

## THE IMPACT OF ENFORCEMENT: A REFLECTION

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In response to John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229 (2007).

Professor John Coffee is one of the most insightful and imaginative scholars of modern corporate finance, and I am delighted that he has turned his fertile mind to the study of enforcement in securities regulation. On the view that extension is the sincerest form of flattery, I am especially pleased to see that Professor Coffee has found my own earlier work on regulatory intensity as a useful starting point for aspects of his analysis.<sup>1</sup>

When I first identified the striking differences in regulatory intensity across jurisdictions, I had hoped that others would do just what Professor Coffee has attempted in his article: refine my preliminary data and develop a better theoretical understanding of the significance of variations of regulatory intensity for the quality of financial markets.<sup>2</sup> Professor Coffee has made progress on both fronts. His article introduces new data on formal enforcement actions and budgets in the United Kingdom, Germany, and Australia<sup>3</sup>—and makes a compelling argument that the high level of enforcement activity in the United States explains, in part, why foreign issuers have been attracted to U.S. public capital markets in recent years and why some classes of foreign issuers still are.<sup>4</sup> This second point has important policy im-

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<sup>1</sup> See John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229, 258 (2007).

<sup>2</sup> See Howell E. Jackson, *Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications*, 24 YALE J. ON REG. 253, 271-80 (2007) (presenting cross-jurisdictional data). In a similar spirit, my colleague Mark Roe and I have produced an empirical study showing the positive impact of real resources committed to public enforcement on robust capital markets. See Howell E. Jackson & Mark J. Roe, *Private and Public Enforcement of Securities Laws: Resource-Based Evidence* (Feb. 22, 2008) (unpublished manuscript), available at <http://ssrn.com/abstract=1003177>.

<sup>3</sup> See Coffee, *supra* note 1, at 276-83.

<sup>4</sup> See *id.* at 235-36 (explaining the “bonding hypothesis,” which says that “by subjecting themselves to the SEC’s higher disclosure standards and the greater prospect of enforcement in the United States, foreign firms reduce their agency costs”).

plications for the ongoing debate over the competitiveness of U.S. financial regulation, as it suggests that a relaxation of U.S. regulatory standards and a retreat from the SEC's traditional emphasis on enforcement may in the long run actually reduce this country's ability to compete for foreign listings and capital market dominance.<sup>5</sup> The uniqueness of U.S. enforcement efforts that Professor Coffee identifies also raises potentially serious questions about the wisdom of recent proposals to accept foreign regulatory regimes as systems of substitute compliance for U.S. oversight of foreign exchanges and securities firms.<sup>6</sup>

In a post-legal-realist world, the proposition that the law on the books does not fully capture the significance of legal regimes is uncontroversial. The frequency with which laws are enforced and the consequences of successful enforcement actions quite plausibly have real economic consequences. Thus, one might readily expect that financial markets with stronger mechanisms for enforcing legal requirements will behave differently than those financial markets in similar jurisdictions with identical legal requirements and less enforcement. Hence, the core of Professor Coffee's thesis—that higher levels of enforcement in the United States benefit U.S. financial markets—seems eminently reasonable. But to validate this claim, one needs to devise an objective measure of enforcement efforts, and then (ideally) to undertake empirical tests of the relationship between that measure of enforcement and other measures of financial market performance in a number of different settings.

In this Response, I will touch briefly upon the not inconsiderable challenges confronting researchers seeking to confirm or rebut the claims that Professor Coffee advances. There are substantial complexities involved in comparing levels of international regulatory intensity. Moreover, the globalization of financial markets and the increasing collaboration among regulatory bodies makes it even more difficult to structure clean tests of the impact of the supervisory efforts of individual countries. While there are alternative mechanisms

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<sup>5</sup> Cf. COMM. ON CAPITAL MKTS. REGULATION, INTERIM REPORT OF THE COMMITTEE ON CAPITAL MARKETS REGULATION 71-91 (2006), [http://www.capmksreg.org/pdfs/11.30Committee\\_Interim\\_ReportREV2.pdf](http://www.capmksreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf) (arguing that the high level of regulatory intensity in the United States disadvantages U.S. markets).

