

# Financial reform

New frontiers in transparency  
and accountability

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# Executive summary

The term 'financial reform' is used by participants in the Transparency and Accountability Initiative collaborative in three different but overlapping senses: reform of the defects and abuses in the banking system that caused the recent financial collapse; reform of the financing of economic development; and reform of financial flows that are often opaque, leading to corruption, tax evasion and other failures of accountability. Below are some core insights and questions that grew out of the research and interviews for this strategic review.

## The imbalance of resources

In all three areas of financial reform, there are extreme disparities of resources between forces favouring reform and industry and governmental entities that thrive on opacity. Much of this paper deals with strategies for increasing countervailing power, access and capacity on the part of civil society organisations (CSOs) and other reform groups. The paper uses case studies of reform campaigns and of strategies to increase access, influence and transparency in all three areas of financial reform. The asymmetry seems most extreme in the area of core reforms of the banking system. NGOs have had some success in influencing reform legislation in North America and Europe, but going forward the details of complex regulatory issues are being decided by government executive agencies, in some cases with little or no participation by civil society, leaving the field to be dominated by self-interested industry actors.

## The potential for new capacity and synergy

The research suggests that there are often parallel campaigns by groups with broadly similar reform objectives, but that these groups often do not collaborate. A development frame informs one set of reform NGOs; a banking-reform frame informs others; a secrecy and transparency frame informs a third set. At the same time, in recent years, new and broader coalitions have been built. For example, development-oriented NGOs have begun engaging banking reform because the financial crisis and banking system abuses impinge on development goals, and new collaborations are emerging. The paper maps groups and issues. Its recommendations suggest both gaps in areas needing reform, and potential areas for greater synergy.

## The connection between transparency and accountability

Transparency is both a means of mobilising support for reform and often the essence of the reform itself. However, there are some areas of policy where increased NGO participation is desirable but where other substantive reforms, such as outright prohibitions of abusive products and practices, are the preferred remedy. A question for the T/A collaborative to consider is whether only initiatives built explicitly around transparency reforms should qualify for inclusion in this project, or whether other substantive reforms are pertinent as well.

This paper identifies 14 promising areas for new initiatives, often deliberately cutting across the three different realms of financial reform. It proposes criteria for successful initiatives. Its companion report then narrows these down to five recommended new projects, which are laid out in detail.

## Summary of recommendations

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### 1. A general campaign to abolish secrecy jurisdictions

Tax and Regulatory havens are an affront to transparency and the rule of law. There is already a campaign against tax havens, and a weak OECD initiative against them. This could be generalised to a broad coalition of NGOs with a goal of shutting down secrecy jurisdictions down.

### 2. Shadow banking, sustainable development, and systemic risk

Abuses by derivatives, hedge funds, and private equity companies bridge the concerns of NGOs addressing banking reform and those concerned with development. Systemic risks persist, regulation is still weak, and commodities speculation in foodstuffs is responsible for recent spikes in the price of food. Despite recent reforms, these areas remain the most inadequately regulated and opaque of the financial system. A broad civil society coalition could wage a common campaign for transparency and accountability.

### 3. Credit rating agencies

Credit Rating Agency abuses were at the heart of the financial collapse. Without corrupt and non-transparent triple-A ratings, there would have been no mass market for securitised sub-prime loans. Because of their power over sovereign debt, rating agencies are also implicated in high capital costs for poor countries and those hard hit by the recession. Credit rating agencies are essentially unregulated and opaque, yet there is no civil society campaign for reform, and this is fertile ground.

### 4. Accounting reform and beneficial ownership

There is the beginning of a general campaign for greater disclosure and transparency in all forms of accounting, including country-by-country disclosures of corporate profits, and full transparency of true ownership. This has been the work of development-oriented NGOs, but could be linked to banking system reforms, where off-balance-sheet accounting and other fraudulent bookkeeping was a key cause of the financial bubble and collapse.

### 5. New strategies for resources, funding, and capacity building

This review has revealed a vast disparity of resources between CSOs and industry groups resisting transparency and accountability – and foundation funding alone will never make up the gap. This initiative proposes systematic exploration of complementary funding sources: mass membership organisations, payments to CSOs as experts and intervenors, arms-length funding by states and international governmental organisations, and official status for CSOs including funding.

# 1. Introduction: Concepts, definitions and challenge

This strategic assessment is one in a series of five papers that are part of the New Frontiers collaborative initiative on transparency and accountability.

This strategic assessment is one in a series of five papers that are part of the New Frontiers collaborative initiative on transparency and accountability. Financial reform has a variety of facets and definitions. One is the **regulation of the banking system**, whose speculative abuses and near collapse in 2007–09 set off a global recession that is still causing a prolonged period of economic stagnation and human suffering. A second realm is reform of **global financial flows**, including payments to governments by extractive and other industries, illicit or opaque money transfers, money laundering, the role of non-transparent players such as sovereign wealth funds, capital flight from developing countries and flows of funds into tax and regulatory havens as a way to avoid regulatory scrutiny and tax collection. A third realm is the **financing of third world development**, where such issues as debt relief, IMF conditionality, World Bank practices, terms of private investment and constraints on domestic financial policies imposed by the WTO have long been contested by civil society organisations (CSOs) both North and South. This last topic partly overlaps another paper in this project, but it also intersects with financial reform in the other two senses, since some of the same NGOs are involved and similar strategies and campaigns have been employed.

So one of the challenges for this paper and for this collaborative is to sort out financial reform in its several dimensions, and to determine where transparency can make a significant difference for accountability, for the energising of civil society and for substantive reforms beyond transparency as a desirable end in itself. The research and interviews conducted for this paper reveal that there is substantial activism of CSOs in some areas of financial reform, while in others there is little presence. This assessment also finds some areas of collaboration among

groups working on different aspects of financial reform, but other areas where potential synergies are not pursued. Typically, this fragmentation occurs because groups each focus on their core issues, or because conceptions of mission differ, or because parallel campaigns operate with little cross-fertilisation, mainly because NGOs are so under-resourced and spread thin. This paper also identifies where opportunities exist for increased collaboration and impact.

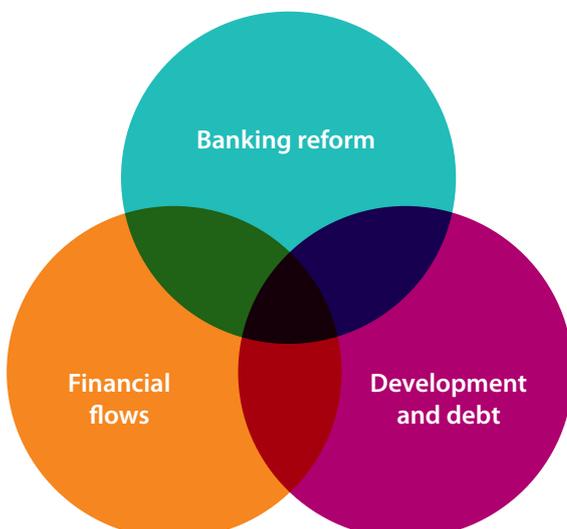
## Transparency

The premise of the New Frontiers project and this consortium generally is that greater transparency is valuable both as a strategy of CSO mobilisation to promote reform and as policy. Since other papers have addressed definitions and benefits of transparency at great length, I will not repeat that general exercise here except to offer some observations about how transparency applies in different areas of financial reform, and its relationship to accountability.

Transparency seems a better fit with reform objectives in some areas of financial reform than in others—as a tactic, a means of mobilising campaigns for substantive reform, and as the substantive reform itself. So we need explicit criteria for identifying when transparency is a strategy of choice, and when it can lead to breakthroughs in public policy as well as serving to further mobilise civic counterweights to financial interest groups that thrive on opacity. This is addressed in detail in Section 3 below.

For example, the Publish What You Pay (PWYP) campaign demonstrated the power of transparency on multiple fronts. The campaign defined and then dramatised an abuse—corrupt uses of payments by extractive industries to third world governments. It called for disclosures by companies; had some success in rallying media and public attention; built a broad coalition of NGOs; elicited some voluntary compliance by corporations; succeeded in getting disclosure requirements included in the recent Dodd-Frank Act in the United States – which in turn will produce a virtuous circle of more transparency, more disclosure requirements elsewhere, and more of a rallying point for advocacy and deeper reform of corrupt practices.

FIGURE 1.



Another example is the anti-redlining campaign in the USA, which began in the 1970s when community groups began using data on mortgage loans to embarrass banks that were refusing to lend to minority or low-income communities. These data were not available in a form that could easily be tabulated and had to be gathered one transaction at a time from local registries of deeds. So a broad coalition of civil society groups petitioned Congress to require banks to aggregate and publicly disclose the number and value of their mortgages, by postal code. Congress obliged; and armed with the data the groups were able to recruit more members, intensify calls for affirmative service to formerly excluded communities, and make redlining a more prominent local and national issue. This strategy led to additional gains, a more effective NGO movement for community reinvestment, allies inside the banking sector, and a strong, continuing coalition that builds on past gains.

In both of these cases, in quite different policy areas, transparency proved to be very powerful as an instrument of reform, both substantively and as an organising tool. But this is not the case in every area of potential reform.

For example, in the case of sub-prime mortgages and the related packaging and securitisation of high-risk debt, the abuse was hidden in plain view. The increasing proliferation of sub-prime mortgages was a matter of public record. So were the typical terms, though they were often deceptively packaged to retail borrowers. The abuses and risks were noted by journalists (including this writer), civil society organisations and scholars, by a vocal minority of financiers such as Warren Buffett, at Congressional hearings, and by dissenting regulators including at least one governor of the U.S. Federal Reserve Board who wrote an entire book on the subject.<sup>1</sup> But the well-documented alarm gained no political traction and the crisis continued to incubate and intensify until the crash came.

Clearer disclosure of deceptive terms to borrowers at a retail level could have discouraged some sub-prime lending, but the public information was already more than adequate to signal serious policy problems, had elites not been compromised by the influence of the immense sums of money being made. The problem was less a lack of transparency per se than a combination of a market failure to appreciate the risks coupled with a political and regulatory failure to address plainly visible abuses. For example, essentially unregulated credit rating agencies were permitted to engage in corrupt conflicts of interest and to issue falsely reassuring ratings on securitised sub-prime loans. These regulatory failures in turn, reflected a gross political imbalance between the financial industry and its critics. Stronger NGOs definitely could have helped right this imbalance; better disclosure is part of the remedy though not its entirety. Certain abusive practices simply needed to be prohibited.

In short, transparency as both tactic and substantive reform is a good fit with some reform objectives, but not all. Our task is to clarify the targets of opportunity, and to decide whether transparency is viewed by the T/A collaborative as the *sine qua non* in our efforts to enhance the role of civil society to promote financial reforms. One finding of this paper is that NGOs that work primarily on reform of the structure and regulation of the banking system are relatively weaker than those that work on reform of financial flows and on development and debt issues – though some promising synergies and coalitions have begun to appear. So another key issue for the collaborative is whether promotion of these synergies is a primary goal in identifying and prioritising promising new initiatives.

## Accountability

The term 'accountability' is an even more slippery word than 'transparency', because it invites the question: accountability to whom? We can mean accountability to communities, to workers, to shareholders, to other stakeholders, to NGOs, to democratically elected governments. One form of accountability is not necessarily tantamount to others. For example, a corporation can be admirably accountable to its shareholders and still rapacious to the rest of society, even more so when its shares are closely held. A popular and spurious form of shareholder accountability is the leveraged buyout, which temporarily raises the value of the stock thereby enriching shareholders, especially the middlemen who orchestrate the takeover, but usually at the expense of other stakeholders and society in general.

This paper will benchmark the value of transparency and accountability both as a means and as an end, against the broad goal of bringing reform to diverse realms of finance. It will address the feasibility and impact of using transparency as a basis for increased and more effective engagement of civil society. The mapping exercise below suggests a wide range of presence and absence of CSOs in different areas that invite greater transparency and accountability. CSOs, for example, are deeply involved in debt-relief efforts and with efforts for more transparency in financial flows. However, there are no CSOs of any size that keep track of several large issue areas that were at the core of the recent financial crisis, such as governance of credit rating agencies or reform of the use of credit derivatives. There is substantial CSO engagement with the IMF and the World Bank, to some degree with the WTO, but very little engagement of civil society with the Financial Stability Board, a key post-crisis standard-setting institution.

<sup>1</sup> Edward M. Gramlich, January 2007, *Subprime Mortgages: America's Latest Boom and Bust*, Washington: Urban Institute Press.

## The politics of regulation and reform

We also need to define reform, which means different things to different people. In this paper, reform means the harnessing of financial flows for the broad common good and for the efficient workings of the rest of the economy and society, rather than for the enrichment of financiers and their cronies. Reform means bringing about a banking system that is more servant of economic development than master, and it means the prevention of excess risks, onerous terms, and plain corruption.

This paper will rely on some concepts from political science and political economy to inform our discussion of transparency and accountability as it applies to financial reform. One is the theory of **countervailing power**. In a capitalist democracy, it is not surprising, as the political scientist Charles E. Lindblom<sup>2</sup> and the economist J.K. Galbraith<sup>3</sup> have pointed out, that concentrations of wealth should enjoy disproportionate political power, notwithstanding the formal democratic principle of one person/one vote. What can neutralise that excess power, in Galbraith's phrase, is a set of strong countervailing institutions, in this case NGOs and accountable government.

A second well established concept is the **separation of ownership from control**<sup>4</sup>, and the related failure of corporate governance and accountability. In theory, large corporations are controlled by their shareholders. However, research has long demonstrated that corporations are effectively controlled by their executives, who often manage to extract disproportionate compensation that is not well correlated with the actual performance of the corporation or the well-being of its multiple stakeholders. This failure of accountability allows executives to devise abusive practices that serve their own short-term gain but put the institution and the broader economy at risk. The financial crisis was replete with examples. Here again, greater transparency is part of the remedy, though greater rights for small shareholders and other stakeholders, as well as better regulation, are also key parts.

This failure of accountability is multi-dimensional. There is no large general CSO representing shareholders. Mutual funds, ostensibly representing far-flung small shareholders, generally vote their shares passively, on behalf of management. Individual shareholders are ineffective sources of discipline because they are fragmented and if they are unhappy with management they typically sell the stock rather than investing time and energy in disciplining management. The exception is the controlling management group of shareholders that owns most of the stock. So even if managers were more accountable to shareholders, ownership of shares is so

narrowly concentrated that the shareholder is a poor proxy for a broader public interest. One share one vote is a far cry from one citizen one vote.

In recent years, a radically free market proposition has gained ground – namely the idea that managers will serve shareholder interests and by extension economic efficiency, by 'maximising shareholder value'<sup>5</sup> via the short run price of the stock. This cure, however, has often been worse than the disease, by introducing new, non-transparent forms of conflict of interest. The recently fashionable strategies of maximising shareholder value by such maneuvers as leveraged buyouts and hedge fund and private equity takeovers are the antithesis of transparency (they are often insider deals) or of broad stakeholder accountability (they often come at the expense of workers, pensioners, and local communities.) And these techniques are illustrations of the broader financialisation of the economy, which is replete with adverse consequences that require reform.

A third useful concept is the theory of **regulatory capture**.<sup>6</sup> It is well established that when power imbalances are pronounced, even institutions that are designed as regulatory counterweights are vulnerable to capture by industry. This insight is as old as economic regulation itself, for as soon as regulations came into existence, the targets of the regulation sought to dominate the process and turn it to advantage. In the past three decades, as finance has become more dominant in the structure of economic and political life, one can identify three distinct forms of capture, which are mutually reinforcing: ideological capture, institutional capture, and economic capture.<sup>7</sup>

Ideologically, since the 1970s the dominant view in the economics profession, in most governments run by center-left as well as center-right parties, and in the financial industry, has been that markets are by definition efficient and that financial regulations intended to protect against either market misallocation of resources or against catastrophic market failures usually have more costs than benefits. Hence, scholarly experts, financial journalists, NGOs, or public officials who argued otherwise were swimming upstream against an immensely potent ideological consensus. (The theory of regulatory capture is ideologically double-edged. For market fundamentalists, the likelihood that the target industry would soon capture the regulator made regulation a fool's errand. For advocates of managed capitalism, the risk of industry capture meant that the system needed stronger countervailing institutions and more airtight regulations.)

Institutionally, governments were either under pressure from, or in league with, financial institutions. 'Light touch' regulation<sup>8</sup> was in fashion, and civil servants seen as heavy handed were taking career risks. Conversely, it was easy to

<sup>2</sup> Charles E. Lindblom, *Politics and Markets* New York: Basic Books, 1977.

<sup>3</sup> John Kenneth Galbraith, *American Capitalism: The Concept of Countervailing Power* Boston: Houghton Mifflin, 1952.

<sup>4</sup> A.A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* New York: MacMillan, 1932.

<sup>5</sup> See Michael Jensen and William Meckling, 'Theory of the Firm,' *Journal of Financial Economics* 3, 1977 305-60. For a critique, See Michael Lazonick and Mary O'Sullivan, 'Maximising Shareholder Value: a New Ideology for Corporate Governance,' *Economy and Society* 29, (2000) 13-35.

<sup>6</sup> See S. Huntington, 'The Marasmus of the I.C.C.,' *Yale Law Journal* 614, 1952, 467-509.

<sup>7</sup> Thanks to Leonardo Burlamaqui for this distinction.

