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The G-20 Summit: Potential Threats to U.S. Interests

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Key European leaders have revealed their agenda for the G-20 summit on the global financial crisis. While a few of their critiques are well-taken, their pre-summit positions raise serious concerns.

In particular, the "charter of sustainable economic activity," trumpeted especially by France and Germany, mixes statements of the obvious with rhetoric that baldly calls for the U.S. to relinquish its sovereign authority over economic policy to a global government. Of immediate concern is the charter's appeal for global, supranational financial regulation—a clear European power grab to contain and diminish the role and freedom of the U.S. financial sector.

The U.S. must reject any proposals at the G-20 summit (to be held in London on April 2) that would reduce its economic freedom or restrict its sovereignty. Instead of following these proposals, the U.S. should lead by pursuing an agenda that rejects protectionism and any further fiscal stimulus packages or corporate bailouts and by encouraging international cooperation—on a basis of national sovereignty—on reforms to the financial sector. These measures will both mitigate the severity of the current crisis and reduce the chances that hasty action now will lead to a worse crisis later.

The Background of the G-20 Summit. The G-20 is composed of 19 nations with leading economies or ones (such as Saudi Arabia) that are of particular importance for other reasons. The European Union is the 20th member. The International Monetary Fund (IMF) and the World Bank are also represented.

According to British Prime Minister Gordon Brown, the April summit will address "major questions of economic action" related to the global financial crisis.[1] The U.S. will attend the summit but has not announced what it hopes to achieve at it.

Europe's Unacceptable Plans. By contrast, Europe's leaders are well prepared. On February 22, officials from Britain, France, Germany, Italy, Luxembourg, Spain, the Netherlands, and the Czech Republic agreed on a seven-point program, which aims to ensure that all financial market activities reduce economic "imbalances" and promote market "stability."

The program includes a "charter of sustainable economic activity" that "would subject all financial market activities around the globe to regulation, including credit rating agencies." German Chancellor Angela Merkel said the charter would be "based on market forces but prevent excess and ultimately lead to the establishment of a global governance structure." French President Nicolas Sarkozy, supporting the charter, has stated that "a new system of regulation without sanctions would not have any meaning." Other key points in the program include action against so-called "tax havens" and a strengthening of the IMF and a doubling of its resources.[2]

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The Threats to American Interests. The threat to the U.S. is twofold.

1. The Threat to the American Economy. First, there is an economic threat to free markets and financial institutions, including banks, insurance companies, hedge funds, and private equity funds. The European program calls for financial market activities around the world to be regulated to ensure that they foster "sustainable economic activity," promote economic "balance," and do not upset market stability. On a national level, U.S.-style financial regulations relating to the safety and soundness of institutions and markets—regulations that ensure the financial system can properly service the rest of the economy—are appropriate. But on the supranational level contemplated by the EU, calls for this kind of regulation raise serious concerns about economic freedom.

For this reason, there should be significant concerns with British Chancellor of the Exchequer Alistair Darling's call for the creation of a "college of supervisors" and European demands for the establishment of a "global government structure" that will prevent the development of all market "excess." In light of the ongoing financial crisis, no country can say that its financial regulatory structure was up to the task: All have lessons to learn, reforms to enact. And every country should consider the policies of other nations as they search for solutions appropriate to their own circumstances and markets and as they pursue best practices. In addition, these reforms will be most successful if they present financial markets with consistent regulatory principles and approaches across countries. This does not mean, nor require, that governments give up their regulatory sovereignty to a global markets regulator.[3]

Likewise, the key leaders of the various monetary and regulatory authorities ought to meet regularly to exchange observations and views, and they do so in a multitude of fora. However, empowering a formal global "college of supervisors" to supersede these many ongoing discussions makes sense only as a preliminary step toward granting this college powers over national regulatory systems. Yet the college itself is more likely to be sclerotic, reacting too late if at all to the rapid changes of a nimble financial system.

Nor does it make sense to argue the crisis must be met by expanding the powers and resources of the IMF.[4] While the IMF, which had been on a path of contraction to oblivion prior to this financial crisis, cannot be charged with contributing to the crisis, it also completely missed the many causes of the crisis. Nor does the IMF's expertise suggest it has anything material to add to the resolution of this crisis or the prevention of any future troubles.

The EU's demand for action against "tax havens" poses another economic danger. In Europe, "tax haven" is code for any jurisdiction that has lower taxes than Europe that might lure Europeans into well-concealed tax evasion. The Brussels solution to the problem of "tax havens" is to compel these jurisdictions to report the financial activities of foreign investors investing in the tax haven country (e.g., Switzerland) and tax harmonization, which seeks to force low-tax countries to raise their taxes. Nations have every reason to protect their tax bases and to ensure their own citizens pay the taxes due. However, Europe's efforts to force other nations to have as anti-growth, anti-competitive tax regimes as it imposes on itself is little more than a subtle new form of protectionism and should be opposed in the United States and elsewhere.

2. The Threat to American Sovereignty. Second, and even more important, is the threat the European proposals imply to American sovereignty. Taken to its intended conclusion, the European

1. Press release, "UK to Host G20 Financial Summit," Office of the Prime Minister, November 26, 2008, at *http://www.number10.gov.uk/Page17594* (March 16, 2009).
2. Patrick McGroarty, "EU Leaders Back Wide Finance Reforms," Associated Press, February 22, 2009, at *http://www.washingtontimes.com/news/2009/feb/22/eu-leaders-back-sweeping-financial-regulations* (March 16, 2009).
3. *Ibid.*; Alistair Darling, "International Cooperation Is the Way Out of the Financial Crisis," *The Wall Street Journal*, March 13, 2009, at *http://online.wsj.com/article/SB123690430171914125.html?mod=googlenews_wsj* (March 16, 2009).
4. Darling, "International Cooperation Is the Way Out of the Financial Crisis."

charter reflects the latest variation on the long-standing European call for global, supranational financial regulation dominated by Europeans and backed by a system of inescapable sanctions. The ultimate goal, according to Chancellor Merkel, is the "establishment of a global governance structure."[5] Such a structure would transfer Americans' freedom to regulate their own markets to a global government entity.