<sup>6</sup> See Howell E. Jackson, *A System of Selective Substitute Compliance*, 48 HARV. INT'L L.J. 105 (2007) (discussing the proposals of Ethiopis Tafara and Robert J. Peterson in their article, *A Blueprint for Cross-Border Access to U.S. Investors: A New International Framework*, 48 HARV. INT'L L.J. 31 (2007)).

whereby one could evaluate the efficacy of regulatory oversight, it is not clear which approach will generate the most meaningful results in validating Professor Coffee's hypotheses that U.S. public enforcement provides a unique benefit to American markets and that lesser degrees of enforcement activity in other jurisdictions mean that their supervisory approaches should not be considered acceptable substitutes for U.S. oversight.

#### I. CHALLENGES IN DEVISING OBJECTIVE MEASURES OF REGULATORY INTENSITY

The two basic approaches that Professor Coffee and I have utilized to measure the regulatory intensity of supervisory regimes are regulatory inputs, such as staffing or budgets, and regulatory outputs, such as enforcement actions or monetary sanctions. As Mark Roe and I have discussed elsewhere,<sup>7</sup> each of these approaches has its advantages, but both are also susceptible to a number of criticisms, which could be categorized as incompleteness, misdirection, and inadequate granularity.

##### A. *Incompleteness*

No matter how one attempts to measure regulatory intensity across jurisdictions, there is always a concern that one has failed to identify all relevant regulatory inputs. This problem is most apparent for staffing and budget measures, with the United Kingdom offering a good example. While the U.K.'s Financial Services Authority (FSA) is perhaps the premier example of a consolidated supervisory agency, the British actually maintain several other regulatory bodies that fulfill functions comparable to those of the U.S. SEC. The British Financial Reporting Council employs a staff of fifty-five with a budget of £14.5 million, polices auditing firms and the accounting statements of corporate issuers, and undertakes activities comparable to those of the SEC's Division of Corporate Finance and the Public Company Accounting Oversight Board (PCAOB).<sup>8</sup> The Panel on Takeovers and

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<sup>7</sup> See generally Jackson & Roe, *supra* note 2 (comparing the merits of public and private securities regulation). Another complexity not discussed in this Response is the need to make adjustments to account for economies of scale that likely occur in financial regulation based on market size and perhaps also the size and number of regulated firms.

<sup>8</sup> See Devon Kirk & Tonbofa Ashimi, An Overview of Securities Enforcement in the United Kingdom 16-18, 22-23 (Nov. 20, 2007) (unpublished manuscript, on file with author).

Mergers also plays an important role, somewhat comparable to the SEC's with respect to proxy fights and tender offers.<sup>9</sup> Regulatory comparisons that rely solely on FSA staffing or budget levels miss these other important regulatory components.

The supervisory functions of stock exchanges also complicate comparative head counts. In the United States, the supervisory activities of the NYSE and NASD have, for a number of years, been isolated in separate operational units, and are now fully removed into the Financial Industry Regulatory Authority (FINRA).<sup>10</sup> Around the world, the supervisory roles of exchanges have diminished with the demutualization of all major exchanges and the dictates of EU listing directives.<sup>11</sup> However, regulatory functions do still take place in many exchanges, especially with respect to the review of new listing applications, where exchange personnel often take on roles similar to, though invariably less intensive than, those of SEC staffers who review registration statements for IPOs. The Hong Kong stock exchange's oversight of new listings would be a good example of this role.<sup>12</sup>

Finally, there is variation in the reliance that different regulators make of private assistance. Within the German civil law tradition, this reliance seems particularly striking. As Professor Coffee notes, Germany's BaFin makes use of outside audits to supplement regulatory oversight.<sup>13</sup> The Swiss Federal Banking Commission makes even more extensive use of outside auditors, requiring them to undertake annual supplemental (and confidential) reports with respect to regulatory compliance.<sup>14</sup> These reports are comparable to what the SEC's Office of Compliance Inspections and Examinations might produce, but the Swiss personnel who undertake these reviews do not show up on government payrolls.

Similar problems of completeness exist in collecting comprehensive data on enforcement outputs. For example, in evaluating enforcement efforts in the United Kingdom, one would want to consider

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<sup>9</sup> *Id.* at 13-15.

<sup>10</sup> Stavros Gadinis & Howell E. Jackson, *Markets as Regulators: A Survey*, 80 S. CAL. L. REV. 1239, 1330-31 (2007).

<sup>11</sup> *See id.* at 1244-45 (discussing the impact of demutualization on regulator decision making).