<sup>8</sup> 'Light touch regulation' was the slogan of the UK's Financial Services Authority (FSA) in the period before the collapse.

for government bureaucrats or politically appointed officials to move from public regulatory institutions to the private financial industry and increase their personal earnings tenfold or a hundredfold. This 'revolving door' prospect often tempered any inclination to regulate aggressively. Further, the relative weakness of CSOs addressing financial issues meant that agendas (typically of deregulation) were largely set by industry rather than by civic groups, and that dubious and risky policies often went largely uncontested except by outsider critics who were often dismissed as either out-of-date, poorly informed, or ideologically unsound.

The sheer economic weight of financial institutions intensified regulatory capture. In nations where democratic elections are heavily influenced by private political donations, the financial industry is invariably one of the largest donors. CSOs, with the exception of some trade unions, do not typically make monetary investments in politics, so this is one more source of structural imbalance. Interestingly, however, even in nations where elections are relatively abbreviated and publicly financed, the same kind of solicitude on the part of governments for large financial institutions has tended to operate. So economic capture has more than one dimension.

In government circles, there is anxiety about effective regulation being seen as producing an unfriendly 'business climate' and driving the financial industry offshore. The financial sector and its intellectual allies have been politically adroit at stoking these concerns. So the economic influence of the banking sector on governments extends far beyond political donations. CSOs have been too weak a counterweight to effectively promote an international regulatory schema in which all large financial institutions are subject to the same basic set of effective regulations, which is necessary to neutralise the tacit or explicit threat to move business to regulatory havens. All of this is mutually reinforcing, and indicative of a gross disparity of influence despite a nominally democratic process.

## 2. Financial abuses and reforms: a map of broad issues

As noted, the term 'financial reform' refers to multiple issue areas, some of which overlap and others of which operate in relative isolation from one another.

## Reform of the banking system

The financial collapse of 2007–09 and the continuing damage to the wider economy and society can be understood, in part, as a failure of accountability and transparency. Regulatory forms of accountability and market forms of accountability both failed. Neither kept the financial system from devising instruments that were mispriced and under-capitalised, and that turned out to be a massive bubble once markets lost confidence in them. The aftermath has created a general and prolonged economic crisis.

Markets proved incapable of policing excesses in the financial system. Market prices became disconnected from underlying values or risks. Market mechanisms of transparency and accountability, such as a very lightly regulated accounting profession, credit-rating agencies, or financial industry institutions of self-regulation, were corrupted. Market forces also overwhelmed extra-market stabilisers such as regulatory institutions. There was a political loop to this process: the political power of private market institutions (banks, corporations, investors) successfully resisted modernisation of regulation to keep up with either benign innovations or deceptive marketing practices; political influence also undermined enforcement of regulations that remained on the books, while others were simply repealed.

This shift occurred as financial markets and products became more abstract and opaque, and as an increasingly global economy failed to produce public or civic institutions of accountability at a global scale. On the contrary, the globalisation of finance made it easier for private actors to practice 'regulatory artibrage' -- to outrun regulatory institutions and civic counterweights that remained primarily nation-bound.

The financial economy exists to serve the real economy. In recent decades the financialisation of the economy has caused an ever increasing share of total corporate profits to flow to financial institutions themselves, peaking at 41 percent of all corporate earnings in the U.S. by 2006. Ever higher target rates of return led to ever riskier strategies combined with the shifting of risks, with increasing costs to the rest of the economy.

Unlike many other financial crises of recent years, these failures and the ensuing loss to worldwide output mainly had their origins in the supposedly advanced countries, especially the U.S. and the U.K. Financial products that avoided either domestic or international forms of transparency and accountability were exported from the advanced countries to each other and to the developing ones. The consequence was global contagion as in the third world debt crisis of the early 1980s and the Asian currency crises of the late 1990s – but in reverse. The direction of contagion was North to South.

In late 2008, Dr. Yaga Reddy, who had just retired as Governor of the Bank of India, was asked how India had avoided the financial crisis that was then enveloping most of the world. He replied puckishly, 'We are a poor developing country. We don't really understand these complex financial products, so we leave them to the advanced countries like you.'<sup>9</sup> It was a charming reversal of the usual direction of expert advice, and indeed Dr. Reddy used his regulatory authority to require very high reserve requirements for Indian banks that sought to dabble in complex structured financial products or credit derivatives of the sort that collapsed banking systems in the west. There was resistance to his regulations at the time, though today his efforts are regarded with veneration.

But in most nations, the banking system turned out to have unacknowledged high ratios of debts to assets, much of it in short term debt instruments dependent on the confidence of money markets. This reality was opaque both to regulators and to the general public because of deceptive accounting and misleading products. When investors belatedly realised the risks and lost confidence, a selling panic ensued, wiping out trillions of dollars worth of presumed value. A great unwinding occurred. A financial crisis has become a general economic slump, with persistently high unemployment, and a knock-on crisis of confidence in sovereign debt as well. In principle, stronger CSOs with better access to data could help balance these asymmetries of information and influence, leading to a virtuous circle of better accountability, and more prudent industry behavior.

There are two broad ways of holding financial institutions accountable so that they deliver safety and efficiency and serve their purpose of evaluating credit risk and channeling savings into productive investment at reasonable transaction costs. These can be understood as **market accountability** and **regulatory accountability**. In the free-market view, markets are essentially self-regulating. In theory, the crisis that collapsed the system could not have occurred, because markets are efficient and would not have permitted the mis-pricing. The crisis, of course, is proof that market accountability must be complemented with regulatory accountability – which in turn requires engaged NGOs to keep regulators honest. This is the second time we have learned this lesson. After the severe costs and lessons of the Great Depression of the 1930s and well-documented patterns of market failure, such as asymmetry of information, self-dealing, moral hazard and catastrophic risk, for much of the 20th century public policy complemented market accountability with regulatory accountability. But over the past three decades these regulations were deliberately undermined and overtaken by innovations and end-runs. In the run-up to the crisis, both market accountability and regulatory accountability failed.

<sup>9</sup> Yaga Reddy: communication with the author.

Greater transparency is necessary for both realms of accountability. If markets are to price financial instruments accurately, they cannot be opaque or deceptive. And if regulators are to compensate for market failures, they need accurate information as well as effective regulatory criteria, political resolve, and popular constituencies to offset the political power of industries that resist transparency and accountability.

It turns out that markets, to function efficiently, need basic rules that are the work of extra-market forces. Those can be public regulations created and enforced by nation states accountable to citizens, or actions by nonprofit groups representing global civil society. It is neither practical nor desirable for regulators to anticipate every new financial product that innovators can dream up. But it is practical – and necessary – for publicly accountable authorities to devise some basic principles of transparency and accountability, using mechanisms such as disclosure, reserve requirements, strictures against conflict of interest, and bright lines of proscribed conduct that cannot easily be circumvented, as well as regulatory strategies that engage and promote civil society groups as counterweights. Since the financial market is the mainspring of a capitalist system, the consequences of failure in the honesty and accurate pricing of financial instruments are more important than their counterparts in any other market, since catastrophic financial failure can bring down the entire system.

Another caveat: more efficient and transparent markets are necessary but far from sufficient for goals of balanced and sustainable development. Even markets that are clean and ‘efficient’ in terms of orthodox market principles miss positive and negative externalities such as the costs of carbon emissions. They undervalue public goods such as education and health. And they are ‘efficient’ relative to the pre-existing distribution of income and wealth, which can be socially indefensible. Even with better transparency, therefore, we still need to complement and sometimes constrain market capital-allocation decisions, in order to promote development and to compensate for well known externalities such as the market’s failure to accurately price the cost of environmental degradation or the benefit of human capital.

One of the things that the financial market most undervalues is transparency itself. This is seemingly odd, because an efficient market depends upon it. Yet it is a conceptual mistake to confuse ‘the market’ as a system with the self-interest of its individual players who thrive on opacity and do their best to promote it. This was a paradox well articulated by Adam Smith.<sup>10</sup>

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<sup>10</sup> See Smith in *The Wealth of Nations*: ‘People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public.’

## Case study: Americans for financial reform

In early 2009, when it became clear that the Obama administration would soon introduce major financial reform legislation, a number of leaders of consumer and labour organisations, as well as some think tanks, organised Americans for Financial Reform (AFR). This coalition eventually came to include some 250 organisations. AFR hired as its executive director a person who was not expert in financial issues but who had wide respect as an organiser and facilitator.

There had never been any comparable coalition in the USA. Rather, in previous reform legislation involving financial issues, a small number of organisations would testify and lobby the administration and Congress individually, sometimes forming smaller ad hoc coalitions. Often, on highly technical issues, civil society was almost totally absent. In some key areas, such as regulation of securities (which is based heavily on the use of disclosure and transparency), there was little if any consumer representation in the debates, and only the occasional scholar, trade union economist and the association of attorneys representing plaintiffs in securities cases.

Although AFR spoke for some 250 groups, in practice about 30 groups participated actively in its deliberations and donated staff. The group's executive committee had weekly meetings in person or by phone, and subcommittees met almost daily as the legislation advanced. It divided into several task forces, each specialising on an aspect of the pending legislation, such as consumer protection, derivatives regulation, or reform of the Federal Reserve. The coalition endeavored to come up with a single position, though member groups were free to take their own positions.

Well before the Obama administration translated its June 2009 statement of reform principles into legislation, AFR was ready with its own initial recommendations. As the legislation evolved during late 2009 and into 2010, AFR tracked it closely. It developed relationships with key legislators and staff, taking advantage of pre-existing contacts. When a legislator or senior staffer was reluctant to offer time for a meeting or for testimony, the president of the American Federation of Labor and Congress of

Industrial Organisations (AFL-CIO) was willing to make phone calls.

AFR coordinated all of the expert pro-consumer testimony on different aspects of the legislation. It made sure that expert witnesses were available and insisted that the consumer viewpoint be represented at hearings. It also coordinated the consumer lobbying before Congress and in states and districts of senators and members of the House. Using relationships with key legislators and staff, AFR was able to obtain drafts of provisions of the pending legislation as it evolved. But according to one leader, 'Industry usually had the drafts before we did.' Too often, CSOs lacked the staff or organisation to reach comparable levels of analytical sophistication, while industry groups were able to follow and influence evolving legislation at every level of detail, giving them a substantial advantage. By the time a provision came to a final vote, the support had been lined up and it was often too late to influence or change it. CSO leaders associated with AFR also pointed out that the industry lobbies had the further advantage of being closely associated with groups that gave large campaign contributions, a source of leverage that the AFR coalition could not bring to the table.

Nonetheless, according to interviews with legislators and other players, AFR's engagement made a major difference in countless provisions of the bill that were heavily lobbied by industry. It did so despite having a very small budget and fewer than ten staff. Virtually all of the staff donated by other organisations were not compensated by AFR, and were taking time away from their primary assignments and working evenings and weekends.

At the time of writing, the process of implementing the financial reform law has just begun. The executive branch rule-making procedures are elaborate. Because Congress was not able to agree on many aspects of the bill, much of the detail has been delegated to agencies of government. This administrative process, where key decisions will be made, is more intricate and ramified than the legislative process. AFR continues, but with an even more modest budget and a skeleton staff.

## Finance, aid and development

There is a set of longstanding arguments, often raised by spokesmen for developing countries, by dissenting economists and critics representing civil society about the way that the system of private capital flows is structured to favour investors in the wealthy North over poorer, capital-importing nations in the developing South. Looked at in terms of social classes rather than nations, some would argue that the system has favoured owners of capital in both the South and the North at the expense of wage and salary workers in both regions, who would benefit from

a more regulated form of capitalism. The players in this drama are institutions such as the IMF, the World Bank, the WTO, governments of nation states and banks in their role as financiers and debt collectors. Despite the general predisposition of intergovernmental organisations (IGOs) to national deregulation and a philosophy of laissez-faire, their requirements can be understood as a form of regulation since they impose rules on capital flows and on nations. So the issue is less whether to regulate than on what terms and for whose benefit.

For the most part, these are government-to-government organisations. The subjects at issue include IMF 'conditionality', onerous terms to collect past debts, the imposition of sometimes perverse austerity programmes as a cure for recession and the use of trade negotiations to privilege property rights over economic and financial deregulation. In general, there is only a modest official role for CSOs in these institutions and not a great deal of formal transparency. Yet NGOs and networks of dissidents have had some success in influencing prevailing policies.

The Jubilee 2000 campaign was one of the most successful initiated by civil society. It ended up enlisting several heads of government and celebrity spokesmen such as Bono and Bob Geldof, organised an effective global network and succeeded in changing the G8 agenda, actually delivering substantial debt relief for the poorest countries. Pressure from NGOs coupled with efforts of third world governments and cooperating OECD governments resulted in the Millennium Development Goals being embraced as official policy. However, the larger goals remain unfulfilled and the work continues. And there is far too little transparency in benchmarking 'who is doing what toward which goal and to what effect', as Bono recently wrote.<sup>11</sup>

A longstanding campaign to modify the terms of IMF conditionality, as well as a boycott of IMF credits by some developing countries, combined with increasing dissent from economists from within and outside the IMF, has led to somewhat more flexible IMF credit terms. A parallel process has occurred with the World Bank. This was spearheaded by groups such as Fifty Years is Enough and the Bretton Woods Project, other groups (see chart below) and a variety of ad hoc protests. One of the most scathing critiques of the current financial crisis and the role of deregulation and corruption comes from the IMF's former chief economist, Simon Johnson.<sup>12</sup> The current IMF chief economist, Olivier Blanchard,<sup>13</sup> has warned against austerity at a time when major governments are using austerity programs as anti-recession remedies. By the same token, civil society protests against IMF and World Bank structural adjustment policies have led to a partial easing of terms.

UN agencies such as UNCTAD, the UNDP and the UN Special Rapporteur on the Right to Food have also served as quasi-official voices articulating a different viewpoint. The current director-general of the IMF, Dominique Strauss-Kahn, a possible candidate for the Socialist Party in the next French presidential election, has prided himself on playing against type, and has gone out of his way to interact with traditional critics of the IMF. As a response to the financial crisis, he has also urged a programme of expansion rather than the IMF's traditional austerity recipe.<sup>14</sup>

The IMF and World Bank do engage civil society organisations. But efforts to hold large IGOs accountable have operated less through formal mechanisms of consultation and participation and more through public education, protest, and pressure on the national governments that are the constituent members of bodies like the IMF. Another case

in point was the rather less polite and ultimately successful campaign in the late 1990s by a global coalition of insurgent groups to block the OECD's proposed Multilateral Agreement on Investment (MAI),<sup>15</sup> which would have used the doctrine of freedom of international investment to undermine domestic financial and social regulation. It helps when civil society groups have at least some national governments on their side, both as sources of diplomatic pressure and of leaks of information.

These international organisations, of course, are still far more receptive to informal influence from the financial industry than from civil society. However, to the extent that a shift has begun, in some respects it takes the IMF, World Bank, and WTO full circle to the circumstances of their founding in 1944 at Bretton Woods. In the original Bretton Woods design, the IMF was created to be a public and Keynesian counterweight against the deflationary bias of private creditors.<sup>16</sup> Yet for this role to be meaningful, there also need to be effective civil-society counterweights to the persistent power of private finance.

The traditional North-South axis of division has also been complicated by the fact that China has become a key capital-exporting nation, and the direction of capital flows, especially during periods of financial stress, has been from South to North. Some of this has to do with capital flight, but the larger context is the emergence of the USA as a prime debtor nation, though the US private financial sector remains a principal capital market for investment in the developing world. Logically, of course, capital should be flowing from rich nations to poor ones, not vice versa.

The issue is further complicated by the emergence of sovereign wealth funds generally and, with the exception of Norway, their relative lack of either transparency or accountability to democratic governments, much less to CSOs. To my knowledge, there are no mechanisms of consultation between CSOs and the large sovereign wealth funds of the Middle East and Asia. It is ironic that at precisely the same period of history when relatively transparent and democratically accountable forms of public ownership – for example of railroads, banks and postal and telephone services – and public subsidy of core industries have fallen into disfavour in Western society and under the recent rules of the EU and WTO, large government stakes in private enterprises via far more opaque sovereign wealth funds have been given a safe conduct pass by the trading system.

<sup>11</sup> Bono, *New York Times*, September 18, 2010, <http://www.nytimes.com/2010/09/19/opinion/19bono.html>

<sup>12</sup> Simon Johnson and James Kwak, *13 Bankers* New York: Random House, 2010.

<sup>13</sup> Olivier Blanchard and Carlo Corraelli, 'The Great False Choice: Stimulus or Austerity,' *Financial Times*, August 11, 2010.

<sup>14</sup> See Strauss-Kahn's 14 September 2010 remarks to the ILO: <http://blog-imfdirect.imf.org/2010/09/14/saving-the-lost-generation/>

<sup>15</sup> MAI: [http://www.citizen.org/trade/article\\_redirect.cfm?ID=5624](http://www.citizen.org/trade/article_redirect.cfm?ID=5624)

<sup>16</sup> Richard N. Gardner, *Sterling-Dollar Diplomacy*, New York: Columbia University Press, 1980.

