expectations about the effects of centralizing authority on transatlantic regulatory relations correspond well with the direction and timing of change in four of the six cases. For these disputes, a close match between predictions and actual outcomes provides a degree of confidence in my explanation for why the United States became more accommodating and for why the timing of change differed among the conflicts. But it also raises new questions that call for different investigative techniques.



Notes: NL = New legislation that centralizes regulation. Th = Threat to create new legislation that centralizes regulation. TP = Turning point from cooperation based on U.S. preferences to cooperation based on mutual accomodation.

FIGURE 2. *Transatlantic dispute management over time*

In the financial conglomerates conflict, EU member states agreed to apply the principle of highly centralized regulation in May 2002 by replacing national

approaches with a single set of rules. Soon afterward, in response to the equivalency provisions of EU law, the SEC began a two-year process of making adjustments to U.S. rules. The accounting standards conflict followed a similar pattern. Three months after European policymakers passed a July 2002 regulation mandating that companies listed on EU stock exchanges apply the same set of accounting standards by 2005,[94] U.S. officials began what became a series of conciliatory policies.[95] The public company auditors dispute veers slightly from the pattern—U.S. authorities made conciliatory changes following European threats to adopt legislation (rather than actually passing a law based on the principle of highly centralized regulation). In July 2003, U.S. officials began to back down from a narrow interpretation of the Sarbanes-Oxley Act after EU officials threatened to retaliate by creating future EU auditing legislation that would have the same extraterritorial effects as the U.S. law.[96] In the stock exchange dispute, there is also a basic congruence between my expected causal factor (a change in the level of regulatory centralization) and the outcomes. Until September 2006, EU policymakers could not agree to higher degrees of centralization, so the pre-existing minimally centralized regime,[97] based on the principle of mutual recognition and minimal harmonization, characterized the subsector in Europe. U.S. officials refused to bend to demands for a transatlantic mutual recognition regime. In early 2007, in advance of the 1 November implementation of a new EU law, SEC officials signaled a new willingness to make adjustments. The EU legislation, Markets in Financial Instruments Directive (MiFID), centralizes the rules governing stock exchanges, albeit by increasing the degree of harmonization and coordination rather than imposing a single set of rules.[98]

The corporate board composition and deregistration of foreign issuers conflicts also ended with the U.S. making adjustments. However, these outcomes occurred in the absence of centralizing EU regulation in the respective subsectors. EU policymakers neither passed legislation that centralized regulation nor threatened to do so.

Testing for Sequencing Effects

To delve beneath the correlative logic of congruence analysis, I use process tracing to search for possible sequencing effects and to examine the mechanisms at

94. Regulation (EC) no. 1606/2002 of the European Council and Parliament, 19 July 2002.

95. Robert K. Herdman, "Moving Towards the Globalization of Accounting Standards," Cologne, Germany, 18 April 2002, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

96. See *Financial Times*, 12 June 2003, 8; 9 July 2003, 29; and 23 April 2004, 9. Also author's interview with European Commission official, Brussels, 9 June 2004.

97. The regime was based on the 1993 Investment Services Directive (Council Directive 93/22/EEC). Coleman and Underhill 1995.

98. MiFID (Directive 2004/39/EC of the EP and Council of the EU) repealed the ISD. While passing the law in April 2004, EU policymakers did not clarify the degree of harmonization until September 2006. Compare Article 42 of the MiFID with Article 15 of the ISD.

work that helps to discern whether my specified causes were actually responsible for the outcomes in the four confirming cases and to uncover the determinants of the other two. I also use these methods to evaluate competing explanations and how they interact with my own.

Careful inspection of event sequence shows that the first disputes to be resolved through mutual accommodation affected the outcomes of later cases. This conclusion about the endogeneity of the causal process goes a long way to explain several cases, especially the two that were not consistent with my original expectations. In the corporate board case, for example, where no new EU legislation preceded U.S. concessions, linkages to its sister Sarbanes-Oxley conflict, the public company auditors dispute, suggest that cooperation ultimately rested on the EU's ability to retaliate. Officials knit the two conflicts together, using credible threats to pass new retaliatory legislation related to the latter case to force U.S. adjustments in both. Adding even more complexity, EU authorities linked these two Sarbanes-Oxley cases to the existing conglomerates legislation—which had an equivalency clause, their strongest ammunition for punishing U.S. financial services companies.[99] By dragging out the process for accepting U.S. holding-company regulation in Europe, EU officials were able to influence the other disputes.[100] Thus, in a very real sense, the new bargaining strength that European officials derived from the centralization of conglomerates regulation—the first dispute to be resolved cooperatively—was also a causal factor in the management of two subsequent conflicts.