<sup>12</sup> *See id.* at 1284 tbl.6, 1286 (detailing Hong Kong's regulatory framework).

<sup>13</sup> Coffee, *supra* note 1, at 280-81.

<sup>14</sup> *See* Sweetha Ballakrishnen et al., *An Overview of Securities Enforcement in Switzerland 7* (Nov. 21, 2007) (unpublished manuscript, on file with author) (describing the role of authorized outside auditors in the Swiss system).

both the oversight functions of the Financial Reporting Council mentioned above and also the Financial Ombudsman Service, which provides mediation services for a large number of matters each year,<sup>15</sup> but whose enforcement actions are not included in the data reported in Professor Coffee's article. One should also probably take into account the predilection of some regulatory bodies to resolve enforcement actions informally and without public disclosure. Again, this is a common practice for the British FSA, but it is also employed by many other jurisdictions, including, for example, Switzerland, where many enforcement actions are reported only on an anonymous basis.<sup>16</sup>

### B. *Misdirection*

By misdirection, I mean the possibility that both publicly reported regulatory resources and enforcement outputs may not actually be intended to produce supervisory services. To begin with, there is an obvious question of whether all resources allocated to regulatory agencies are in fact employed in bona fide supervisory functions, as opposed to serving as sinecures for cronies of political elites or positions from which to extract bribes and other economic rents.<sup>17</sup> While all of the major financial centers of the world—the United States, the United Kingdom, Hong Kong, Luxembourg, Singapore, and Amsterdam—do report above-average levels of regulatory staffing and budgets, one can also find some more surprising jurisdictions (like Nigeria and Jordan) that report devoting substantial resources to regulatory agencies. The possibility of graft and sinecures may produce nontrivial levels of “noise” in measures of regulatory input, especially for samples that include the developing world.

One might also imagine similar misdirection in reported enforcement activities, if, for example, financial sanctions were being imposed to penalize political opponents of the parties in power, or to punish industry participants for failing to pay bribes to regulatory officials. While this may seem to be the kind of problem one would encounter in seriously corrupt jurisdictions, there is a possibility that the problem is more widespread. In the United States, for example, the monetary penalties imposed earlier this decade by state authorities, led by former New York Attorney General Eliot Spitzer, materially in-

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<sup>15</sup> Kirk & Ashimi, *supra* note 8, at 20, 31.

<sup>16</sup> See Ballakrishnen et al., *supra* note 14, at 17-18.

<sup>17</sup> See generally ANDREI SHLEIFER & ROBERT W. VISHNY, *THE GRABBING HAND: GOVERNMENT PATHOLOGIES AND THEIR CURES* 81-108 (1998) (examining the destructive impact of rent-seeking and corruption).

creased the level of overall U.S. monetary sanctions.<sup>18</sup> The most uncharitable critics of Mr. Spitzer claimed that these actions were primarily designed to advance his own political ambitions;<sup>19</sup> if true, the inclusion of these actions in aggregate U.S. data could confound analysis that proceeds on the assumption that all monetary sanctions are imposed to deter wrongful market behavior.

### C. *Inadequate Granularity*

One of the virtues of Professor Coffee's analysis is that it attempts to provide greater granularity to the subject of regulatory inputs by examining the portion of regulatory staffs dedicated to enforcement activity.<sup>20</sup> Extending his analysis, one could imagine decomposing the allocation of staffs into supervisory building blocks of rule formulation, examination and inspection, enforcement, and other sectors. While one would face considerable challenges in assembling such data—currently regulatory agencies are remarkably eclectic in job classifications, and the lines between examination and enforcement often blur—the development of more refined staffing data would be of considerable interest. One might, however, imagine other ways in which to subdivide regulatory personnel to generate equally interesting granularity. The professional backgrounds of regulatory personnel vary substantially across jurisdictions. The SEC hires many lawyers and accountants; in contrast, the British FSA employs more economists and high-level staff drawn from industry ranks. There are also differences in the extent to which regulatory personnel move back and forth between industry and government, as opposed to staying largely within a civil service path. In addition, the degree to which regulatory personnel turns over with changes in political leadership also varies a good deal across jurisdictions. It is not entirely clear which staffing divisions are most closely tied to strong financial mar-

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<sup>18</sup> See Jackson, *supra* note 2, at 280 tbl.3 (showing that monetary sanctions by state agencies between 2002 and 2004 accounted for slightly more than one-fifth of the total amount of public sanctions imposed in the United States).