## Case study: Trade and financial reform

Trade presents several cross-cutting issues that tend to divide as well as unite potential civil society coalitions. Officially, the WTO process is also largely closed to civil society, being government-to-government. The prevailing ideology of the major G-8 governments has been that all barriers to trade are economically inefficient, even ones that overcome market failures and promote economic development. This ideology is nonetheless attractive to most developing country governments to the extent that protected agriculture and industry in the North reduce opportunities for export. 'Free trade' is less attractive when removal of barriers is defined to include repealing social and financial regulation and constraining local industrial policies. Labor standards in trade have also divided potential allies, in that they can be seen either as efforts to protect a well paid workforce tied to traditional industries in the global North, or as worldwide efforts to raise wages and improve worker rights in both North and South.

In the Uruguay Round of trade negotiations under what was then the GATT, several 'non-traditional' issues were put on the agenda mainly by the USA, including trade in services, through the General Agreement on Trade in Services. Free trade in financial services came to be defined as requiring restrictions on the ability of national governments to engage in many forms of financial regulation – a premise that has been overtaken by the realities of the financial crisis which requires more regulation rather than less. But on both bilateral free trade agreements and in the efforts to launch a successor Doha Round, there have been continuing diplomatic efforts to tighten these strictures against prudential regulation. What became the (now defunct) Multilateral Agreement on Investment (MAI) began as a proposed Multilateral Investment Agreement under the proposed terms of the Doha Round, but this ran into significant governmental opposition from Southern nations, since it came on the heels of the Asian financial crisis which had partly been triggered and then exacerbated by already liberalised rules for currency speculation. Pressures under trade law to limit national limits on financial speculation worked in tandem with the leverage of the IMF and World Bank on debtor nations.

NGOs working with a relatively small number of skeptical governments have had substantial success in blocking further efforts to use trade law to limit financial regulation. The timing has been fortuitous, since the G-20, the Financial Stability Board, and the reality of recent events have all been calling for more, not less, financial regulation.

The proposed Doha Round has been advertised as a series of grand trade-offs, in which the advanced countries open their economies to exports from the South and increase outward flows of private capital, and in return the South becomes more hospitable to global investment. Part of that hospitality is defined as removal of barriers, including regulatory barriers to capital, which translates as dismantling of financial regulation including emergency resort to currency controls and measures against illicit capital flight.

In this context, a global coalition of more than 100 civil society groups has been working since the late 1990s to challenge some of the terms of the proposed Doha Round. That full story is beyond the scope of this paper, but one of its elements is proposed further liberalisation of the terms of private investment and further deregulation of financial markets. Since the South has experienced repeated debt and currency crises, often the results of speculative capital inflows and outflows to and from the North, much of the South and allied CSOs are sceptical of further relaxation of regulations of capital and currency markets under the banner of free trade. This and other divisions, including over agriculture, have contributed to a continuing stalemate in the Doha Round.

The campaign to block or drastically revise the terms of the Doha Round is coordinated under a loose global NGO network, Our World Is Not for Sale, which includes both mainstream and radical groups, and which also works on other issues. Its leading national member groups and networks include Public Citizen Global Trade Watch in the United States, Third World Network, Greenpeace, Friends of the Earth, Public Services International, War on Want, Via Campesina, among others. To the extent that trade unions and union federations work on aspects of these issues, the anti-Doha coalition also enlists their involvement.

Interestingly, there is not a great deal of overlap or cross-fertilisation among the groups that work on financial deregulation in the context of trade rules and those that work on financial reform generally, though some groups, such as Public Citizen in the USA, the Third World Network and some of ATTAC's national affiliates, do work on both sets of issues. Transparency is important to this coalition, but less in the sense of having formal status in consultations or official access to draft protocols and more in the informal sense of using leaked documents to pursue strategies in the context of a campaign, such as the campaign to block the MAI. By its very nature, trade negotiation entails successive drafts of documents and ongoing closed-door negotiation, nearly all of it government-to-government, though private industry players have far more access and far more institutional capacity than CSOs.

Further, trade negotiations in many countries are deliberately and unapologetically shielded from public debate, on the premise that all of the elements of a pending trade deal are mutually interdependent. Presumably, if a change is made in one key element at the behest of public deliberation and criticism in a given nation, then the whole global deal could fall apart. In the USA, a 'fast-track' ratification process shields a proposed trade agreement from the usual legislative process and permits only a quick up-or-down vote. Conversely, the ability to publicise provisions that may disadvantage regions or social classes can serve to resist pressure for a quick deal on dubious terms. Key nations of the global South, working with CSOs, have been able to use such tactics to hold out for better terms. Rules for financial flows and financial regulation are among the most contentious issues.

## Illicit money flows

A third dimension of financial reform is opacity of international financial flows. One set of issues involves multiple abuses facilitated by the existence of tax and regulatory havens such as the Cayman Islands. These secrecy jurisdictions allow illicit flows such as tax evasion, concealment of beneficial ownership via shell companies and hidden trust agreements, a range of other abuses by hedge funds and private equity companies, and money laundering for criminal purposes for drug traffic and terrorism. To the extent that better transparency and accountability exist in the OECD countries, tolerance of these secrecy jurisdictions seriously undermines regulatory mechanisms that exist on paper.

In 1998 the OECD, encouraged by then centre-left governments in the USA, UK and Germany, launched an initiative to crack down on tax and regulatory havens.<sup>17</sup> But after years of negotiation by expert working groups, the initiative was severely weakened in 2001 when the newly installed Bush administration in the USA objected to most of its key provisions, and there was no significant presence of CSOs on the other side of the debate. Lobbying to weaken the proposed agreement was well informed and carefully orchestrated by major transnational corporations.<sup>18</sup>

Tax experts have estimated that several hundred billions of dollars of tax revenues from taxable transactions are lost to OECD governments every year through the use of creative accounting that is beyond the practical reach of law enforcement because of the absence of tax treaties and information exchange with tax haven nations.<sup>19</sup> Despite the obvious appeal of cracking down on these abuses, the imbalance of political power between major multinational corporations and reform groups has left governments with most of the pressure coming from one side.

After the attacks of September 11, 2001, the Bush administration sponsored emergency legislation and took executive actions to crack down on money-laundering operations that allowed sponsors of terrorism to move funds across international borders. These initiatives required and enlisted the cooperation of banks. However, they were explicitly structured so that the information thus gathered was not to be used for systematic tax enforcement and the structure of tax havens for purposes of tax evasion was left largely intact. This exemption reflected the lobbying influence of banks and multi-national enterprises, with little or no counter-pressure from civil society.

Watered down OECD guidelines did take effect after 2002. However the bar for cooperation was set so low that none of the notorious tax havens in the Caribbean is currently included on the OECD list of non-cooperating nations.<sup>20</sup> Under the current guidelines, nations are expected to cooperate with case-by-case requests for information from OECD tax authorities, but not to clean up their entire systems.

By contrast, there has been more progress in reforming tax havens within Europe. Tax havens such as the Channel Islands, Lichtenstein, and Switzerland have been compelled to limit their roles in facilitating the hiding of assets and earnings on the part of other EU citizens. The September 11 attacks, the regulatory crackdown against abuses by the Swiss bank UBS in the financial collapse, long-standing efforts by the German government against the hiding of assets in Switzerland, Luxembourg, and Liechtenstein, and EU directives against concealment of investment income, have all played a role in these reforms. The fact that governments are at least intermittent allies is an important factor. And the OECD process is now slowly moving in the directing of demanding more active and ongoing information sharing between tax havens and OECD tax and law-enforcement authorities.

<sup>17</sup> OECD, 1998 'Harmful Tax Competition: An Emerging Global Issue', Paris: OECD, 1998.

<sup>18</sup> Daniel Mitchell, 2000 'An OECD Proposal to Eliminate Tax Competition Would Mean Higher Taxes and Less Privacy,' (Washington, D.C., Heritage Foundation, September 2000.)

<sup>19</sup> Joseph Guttentag and Reuven S. Avi-Yonah, 2005 'Closing the International Tax Gap,' in Max Sawicki, ed., *Bridging the Tax Gap*, Washington, D.C.: Economic Policy Institute, 2005, pp. 101-18.

<sup>20</sup> [http://www.oecd.org/document/57/0,3343,en\\_2649\\_33745\\_30578809\\_1\\_1\\_1\\_37427,00.html](http://www.oecd.org/document/57/0,3343,en_2649_33745_30578809_1_1_1_37427,00.html)

## Case study: The tax justice network

In this evolving reform process, a small but influential NGO, the Tax Justice Network (TJN), has been an important player. Simply by being present, by keeping track of these issues, and by publicising the abuses, the network has been able to demand information and consultation with national and international governmental organisations such as the OECD, to alert the media to these issues and to shine a spotlight on embarrassing or indefensible practices.

The TJN has also been able to gain entrée to the International Accounting Standards Board, and to put greater transparency on the agenda of the G-20. Fortuitously, the September 11 attacks and subsequent terrorist attacks in the U.K., Spain, and elsewhere kept attention focused on abuses of money-laundering. The financial collapse gave unwelcome publicity to large banks that colluded in hiding assets from tax authorities. The resulting financial crisis created a fiscal gap that left government eager to increase revenues without taking unpopular decisions to raise tax rates. Even so, the gains in the OECD standards exist mainly on paper, and there is an ongoing struggle to make the standards meaningful and to move from ad hoc, case-by-case information sharing to systemic reforms of tax haven nations, most of which are still not serious about collecting, much less sharing, financial data.

Moreover, the disparity of resources is staggering. Banks and multinational corporations seeking to preserve their ability to move money to tax and regulatory havens and to use spurious 'transfer pricing' to book profits in low tax jurisdictions have legions of lobbyists and lawyers who interact almost daily with bodies such as the OECD committee, national ministries of finance and legislatures, and other standard-setting bodies. The TJN operates with a handful of fulltime professionals complemented by volunteers, and is able to exercise influence mainly by networking and by leveraging its organising efforts via adroit use of media. There are a relative handful of academic experts providing scholarly back-up to these efforts. Many governments are hesitant to lead, for fear of seeming 'anti-business.' But the tax transparency cause is ahead of other areas of financial reform because at least it has a CSO as a major player. In other realms there is a complete vacuum.

This assessment reveals some notable successes on the part of CSOs, but also the need for increased activity and opportunities for greater collaboration. While there is substantial NGO activity in areas such as tax evasion and disclosure of true beneficial ownership, etc., there is no generalised campaign against the toleration of secrecy jurisdictions per se. Since these are typically very small countries, whose power derives solely from their use as flags-of-convenience for the financial industry, the world's major governments could easily crack down on these general abuses if the distribution of political power between the financial industry and civil society were different.

A related broad campaign for greater transparency addresses the secrecy of payments to governments. Here, civil society organisations, though massively outspent by industry, have begun to make a constructive difference. A good case in point is Global Witness and Publish What You Pay.

## Case study: Global witness and the Publish What You Pay campaign

A second notable success has been achieved by NGOs in the effort to increase the transparency of payments by extractive industries to governments, mainly in developing nations reliant on mining and petroleum. The Publish What You Pay campaign (PWYP), spearheaded by Global Witness and a network of other NGOs, succeeded in creating, defining, and then mobilising support for a public issue, where transparency is not only the main instrument against corruption in host governments but also a means of greater disclosure of the financial operations of large multinational corporations with benefits on several other fronts.

A broad coalition, first created by Global Witness in 2002, was possible because this cause was of interest to a wide range of groups that do not always collaborate – environmental groups concerned that lenient or corrupted regulatory terms allow environmentally destructive practices in drilling and mining as well as human exploitation of workers in extractive industries; social justice and anti-poverty groups interested in assuring that government funds in poor countries go more to human development and less to corrupted government officials; war-peace groups concerned to reduce the flow of illicit funds that finance regional and tribal conflicts; and other NGOs pursuing transparency and honest government both as an end and as a means. The campaign soon enlisted NGOs such as Oxfam GB, Catholic Relief Services and Human Rights Watch and eventually affiliates in more than 50 countries. Global Witness bridges these several NGO constituencies and issue areas with demands for greater transparency on multiple fronts.

Global Witness bridges these several NGO constituencies and issue areas with demands for greater transparency on multiple fronts.

The PWYP campaign is a fine example of how what is ostensibly a single issue – disclosure of payments – can have multi-issue synergies. The presence and activism of the PWYP campaign set the stage for a lucky breakthrough in the context of the recently enacted financial reform legislation in the USA. (although, on the other hand, there is a lot of truth to the saying that ‘You make your own luck.’)

Had PWYP not been mobilised, this legislative gain would not have occurred. In the final round of jousting over the particulars of the Dodd-Frank Act, Republican legislators were mostly opposed to the bill. Sponsors were frantically lining up a handful of Republican votes in order to avoid a filibuster in the Senate. One Republican senator, Richard Lugar of Indiana, was not particularly friendly to the overall bill, but had an interest in anti-corruption measures in third world countries, and was a supporter of publish-what-you-pay legislation. So a publish-what-you-pay provision not included in either the House or Senate bill was added to the final conference draft at the 11th hour, in the hope of enlisting Sen. Lugar’s vote for the whole package. The fact that this was a total surprise to the corporate community meant that there was no time for the usual lobbying, and the final bill did include the publish-what-you-pay requirement.

In the end, Sen. Lugar did not vote for the reform package, but PWYP became law.<sup>21</sup> A critic might point out the irony of a less than fully transparent legislative maneuver leading to a great victory for transparency in the area of tax and royalty payments. Multinational companies in extractive industries must now include in their public filings with the U.S. Securities and Exchange Commission their payments to governments. This breakthrough will facilitate gains in other countries and on other issues. The measure would never have been added to the bill but for the prior organising and publicity work of the campaign.

What is worth further exploration, is the potential of greater synergy across other issue areas under the larger rubric of financial reform. Interestingly, while groups such as Global Witness and the Tax Justice Network do work on issues that impinge on some dubious activities of banks, such as bank complicity in tax evasion (TJN) or banks facilitating black market financial flows to corrupt governments (Global Witness), these groups and networks have not generally worked on the structure of the banking system or the kind of regulatory failures implicated in the recent financial collapse.

Another emblematic illustration is the good work of the Task Force on Financial Integrity and Economic Development. A core concern of the Task Force is the disparity between official development aid (ODA) of about \$100 billion a year and illicit capital flight, estimated at \$1 trillion a year, nearly all of it from developing countries to affluent ones. As long as these illicit flows continue to dwarf both official aid and legitimate investments, capital movements are distorted and development retarded. The Task Force’s related issues, built heavily on a strategy of disclosure, are the curtailment of trade mispricing, the need for country-by-country reporting, disclosure of beneficial ownership of bank accounts, automatic tax information

exchange, and the harmonisation of offenses under anti-money laundering laws. These are all immensely worthy goals in the broad context of economic development goals. The Task Force has also begun to organise what it calls Allied Organisations to complement its core institutional members, so there is a powerful network in the making. However, like other groups working on illicit financial flows, the taskforce, though it deals with banks’ role in concealing beneficial ownership and facilitating improper financial transfers, does not address financial reform in the sense of the structure of the banking system itself.

<sup>21</sup> <http://resources.revenuewatch.org/en/official-document/us-pwyp-law-2010-sec-1504-dodd-frank-wall-street-reform-act>

# 3. Dynamics of change

Key question for our deliberations include our theory of change, our goals for substantive reform, and our assumptions about the role of transparency as a norm and of NGOs as players in bringing reform about.

## Theories of reform

We need to be precise about our theory of the relationship of transparency to better functioning financial markets, better engagement of citizens, and better substantive outcomes. Are greater transparency and accountability sufficient as well as necessary? Do we expect that transparency will logically bring to light defects and thereby facilitate better market mechanisms of accountability? Do we also envisage a dynamic by which greater transparency will lead to a cumulative shift in the balance of political power over the rules of governance of the financial system? Do we imagine that more and better direct engagement between civil society and financial institutions will lead to constructive change based on enlightened industry self-interest?