The deregistration conflict, the other nonconforming case, follows a similar pattern. By the 2004 onset of this conflict, the institutionalized and friendly EU-U.S. dialogue was well-established.[101] Yet despite the new context, European authorities connected the outcome of the dispute to other domains in which they could credibly threaten to retaliate.[102] Thus, even without the brazen public threats so prevalent in 2002 and 2003, EU officials could link the deregistration outcome to other vulnerable aspects of the transatlantic relationship.

Officials on both sides of the Atlantic, in public pronouncements and my interviews, made the deliberation argument (CE1b in Table 1), consistently mentioning the importance of the "EU-U.S. Financial Regulatory Dialogue" in managing all six conflicts. They lauded the new, more cooperative relationship and maintained that consultations helped to clarify respective regulatory systems, build trust, manage problems, and coordinate reforms.[103]

99. See *Financial Times*, 16 June 2003, 8 and 9 July 2003, 29.
100. See Lackritz 2005.
101. Campos 2006.
102. David J. Wright's Comments, 2, (1 March 2006) on SEC Proposed Rule Release No. 34-55005, 22 December 2006, available at ⟨www.sec.gov⟩, accessed 30 June 2009.
103. See Quarles 2003; Nicolaisen 2004; and Schaub 2004; Wall Street Journal, 26 March 2004, B2. Also, author's interview with EU official, Washington, D.C., 4 November 2005; author's interview with European Commission official (Internal Market), Brussels, 9 June 2004; and former U.S. Treasury official's correspondence with author, 31 May 2006.

The historical record offers substantial evidence that regularized and intensified transatlantic communications since 2003 resulted not only in improved understandings of one another's positions, but also in persuasion and expanded expectations about the possibilities of cooperation.[104] After 2003, in fact, disputes became successively easier to manage and officials claim to have averted new problems with personal phone calls.[105] One can safely surmise that European arguments helped to persuade U.S. authorities of the untenable (and unintended) implications of the hastily passed Sarbanes-Oxley Act.

Nevertheless, and without denying the import of new processes built on trust, evidence suggests that the causal role of deliberation depended on previous change in the distribution of power. In the corporate board dispute, U.S. officials indicated a willingness to discuss plausible solutions and make adjustments in April 2003, only after EU authorities had threatened retaliation against the extraterritorial aspects of the auditing provisions. Even in the deregistration case where deliberation arguably played a bigger role than threats to retaliate, European officials ceaselessly reminded their U.S. counterparts of the EU's newfound capabilities.[106] To argue that deliberative processes account for the resolution of these and other conflicts ignores the sequence of events and mistakes outcome for cause. The new formal and frequent interactions and communications among transatlantic officials came about only after the EU had improved its retaliatory capacities and U.S. officials had shown a new willingness to make concessions.[107]

In sum, a causal process beginning with the financial conglomerates dispute was largely responsible for the management of the two conflicts that did not conform to my original empirical expectations. The trigger for, and supporting pillar of, this process was regulatory transformation inside the EU, which altered the retaliatory potential of European authorities. Deliberation, while an important factor in both nonconforming cases, was itself an output of a new configuration of power.

Testing for Causal Mechanisms in the Financial Conglomerates Dispute

Given the dependencies among the cases, the causes behind the new terms of cooperation in the first dispute—the financial conglomerates conflict—are important for explaining the later outcomes too. What then accounts for the management of

104. For proposed agendas for transatlantic cooperation, see EU-US Coalition on Financial Regulation 2005; and Lackritz 2005.