<sup>19</sup> See, e.g., Posting of William J. Holstein to The Corner Office, Eliot Spitzer's Legacy on Trial, <http://blogs.bnet.com/ceo/?p=1081> (Jan. 7, 2008, 06:31) (“[I]t was obvious [Spitzer] was using his powers as attorney general to win the gubernatorial race in New York . . .”). Note, however, that Mr. Spitzer's enforcement actions might still have had positive deterrent effects on financial misbehavior, even if the actions were partially motivated by personal advancement.

<sup>20</sup> See, e.g., Coffee, *supra* note 1, at 272-73 (noting that despite similarities in staffing and budgetary levels among the major regulators in Canada, the United Kingdom, and the United States, “the United States punishes more severely”).

kets, but to the extent that staffing allocations are significant—an assumption of Professor Coffee’s discussion of enforcement staffing levels in the United States and Australia—then one might want to examine the relationship on multiple dimensions.

Similar distinctions could also be made with respect to enforcement actions and penalties. In most jurisdictions, regulatory officials have jurisdiction over a wide range of activities—including the quality of corporate disclosures, insider trading and market manipulation, the sales practices of securities firms, and a host of technical rules regarding financial institutions’ solvency and the technical operation of markets. The distribution of enforcement efforts varies a good deal from jurisdiction to jurisdiction, with the SEC placing more emphasis on the review of disclosure documents and enforcement actions against other issuers than do other jurisdictions.<sup>21</sup> And, of course, the incidence and distribution of private enforcement actions against both issuers and securities firms varies from country to country. Aggregate data about overall enforcement actions and sanctions may obscure important differences across enforcement categories.

## II. UNDERSTANDING THE MECHANISMS OF ENFORCEMENT

Even assuming one could assemble data, with an appropriate degree of granularity, about the real resources allocated to legitimate public oversight of financial markets and the associated measures of formal enforcement actions, one might still be a long way from divining whether a particular jurisdiction’s level of regulatory intensity ensures an adequate level of compliance or sufficient oversight to foster robust capital markets. The linkage between regulatory intensity and positive economic outputs is not well understood and may vary from jurisdiction to jurisdiction.

Consider, for example, the possibility that the regulated entities in one jurisdiction—think Sweden—are more apt to comply with newly promulgated legal rules than their counterparts in other jurisdictions—say Italy.<sup>22</sup> This commonly accepted stereotype of the North-

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<sup>21</sup> See, e.g., Howell E. Jackson, *Regulatory Intensity in the Regulation of Capital Markets: A Preliminary Comparison of Canadian and U.S. Approaches*, in THE TASK FORCE TO MODERNIZE SECURITIES LEGISLATION IN CANADA, CANADA STEPS UP: RESEARCH STUDIES: STRENGTHENING MARKET CREDIBILITY AND INTEGRITY 118-19, 120 fig.5 (2006), available at [http://www.tfmsl.ca/docs/V6\(2\)%20Jackson.pdf](http://www.tfmsl.ca/docs/V6(2)%20Jackson.pdf) (providing data showing that the SEC puts forth great effort to prosecute issuer-related violations).

<sup>22</sup> See Jackson, *supra* note 2, at 265 (“Some jurisdictions may be populated with scofflaws, prone to abusive practices and needing intensive and continuous oversight.”)

South European divide would imply that fewer enforcement actions are necessary in some jurisdictions than in others in order to generate the same impact on private market behavior. One does not, however, need to posit transjurisdictional variation in inherent lawfulness in order to have concerns about the comparability of enforcement efforts from one country to the next. The means by which regulators enforce legal requirements may well differ materially around the world. The light-touch regulation of the British FSA includes numerous mechanisms of public-private exchange, ranging from the raised eyebrow on official Albion foreheads to the quite complex network of advisory committees and consultations that characterize British supervisory practices. Somewhat similar in effect is the use of informal guidance in Japan. All of these alternative mechanisms of social control are plausible substitutes for the formal enforcement actions that characterize the regulatory activity in the United States and a few other jurisdictions. The relative scarcity of enforcement actions in these other jurisdictions does not necessarily imply greater noncompliance or economic drag.