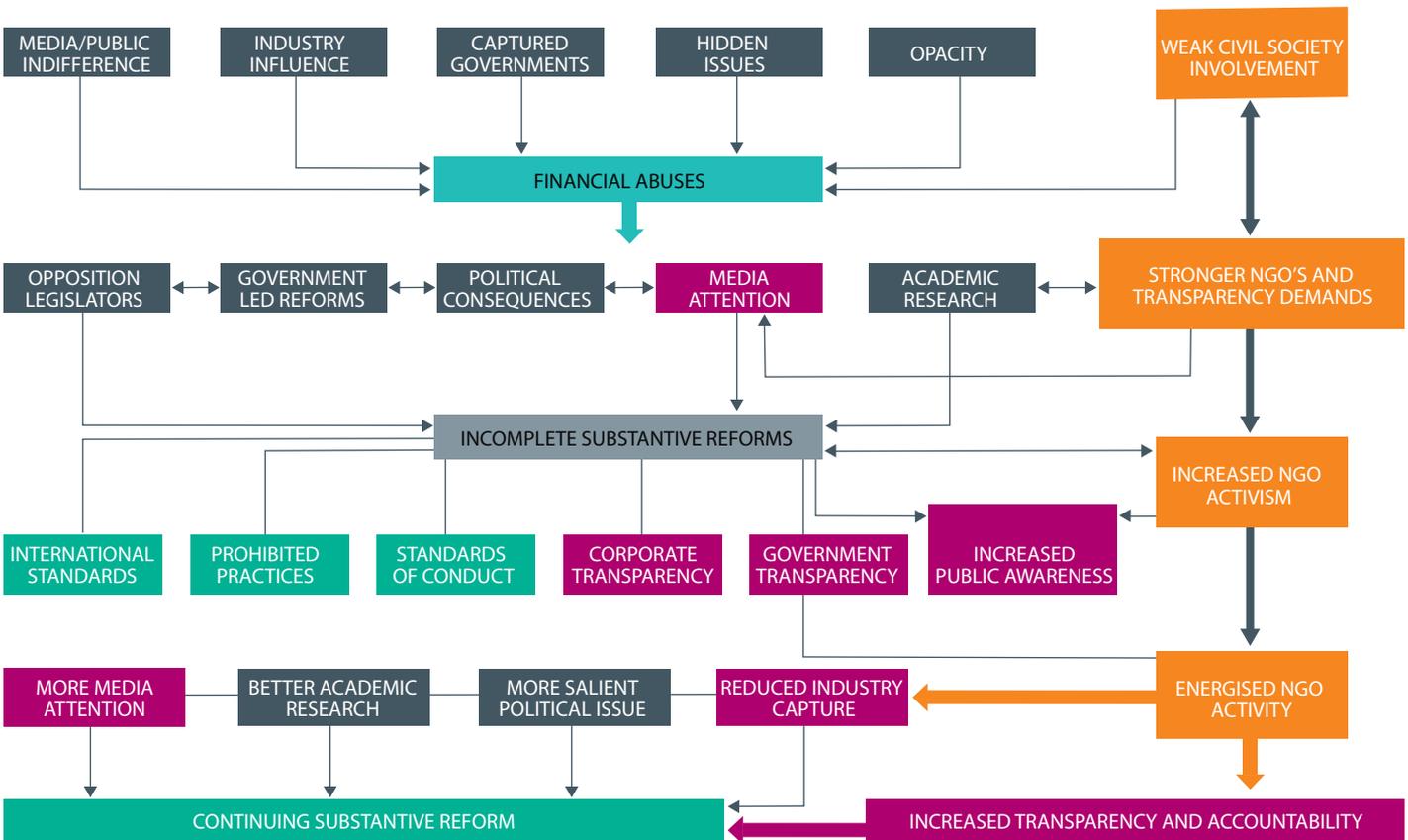
Do we view greater transparency as a cumulative process, in which the opportunity to access information in turn energises CSOs and gives them a greater role, which in turn offsets the structural influence of industry? How, concretely, can greater transparency attract and incubate stronger institutions of civil society and political engagement, which in turn lead to substantive reforms? Is our model vis-à-vis the financial industry collaborative, adversarial, or some of each?

A related question is whether transparency and accountability, assuming they produced a more efficient and prudent financial sector, would be adequate reforms. For example, we might achieve a more transparent and technically competent financial system that 'efficiently' channeled savings into investment and avoided periodic bouts of crisis and collapse--but one that still failed to serve goals of balanced human development.

Can we reasonably expect a private financial system to better serve such goals if it is more transparent and accountable to democratic and civic institutions? Or does the achievement of a substantive shift in the ends of the financial system also lie in other political processes as well such as the election of reform-minded governments?

The accompanying chart suggests one possible theory of cause and effect, relying on transparency as both a tactic and an end product. Pre-reform, processes are relatively opaque, and there is a gross imbalance between industry groups that promote little or no regulation and opacity of financial products. Government regulators are substantially captured by industry clients. Public awareness is low, and media are not paying attention.

FIGURE 2. TRANSPARENCY, NGO ACTIVITY AND REFORM



After an initial round of still partial reforms, the presence of better informed and better equipped NGOs helps to provide better balance in the monitoring of the implementation of substantive reforms. We can imagine a virtuous circle in which greater availability of information helps to energise and empower civic groups as well as political critics of incumbent policy. The civic groups, in turn, function as watchdogs on the regulatory process and identify gaps in the structure of transparency as well as substantive regulatory weaknesses. They work in concert with the media to bring abuses to light and to press for further transparency. They serve as citizen lobbyists to counter industry lobbyists.

Post-crisis, media and official investigative bodies are shining a spotlight on abuses, but are hampered by a relative lack of transparency. Pressures increase for more disclosures both to the public and to regulators. NGOs and academic critics become more engaged. Governments are pulled between public demands for fundamental reform and industry pressures for business as usual. In the context of partial reform, there are partial gains for transparency, which in turn provide grist for NGOs, media, insurgent politicians, and academic critics to play more of a watchdog role and to push for still more disclosure.

A great deal of consumer regulation has been based on the assumption of market accountability—the premise that better disclosures will lead to better-informed consumers, and hence to more accurately priced financial instruments. The tacit paradigm here is that of retail transactions, and fairly straightforward ones. For example, a consumer can weigh the risks and benefits of a fixed-rate versus a variable-rate mortgage, or of a credit card with lower fees and interest rates but higher penalties for late payments. Vigilant consumers, in this view, will produce more accurately priced financial products, just as they keep producers roughly honest by shopping around for more tangible products such as ordinary consumer goods.

Elizabeth Warren, who devised the proposal for a consumer financial protection agency and is now its interim director, points out that better transparency for retail financial products can prevent many of the kinds of wholesale abuses that led to the collapse. If deceptive products have less of a retail market, then exotic wholesale derivatives based on shaky consumer loans will be less of a systemic threat. Warren observes, however, that retail transparency and accountability are only partial remedies, and the system can still be at risk due to opaque wholesale products such as credit default swaps.<sup>22</sup>

## Strategic criteria

There are myriad possible areas for new initiatives. But which potential areas show the most promise for engagement by NGOs and for the use of transparency to achieve substantive reforms beyond transparency itself? This assessment evaluates possible initiatives in terms of their impact, the importance of the policy area as a lever for significant change, their feasibility, and their capacity to produce new synergies and collaborations.

### Impact criteria

- Potential of transparency as a lever to influence policy and promote substantive reform
- Potential of the initiative for enlisting media attention and promoting public education
- Benefit in engaging new constituencies
- Value for creating a virtuous circle of additional CSO involvement
- Financial potential in creating new strategies for enhancing capacity-building or funding for NGOs.

### Feasibility criteria

- Do CSOs have adequate capacity to monitor and disseminate findings?
- Does the issue have a human face and can it be dramatised?
- Does the issue/strategy lend itself to broad-based activist campaigns?
- Does the issue entail blocking bad outcomes, or creating a new initiative?
- Does the proposal have a practical chance of enactment? Or, failing that, is it a good organising and mobilising tool that can promote incremental progress?

### Substantive importance criteria

- Does the initiative promote first-order reform with transformative effects?
- Does the initiative promote reform that logically leads to broader reform?

### Synergy criteria

- Does the issue create new coalitions?
- Does the issue promote new strategies of empowerment?
- Does the strategy have spill-over benefits to other policy areas?
- Is there the potential to take advantage of new technologies

<sup>22</sup> Elizabeth Warren, interim director, Consumer Financial Protection Bureau: communication with the author.

# 4. Map of CSOs and issues of financial reform

There are many hundreds of NGOs, large and small, working on different aspects of financial reform.

The chart below is meant to be illustrative, not comprehensive. It includes major coalitions and networks, as well as individual NGOs that have had serious impact. The colour coding (see key) divides these into coalitions/networks;

research/advocacy groups; labour federations or associations; and academic research centres. This chart, by definition, is incomplete and is meant to be a work in progress. Apologies to groups that have been inadvertently excluded.

FIGURE 3. CSOS AND ISSUES OF FINANCIAL REFORM

REFORM ISSUE	NATL/INTL	COALITIONS, SYNERGY	KEY NGOS	NGO ENGAGEMENT
<b>Banking system reform</b>				
Capital standards, financial market supervision, basic rules of banking system	Both	Some	AFR, EFR, Eurodad, Third World Network, AFL-CIO, CTW, TUAC, UNI, GW, Roosevelt Inst., TNI, SOMO, BankTrack, Public Citizen, Financial Markets Center, Demos, New Rules for Global Finance, WEED, CRBM, Levy Inst., CEPREMAP, PERI, INET	Efforts present but outmatched and fragmented
Governance of IFIs	Both	Some	BWP, TWN, EURODAD, OWINFS, NRGF, WEED	Active campaign
Transparency of central bank policies	National	None	AFR, AFL-CIO, PC, NRGF	Low
Transparency of sovereign wealth funds	Both	Yes	GW, Peterson Inst., Carnegie Endowment, no active campaign	Low
Standards for credit rating agencies	Both	No	ETUC, PC, Demos, BankTrack, PERI, FMC	No active campaign
Regulation of hedge funds & private equity	Both	Weak	AFT, EFR, TWN, AFL-CIO, CTW, ETUC, IUF, Eurodad, CMOC	Low
Regulation of derivatives	Both	Some	AFR, EFR, TWN, AFL-CIO, CTW, IUF, ETUC, Eurodad, SOMO, CMOC, CEPREMAP, Levy Inst.	Low
Financial standards in WTO rules	Both	Yes	OWINFS, TWN, PSI, SOMO, PCGTW, FOE, WOW, Via Campesina,	Active campaign
Consumer protection	National	Some	CFA, PC, AFR, Ctr. For Responsible Lending; diverse single-issue groups	Active but fragmented
Securities regulation	National	No	AFR, EFR, Council of Institutional Investors, AFL-CIO, CTW, BankTrack, CEPREMAP	No active campaign
<b>Debt and development</b>				
Increased ODA	Both	Yes	TWN, Eurodad, BWP, Oxfam, Jubilee Debt Campaign Action Aid	Active campaign
IMF and World Bank reform	International	Yes	OWINFS, TWN, Eurodad, BWP, CRBM	Active campaign

REFORM ISSUE	NATL/INTL	COALITIONS, SYNERGY	KEY NGOS	NGO ENGAGEMENT
Trade, finance and development	Both	Yes	OWINFS, TFFIED, IUF, Eurodad, PCGTW, SOMO, TWN, Via Campesina, Seattle to Brussels Network, Greenpeace	Active campaign
Food speculation	Both	Some	SOMO, Oxfam, CMOC, Grassroots Int'l	Fragmented campaign
Capital Flight	Both	Yes	TFFIED, GW, BWP, BankWatch, GFI, RWI	Active campaign
Privatisation of Dev't finance	Both	Some	SOMO, BankWatch, BWP	Fragmented campaign
Finance and sustainable dev't	Both	Yes	BankTrack, WEED, Make Finance Work Jubilee Debt Campaign	Active campaign
Debt relief and restructuring	Both	Yes	OWISFS, TWN, Eurodad, BWP, Oxfam Jubilee Debt Campaign	Active campaign
Financial flows				
Taxation of financial transactions	Mainly National	Yes	ATTAC, TFFIED, GW, TJN, Robin Hood Tax, CTJ, CRBM SOMO, Make Finance Work, RWI	Active campaign
Tax reform and regulatory havens	Both	No	ATTAC, EFR, TFFIED, Eurodad, GW, TJN Robin Hood Tax, SOMO, CTJ, CRBM, GFI, RWI	Fragmented efforts
Disclosure of payments to States	Both	Yes	PWYP, TFFIED, GW, SOMO, TI, Action Aid, GFI, RWI	Active campaign
Accounting reforms	Both	No	TFFIED, GW, TA, SOMO, GFI, RWI	Fragmented efforts
Pension reforms	National	No	TFFIED, AFL-CIO, CTW, ETUC, PRC, CDSS, RWI	Fragmented efforts

KEY: Coalitions/networks Labour federations/associations Research/advocacy Groups Academic centres

## Abbreviations

<b>AFR:</b> Americans for Financial Reform	<b>Development</b>	<b>PSI:</b> Public Services International
<b>ATTAC:</b> Association pour la Taxation des Transactions pour l'Aide aux Citoyens	<b>FMC:</b> Financial Markets Center	<b>PWYP:</b> Publish What You Pay
<b>BWP:</b> Bretton Woods Project	<b>FOE:</b> Friends of the Earth	<b>RWI:</b> Revenue Watch Institute
<b>CEPREMAP:</b> Centre pour la Recherche Economic et ses Applications (France)	<b>GFI:</b> Global Financial Integrity	<b>T/A:</b> Transparency international
<b>CMOC:</b> Commodity Markets Oversight Coalition (mostly USA)	<b>GW:</b> Global Witness (UK)	<b>TFFIED:</b> Task Force on Financial Integrity and Economic Development
<b>CRBM:</b> Campagna per la Riforma della Banca Mondiale (Italy)	<b>INET:</b> Institute for New Economic Thinking	<b>TUAC:</b> Trade Union Advisory Committee (to OECD)
<b>CTJ:</b> Citizens for Tax Justice (USA)	<b>IUF:</b> International Union of Food Workers	<b>TWN:</b> Third World Network
<b>CTW:</b> Change to Win federation (USA)	<b>NRGF:</b> New Rules for Global Finance	<b>SOMO:</b> Centre for Research on Multinational Corporations (Netherlands)
<b>EFR:</b> Europeans for Financial Reform	<b>OWINFS:</b> Our World is Not For Sale	<b>WEED:</b> World Economy Ecology and Development (Germany)
<b>ETUC:</b> European Trade Union Confederation	<b>PC:</b> Public Citizen (USA)	<b>WOW:</b> War on Want
<b>Eurodad:</b> European Network on Debt and	<b>PCGTW:</b> Public Citizen Global Trade Watch	
	<b>PERI:</b> Political Economy Research Institute (USA)	
	<b>PRC:</b> Pension Rights Center (USA)	

## Case study: The Basel Process, opacity and weak CSO engagement

The Basel Capital Accords, including Basel I (created in 1988); Basel II (devised and refined beginning in the late 1990s); and III (released in September 2010) have attempted to use capital reserve requirements both to create a level playing field among large multinational banks operating in diverse countries, and to assure capital adequacy as a cushion against catastrophic loss. However, not only has the Basel system failed; it has backfired. Although the standards specified under Basel II were not yet in force at the time of the collapse, research by the U.S. Treasury in 2005 showed that several large banks would actually have had reduced capital adequacy standards had they been implemented.<sup>23</sup> Few of the abuses that caused the financial collapse were captured by the Basel metrics, and the Basel standards themselves unintentionally created incentives for banks to invent forms of off-balance-sheet accounting that would not be included in the Basel standards.

The Basel Accords can be understood as an early effort at transnational regulation and accountability. But the Basel process also epitomises the transnational lack of transparency to civil society. Why Basel? The Bank for International Settlements, based in Basel, is a kind of central bankers' central bank. The Basel-based Financial Stability Forum (FSF), founded in 1999 by central bankers

and finance ministers, was given additional authority by the London G-20 summit of April 2009, and is now called the Financial Stability Board. It recommends international banking standards to be ratified by collaborating nations, but is still largely the creature of central bankers and finance ministers. At present, the FSB has no mechanisms of transparency or consultation with civil society, except for very infrequent and ad hoc efforts, but it has myriad and ongoing informal contacts with the financial industry.

Other international associations of financial regulators and private or quasi-public standard-setting bodies, such as the Basel Committee on Banking Supervision, the International Accounting Standards Board, the International Organisation of Pension Supervisors, and so on, have very little formal or informal contact with CSOs either.

<sup>23</sup> Basel Accords: Daniel K. Tarullo, Testimony to U.S. Senate Banking Committee, November 10, 2005.

# 5. Some generalisations and questions

Mind the gaps.

The gaps in the map of engaged civil society organisations can be understood as both a problem of demand and of supply. There is far too little receptivity to CSO engagement on financial issues, especially by IGOs. When consultations do occur, they are either the result of protests or formalistic, and designed to demonstrate openness rather than be emblematic of genuine access, welcome, or influence.

CSOs dealing with financial issues have made some headway on influencing agendas on a few issues, such as debt relief, moderation of IMF conditionality, promotion of greater flexibility on the part of the World Bank, modest increases in ODA, and resistance to some questionable aspects of the proposed Doha Round. They have had less success on core elements of financial reform. At the national level, there is often more transparency in the policy process and more opportunity both to access information and to

participate. But here the problem is a gross disparity of resources. One strategic question is the relative weight to give engagement with national governments versus international governmental and quasi-governmental institutions.

Several persons interviewed for this review reported that for the most part real influence is exercised over the political and regulatory process (or not) in national governments or the EU, or by gate-crashing government-to-government processes such as the G-20 meetings and trade rounds. Demands for greater transparency and access to international bodies can nonetheless be useful in influencing agendas and offsetting the access that the financial industry enjoys.

## Case study: The Trade Union Advisory Committee to the OECD (TUAC)

Among large international governmental organisations, the OECD is unusual in that it has the remnants of a tripartite process that dates back to the 1940s and the era of the Marshall Plan for European Recovery. The OECD has both a Business and Industry Advisory Committee (BIAC) and a Trade Union Advisory Committee (TUAC).

TUAC has become a kind of listening post and key node in the network of NGOs that follow financial reform. Although TUAC is formally attached to the OECD, it has not limited its activities to those under OECD purview. In recent years, TUAC has helped coordinate civil society efforts to influence the G-8 and later the G-20 agendas to get priority consideration for financial reform. Though reform of the financial system is not, strictly speaking a 'labor issue,' TUAC and its constituency union members view the general deregulation and financialisation of the economy as part of the process that has left workers and unions more economically vulnerable, and the global labor movement also opposes austerity as the cure for past excesses of the financial system.