105. Author's interview with EU official, Washington, D.C., 4 November 2005; and SEC Press Release 2007-8, 25 January 2007, available at ⟨www.sec.gov⟩, accessed 30 June 2009. See also "MoU Concerning Consultation, Cooperation and the Exchange of Information Related to Market Oversight (2007)," 25 January 2007, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

106. David J. Wright's Comments, 2, (1 March 2006) on SEC Proposed Rule Release No. 34-55005, 22, December 2006, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

107. On power and argumentative rationality, see Risse 2000, 11 and 16–19.

the conglomerates conflict? My argument rests on a verifiable connection between EU regulatory centralization and the SEC decision to create a new holding company rule. Careful examination strongly suggests such a connection exists. The SEC was responding primarily to the lobbying of American investment banks, concerned about possible negative implications of the new EU financial conglomerates directive to their European businesses.

Beginning even before Brussels formally opened the directive's consultation period in December 2000, these U.S. financial services companies pressured U.S. lawmakers and regulators until their interests were protected.[108] Represented primarily by the Securities Industry Association (SIA), the U.S. investment banks successfully persuaded politicians in Congress, as well as officials at the SEC and the Treasury, to find a solution to the dispute and develop more cooperative relations with their European counterparts.[109] In addition to a paper trail that includes press reports, transcriptions (and my own observations) of testimony before the U.S. Congress, and SIA documents, my interviews on both sides of the Atlantic without exception confirm the significant role of this lobby group in convincing U.S. authorities to make adjustments, end the conglomerates dispute, and institutionalize a transatlantic regulatory dialogue.[110]

It is hard to imagine U.S. regulators would have been part of a new dialogue, created the new holding-company rule, and done so when they did if they had had another option acceptable to American investment banks. The FCD thus deeply constrained the choices available to U.S. officials.[111] Making no adjustments was not tolerable from the perspective of U.S. firms, which successfully lobbied Congress and found support for their cause in an SEC eager to expand its powers.[112] Despite little evidence of actual EU regulatory capacity or intentions, the United States made concessions because Wall Street firms argued that not doing so would have placed them in a precarious position and jeopardized the SEC's role as their primary regulator.[113]

Because the solution in the conglomerates conflict affected the management of others, it is imperative to know whether competing arguments better account for, or are more important to, its outcome. Issue areas, as constants, cannot logically account for abrupt changes in positions (CE4 in Table 1). Conflicts in the same

108. See EC Proposed Rule No. 34-48694, 24 October 2003; Alix 2004, 3; and SIA 2004.

109. The SIA changed its name to Securities Industry and Financial Markets Association or SIFMA, ⟨www.sifma.org⟩. Also see reports by the Financial Services Roundtable's Global Financial Issues Committee, available at ⟨www.fsround.org⟩, accessed 30 June 2009.

110. Author's interview with staff official, U.S. House of Representatives, 6 May 2004, Washington, D.C.; and former U.S. Treasury official's correspondence with author, 31 May 2006.

111. In 2008, the SEC chairman acknowledged that the new U.S. rules had origins in the EU law. See Cox 2008.

112. Author's interview with a staff official, U.S. House of Representatives, Washington, D.C., 6 May 2004.

113. Once the new U.S. rules were in place, the investment bank lobby managed to water down SEC enforcement. See *New York Times*, 3 October 2008, 1.

issue areas over time presented different sets of incentives and different bargaining dynamics. Since the 1930s and until several months into the conglomerates dispute, U.S. authorities had made decisions about how to regulate investment banks without considering developments in Europe or elsewhere. The conflict spawned by the EU's FCD dragged U.S. authorities into an interdependent decision-making "game."

Nor were common or clashing understandings important causal factors behind the new terms of transatlantic cooperation in the conglomerates dispute or in four of the five other cases (CE1a in Table 1). Conflict over the regulation of conglomerates occurred despite an EU directive based on the 1999 principles of the Joint Forum on Financial Conglomerates, which U.S. regulators supported and used as their model.[114] U.S. and EU officials thus accepted similar regulatory principles. Yet a common approach to conglomerates, while perhaps making cooperation possible at a later date, was not initially apparent to U.S. officials, did not alleviate their deep suspicions of European motives, and thus cannot account for the management of the conflict.