Ever since the Second World War, Europe has worked toward creating a unified, centralized government of nation states, similar to but different from the United States. Ever since their economic model of large social payments, heavy regulation, and heavy taxation began to stumble in the face of more competitive economies in the United States, Asia, and elsewhere, the Europeans have sought to extend Brussels' growing control over Europe to other countries. In effect, Europe has sought to protect its struggling economic model by forcing it on others. A global regulator with a mandate to ensure the stability and balance of the world economy would be a tremendous step toward this objective.

This is an issue about which all Americans should feel strongly. The United States was founded upon the inalienable right of self-government. It is one thing to argue that the U.S. government, which is ultimately subordinate to the sovereign will of the people, should follow one policy or another. It is entirely different to argue that the people themselves should be deprived of the power to govern their economic life through their elected representatives and should thereby lose much of their political freedom. Global economic governance is not simply an economic fallacy; it is a fundamental assault on the political liberties of all Americans and on the concept of free and popular government around the world.

What the G-20 Summit Should Do. The G-20 summit can provide real assistance to the global economy simply by not doing anything destructive. But it can and should also take constructive measures.

- First, the summit must reject protectionism. Economists and historians alike agree that the Smoot-Hawley Tariff Act of 1930, introduced to protect American jobs, played a significant role in deepening the Great Depression.[6] The 'Buy American' provisions of the economic stimulus, like Prime Minister Brown's 2007 pledge of "British jobs for British workers," threaten to start a similar economically destructive beggar-thy-neighbor trade war.[7] The summit should not simply proclaim the virtues of free trade; it should demonstrate it is serious by committing to completing the soporific Doha Round through the World Trade Organization.
- Second, the summit should urge all states to reject further stimulus packages and corporate bailouts. Here, the U.S. has been in the wrong, as some European leaders have responsibly pointed out. As Axel Weber, the president of Germany's Bundesbank, said, "The expectation that we could neutralize this synchronized recession through short-term fiscal policy measures is false. We should not even try."[8] The costs of trying are high: The rising levels of government debt associated with stimulus packages—and the much more dangerous, if less immediate, entitlements crisis—have potentially catastrophic economic consequences.[9]

  Similarly, German Chancellor Merkel was correct to remark with skepticism that "when I look at

5. McGroarty, "EU Leaders Back Wide Finance Reforms."
6. Daniella Markheim, "Buy American Hurts America," Heritage Foundation *WebMemo* No. 2256, January 30, 2009, at *http://www.heritage.org/Research/tradeandeconomicfreedom/wm2256.cfm.*
7. Ted R. Bromund, "It's Beginning to Look a Lot Like the 1970s," The Foundry, February 6, 2009, at *http://blog.heritage.org/2009/02/06/it%E2%80%99s-beginning-to-look-a-lot-like-the-1970s*.
8. J. D. Foster, "One (Small) Reason for Optimism at the G20 Meeting," Heritage Foundation Foundry, March 11, 2009, at *http://blog.heritage.org/2009/03/11/one-small-reason-for-optimism-at-the-g20-meeting*.
9. International Monetary Fund, "The State of Public Finances: Outlook and Medium-Term Policies After the 2008 Crisis," March 6, 2009, p. 45, at *http://www.imf.org/external/np/pp/eng/2009/030609.pdf* (March 16, 2009).

the restructuring plans of some American [auto] companies, there are a lot of state funds flowing into them."[10] Corporate bailouts of industrialized firms are a disguised form of protectionism and a poor use of tax revenues. The right course of action is not to bail out failures but to allow them to go bankrupt and—if they are viable—to be reorganized through the Chapter 11 process.[11]

- Third, the summit should emphasize sensible reforms in the financial sector. These reforms should not be headline-grabbing expropriations of national sovereignty, nor should they be hastily agreed to in detail at the summit. Rather, as Chancellor Darling has suggested, the summit should commit to the broad goals of improving the practices of the financial sector by focusing additional attention on transparency, leverage, and market operations.[12] To avoid a politicized rush to judgment, the summit should leave the negotiation of these reforms to the experts in the respective countries and their legislative and executive authorities.

Reject Dangerous EU Plans. Early reports suggest the EU's plans for the G-20 summit are economically dangerous and politically unacceptable. For the sake of the world's recovery and future prosperity, and its own national sovereignty, the U.S. must reject these plans completely. The G-20 should find common ground on defending free trade, opposing further unwise government spending, and reforms to the banking sector that are designed and implemented to achieve financial, not political, goals. Any other course of action would be an unacceptable subversion of America's freedom.

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10. Ted R. Bromund, "Europe's Answer to the Financial Crisis?: Bigger Government," The Foundry, February 24, 2009, at *http://blog.heritage.org/2009/02/24/europe%E2%80%99s-answer-to-the-financial-crisis-bigger-government*.
11. Andrew M. Grossman, "Ailing Automakers Need Bankruptcy, Not Bankruptcy-Lite," Heritage Foundation *WebMemo* No. 2342, March 12, 2009, at *http://www.heritage.org/Research/Regulation/wm2342.cfm.*
12. Darling, "International Cooperation Is the Way Out of the Financial Crisis."