Among TUAC's other initiatives dealing with financial reform, it has:

- Pressed the Financial Stability Board to devise a process for consulting with CSOs so that its information is not solely from governments, central banks, and the banking industry
- Helped provide information to national CSOs seeking to influence G-8 and G-20 agendas
- Represented a reform viewpoint at OECD events, including the annual Ministerial conferences.
- Been an advocate for financial reform in the processes of the European Parliament.
- Persuaded the OECD to include guidelines for multinational enterprises in its membership criteria, and
- Been a counterweight to industry views in the controversy over the MAI and similar initiatives.

TUAC is effective because its core constituent groups are national trade unions and global union federations that have become active on financial reform issues. These include unions from the global South as well as the North. However TUAC also works with other NGOs concerned with various facets of financial reform and helps build coalitions among unions and other CSOs, as well as across different arenas of financial reform.

## Capacity, asymmetry, and the case for supply

Improvements in transparency are valuable to the extent that CSOs and other countervailing political players exist with adequate capacity to make good use of them. Recently, the Obama administration pledged to make implementation of the recently enacted financial reform law the most open process in American history. The heads of two major financial regulatory agencies, the Securities and Exchange Commission and the Federal Deposit Insurance Corporation, have gone beyond the transparency required by current law, and have committed to making their internal deliberations open to the public. But in the absence of a critical mass of CSOs, the effective 'public' is mainly the affected industry. The intent of the Freedom of Information Act has sometimes backfired in this fashion. In all of the NGOs in the USA, politically engaged people expert in the details of financial reform number in the dozens while in the financial industry lawyers, lobbyists and expert witnesses number in the thousands, if not tens of thousands.

In mapping issues and organisations, one finds entire policy areas that are largely uncontested by CSOs, as well as major quasi-governmental international institutions that have no procedures for giving access to CSOs. As noted, the stronger CSO presence is in areas dealing with development, debt and tax issues. The weaker ones are those dealing with reform of the financial system. However, several Europe-based NGOs that began with a commitment to environmental, development or anti-corruption goals, such as Eurodad, have lately moved into financial system issues as well, because the defects in the financial system affect their core concerns.

The United States presents a paradox. The USA has a governmental system that is relatively open to formal and informal participation by civil society, but that is substantively dominated by industry interest groups. So the myriad voluntary associations of civil society celebrated by de Tocqueville do not aggregate to a collective force for fundamental reform. The US has many thousands of NGOs, but they tend to operate in a fragmented fashion. Sometimes, the competition for foundation funding exacerbates the fragmentation, as each seeker of funding endeavours to demonstrate its unique worthiness to receive support.

Formalistically, the policy process in the USA is admirably transparent. In the development of public policy, CSOs have access to the process at four distinct stages: the development of policy by the executive branch; legislative hearings; the executive 'rule-making' process after legislation is enacted; and Congressional oversight hearings that monitor the implementation of laws and regulations. Yet in the area of financial reform, industry lobbyists vastly outnumber consumer, labour and other civil society representatives. For example, in the case of

the implementation of the newly enacted provisions on the regulation of derivatives, one leading NGO expert on derivatives reform points out that the US agency responsible for defining and implementing the law, the Commodity Futures Trading Commission, has fewer officials assigned to the process (about 35) than a single large investment bank, JPMorgan Chase (which has over 100 working groups), and that fewer than five part-time experts representing civil society will participate.

## The importance of allies in government

Points of leverage for CSOs are not limited to formal mechanisms of transparency or consultation. They also include winning legitimacy for an issue by enlisting the backing of heads of government. Some examples are support for third world debt relief and increased ODA by several heads of European governments in the 1990s; the German and Danish governments' criticism of hedge funds and private equity takeovers; the pushback by a number of third world governments against elements of the proposed Doha Round that would compromise their ability to have autonomous regulatory or monetary policy; the nominal support by the heads of many OECD governments for a crackdown on tax and regulatory havens; leaks by friendly governments, mostly in the global South, of draft documents such as the now defunct MAI, that become rallying points of opposition.

Even though the G20 is a government-to-government process, the active engagement of NGOs can influence agendas that then flow back into influences upon national policy. The financial reform issues that have been addressed at G20 meetings since the crisis began – such as asset requirements, regulation of derivatives, regulation of hedge funds and private equity, and strategies for containing systemic risk – all entail primarily national regulation. International standard setting, such as the Basel capital standards, are both too weak to contain the problems and are largely closed to civil society. Even if they were more open, the actual policies are made by national governments. So NGO alliances with sympathetic national governments, now that the G8 has been expanded to the G20, can be of great strategic value. Government agencies with conscientious civil servants, or opposition parties and individual legislators and committees can also be important allies in ferreting out information or analysing data that are on the public record.

## The role of scholars and think tanks

Because NGOs working on financial reform are so thinly spread and lack in-house expertise on complex issues, academic researchers are natural and necessary allies. Economists and political scientists, of course, span the entire political spectrum in their views about the self-correcting nature of financial markets and the appropriateness of regulation, accountability and transparency. Indeed, some of the most potent support for deregulation and financialisation came from academic economists. Moreover, many academics, for personal or career reasons, choose not to become involved in public controversies, while others relish the role of the engaged scholar.

A number of experts at think tanks have become important allies of CSOs in the effort to reform financial practices. These include 'celebrity scholars' who are also Nobel laureates, such as Joseph Stiglitz and Paul Krugman, as well as academics such as Jeffrey Sachs who have amplified their own reach by founding institutes. A map of such institutes concerned with financial reform would include CEPREMAP in France, research/advocacy groups such as SOMO based in the Netherlands, state-financed foundations affiliated with political parties such as the Friedrich Ebert Stiftung in Germany and the Wiardi Beckmann Foundation in the Netherlands, the Roosevelt Institute, PERI at the University of Massachusetts, the Economic Policy Institute and the Jerome Levy Institute in the USA and, at an international level, the new Institute for New Economic Thinking (INET), which is a global network of scholars, as well as many hundreds of individual academics who have lent both technical expertise and scholarly legitimacy to CSO efforts at reform. Engaged scholars also work on financial reform through ad hoc commissions sponsored by UN agencies, such as the 2009 Commission of Experts<sup>24</sup> chaired by Joseph Stiglitz, which made recommendations for global financial reforms. This work complements the efforts of NGOs. Yet most events dealing with financial reform are either scholarly conferences or part of advocacy campaigns, with not much overlap between them. Most scholars deal with reform efforts only incidentally, and most advocacy efforts enlist the rare academic expert only incidentally.

## The fragmentation problem

Often, NGOs working on aspects of financial reform operate in issue silos. Organisations tend to be understaffed and overworked. As a consequence, potential synergies are often unexploited because people are too busy keeping up with their core issues. The global labour movement does work on issues that go beyond its core franchise to address issues of labour standards. Because of the linkages between conditions of labour and the architecture of the global trade and financial system, groups such as the ITUC, the ETUC and global labour federations such as UNI and the IUF do allocate staff to issues of financial reform, trade, debt relief,

abuse of hedge funds and private equity, and they work with global coalitions. However, like other NGOs, their staffs are spread very thin, and they are subject to pressure from their member unions, who often wonder why they are not devoting more of their time to core labour issues.

## Areas of potential overlap and synergy

In recent years, there has been more collaboration among different kinds of specialised NGO working on different issue areas. For example, the campaign for taxation of short-term financial speculation (the 'Tobin Tax') bridges NGOs concerned with development and those concerned with reform of the practices of large financial institutions. Development- and poverty-oriented NGOs have supported such a tax in part because speculation in commodities has led to an increase in the price of basic food products and other staples. NGOs concerned with reforming the structure of the banking system support such a tax because it will deter non-productive and inherently risky uses of bank assets and excess leveraging that produces risks to the system.

Another interesting example of cross-issue collaboration is the coalition of development-oriented NGOs and trade unions that is continuing to challenge the orthodox trade model. In the past, this coalition has come together on an ad hoc basis, as in the 1999 Seattle protests. Collaborating groups include War on Want and World Economy Ecology and Development (WEED), as part of the coalition known as 'From Seattle to Brussels', plus nearly all of the major European and North American trade union federations, plus leading trade unions from the global South such as South Africa's COSATU, Colombia's CUT, KCTU of Korea and APL of the Philippines. This alliance is of major importance, since trade has often divided civil society forces geographically and ideologically. In the past, challenges to the orthodox paradigm have often been dismissed as the North's self-interested 'protectionism'. However, the basic rules of trade relate to several cross-cutting financial reform questions, including the privatisation of development and of World Bank credit programmes, and the ability of developing nations to pursue financial regulations, industrial policies and capital controls.

The connection between reform of speculative global finance as a banking issue and other financial reform issues is multi-faceted. For example, the push for super-normal rates of return drives a number of other abuses, such as the stripping of forests, the promotion of mono-cultural agriculture, the paradigm of unsustainable growth that is mindless of the costs in carbon emissions and climate change, and the overriding of national development strategies by trans-national banks.

There is yet another important connection to climate change issues, since after the blowup of profit centers in sub-prime loans and credit default swaps, global investment banks are hoping to have a major role in the design and

<sup>24</sup> [http://www.un.org/ga/president/63/commission/financial\\_commission.shtml](http://www.un.org/ga/president/63/commission/financial_commission.shtml)

execution of carbon trading schemes, so carbon trading will become a major source of profit for banks rather than a source of funding for technology transfer and sustainable development. This is another huge area of potential collaboration for NGOs concerned with financial reform in the sense of harnessing banking abuses and NGOs concerned with development, resource and climate issues. Opportunities for greater coalition among NGOs working in different issues should be of great interest to the T/A collaborative. Some, but not all of these potential reforms have transparency measures as their core substantive reform.

## The funding challenge

All of the NGO leaders interviewed for this paper discussed the wide disparity between their own resources and those of industry groups. The successful ones have been able to use guerrilla tactics to leverage media publicity, alliances with friendly governments or friendly individuals in government, and alliances with other groups via networks.

Finding adequate funding to support financial reform has no simple solution. In areas other than finance, such as the environment, poverty relief, human rights and civil liberties, the most reliable source of funding may well be the individual membership and donor model. The financial crisis, though it affects everyone on earth, may not be as good a candidate for a mass membership organisation because the policy issues are very complex, and it is harder to give them a human face. It is easier to imagine giving a donation to save a child or a forest than to regulate a bank.

Foundation funding has been a major source for NGOs generally and for those concerned with financial reform. However, these issues are heavily politicised and controversial. The ideological and economic sway exercised by banks does not carve out an exception for the boards of many foundations. Many funders are uneasy about funding insurgent or radical groups. Token forms of transparency do not produce much substantive accountability. Some of the success stories reported in this paper suggest that there is a middle ground where mainstream tactics can produce real progress, yet total dependence on foundations for reform groups is neither politically nor financially prudent.

Government funding can be similarly problematic, though the British, Norwegian, Dutch, and German governments, among others, have demonstrated that they can be arms-length funders of robust NGO efforts towards greater transparency. The German government funds civil society through foundations that are controlled by the major political parties, with funding roughly in proportion to the parties' parliamentary strength. A similar system is being implemented in the European Parliament. My interviewees suggested that government funding of NGOs is more of a challenge in the South, where many if not most governments expect explicit loyalty in return for financial help.

It is also tempting to explore budgets from international governmental organisations to finance official participation by CSOs. But this raises the immediate question of which CSOs are to be recognised, and the risk that docile ones will be given official recognition.

# 6. New initiatives for transparency and accountability

These recommendations are divided into two broad areas:

1. Policy initiatives that pursue greater accountability and substantive reform, where transparency is central as either an organising strategy or reform outcome, or both; and that hold the potential of creating broader and more effective civil society coalitions.
2. Initiatives that produce new strategies and processes for increasing CSO capacity and resources.

This subsection will describe these proposals and assess each in terms of their strengths and weaknesses. The companion paper will narrow these down to five proposed major new initiatives, elaborated in more detail, based on the selection criteria noted above. However all of the initiatives suggested below deserve consideration.

## 1. Increased accountability through greater transparency

### Beneficial ownership

The true ownership of financial corporations and assets is often disguised via trusts, hedge fund or private equity holdings, the use of 'straw' owners, banks voting corporate shares, and the like. This opacity frustrates campaigns for greater accountability on several fronts, including environmental and human development goals, anti-corruption, tax reform, labor standards, human rights, abuse of regulatory havens, as well as enforcement of capital adequacy and risk criteria. Disclosure of beneficial ownership cuts across our three major categories of financial reform.

A generalised campaign for comprehensive disclosure of beneficial ownership, unlike some areas of financial reform, is not abstruse or esoteric. It appeals to common-sense notions of fairness. Opacity of ownership is an affront to the rule of law, since within nations disclosure of ownership is the norm. For publicly traded corporations, ownership is generally a matter of public record under securities laws. Such a general campaign has important synergy benefits, in that it would enlist in a common campaign diverse groups and coalitions working on different conceptions of financial reform. Transparency is absolutely central to this initiative.

### Secrecy jurisdictions

As noted above, tax and regulatory havens use opacity for a variety of illicit or dubious purposes. Their existence facilitates money laundering, tax evasion, capital flight, drug trafficking, financing for terrorism and avoidance of normal financial regulatory standards and disclosures. To the extent that the OECD member nations have decent standards of accountability, disclosure, substantive regulation and tax collection, secrecy jurisdictions undermine them and set off a competitive race to the bottom. As new regulatory challenges have arisen, such as more adequate standards for 'shadow banks' such as like hedge funds and private equity hedge funds, the availability of registration in regulatory havens undermines reform efforts as well as transparency.

As with a general campaign on disclosure of beneficial ownership, a broad coalition to shut down secrecy jurisdictions could link single-issue groups currently working on one area where havens are a prime problem, such as tax evasion or private equity abuse. So it has broad synergy benefits. This campaign is also attractive because governments and the OECD nominally support these goals, albeit in a watered down form, so the argument is about details and not about first principles. This general idea, unlike some arcane areas of financial reform, is not difficult for the public to grasp and is hard to argue with. And this is another area where transparency is both the organising tactic and the essence of the substantive reform. Technically, reform is not difficult to achieve. The fact is that if the major OECD governments could be persuaded that secrecy jurisdictions were a generalised menace, such jurisdictions could be required to share banking and tax data with OECD countries, or be blacklisted for banks and corporations based in OECD countries to do business with.

### Derivatives reform

Secrecy and opacity in the creation and trading of financial derivatives were at the heart of the financial collapse. The creation of exotic derivatives, as well as related financial products such as credit default swaps which in effect were insurance policies on derivatives bets, allowed dangerous levels of leverage that made a mockery of ostensible capital adequacy standards. This failure of both market accountability and regulatory accountability assured that when the crash came, it would be massive. So-called customised derivatives allowed the evasion of even modest national transparency standards, because they are not traded on public exchanges, and hence are not subject to disclosure or conflict-of-interest standards.

Reform groups have urged that all derivatives should be traded and cleared on public exchanges which have clear disclosure requirements, and that privately created customised derivatives be limited to very narrow special cases. Disclosures and public trading are essential for both regulators and investors, as well as for the general public, if abuses are to be avoided. In the recently enacted Dodd-Frank Act, exchange trading is required only in some cases; there are large loopholes for 'customised' derivatives to be created and traded off exchanges; and most of the details are left to regulatory agencies heavily subject to industry pressures as well as industry ingenuity to invent new products. So there is an urgent need for greater engagement by civil society.

As noted, this is another area of potential synergy across different conceptions of financial reform. In addition to contributing to the financial crash, speculation in derivatives has led to sharp increases in prices of basic food crops – price increases that are purely an artifact of traders seeking to manipulate markets. An embryonic organisation called the Commodity Markets Oversight Coalition includes industrial groups that use derivatives legitimately to hedge against price increases, plus consumer groups such as Public Citizen and Consumer Federation of America, and global anti-poverty groups such as Food and

Water Watch, Grassroots International, and the Maryknoll Office for Global Concerns. This coalition, in turn, has spun off a new NGO called Better Markets, whose goal is more transparent financial markets generally. A disadvantage is that the issues are somewhat technical. On the other hand, the direct connection to hunger and poverty puts a human face on the subject.

## Credit rating agencies

Abuses by credit rating agencies were at the very center of the financial collapse. Securities backed by sub-prime loans were able to attract buyers only because they were assigned investment-grade ratings by the rating agencies. Though they use the term, 'agencies,' these are not public or publicly accountable entities, but secretive private corporations. The large ones enjoy official recognition from the Securities and Exchange Commission as 'nationally recognised statistical rating agencies,' though they have little government supervision.

These entities are rife with conflicts of interest, because the issuer of the security pays for the rating and the agencies have consulting-firm affiliates that will advise the issuer on how to game the system to get a high rating. The abuse is precisely parallel to the conflicts of interest that disgraced leading accounting firms in the 1990s, with the difference that there has been no serious reform. The recently enacted Dodd-Frank law in the U.S. gives the SEC authority to establish standards for the rating agencies, but this will be subject to extensive industry lobbying.

This is an issue where transparency is central, because the rating models that the agencies use are considered proprietary information. Some critics have proposed abolishing these private agencies in favor of public institutions. Others call for a change in the way they are compensated. This is a key area that also affects economic development and reform of financial flows, since credit rating agencies rate sovereign debt as well as corporate and other private securities. Despite the potential for a broad civil society coalition, there has been very little CSO activity to counter the influence of industry. Although there have been a small number of reports proposing reforms, there is no ongoing coalition of campaign to reform rating agencies.