Testing for Causal Mechanisms in the Accounting Standards Dispute

The accounting standards conflict offers a vivid illustration of the pitfalls of the issue areas argument. The approach simply cannot explain change over time. For at least a decade, network externalities conferred first-mover advantages to the United States, whose officials had few incentives to engage in mutual recognition agreements or convergence projects and good reasons to believe market forces would pressure Europeans to adopt U.S. standards eventually.[115] By 2002, however, the bargaining dynamics had changed, as the United States had to exert extensive political resources to achieve its goals (as exemplified in the U.S.-European battle of IASB's governance structure).[116] By the mid-2000s, the dynamics seemed closer to a deterrence game in which credible threats on each side prompted new U.S. stances and cooperation based on mutual adjustments.[117]

The constructivist explanation emphasizing the diffusion of a common normative framework, in contrast to the issue areas proposition, is important in the accounting standards conflict. Unlike in the other cases, the dissemination of shared

114. Joint Forum of Financial Conglomerates, "Supervision of Financial Conglomerates," BCBS/IOSCO/IAIS, February 1999. Available at ⟨http://www.iaisweb.org/_temp/Supervision_of_Financial_Conglomerates_table_of_contents_and_intro.pdf⟩, accessed 30 June 2009.

115. Simmons 2001, 609–11.

116. Telephone interview with former SEC Chief Accountant, 8 July 2007; and Camfferman and Zeff 2007, chap. 13.

117. See SEC 2003; MacDonald 2002; FASB 2004; Financial Times, 30 June 2005, 18 and January 2006, 21; and U.S. Sarbanes-Oxley Act of 2002 (Title I, Section 108, b.1.A.v and d).

principles for accounting standards—hashed out inside the International Accounting Standards Committee, IASB's predecessor, and approved by IOSCO—contributed directly to the timing of the American reversal.[118] Yet the causal role of shared understandings should not be overstated. The accounting standards outcome is over-determined, making it the most difficult of the six cases for drawing causal inferences. Multiple factors contributed to the new proclivity of U.S. regulators toward a mutual recognition regime. It is simply difficult to weigh the importance of the many causes (which include a Republican Congress and presidency, a long-standing interest in Congress to promote a more principles-based accounting system, changing perceptions in the face of corporate scandals, and the rise of an international private authority).[119]

Still, the historical record strongly suggests that EU regulatory centralization ranks among the more salient causes. The basic congruence between the 2002 passage of EU accounting standards legislation and the timing of the U.S. shift is no accident: strong evidence suggests a causal relationship. European officials believed that their new law gave them capacities, which they deliberately used to pressure U.S. authorities to make adjustments. Side legislation related to the EU accounting standards regulation contained equivalency clauses.[120] For foreign firms raising capital or listing securities through regulated markets, the legislation required either adoption of the new accounting standards or approval that home accounts met EU requirements. The EU thus put itself in a position to decide whether more than 200 U.S. companies had to reconcile U.S. GAAP with IFRS.[121] European policymakers used the equivalency clauses, first, to keep pressure on the SEC to make concessions and, then, to live up to its commitment to implement a mutual recognition regime.[122] In fact, the European Commission delayed clarifying the meaning of equivalency until the SEC agreed to recognize IFRS without the reconciliation requirement.[123]

118. "A Resolution on IASC Standards," IOSCO, May 2000, available at ⟨www.iosco.org⟩, accessed 30 June 2009. See also Robert K. Herdman, "Moving Towards the Globalization of Accounting Standards," Cologne, Germany, 18 April 2002, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

119. See articles in *Business and Politics* 2005.

120. See European Commission Regulation (EC) No. 809/2004, 29 April 2004 (Prospectus Regulation); and Directive 2004/109/EC of the EP and the Council of 15 December 2004 (The Transparency Directive).

121. CESR estimates that 233 U.S. companies listed on EU regulated markets used U.S. GAAP and were therefore subject to the equivalency provisions. See CESR, Ref: CESR/07-138, 6 March 2007, available at ⟨www.cesr-eu.org⟩, accessed 30 June 2009.

122. See Dam and Scott 2004, 4; *Financial Times*, 8 November 2005, 28; and "CESR's Advice on the Equivalence of Chinese, Japanese and U.S. GAAPs," CESR, CESR/08-179, March 2008, available at ⟨www.cesr-eu.org⟩, accessed 30 June 2009. Author's interview with European Commission official, Washington, D.C., 5 May 2004.