It is also important to examine the relationship between public enforcement efforts and private sanctions. As Professor Coffee notes, private litigation in the United States often follows on the heels of public sanctions.<sup>23</sup> And thus the significance of public enforcement efforts in the United States, as compared with the United Kingdom or Germany, may be even greater than the raw numbers suggest. However, litigation may not be the only, or even the most, important private response to public enforcement actions: market movements in the form of price declines for shares and career consequences for implicated individuals may be far greater.<sup>24</sup> Plus, to the extent that viola-

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Other populations may be more lawful . . . and hence less in need of supervisory oversight.”).

<sup>23</sup> See Coffee, *supra* note 1, at 275 (describing the “tendency for public and private penalties to be imposed on a cumulative and overlapping basis”); see also James D. Cox et al., *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737, 763 (2003) (finding that the defendants in 37 of 248 securities class actions had also been sued by the SEC).

<sup>24</sup> See Jonathan M. Karpoff et al., *The Cost to Firms of Cooking the Books*, J. FIN. & QUANTITATIVE ANALYSIS (forthcoming) (manuscript at 1), available at <http://ssrn.com/abstract=652121> (stating that the largest monetary penalties for misconduct are imposed by the market, not regulators or the courts); Jonathan M. Karpoff et al., *The Consequences to Managers for Financial Misrepresentation 1-3* (Apr. 16, 2007) (unpublished manuscript), available at <http://ssrn.com/abstract=972607> (asserting that shareholders sustain losses and culpable managers lose their jobs when companies are accused of misconduct).



tors are public firms, the proxy process and voting power may impose additional sanctions on management. At this stage, most of the work done on market reactions to public enforcement efforts has focused on U.S. markets; thus we do not know whether foreign markets impose similar knock-on sanctions. It is, however, conceivable that in some foreign jurisdictions private monitors do a better job of amplifying public sanctions than do U.S. markets. In London, for example, shareholders are said to have more power in the boardroom and so British investors may respond to FSA sanctions more effectively than their U.S. counterparts respond to SEC sanctions.

### III. GLOBALIZATION AND ENFORCEMENT

Globalization also complicates comparative evaluations of enforcement data on many dimensions. Cross-listed firms are one case in point. If one considers the number of enforcement actions in Canada and adjusts for the relative size of the Canadian market, one would likely conclude that the level of securities enforcement in Canada is substantially lower than in the United States. However, it turns out that quite a large number of leading Canadian firms are cross-listed in the United States, and therefore are also subject to many U.S. regulatory requirements, supervisory standards (including exchange oversight), and even private liability rules. Accordingly, the Canadian system of securities oversight does not constitute the entire universe of legal constraints on a major portion of the Canadian stock market. To some degree, Canadian securities markets free-ride off of U.S. regulatory intensity.<sup>25</sup>

The increasing collaboration across jurisdictional boundaries complicates our evaluation of national regulatory efforts in other ways as well. With the globalization of financial markets, regulatory officials routinely refer matters to their counterparts in other jurisdictions. Often, a problem like insider trading or market manipulation will be detected in one market but will be referred to a second or third jurisdiction, where the investor making the trades or the firm in whose stock the trade is affected is located. Referrals of this sort happen hundreds and perhaps even thousands of times each year, and

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<sup>25</sup> See Jackson, *supra* note 21, at 97. Alternatively, when one normalizes the amount of regulatory activity in Canada, one could reduce the market capitalization of Canadian domestic firms to account for the fact that the United States oversees some portion of that market capitalization. Of course, one should then adjust upward the level of market capitalization of U.S. markets, at least for determining the effective level of U.S. market oversight. *Id.*

greatly expand the investigatory powers and enforcement reach of national regulatory authorities. For many jurisdictions, these cooperative arrangements may substantially enhance their regulatory capacity beyond those suggested by the countries' own supervisory forces.

A similar point can be made about the development of new regulatory policies and legal standards. In the past, such activities were largely conducted independently at the national level, with relatively little cross-border collaboration. In recent times, however, a relatively small number of jurisdictions—the United States and the United Kingdom being the most prominent examples—have dedicated substantial resources to policy analysis and the development of new rules for emerging issues such as hedge funds and derivatives transactions, and then have shared their conclusions with other jurisdictions (often with the assistance of multilateral bodies, such as the International Organization of Securities Commissions (IOSCO) or the Basel Committee, or regional treaty arrangements, such as the European Union). As a result, smaller countries—even those with quite substantial financial markets—benefit from policy and rule development occurring beyond their borders. Analyses that focus solely on local resources miss this important regulatory networking.