## The shadow banking system

Hedge funds and private equity companies make most of their money by borrowing against operating companies that they take over, increasing the ratio of debt to equity. Often, they strip assets, lay off workers, and abrogate explicit and tacit contracts, for example using bankruptcy to terminate pension funds. They take advantage of regulatory arbitrage, often locating their nominal headquarters in regulatory havens such as the Cayman Islands. Ostensibly, hedge fund and private equity abuses were not directly implicated in the recent financial collapse, but are indirectly implicated in three respects. First, hedge funds and private equity leveraging are part of the excessive non-productive debt buildup. Second, they are prime customers of investment and merchant bankers who finance leveraged buyouts (LBOs) and mis-price assets. Third, they are prime traders in abusive products such as credit default swaps, and as such they serve as enablers of crisis. As highly leveraged financial transactions from the boom years continue to

unwind, hundreds of billions of dollars worth of bonds that financed such LBOs are expected to default, creating a continuing drag on worldwide economic recovery.

Because these companies are privately held and their shares are not traded on stock exchanges, they are not required to make even the modest disclosures required of conventional corporations and banks. In the recent rounds of national regulatory reform in the USA and Europe, there was little change in the treatment of hedge funds and private equity, setting up another round of abuses and another crash. A European Commission directive was approved, but remains to be implemented. Very modest disclosures (to regulators, not to the public) were included in the Dodd-Frank bill.

However, there is a near total vacuum in the engagement of NGOs with these issues, except to the extent that trade unions shed a spotlight on private equity and hedge fund practices in the context of resisting asset-stripping and outsourcing or seeking to organise operating companies owned by private equity. In principle, a campaign for hedge fund and private equity reform could bring together CSOs concerned with private financialisation of development, reform of tax and regulatory havens, greater transparency of corporate governance and financial flows generally, and reform of the banking system. A disadvantage is that the details of reform are fairly arcane, though the consequences of the absence of reform are vivid and real.

## Increased access to international governmental organisations

As noted, there are no consultative mechanisms for NGOs to express views to the Financial Stability Board or the other Basel institutions which are now playing a key coordinating role in the effort to fashion common standards for capital adequacy and other reforms in the aftermath of the crisis. Although the constituencies of these bodies are national governments, bank lobbyists manage to insert themselves into the process, and there needs to be a countervailing role for NGOs. CSOs have succeeded in intervening formally and informally to good effect before other bodies such as the IMF and the World Bank and in the G20 process, even though these are ostensibly also government-to-government institutions.

There is a whole other set of quasi-private international standards-setting bodies such as the International Accounting Standards Board, which are effectively governmental but which have little transparency in their own deliberations, with almost no engagement with civil society but very substantial consultation with the affected private financial industries. In some cases, these international bodies are literally the creation of the industry, whose self-devised standards are then given tacit or explicit government recognition. It may be worthwhile to pursue a general campaign for greater transparency and NGO access to all such standard-setting bodies. The disadvantage is that any such campaign would be far-flung and diffuse rather than targeted and easy to dramatise to a broad public.

## Accounting reforms

Accounting standards literally determine the accuracy and degree of transparency of banks and other financial corporations. The challenge is that this issue means different things to different NGOs, and plays out before different public and private regulatory arenas. Better accounting is a prime goal of banking reform, since 'off-balance-sheet accounting' (hiding liabilities and mis-pricing assets) was one of the prime causes of the financial collapse. In the USA, the Securities and Exchange Commission has general authority for accounting standards. Even now, the SEC is belatedly going after the common abusive practice of pumping up balance sheets with short term borrowing just in time for quarterly reporting requirements, and then reverting to more accurate and much shakier finances the rest of the time.<sup>25</sup>

The SEC is an extreme case of the imbalance of industry and NGO lobbying. Its entire regulatory regime is based on disclosure. Corporations that sell stocks to the public are required to make disclosures of material information. As new regulatory challenges arise, the SEC issues new rules. Thousands of industry lawyers and lobbyists monitor and influence SEC activity, while a handful of representatives of consumer groups, public pension funds, and trade union economists represent the public interest. There are frequently rule-making procedures where the only participants are from industry. Some groups that once expressed more of a consumer/civil society perspective, such as the Council of Institutional Investors, now reflect more of an industry perspective.

In the run-up to the financial collapse, the true condition of very large banks was disguised by deceptive accounting. Despite 'stress test' exercises conducted in Europe and the USA, the Congressional Oversight Panel believes that the true condition of large banks continues to be disguised,<sup>26</sup> with the complicity of regulators, and accounts for the reluctance of banks to extend credits to any but the most blue-chip of borrowers, which in turn prolongs the crisis. In the USA, a quasi public nonprofit agency known as the Financial Accounting Standards Board (FASB) has authority delegated by the SEC to determine standards for accounting. During and after the financial crisis, the FASB was pressured into relaxing certain standards, such as 'mark-to-market' accounting, in order to disguise the severity of the crisis and the weakness of the banks.

Globally, the International Accounting Standards Board plays a similar role, and there is ongoing conflict over whether corporate accounting should be subject to FASB or IASB rules. Accurate and transparent accounting is of great importance in all realms of financial reform. That is both an opportunity and a challenge for civil society. For the most part, NGOs are largely absent from the insider battles over accounting standards. For example, other than the unions, there was little counter-pressure when the FASB was strong-armed into relaxing its mark-to-market accounting rules. In principle, one could imagine a generalised campaign for more accurate accounting standards and for CSO access to the deliberation of these bodies. In practice, the issues are far-flung and diverse, and NGO involvement is more of a supply-side problem – i.e. do NGOs have enough troops,

and is this their best use? There is also the challenge of humanising a generally arcane and technical set of issues.

## Increased central bank transparency and accessibility

Central banks have emerged as crisis managers in the recent financial collapse and its economic after-effects. Classically, central banks have four functions. They conduct monetary policy. In some countries such as the USA they also are key bank regulators. In addition, they are lenders of last resort, providing liquidity to the system. And in the crisis, a new power was added – they selectively gave emergency aid to individual damaged banks.

These are enormous economic powers, yet central banks are among the least transparent of governmental institutions. They are deliberately insulated 'from politics' on the premise that short term pressures on monetary policy by politicians (to create an artificial boom in anticipation of an election, for example) should not influence central bank decision-making. However, central banks conduct much more than monetary policy, yet they operate at several removes from democratic accountability. In the Dodd-Frank bill, a provision was included to have the normal audit authorities that audit other government agencies conduct an annual audit of the Federal Reserve. This was weakened in the final Act under lobbying pressure from the Federal Reserve. Two years after the bailout, the Federal Reserve has still failed to disclose details of what securities received emergency guarantees and how they were valued. Minutes of Federal Reserve meetings are disclosed only after a time lag, and much of its processes are conducted in secret. To a greater or lesser degree, the pattern with other central banks is similar.

A general campaign for increased transparency and accountability for central banks could create a common objective for NGOs in different countries and help build a broader coalition for financial reform generally. Unlike some reform issues, this one is relatively straightforward.

## Pension reforms

A large number of NGOs have been pursuing reform of national pension systems. However there are multiple definitions of the policy problem. Transparency and accountability for pension funds mean different things in different contexts. For example, NGOs concerned with labor practices and natural resources issues want pension funds to disclose their investments, to avoid socially destructive ones, and put salutary pressure on pension funds to use their investment powers for social good.

Other sets of pension reform advocates are interested in making sure that pension funds have adequate funds to pay out pensions to retirees. Their conception of pension reform entails accurate accounting. Many corporate-controlled pension funds play an accounting game of projecting implausibly high future rates of return in order to reduce the required annual contribution of the corporation. In some cases, goals of pension adequacy from the perspective of retirees can collide with goals of accurate accounting because if a pension plan is under-funded the political course of least resistance is to reduce projected payouts.

<sup>25</sup> 'Regulators to Target 'Window Dressing'', Wall Street Journal, September 16, 2010.

<sup>26</sup> <http://cop.senate.gov/reports/library/report-091610-cop.cfm>

Private equity and hedge fund owners have frequently taken corporations in and out of bankruptcy in order to shut down pension funds and pension obligations. There is a whole other set of issues of accurate accounting, transparency, and corruption as many governments shift to privatised or semi-privatised systems of pensions in order to get liabilities off the government's books, and as corporations engage in a parallel process, shifting from defined benefit programs (which make the company responsible for a set pension payout) to defined contribution plans that shift the risk to the worker/pensioner.

Trade unions, which are among the principal NGO actors on pension issues, sometimes find themselves awkwardly on both sides of issues. In their role as pension plan trustees, they have a fiduciary responsibility to pursue maximum safe rates of return. But in their capacity as representatives of workers, unions discourage pension funds from investing in socially retrograde corporations and promote socially responsible investing. In some cases, they have used their pension leverage to pressure for hedge fund and private equity reforms, only to relent when an operating company owned by the hedge fund agreed to recognise the union.

In principle, pension fund reform could bring together a large and diverse array of NGOs. It is also an issue that lends itself to vivid and accessible public education. The practical issue is whether there is sufficient common ground, amid diverse conceptions of the problem and varied reform goals, to create a grand NGO coalition with common objectives.

## Restoration of the original roles of the IMF and the World Bank

At the Bretton Woods conference of 1944, the International Monetary Fund and the World Bank were created partly to prevent private financial institutions from exercising a deflationary effect on economic growth. In the interwar period, private money markets had put pressure on nations that ran payments deficits to contract their economies, rather than putting pressure on surplus nations to expand. The core idea of the Bretton Woods system was to create public global institutions and funding mechanisms that would bias the global system towards growth rather than austerity. (The issue of sustainable growth is an entirely separate question, but for purposes of this paper let us stipulate that there is such a thing as sustainable growth.)

In the six decades since their founding, the IMF and the World Bank have mutated into something close to the opposite of what their founders intended. Rather than being a counterweight to the austerity pressures of private finance, they have often served as collection agencies for private finance and enforcers of austerity. In the current financial crisis, austerity demands imposed on governments presiding over depressed economies that have temporarily lost the confidence of private money markets are an especially perverse policy response. A campaign for greater transparency and accountability for the IMF and World Bank could bring together NGOs concerned with debt and development with those concerned with recovery from the global recession and reform of private finance.

## Sovereign wealth funds

As noted, sovereign wealth funds have become huge global investors, and in terms of what they disclose they are regulatory black holes (with such best-practice exceptions such as Norway.) This is an issue that has ramifications for cross cutting issues such as development, sustainability, corruption, and also governance of the financial system, since western governments have relied on sovereign wealth funds to bail out both impaired banks and the balance sheets of entire countries. As long as most sovereign wealth funds disdain even the weak brand of disclosure common to the private financial institutions based on the OECD countries, there will be a huge gap in the international disclosure regime.

A campaign to specify a code of best practices and then to promote their adoption may have some organising and coalition-building value, as long as we recognise that it is probably a long-shot. For the lack of transparency of sovereign wealth funds is part of a much larger problem, since they are typically embedded in nations that are autocracies and that do not recognise even the more basic democratic and human rights. They also have the tactical advantage of being creditors, which reduces both the practical leverage of western governments, especially the USA.

## 2. Strategies for enhancing NGO capacity

### Transparency as citizen regulation and empowerment

Public policy can structure the regulatory process to deliberately increase the role of civil society rather than merely expanding regulatory bureaucracies that are too easily captured by the regulated industry. The Home Mortgage Disclosure Act, and the successor Community Reinvestment Act, engaged citizens in the project of monitoring bank performance. After HMDA was enacted in 1975, as an initiative proposed by NGOs, citizen groups were re-energised by the availability of the data and became a well-informed and constructive educational and pressure group not only on banks but on bank regulators, partly offsetting the immense influence of the industry. The legislation also had beneficial second and third order consequences for civil society. The existence of the data reinforced a very tangible organising project, and gave community groups a template for recruiting activists and training them in the fundamentals of mortgage finance. As individual banks agreed to cease redlining, the result created a snowball effect in which success built on success.

One such success was the Community Reinvestment Act (CRA), a companion law enacted in 1977, which required regulators to evaluate banks and savings institutions in terms of their success in meeting credit needs of their local communities. A bank's CRA rating, in turn, was used by regulators when banks applied to merge, or to open new branches. The CRA also gave financial reform activists a reason and a mechanism for engaging with banks to review their ratings. At the local level, some of the most successful community organisations exist literally because of the leverage provided by the CRA. Here again, the role of these groups means that regulation is not left to the regulators, and there is a far more transparent process in the evaluation of banks' community service record.<sup>27</sup>

Yet another benefit of the HMDA/CRA impact on civil society is that an entire cohort of community bankers has come of age internalising the values of community reinvestment. These bankers grew up viewing their job as engaging with the community. Relations are occasionally adversarial, but often collaborative. This culture has facilitated the growth both of community organisations that combine advocacy with economic development and of a new kind of bank whose prime purpose is community development finance. In legislative and regulatory deliberations, experts/advocates who have experience of actually doing housing and economic development work are among the most persuasive witnesses. So this process enhances accountability, transparency, citizen expertise and the role of civil society in multiple respects. An interesting question is whether there is a general model here, one that can be built upon in the design of other regulatory strategies and the architecture of public agencies to deliberately energise civil society groups.

### New models of financing NGOs

As this paper has made clear, there is a massive imbalance between NGO resources and industry resources on financial reform, most dramatically on the issue of reform of the financial system. There will never be enough foundation funding to support NGOs concerned with financial reform at an adequate level. Three other financing strategies are worth considering.

**Mass membership:** Some groups concerned with human and civil rights, with poverty, with consumer issues, and with the environment finance themselves with mass memberships, complemented by foundation grants. These include Oxfam, the American Civil Liberties Union, Consumers' Union, the Sierra Club, Greenpeace, and so on. It is worth exploring where some set of financial reform issues lends itself to a mass membership organisation.

**Intervenor support:** In some countries, plaintiffs who sue for relief under consumer statutes can collect treble damages in cases of serious abuse. Witness fees can also be paid. In some American states, including Illinois and Oregon, an innovative program creates consumer utility boards (CUBs), which are financed by a voluntary check-off on consumer gas, electricity and telephone bills. The CUBs, in turn, represent consumers' interests in proceedings before state public utility commissions, where the industry viewpoint would otherwise dominate. An initiative on this front would explore ways of institutionalising the financing of CSOs via the regulatory process.

**Official CSO status:** In some Northern European countries, the remnants of a tripartite or corporatist approach gives official recognition and some financial support to labor and business representatives. Germany and the Netherlands have non-profit foundations financed by government in proportion to their parliamentary representation. TUAC, which has official standing at the OECD, has considered seeking official funding, but has rejected the idea out of concern that its independence might be compromised. It may be worthwhile to consider which models of public or IGO support for civil society groups concerned with financial reform might provide resources without giving the official body the authority to define which CSOs are legitimate.

**Parliamentary support:** EU funds have underwritten a number of ad hoc reports by European financial research and action institutes such as SOMO. In the summer of 2010, the Economic and Monetary Committee of the European Parliament proposed a draft directive to regulate hedge funds and private equity companies. The small staff was confronted with some 1,700 requested amendments from lobbyists for the financial industry, and about 30 from civil society. A group of parliamentarians from both the center-left and the center-right proposed an initiative to enlist and possibly underwrite the cost of more independent experts from NGOs to offset the overwhelming power of industry. The convenors of the initiative wrote:

<sup>27</sup> <http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/cra-is-not-to-blame-for-blame-for-the-mortgage-meltdown.html>

'As European elected officials in charge of financial and banking regulations, we ...call on civil society (NGOs, trade unions, academic researchers, think-tanks...) to organise to create one (or more) non-governmental organisation(s) capable of developing a counter-expertise on activities carried out on financial markets by the major operators (banks, insurance companies, hedge funds, etc ...)'<sup>28</sup>

### Strategic convenings

As this assessment has suggested, NGOs that work on different aspects of financial reform often work in parallel but without very much cross-fertilisation or collaboration. It may be useful to convene one or more working conferences of leaders of key NGOs to explore potential areas for greater coalition and collaboration.

By the same token, academic experts occasionally give ad hoc advice to CSOs working on particular issues of financial reform, but for the most part scholars and activists do not attend each other's conferences. North American NGOs working on financial reform rely on activist/scholars from

perhaps a dozen academic research institutes noted above; there is a tradition of engaged scholarship in Latin America, but there appears to be less of this cross-fertilisation in Europe and Asia. Interviews suggested that in Europe, scholarly critics of financial abuses and NGOs pursuing reform campaigns largely work in isolation from one another. A similar convening of leading academic experts on financial reform and leaders of NGOs might provide avenues of increased collaboration.

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<sup>28</sup> <http://triplecrisis.com/u-s-financial-regulations/>

# 7. The use of disclosure and technology

As noted in the discussion of the abuses of sub-prime loans, disclosure by itself does not accomplish much without some organised group to make use of the disclosure. And the disclosure, as in the case of the Home Mortgage Disclosure Act, needs to be tailored to meet a well-defined strategic purpose.

The same is true of technology. A massive data dump can superficially meet demands for greater transparency while frustrating the larger goal of increased accountability. Indeed, the random release of data can actually force groups to waste scarce resources searching for needles in haystacks.

However, the increased presence of technically knowledgeable NGOs is essential for defining which kinds of data need to be tabulated and released, and in what technical form. The computer and the internet, obviously, make it much easier as a technical matter to mine and evaluate data.