123. Charles McCreevy, "EU-US Cooperation on Reporting Standards, Audit Oversight and Regulation," Brussels, 27 November 2007, SPEECH/07/757; and "Proposal for a Commission Regulation (EC)," 2 June 2008, available at ⟨www.europa.eu⟩, accessed 30 June 2009.

Testing for Causal Mechanisms in the Stock Exchanges Dispute

Among the six disputes, the stock exchange conflict stands out for its longevity. Despite persistent EU demands and threats, as well as successful management of regulatory conflicts overall, the SEC avoided making accommodations through 2006.

The timing of the SEC's shift, as shown in the congruence analysis, corresponds well with my empirical expectations. Careful examination, however, reveals interesting differences among the mechanisms at work in this case and others. In the conglomerates dispute, U.S. financial services firms responded to the new EU law and acted as the main conveyers of European developments to U.S. authorities. In the subsequent cases, a new confidence in the ability to retaliate against U.S. policies emboldened European officials and companies, often working in tandem, to press for U.S. concessions to new and old grievances, and the institutionalized dialogue gave them a forum for persuading their counterparts. Unlike earlier cases, by 2006 SEC officials were all too aware of EU developments and needed neither U.S.-based financial companies nor Europeans to prompt reconsideration of the decades-old insistence that foreign stock exchanges and brokers register with the SEC and be subject to its oversight before gaining access to American investors.

More centralized EU legislation was certainly a factor behind the SEC's new interest in mutual recognition.[124] MiFID's implementation promised to capture a large number of U.S. securities trading firms, including exchanges, under a comprehensive set of rules. U.S. exchanges and investment banks believed they would be less able to play one EU regulator against another, a change that would give European authorities considerably more regulatory clout.[125] Yet private-sector developments—some also traceable to the broader EU regulatory transformation—contributed to the SEC turnabout as well. The NYSE's purchase of Euronext not only indicates that European markets had become attractive to financiers in the aftermath of the regulatory overhaul and likely changed the NYSE perspective on mutual recognition[126] but the purchase also included provisions that placed part of the new company's operations under the authority of European regulators and EU laws.[127]

124. SEC Press Release 2008-9, 1 February 2008, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

125. Nasdaq Stock Market, for example, had separate arrangements with British and Belgian authorities to provide trading services in Europe; see *Financial Times*, 10 June 2001, 9.

126. Mutual recognition for stock exchanges is expected to reduce the number of cross-listings and shift Nasdaq and NYSE revenues from EU company listings to their home country exchanges (Steil 2002). NYSE's ownership of the French, Dutch, Belgian, and Portuguese exchanges should balance out revenue declines in the NYSE.

127. "Memorandum of Understanding Between the College of Euronext Regulators and the U.S. Securities and Exchange Commission Concerning Consultation, Cooperation and the Exchange of Information Related to Market Oversight," January 2007, available at ⟨www.sec.gov⟩, accessed 30 June 2009.

As the EU's internal changes unfolded over time, U.S. authorities thus felt the impact of Europe's massive regulatory project via an increasing number of channels, indicating deep and pervasive structural change. The turn toward mutual recognition, relabeled "substituted compliance," was the bid by some SEC officials to ensure that the onslaught of new European rules meet U.S. standards, to prevent regulatory arbitrage and, more broadly, to win back the initiative in setting international regulatory trends.[128]

Summary of Empirical Findings

After 2002, U.S. pre-eminence no longer accurately described the configuration of bargaining leverage in the financial securities sectors (CE3 in Table 1), so the terms of transatlantic regulatory cooperation were altered. The continued and sometimes expanded lead in the size of U.S. capital markets, moreover, belies the market power argument that growth in European markets accounts for improved EU bargaining strength (CE5 in Table 1). In all six disputes, case-specific factors not emphasized here affected outcomes.[129] Yet in each, enhanced EU bargaining strength rooted in internal financial regulatory centralization is a primary factor behind the changed terms of cooperation as well as the timing.