#### IV. HOW ELSE MIGHT WE MEASURE THE ADEQUACY OF REGULATORY INTENSITY?

Let us now return to the key policy issues that Professor Coffee raised in his article. How might we go about determining whether the United States or some other jurisdiction was devoting adequate resources to supervising and policing financial markets? While comparisons of regulatory staffing and budgets, or overviews of enforcement intensity, may help identify instances where a country differs dramatically from international standards—as does the United States in the case of securities class action suits—these measures of regulatory inputs and outputs are likely to be too crude to make sharp distinctions across a wide range of jurisdictions, even if one could establish—as Mark Roe and I have attempted—that the allocation of greater resources to public enforcement is generally associated with more robust capital markets.<sup>26</sup> What other measures of quality exist? In my view, there are two plausible, alternative approaches.

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<sup>26</sup> See Jackson & Roe, *supra* note 2.

The first would focus on technical measures of financial performance. With respect to corporate issuers, one might consider the cost of capital across jurisdictions on the assumption that if domestic firms within a jurisdiction can raise capital at reasonable prices, that jurisdiction must have a reasonably acceptable legal system to oversee the issuance of securities, or, at least, local markets must have developed adequate mechanisms to police serious agency costs by corporate insiders or controlling shareholders. In a similar spirit, one could look to the behavior of trading markets—bid-ask spreads, price synchronicity, and evidence of trading on inside information—to draw inferences about regulatory quality.<sup>27</sup> The evidence of equity premiums for cross-listed firms discussed in Professor Coffee's article has similar probative value,<sup>28</sup> but is potentially available for only a limited number of jurisdictions—the United States, the United Kingdom, and perhaps Hong Kong or Luxembourg—which attract substantial numbers of cross-listings. The vast majority of national stock markets do not compete for foreign listings, and are quite happy if they can simply retain their domestic firms.

Another metric for evaluating financial markets can be found by examining the behavior of market participants. This kind of evidence is often cited in the unfolding debate over U.S. capital market competitiveness. The declining number of new foreign listings and the spike of foreign firm deregistrations in the latter half of 2007 have been seen as evidence that American regulation has become too onerous.<sup>29</sup> Conversely, one could see evidence of a rising number of new foreign listings as a measure of the quality of those markets that actively compete for foreign listings. More widely applicable would be a market test based on the increasing presence in foreign markets of institutional investors (as well as retail investors) from the United States and other developed nations. When sophisticated institutional investors make substantial investments in a country's financial markets and depend on that market's trading systems and support mechanisms,

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<sup>27</sup> Some different technical measures would be necessary to assess the quality of broker-dealer interactions with their customers as well as that of asset managers, such as mutual funds. One could, however, examine the costs of such intermediation services and their impact on portfolio returns to draw inferences about the efficacy of regulatory controls.

<sup>28</sup> See Coffee, *supra* note 1, at 235-36 (noting that equity premiums for cross-listed firms occur only in the United States, which Professor Coffee attributes to the benefits of intense U.S. enforcement activity).

<sup>29</sup> See COMM. ON CAPITAL MKTS. REGULATION, THE COMPETITIVE POSITION OF THE U.S. PUBLIC EQUITY MARKET 3 (2007), available at [http://www.capmksreg.org/pdfs/The\\_Competitive\\_Position\\_of\\_the\\_US\\_Public\\_Equity\\_Market.pdf](http://www.capmksreg.org/pdfs/The_Competitive_Position_of_the_US_Public_Equity_Market.pdf).

such as custodial services and clearing arrangements, that confidence represents another source of market-based information on the quality of foreign markets and may well have some probative value in corroborating the quality of local regulation and legal regimes.

#### CONCLUSION

So what is to be done if we wish to gain better insight into the relative quality of regulatory systems? The short answer, I think, is that no single approach will suffice. Analysis of regulatory intensity—both in terms of regulatory inputs and outputs along the lines that Professor Coffee and I have both attempted—has undoubted value. But one must be careful to draw the comparisons accurately with considerable attention to institutional variation across jurisdictions. Confident normative judgments about the implications of observed variations in regulatory intensity should await empirical validation. One should also consider evidence available from objective measures of quality that are more directly tied to financial performance, as well as the additional information one can derive from observing how market participants, both corporate issuers and sophisticated institutional investors, vote with their feet and their dollars.

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