In the recent dispute over the details of financial reform, there was a great deal of resistance to greater disclosures of various kinds, either to regulatory authorities or to the general public. Much of the piecing together of data was left to official investigative bodies and to the press. The issue is less whether to use technology than to find uses of technology that facilitate the disclosure of strategically useful information, such as the disclosures produced by the Publish What You Pay campaign or those of the HMDA. We live in an age when we are drowning in data, and the biggest challenge is to get data in politically meaningful form.

This is also a challenge of regulatory policy. In recent legislative efforts, some of the most bitterest battles have been over what data needed to be filed with regulators. Ordinary corporations with publicly traded shares are required to make certain disclosures to the public and to disclose other data to regulator authorities, with criminal penalties if the data are materially misleading. Hedge funds

and private equity companies have resisted filing details of their holdings or trades. Bankers creating or trading derivative securities have resisted requirements to trade them on exchanges where they would be subject to greater transparency.

In the internet age, such data can be grist for both market forms of accountability and for regulatory reform campaigns. To take the case of derivatives, one abuse is the attempt to manipulate prices and speculate in futures. Now that regulators have additional authority to require disclosures, they can be better positioned to determine when market manipulation has taken place. But regulators operate in a political cauldron, raising the ancient question of *quis custodiet* – who watches the watchers. CSO's armed with both disclosures and the technical capacity to monitor them can play that role. But again, the need is for adequate capacity in organisations to review the data and make an issue of abuses.

# Annexes

# Annex I: Recommendations

## Recommendation 1. A general campaign to end tolerance of secrecy jurisdictions

### Background

The very existence of tax and regulatory havens is an affront to the rule of law and a form of corruption in which OECD governments tacitly collude by allowing commerce with them. These havens can be divided into two broad categories: small European countries with secrecy guarantees intended to attract capital seeking to avoid taxes or otherwise to escape detection; and tiny offshore nations outside Europe, mostly in the Caribbean, whose entire economies are built around providing a nominal domicile for European or US-based multinational corporations, investors, or financial enterprises. Typically, a single law firm is the address of record for literally hundreds of US or Europe-based investment companies.

There is no licit purpose for these havens. Their banking and corporate registration laws are constructed for the convenience of enterprises and individuals engaging in tax evasion, money-laundering, circumvention of regulatory structures, capital flight, or other forms of asset-hiding. Their existence is also a generalised assault on transparency and the capacity of OECD member nations to collect taxes owed and to enforce regulations against financial abuses. Their explicit purpose is to obstruct corporate accountability.

Since these tiny haven nations have no geopolitical power or strategic leverage over OECD nations, in principle it should be very easy for larger nations to require them to enter into tax treaties and conventions and to cooperate with regulatory enforcement or to place them off-limits for transactions that involve any OECD-based enterprise or citizen. The only explanation for the diplomatic failure by major nations to end this regulatory black hole is the significant influence that the financial sector has over OECD governments, coupled with a race to the bottom on the part of many governments seeking to provide settings that are congenial to capital.

### Concept

If there ceased to be any tax-avoidance or regulatory-avoidance benefit to incorporating in venues such as the Cayman Islands, European and American enterprises and investors would simply stop using them. That would produce a significant gain not just for revenue but for transparency and accountability, since the systems of corporate regulation in the OECD countries are heavily based on disclosure regimes. Ideally, these secrecy jurisdictions should be shut down. No jurisdiction should be tolerated as a haven for financial law-breaking.

As an interim step, OECD countries could ignore the fiction of offshore registration in illegitimate havens, and require that any enterprise, fund, or investor doing business in an OECD country be required to file the usual tax and regulatory reports directly with the appropriate OECD government agency. This remedy is necessary because most tax havens lack adequate capacity to collect information from banks, hedge funds and private equity companies nominally domiciled within their borders. So their agreement to share information is often hollow, unless the information is provided by banks and investment companies directly, as it is under banking, tax, and securities laws in rule-of-law countries.

The OECD's initiative on tax havens began with an effort to require secrecy jurisdictions to provide information to tax authorities at a level comparable with that of OECD member nations. Those that refused were to be blacklisted, and declared legally off limits to legitimate enterprises. This initiative has been watered down to the point where all tax havens are now nominally complying with weakened requirements and none are on the current OECD blacklist. But the main requirement for this seal of approval is a willingness to share tax information in individual cases when requested to do so, rather than general information sharing. Because these states are not serious about tax or regulatory enforcement, they lack enforcement bureaucracies and simply do not collect a great deal of information. So the OECD's progress, while substantial on paper, remains largely pro forma.

What is required, therefore, is increased political will on the part of the large nations. This, in turn, requires a shift in the balance of forces that influence OECD governments, and a more intensive public campaign for reform.

### NGO activity to date

For the most part, efforts by civil society organisations (CSOs) have pursued the tax aspect of these abuses, while there has hardly been any campaigning on the regulatory ones. The Tax Justice Network (TJN) has had success in putting a spotlight on tax-evasion abuses and helping to win partial reforms, as described in the strategic review paper.

In the U.S., legislation has been introduced by Senator Carl Levin to define a 'U.S. person' as one who has beneficial ownership of assets as subject to U.S. law even if the assets are nominally domiciled in a haven. The proposed Levin bill also lists 34 'offshore secrecy jurisdictions' that can be the object of special enforcement proceedings to collect taxes or prosecute violations of the securities laws. Barack Obama,

when he was a senator, was a co-sponsor of this legislation. Unfortunately, this bill lacks majority support, and there is no broad coalition of advocates of tax fairness and critics of hedge fund and private equity abuses to require a generalised crackdown on secrecy jurisdictions.

## Points of leverage

Major governments have already conceded the issue in principle: tax and regulatory havens ought not to exist. Some nations, such as Germany, are politically serious about reform and have succeeded in changing the behavior of Europe's leading secrecy jurisdiction, Switzerland, where many German citizens were hiding income and assets to evade tax collections. The financial collapse and abuses on the part of a leading Swiss bank, UBS, led to unprecedented information-sharing between the Swiss authorities and US and European law enforcement agencies. By the 2009 G-20 meeting, the world's major nations agreed – in principle – that tax havens should be shut down. So a generalised campaign for elimination of secrecy jurisdictions would have important governmental allies.

There is also the issue of tax equity at a time of fiscal crisis. Given that many hundreds of billions of dollars of owed taxes go uncollected every year due to the existence of these havens, OECD governments facing a fiscal squeeze are literally opting for increased taxation or the reduction of services for their law-abiding citizens over reform of these havens and those who take advantage of them. There is much greater potential for publicity and shaming.

A further point of leverage is that a well established process already exists under the auspices of the OECD to increase compliance on the part of secrecy jurisdictions with general norms of tax enforcement. So the campaign does not need to be created from scratch. But the devil is in the detail. CSOs currently do not have the resources to adequately monitor the development of standards or to mount a high-profile general reform campaign, and it will take a much more vigorous effort to balance the influence of industry and improve the currently glacial pace of progress.

## Proposed campaign and goals

### 1. Convening

A broad coalition of NGOs could propose a general goal of shutting down secrecy jurisdictions. The campaign could begin with a convening of NGOs that work on tax fairness, beneficial ownership, prevention of needless cuts in public services, hedge fund and private equity reform, capital flight and financial transparency generally.

### 2. Monitoring, publicity and research

This coalition, and a staff secretariat, could systematically monitor the OECD tax haven process and other regulatory processes in major nations, and press for stronger action. It could publicize abuses and commission research where enforcement gaps exist.

### 3. Expand the OECD tax haven initiative

As an interim step, it could propose that the OECD's tax haven initiative be expanded to include a general regulatory haven initiative.

### 4. Partnership with scholars

The coalition could identify and bring together academic researchers on tax and regulatory haven abuses. Such researchers exist and do excellent work, but for the most part they are disconnected from the NGO advocacy process.

### 5. Participation in regulatory and legislative processes

The coalition could also take more advantage of available processes, such as the hearing process in the U.S. Congress and the committee process in the European Parliament. The coalition could target the G-20 process to make the closure of secrecy jurisdictions a much higher diplomatic priority.

### 6. Goal of shutdown by 2015

The coalition should devise model legislation building on the Levin bill, and build a broad campaign around the abolition of secrecy jurisdictions by a realistic year, for example 2015.

### 7. Financing

Funders could provide support to enable affiliated NGOs to participate in the campaign and to underwrite a small coordinating secretariat.

## Theory of change

The premise is that the closure of secrecy jurisdictions is a ripe target for reform, which has not occurred because of the absence of countervailing political forces. The elements of a potentially much more effective civil society coalition have been working on pieces of this reform, sometimes in isolation from one another. The whole could be more powerful than the sum of its parts.

This initiative also lends itself to popular publicity and citizen indignation, which would shift secrecy-jurisdiction reform from a marginal issue to a winning political issue for governments and opposition parties. The details of tax and regulation may be technical, but the nature of the abuse and remedy are very easy for the public to grasp – some wealthy individuals and firms break the law by pretending to locate their businesses offshore. There is no plausible defense of the practice.

So if a more highly visible and effective campaign were to be launched, it would have a decent prospect of success. This is also an area where success is cumulative. The more that tax and regulatory havens comply with OECD norms, the more evaders get caught and the less attractive the havens are to others.

## Ancillary benefits

Such an initiative would have several spillover benefits beyond increased corporate accountability. It would forge a working alliance among NGOs that begin with a common philosophy and set of goals, and it would demonstrate the importance of efficacy of transparency as a remedy and of NGO action as an instrument of reform. It would provide a model for broader coalitions of NGOs working on different but parallel tracks. It would signal that no havens from tax or regulatory fairness are to be tolerated.

## Key stakeholders and links with existing initiatives

Organisations that might be logical stakeholders include Global Witness, the Tax Justice Network, Citizens for Tax Justice, SOMO, AFR, EFR, The Robin Hood Campaign, Public Citizen, ATTAC, TUAC, ETUC and its constituent members.

## Recommendation 2. Shadow banking, sustainable development, and systemic risk

### Background

The full paper on financial reform stresses the potential of synergies and coalitions among NGOs concerned with different facets of reform. One such cross-cutting issue is greater transparency and disclosure in the regulation of derivative securities and of the 'shadow banking' institutions that traffic heavily in them, such as hedge funds, private equity companies and off-balance-sheet affiliates of large commercial and investment banks.

This issue has the potential to bridge NGOs concerned primarily with the safety and soundness of the banking system and those whose primary focus is poverty, debt and development. There are some NGOs that work on both of these areas, but often they operate in separate silos.

One very important bridge issue is the manipulation of derivatives in futures markets dealing with basic foodstuffs. There is substantial evidence that significant increases in the price of food since 2008 have little to do with underlying supply and demand, but reflect abusive speculation in futures markets. The U.N. Special Rapporteur on the Right to Food, Olivier de Schutter, recently released an authoritative report on this problem.<sup>29</sup> Speculation in commodities prices was also the subject of investigative hearings by the U.S. Congress, and there is increased authority in the Dodd-Frank Act for the Commodity Futures Trading Commission to crack down on market manipulation. There is also very modestly increased authority for the Securities and Exchange Commission (SEC) to require additional disclosures by hedge funds, private equity companies, and affiliates of investment banks. A parallel process is occurring in the EU, where the Commission is finalising an Alternative Investors Fund Managers' Directive aimed at greater transparency and accountability for hedge funds and private equity companies. Proposals for greater transparency are also under discussion in other states.

However, as the strategic review paper indicates, this is an area of extreme imbalance of lobbying activity and political influence. Derivatives are an immense source of both profit and systemic risk. There is a critical need for more transparency and accountability – and for NGOs to play a countervailing role as policy is developed and implemented.

Two other related issues are the financialisation of development and the potential abuse of derivatives securities in the context of carbon trading schemes. In recent years, as the World Bank and its affiliates have relied more heavily on the private financial sector, the use of securitised loans and secondary derivative instruments

has shifted risk onto developing countries. If investors abruptly decide that these financial instruments are at increased risk, nations of the global South can suddenly find themselves financially vulnerable, often for reasons not of their own making. Bankwatch recently reported that the International Finance Corporation's private sector portfolio has more than quintupled since 2002, and that an increasing share of that privatised development funding does not go directly into projects but to financial intermediaries and private equity funds.

Large investment banks view carbon trading as the next great profit center, and the same potential for the extraction of exorbitant profits and the passing along of systemic risks exists in this area as existed in the abuses of derivatives in the recent financial collapse.

In addition, the financialisation of development creates a shadowy environment in which corruption flourishes. Private equity companies can make deals with authoritarian regimes. Corner House has written a case study of a Nigerian corruption case involving the European Investment Bank and a Private Equity firm based in Texas.<sup>30</sup> NGOs concerned with the use of transparency to reduce government corruption are also engaged in these issues.

NGOs that support a tax on financial transactions do so for a number of reasons, but one stated objective is to discourage the use of derivatives detrimental to sustainable and transparent third-world development. That network is potentially part of this effort, too.

So there is potentially a very broad coalition of CSOs that support – for diverse reasons – the common goal of greater transparency and accountability of the shadow banking sector. As noted in the review paper, such a coalition exists on paper, in the form of the Commodity Markets Oversight Coalition (CMOC), but that group it is not currently waging an active campaign and has no real staff. A planning conference is scheduled for London on November 2 convened by the Bretton Woods Project and Counter Balance to broaden the coalition that links financialisation of development to an array of other reform issues.

<sup>29</sup> Olivier de Schutter, 2010, 'Food Commodities Speculation and Food Price Crises', United Nations: September 2010.

<sup>30</sup> [www.thecornerhouse.org.uk/resource/concerns-over-alleged-corruption-cdc-backed-companies-nigeria](http://www.thecornerhouse.org.uk/resource/concerns-over-alleged-corruption-cdc-backed-companies-nigeria)

## Concept

A generalised campaign for greater transparency and accountability for the 'shadow banking' sector – hedge funds, private equity, opaque off balance sheet entities, trading in derivatives, all of which are far less adequately regulated than banks – could bring some increased resources to the reform side of the policy debate. It could bring together NGOs that seldom work together. The humanitarian aspect – the effects of derivatives abuses on the price of food – puts a human face on an issue that is otherwise arcane and technical.

## Points of leverage

As noted, the E.U. Commission is continuing to develop its directive on hedge funds and private equity. Legislation has been enacted in the U.S.A., and now the regulatory process is going forward. U.S. rulemaking proOECDures are admirably transparent. The problem is the disparity of resources. The U.N. has also raised the issue of these speculative abuses. The World Bank and the IMF are under some public pressure to distance themselves from the private banking practices that produced the financial collapse.

## Theory of change

Greater NGO participation in these issues would increase the likelihood that governments would enact laws and rules requiring much greater disclosure and transparency both to regulatory agencies and to the public. The greater availability of data would enhance both market and civic/regulatory forms of accountability. On the market side, there would be less mispricing of financial assets, less opportunity for windfall profits for financial intermediaries, and a lower level of systemic risk. On the civic/regulatory side, NGOs would be better positioned to make these abuses a high-visibility public issue and to help keep regulators from being captured by industry. Progress would enhance the prestige of NGOs, and create the conditions for further progress. And this would dramatically broaden the coalition of NGOs that ordinarily collaborate, and enable the public and lawmakers to better connect the dots between seemingly disparate issues.

## Proposed campaign and goals

**Convening:** Members of the collaborative could convene a planning meeting of a wide array of NGOs interested in better transparency and accountability for hedge funds and private equity; better regulation of derivatives; and resistance to financialised development and perhaps the use of carbon trading as an instrument of speculator enrichment (though that may take us into a whole other area.) This is potentially a very broad coalition. The meeting could define boundaries of the initiative so that it is strategically viable and not overly broad.

**Coordinating committee:** A coordinating committee would be created to set common goals and tactics.

**Research:** The committee would identify useful academic research and friendly scholars, as well as gaps to be filled in.

**Best practice:** The committee and its affiliates would commission papers to define best practice and abusive practices in each of the areas, to identify gaps in NGO engagement and to devise a common public campaign around a small number of key reforms. These could include:

- Enhanced standards of disclosure on hedge funds and derivatives;
- A requirement for all derivatives to be standardised and traded on regulated exchanges, with conflict-of-interest and market manipulation rules;
- Stricter regulation on commodities speculation;
- Limitations on the financialisation of development lending by IFI's.

**Public campaign:** A broad public campaign would be launched, perhaps with some celebrity leaders.

**Key stakeholders:** Eurodad, Bretton Woods Project, Bankwatch, WEED, CRBM, AFR, Public Citizen, ETUC, Corner House, SOMO, CMOG.

## Recommendation 3. Credit rating agencies

### Background

Conflicts of interest by credit rating agencies were central to the financial crash and to ongoing abuses. The largest of these private corporations (e.g., Moody's, Standard & Poor's) have official recognition from governments, and are the de facto worldwide arbiters of creditworthiness. But in the run-up to the collapse, these agencies gave high ratings to junk securities, and were paid to do so by issuers of the securities. Right up until the eve of their collapse, the securities of large banks that either went broke or required massive government aid to stay afloat were given double-A or triple-A ratings by the agencies. The entire system of delegating the work of credit rating to opaque and conflicted private, for-profit companies was a spectacular failure. Neither market mechanisms of accountability nor regulatory ones did their job.

Neither the Dodd-Frank law in the U.S.A. nor its European counterparts fundamentally reform these abuses, though Dodd-Frank does give the SEC the authority to create a monitoring process and establish standards. That regulatory process would benefit immensely if CSOs were part of it.