These findings echo those of other scholars who have considered the international effects of political centralization and fragmentation. For example, decentralized U.S. regulation in the insurance industry has historically given U.S. authorities significantly less international clout than in other more centralized financial sectors,[130] and German policymakers centralized securities regulation in large part to have greater influence at the multilateral bargaining table.[131] More broadly, my conclusions, while highlighting the specific interaction of political centralization and economic interdependence, resonate generally with a promising new body of research that links internal institutions to global regulatory arrangements outside the trade regime.[132]

While my explanation privileging institutions and power does better against the historical record than competing arguments, some of the most compelling evidence emerges from the interaction of multiple variables and the endogeneity of causal processes. The juxtaposition of constructivist arguments with my own points in particularly interesting directions. Common principles developed under years

128. Tafara and Peterson 2007.

129. In the conglomerates dispute, for example, SEC officials probably saw a new holding company as a means for expanding its powers relative to other U.S. banking authorities (Callcott 2003). The accounting standards outcome, as noted, had a range of causes.

130. Singer 2007, chap. 6.

131. Lütz 1998.

132. See Bach and Newman 2007; Farrell 2003; Mattli and Büthe 2003; and Raustiala 1997. The previous generation of work includes Evans, Jacobson, and Putnam 1993; and Risse-Kappen 1995. In the case of Europe, see Jupille 1999; and Meunier 2005.

of U.S. leadership were important causes in only one dispute (that is, accounting standards) yet likely served as a necessary background condition in the others (CE1a in Table 1). Moreover, regularized interactions and communication among European and U.S. officials increased trust (CE1b in Table 1). The deliberative process, the evidence shows, resulted from the shift in bargaining power and thus did not constitute an original cause of the new terms of transatlantic cooperation. Nevertheless, the causal significance of ongoing official interactions increased over time, helping to shape outcomes in the later cases—even though the underlying power dynamics never disappeared. And the newfound trust among transatlantic officials has had far-ranging feedback loops, contributing to the ongoing formation of the EU as a global financial regulator.

Conclusion

Such evidence revealing the interplay among institutions, power, and ideas raises intriguing theoretical and policy issues. Three stand out. The first is the broader significance of my explanatory variable. The causes emphasized in my study—specific EU rules and laws that centralize regulation—are representative events in a slow-moving process of system-transforming change: the evolution of the European integration project.

In part because of disciplinary ontologies that obscure the possibility of the EU as an independent cause (that is, irreducible to globalization or intergovernmental politics),[133] international relations scholars outside a cadre of Europeanists have been slow to grasp the polity's role as a regulation-setter for the world.[134] Revising the very meaning of national sovereignty, the kind of change taking place inside the European regional polity, over time and across multiple sectors, has refashioned national regulatory authority, a core element of the global political economy.[135] This deep transformation of national authority is what Ruggie labeled epochal politics.[136] A third of global cross-border economic activity is taking place in the context of a radical experiment with regulatory sovereignty. The combination is generating international systemic change.

My analysis substantiates EU extraterritorial effects on cross-border financial regulation and offers micro-theoretical foundations by pinpointing sources and mechanisms by which such macro-transformation produces change in regulatory cooperation. Scholars conducting research on telecommunications, data privacy, chemicals, cosmetics, food safety, hazardous substances, environmental issues, and

133. Posner 2009 and 2005.

134. On blinders rooted in IR ontologies, see Barnett and Finnemore 2004. Journalists, in contrast to academic researchers, regularly report on the EU's rise as a global regulator. See *Wall Street Journal*, 23 April 2002, A1; and *Financial Times*, 10 July 2007, 13.

135. On Europeans' shifting conception of sovereignty, see Keohane 2002.

136. Ruggie 1993.

antitrust have arrived at remarkably similar conclusions about the EU's extraterritorial effects on global regulation.[137] As a whole, this research puts Drezner's treatment of the EU as a regulatory great power on sound empirical footing; further exposes the pitfalls of narrow disciplinary ontologies criticized by constructivists and others; and identifies new constraints under which U.S. policymakers operate.

The second issue is the wide-ranging consequences of repeated interactions among authorities from jurisdictions with relatively equal capacities to retaliate.[138] In my study, improved EU bargaining leverage set the stage for serious dialogue, showing that iterative processes may breed deliberation and thereby the trust necessary for mutual recognition and other forms of sovereignty-sharing in contexts that lack formal institutions. But the evidence provides hints of a different dynamic, also identified in the constructivist literature, but with contrasting lessons for policymaking: that ongoing interaction may also generate strategic and opportunistic behavior.[139]

In transatlantic financial regulatory relations, neither side ceased its efforts to outmaneuver the other when opportunities arose. Trust helped to manage disputes but did not stop future ones from emerging. In fact, the historical record indicates that ongoing interactions altered the self-awareness of the participants' capacities and shaped their strategies, goals, and identity. Through repeated efforts to manage disputes, EU officials became more conscious of underlying market dependencies and learned how to wield them for advantage. Within a few years, the EU emerged as a self-aware global rulemaker.[140] Iteration helped give life to an increasingly opportunistic political actor determined to win first-mover advantages whenever assured retaliation was absent. A feedback loop from the dialogue, itself a function of new EU bargaining leverage, helped to construct the kind of actor assumed in realist and other rationalist bargaining models.

These repercussions of transatlantic interactions have penetrated to the core of the European integration project, with implications for scholarship concerning intentionality in institutional design.[141] In the initial stages of the dialogue, European officials seemed surprised by the way reform within the regional polity, carried out for largely internal reasons, had the potential to increase costs for and otherwise negatively affect foreign firms. At least originally, the EU financial regulatory project was a case of institutional change inadvertently doing more than solving problems that the creators intended. In later years, the evidence suggests that EU policymakers made internal regulatory reforms (most notably the use of equiva-

137. See Damro 2006; Newman 2008b; Young 2003; Drezner 2007; Bretherton and Vogler 2006; and Selin and VanDeveer 2006.

138. Newman 2008a.

139. Wendt 1999, chaps. 6 and 7.

140. For example, the European Commission launched an initiative to set up dialogues similar to the transatlantic one. (European Commission 2005, 15).

141. See Barnett and Finnemore 2004; Pierson 2000; and Hawkins et al. 2006.

lency requirements for foreign firms) with an eye to enhancing bargaining leverage. Thus, repeated interactions between transatlantic officials shaped the purposes and meaning of financial integration inside the EU. European policymakers, having reconceived their global regulatory role, added strategic international goals to what had been institutional change with internal objectives: a vivid example of fluid intentionality contingent on historically specific power configurations and cross-border social and political processes.

The third and final issue turns on lingering questions about what the EU stands for, whether it will use its bargaining strength to challenge the normative framework established under U.S. leadership and how its arrival as a global rulemaker will affect governance arrangements after the late 2000s financial crisis. This article demonstrated the effects of bipolarity in bargaining strength on transatlantic financial regulatory cooperation—at a moment in history when both sides abided by common principles. The transformed EU financial system was not presented to the world as an alternative to American principles, and EU negotiators used their enhanced bargaining power to win better terms of cooperation for Europe-based firms within the existing normative framework. The development of the new EU capacities coincided with the rapid growth of financial markets in Asia and the Middle East. However, for a range of reasons, including the relative dearth of foreign firms operating under the ambit of domestic authorities, even China's fast-growing capital markets had not generated international regulatory clout.

If the balance of regulatory leverage remains constant, the events of 2007 and 2008 raise the crucial question of whether my explanation emphasizing institutions and power is ultimately contingent on a shared normative framework as constructivists arguments would hold.[142] The contours of an emerging EU approach are now visible. By fall 2008, EU regulatory reformers were realigning financial markets and social purposes by attacking the most conspicuous manifestations of private authority and self-regulation, two pillars of the U.S. approach. EU critics of the undemocratic nature of private authority appeared to have won their battle against the global economy's exemplar case: a political body will monitor the IASC Foundation that oversees the IASB.[143] EU policymakers, moreover, seemed determined to replace self-regulation of credit rating agencies with oversight centered in Brussels.[144]

Will the U.S. reaction diverge or will political economists have to wait for the ultimate test of the relative importance and interactions of power and ideas?

142. Ruggie 1983.

143. Nicolas Véron, "A Flimsy Triumph for Global Accounting Standards," available at ⟨http://veron.typepad.com/main/files/Tribune_080915_en.pdf⟩. See also ⟨www.iasb.org⟩, accessed 30 June 2009.

144. For EU legislative process, see ⟨www.europa.eu⟩, accessed 30 June 2009. On credit rating agencies, see Sinclair 2005.

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