The process by which these private agencies derive ratings is considered proprietary information. Credit rating agencies have never disclosed their internal processes or criteria either to regulators or to the public. This should be done, and NGOs need to be part of the process of building public awareness and making the case to regulators for full transparency and then monitoring the results as well as monitoring regulators. Other proposed reforms beyond transparency include a new system of replacing private rating agencies with public or non-profit institutions or at the very least devising alternatives to the current practice of having the issuer of the security pay the agency for the rating – which creates a built-in conflict of interest. A further abuse is that rating agencies tend to give the bonds of states and municipalities (which almost never default) a lower than justified credit rating, which raises their cost of borrowing. This occurs because the business of rating states and localities does not generate consulting income and is not a significant profit center for the agencies.

Few NGOs have made this issue a priority. Public Citizen and Demos have written free-standing reports on abuses and possible remedies, and Americans for Financial Reform has testified on the issue. Some unions have been involved, but this is a second or third-tier priority for multi-issue groups. In Europe, the European Council has directed the Commission to create new regulations for rating agencies under the aegis of the new European Securities and Markets Authority (which does not yet exist), but there is little political will for sweeping reform.

Surprisingly, there has been little if any pressure from investor groups that presumably benefit from honest ratings. If there is not expanded civil society involvement, industry influence will dominate the regulatory process both in Europe and the U.S.A., and will lead to weak standards of transparency, accountability, and reform of conflicts of interest.

This is also a key area that affects economic development and reform of financial flows, since credit rating agencies rate sovereign debt as well as corporate and other private securities, and their failure to accurately rate risk intensifies the herd instinct among investors, creating periodic foreign exchange crises and a higher cost of capital for countries that find themselves in temporary recession or fiscal imbalance, often for global reasons totally beyond their control. So this is another area of potential synergy among NGOs concerned with debt and development, those concerned with transparency of financial flows, and groups working on reform of the banking system.

## Concept

A broad, high visibility campaign by a coalition of NGOs could elevate transparency and accountability of the credit-rating process to a first tier public issue. Increased financial support for this initiative could fill a significant gap in the engagement of civil society with a key issue of transparency and accountability.

## Proposed campaign and goals

**Funders could put out requests for proposal (RFPs).**

Interested NGOs could participate in a planning conference. A steering committee of existing NGOs could design the campaign, or a new NGO specifically tasked with this reform could be created. The campaign would include:

- Taking fuller stock of existing resources, including hearings records, investigative reports by official agencies, and academic research.
- Enlisting other NGOs and political allies
- Identifying the range of possible reforms, and selecting preferred measures.
- Educating the public to connect abuses of rating agencies to abuses in sub-prime lending, securitisation, opacity in financial transactions, corruption and the high cost of capital for developing countries as well as nations hard hit by the crisis such as Ireland and Greece.
- Creating a public reform campaign.
- Raising the profile of the issue in the media.
- Considering additional conferences.
- Providing expert witnesses to testify in legislative and regulatory venues.

**Duration of the initial campaign:** two to four years.

## Theory of change and points of leverage

Regulation is just now going forward in the U.S.A. and the E.U. The absence of NGO engagement virtually guarantees that there will be no fundamental reform of institutions that were a prime cause of the financial collapse and that have not changed their business model. Increased public awareness and an increased NGO presence in regulatory forums and in the court of public opinion could change that dynamic.

## Recommendation 4. Accounting reform and beneficial ownership

### Background

Accurate and transparent accounting is literally the precondition to other strategies of accountability. The failure of accurate accounting cuts across all three categories of financial reform – development and debt, financial flows and corruption, and banking system abuses and reforms.

#### The banking crisis

The financial collapse was rife with fraudulent accounting. Banks resorted to ‘off-balance-sheet’ affiliates and subsidiaries to disguise the extent of their liabilities. By definition, a balance sheet is an accurate and complete reckoning of an enterprise’s assets and liabilities. With honest accounting, there is no such thing as off-balance-sheet assets or debts. In the financial crisis, debts were disguised as assets, and asset prices were inflated. Agencies that were supposed to monitor accounting standards were themselves corrupted.

#### Financial flows

Dishonest or incomplete accounting leads to mis-priced imports and exports, tax-evasion both via tax havens and via transfer-pricing, and impenetrable corporate reports that frustrate corporate accountability. The failure of the accounting system to require disclosure of beneficial ownership adds too the opacity and potential for evasion and corruption.

#### Debt and development

The absence of a transparent and systematic country-by-country system of accounting facilitates corrupt payments to governments, capital flight, and distortion of development investment.

### Concept

There needs to be a single, global, and comprehensive set of accounting standards for corporations, financial enterprises, and countries. This is a hugely ambitious goal that cuts across and potentially bridges a number of issues. It also runs into immense political obstacles, since the development strategies of some emerging economies, most notably China, are based on hidden subsidies and incomplete or misleading accounting. Governments of many Western nations side with their corporate sectors in resisting comprehensive reform. Such a campaign is most effectively based on incremental reforms that can be achieved in the near or medium term, and which then can be built upon. For example, convergence of more comprehensive accounting standards in the OECD countries may be a more attainable short-term goal.

There is already a coalition of NGOs promoting accounting reform, including country-by-country disclosures of sales, profits and taxes, as well as disclosure of beneficial ownership in all banking and securities accounts. This coalition, under the auspices of the Task Force on Financial Integrity and Economic Development, recently held an international conference in Bergen, Norway. Interestingly, the conference was heavily weighted to development and transparency oriented NGOs. An even broader initiative could bring in NGOs concerned with reform of the banking system, and have more impact on issues of common concern.

### Theory of change

Very simply, a broader coalition could bridge banking reform constituencies with development, transparency, and anti-corruption constituencies, and have increased impact. Incremental change could lead to more systemic reform.

## Points of leverage

Not only are there incomplete accounting standards – although commerce is global, different nations use different systems of accounting. The International Accounting Standards Board (IASB), which is followed by many nations, uses one system and the US-based Financial Accounting Standards Board (FASB) uses another. The two organisations have been committed to a process of convergence by 2014, but the pace is glacial and deeply politicised. The risk is of a harmonisation downwards. In the recent financial crisis the FASB, nominally a non-profit organisation with an independent board of trustees, succumbed to political pressure and modified some of its standards in order to help banks disguise their weakened balance sheets by avoiding ‘mark-to-market’ accounting. The effort to harmonise IASB and FSBY standards presents an opportunity to harmonise standards upwards. But forces representing the self-interest of industry have far more lobbying power day in, day out than those of civil society, and the issue has generally been framed as accommodating the divergent interests and standards of different countries rather than promoting more transparency. A broader coalition that joined advocates of banking system reform to advocates of more transparent development flows could help rectify that imbalance.

The investor community is divided, in that some investors (as well as leaders of nations) thrive on opacity. But others favor honest and transparent markets and could be enlisted as allies. Greater accounting transparency has been embraced as a general goal by some elements of the business community. The goal is not controversial; all of the conflict is about the details.

Pressure is increasing, mainly in the USA but also in Europe, for China to allow its currency to be accurately valued in money markets and to follow WTO norms of transparency regarding its hidden subsidies. In September 2010, the U.S. House of Representatives by a wide bipartisan margin, passed a bill authorising retaliatory tariffs. Leaders of major nations and of the business community, concerned about an escalating trade war, may come to see greater transparency of currency valuation and hidden subsidies as the lesser evil, and may become converts to the cause of greater accounting transparency.

Much of the implementation of banking reform legislation in the USA and EU involves accounting standards and their regulatory details. This provides an opportunity to shape reforms. Here again a stronger and broader CSO coalition could serve as a countervailing influence.

## Proposed campaign and goals

In this effort, a campaign has already begun and goals have been set, under the aegis of the Task Force on Financial Integrity and Economic Development. To its goals one might add the following banking-system reform goals:

- No off-balance-sheet entities or accounting
- The same public disclosures by hedge funds and private equity companies as are required of publicly traded companies
- Comprehensive accounting and disclosure of all trade-related subsidies on a country-by-country basis
- Harmonisation upward of FSBY and IASB standards
- Transparency of sovereign wealth funds

**A broader, higher profile campaign could link existing NGOs with new ones:** A new convening could set broader goals and strategies, and add banking-reform NGOs to the existing NGOs that are major participants in existing efforts for accounting reform. The biggest challenge for this effort is to put a human face on what is otherwise an arcane and seemingly dull issue – accounting standards.

**Existing major stakeholders:** Global Financial Integrity, Task Force on Financial Integrity and Economic Development, Tax Justice Network, Global Witness, Publish What You Pay, Revenue Watch Institute, Christian Aid, New Rules for Global Finance, Eurodad.

**Potential new major stakeholders:** Public Citizen, Americans for Financial Reform, Europeans for Financial Reform, SOMO, Weed, Third World Network, ETUC, TUAC, IUF, Bretton Woods Project.

## Recommendation 5. New strategies for resources, funding, and capacity building

### Background

This final recommendation is of a different kind. It is not a proposal for a new approach to transparency and accountability, but rather a search for new strategies of underwriting NGO activity in the different areas of financial reform.

As the strategic review paper demonstrates, there is an extreme imbalance of resources between CSOs promoting greater accountability and transparency on the one hand and corporate and state forces that thrive on corruption and opacity on the other. There is ample evidence that additional foundation funding is needed to right this imbalance, but foundations have many other calls on their limited resources and foundation support alone will never be sufficient. Therefore, the movement for financial reform needs to become much more creative in seeking alternative sources of support, and foundation funding can help it to do so.

### Examples of alternative support

The strategic review paper identifies four different categories of possible support. They include:

#### Individual membership

Some groups that promote social reform via greater transparency substantially finance their activity through mass individual memberships and donations. These are typically groups concerned with human and civil rights (The American Civil Liberties Union), with global poverty and development (Oxfam), with consumer issues (Consumers Union), and with the environment (The Sierra Club, Friends of the Earth, Greenpeace.) The trade union movement also finances itself with individual dues. These groups tend to make their case for individual membership on one of two appeals: self-interest coupled with a commitment to reform (the labour movement; consumer organisations) or a vivid large scale threat to humanity that appeals to conscience (global poverty and disease), or a combination of conscience and self interest (saving the planet.)

The recent financial collapse cost ordinary people around the world many trillions of dollars in lost incomes and assets. It is a humanitarian disaster, but it is not generally framed as one. Had there been adequate transparency and accountability, the abuses that caused the collapse would never have reached crisis proportions. The challenge for advocates of financial reform is to devise a comparably vivid appeal and an organisational vehicle to enlist individual memberships. This strategy is worth testing.

### Intervenor support

As noted in the discussion of the Home Mortgage Disclosure Act in the strategic review paper, some forms of regulation can energise and reinforce activism on the part of CSOs. But it is possible to go beyond that dynamic, and build financial support for citizen watchdogs into the regulatory process. In the United States, citizens who bring qui tam lawsuits that uncover abuses can recover fees (under Anglo-American common law, a qui tam suit is one in which a private citizen aids prosecutors). In civil cases, under some statutes plaintiffs who sue for relief under consumer statutes can collect treble damages in cases of serious abuse. The environmental and consumer movements have used both strategies. Expert witness fees can also be paid and often are in civil and regulatory cases. In some US states, including Illinois and Oregon, consumer utility boards (CUBs) are financed by a voluntary check-off on consumer gas, electricity and telephone bills. The CUBs, in turn, represent consumer interests before state public utility commissions. A broad initiative on this front would explore ways of institutionalising the financing of CSOs via the regulatory process.

### Official CSO status

In some Northern European countries, the remnants of a tripartite or corporatist approach give formal recognition and some financial support to labour and business representatives. Germany and the Netherlands have non-profit foundations financed by government in proportion to their parliamentary representation. Ministries in several European nations have given ad hoc support to CSOs. TUAC has official recognition from the OECD and has periodically considered whether to seek financial support, but has never applied out of concern that its independence might be compromised. The practical question is whether a process could be devised so that government or IGO financial support for NGOs concerned with financial reform could provide resources, without giving the official body the authority to define which CSOs are legitimate. The risk is that the most financing would go to the least assertive CSOs.

## Parliamentary and state support

EU funds have underwritten a number of ad hoc reports by European financial research and action institutes such as SOMO. The European Parliament has reached out to CSOs in an effort to improve the balance of lobbying influence. For example, in the summer of 2010, the Economic and Monetary Committee of the European Parliament proposed a draft directive to regulate hedge funds and private equity companies. The small staff was confronted with some 1,700 requested amendments from lobbyists for the financial industry, and about 30 from civil society. A group of parliamentarians from both the center-left and the center-right proposed to enlist and possibly underwrite the cost of more independent experts from NGOs to offset the overwhelming power of industry. The convenors of the initiative wrote, 'As European elected officials in charge of financial and banking regulations, we ...call on civil society (NGOs, trade unions, academic researchers, think-tanks...) to organise to create one (or more) non-governmental organisation(s) capable of developing a counter-expertise on activities carried out on financial markets by the major operators (banks, insurance companies, hedge funds, etc ...).'

Among the state sources that currently support NGOs concerned with different aspects of financial reform are the UK's Department for International Development (DFID), The European Commission; the Irish Department of Foreign Affairs; the Netherlands Ministry of Foreign Affairs; the Swedish International Development Cooperation Agency (Sida); and the Norwegian Agency for Development Cooperation (Norad). With proper safeguards, NGOs could receive increased state support and use it to increase their research and monitoring capacity. Even if the increased funding underwrote research, but not public campaigns, finance is fungible and it would free other resources. SOMO and Global Witness, among others, seem to manage this balancing act without compromising their activism or integrity.

## Theory of change

This recommendation should be understood as an attempt to create greater *countervailing power* on the part of civil society to offset the disproportionate economic and political power wielded by multinational financial enterprises. With increased capacity, CSOs will bring to light more abuses, track more issues and policies in adequate detail, develop more expertise, and wage more effective campaigns.

## Proposed project

**Creation of an NGO collaborative:** Representative NGOs could be invited to send proposals to be part of this project.

**Seed money:** Participating foundations could provide seed money to a collaborative of NGOs representing different facets of the movement for greater transparency and accountability in finance.

**Feasibility study and testing of models:** This body could conduct feasibility studies on different strategies for new forms of financing. One study would test the appeal of a membership model. Another would interview NGOs that received government support to determine whether their independence was compromised. A third would take stock of all the intervenor models. A fourth would interview other NGOs that have received official support to assess their experience and the pro's and con's. A fifth would interview key parliamentary, government, and IGO actors to determine their sympathy for this approach and potential allies.

**Duration:** A report with recommendations would be presented to participating foundations, within one year.

## Annex II. Persons interviewed

**Steven Abrecht** *Policy Director*

Service Employees International Union

**Anders Lustgarten**

Bretton Woods Project / CounterBalance

**Perenche Beres** MEP

Chair of parliamentary inquiry on financial reform

**Heather Booth** *former Executive Director*

Americans for Financial Reform

**Andreas Botsch**

European Trade Union Confederation

former Senior Economist, German trade union movement.

**Robert Boyer** *Senior Researcher* and former co-director

CEPREMAP (France)

**Lisa Donner** *Executive Director*

Americans for Financial Reform

**John Evans** *Director*

Trade Union Advisory Committee to the OECD

**George Goehl** *Executive Director*

National People's Action

**Michael Greenberger** *former Deputy*

to Brooksley Born, adviser to AFR, to the CFTC, and to key legislators

**Pierre Habbard**

TUAC and French trade union movement

**Robert Johnson**

Roosevelt Institute and Institute for New Economic Thinking

**Allan Larsson** *former Finance Minister*

Sweden

**Michael Masters**

Commodity Markets Oversight Coalition

**Poul Nyrup Rasmussen**

former Prime Minister of Denmark

**Peter Rossman**

International Union of Food Workers

**Ellen Seidman** *former Chair*

Office of Thrift Supervision

**Damon Silvers**

Associate General Counsel in charge of financial issues

AFL-CIO

**David Smith** *Chief Economist*

U.S. House Committee on Banking

**Ernst Stetter**

Europeans for Financial Reform

**Joseph Stiglitz**

Columbia University

**Lynn Turner** *former Chief Economist*

Securities and Exchange Commission

**Lori Wallach** *Director*

Public Citizen Global Trade Watch

**Andrew Watt** *Economist*

European Trade Union Confederation

**Elizabeth Warren** *Interim Director*

Consumer Financial Protection Bureau and Chair, Congressional Oversight Panel

**Robert Weissman** *President*

Public citizen

In addition to these interviews, several members of the reference group made comments on drafts, exchanged emails, and responded to an extensive questionnaire.

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## About the author

**Robert Kuttner** is a distinguished senior fellow at Demos and co-editor of *The American Prospect*. He was a longtime columnist for *BusinessWeek*, and continues to write columns for the *Boston Globe* and the *New York Times* international edition. He co-founded the Economic Policy Institute and serves on its board.

He is author of nine books, most notably *Everything for Sale: the Virtues and Limits of Markets*. His other writing has appeared in such publications as *The Atlantic*, *The New Yorker*, *Foreign Affairs*, *Columbia Journalism Review*, *Harvard Business Review*, *Political Science Quarterly*, and the *New England Journal of Medicine*.

Previously, he served as chief investigator of the U.S. Senate Banking Committee, and economics editor of *The New Republic*. He has taught at Boston University, Brandeis University, the University of Massachusetts, and Harvard's Institute of Politics. He was educated at Oberlin College, the University of California at Berkeley, and the London School of Economics.

