

# Inquiring for truth and the re-engineering of the corporate contract

JUSTIN O'BRIEN\*

*University of New South Wales, Sydney*

## ***Abstract***

*The British Prime Minister, Gordon Brown, has called for a global re-negotiation of a social contract between investment banking and wider society. Given the scale of the losses now borne by the taxpayer as a consequence of the global financial crisis in jurisdictions as diverse as Iceland, the United Kingdom, Ireland and the United States, the proposal has undoubted rhetorical strength. It is also exceptionally difficult to render operational, not least because of (purposive) ambiguity over what constitutes and who should decide terms of reference. Moreover, piecemeal change may not only not secure legitimacy but may also have enormous if unintended consequences for the conceptual underpinning of corporate and securities law and the resulting regulatory framework. At a national level, one mechanism proposed to address this issue is through the establishment of a “truth commission” an option chosen by Iceland. A second option is to convene an independent commission, a mechanism used throughout the Commonwealth, or an independent tribunal of inquiry, as used with increased frequency in the Republic of Ireland throughout the 1990s but rejected in relation to the global financial crisis. A third option is to convene a bi-partisan political commission, as deployed in the United States. Each option is exceptionally problematic within the domestic context, not least because of contention over remit and degree to which the findings translate into policy changes. The difficulties are compounded when applied to multi-faceted multi-jurisdictional problems such as the global financial crisis. This article examines whether – and if so how – independent commissions can provide a mechanism to re-negotiate a social and corporate contract capable of external validation and replication, critical factors for the maintenance of legitimacy, or whether official discourse simply reinforces the politics of illusion, privileging symbolic posturing over substantive change.*

## **1 Introduction**

In 1990, Michael Hammer contributed a seminal article to the *Harvard Business Review*.<sup>1</sup> In the face of profound changes to an operating or regulatory environment, Hammer argued that a reliance on piecemeal reform, such as merely speeding up reporting mechanisms through the more efficient deployment of information technology, pre-ordained failure. The management consultant advocated instead a re-engineering of business practice, best achieved through the obliteration of outdated rules, assumptions and processes. For Hammer, this required nothing less than a re-conceptualisation of business purpose. The approach rehearsed, without the social conscience, the “creative destruction”

---

\* Professor of Law, Faculty of Law, University of New South Wales, Sydney, email justin.obrien@unsw.edu.au

1 M Hammer, “Re-engineering work: don’t automate, obliterate” (1990) 7 *Harvard Business Review* 104.

metaphor deployed almost 50 years previously by Joseph Schumpeter.<sup>2</sup> It was a message that simultaneously informed and legitimised the transformation from managerial to financial capitalism. A progressive hollowing out of regulatory and legal frameworks throughout the 1990s, particularly in London and New York, the demise of relational banking and the creation of a shadow banking system combined to displace rather than eliminate risk and responsibility. Fears that the increasing sophistication of financial markets inevitably would be accompanied by enhanced volatility and chronic instability were ignored.<sup>3</sup> The unintended implications of privileging innovation over security across the financial sector are becoming increasingly apparent for the corporation, the market in which it is nested and the underpinning legal and regulatory frameworks.<sup>4</sup> As a consequence, we have reached a tipping point in the theory and practice of financial regulation.<sup>5</sup>

At a technical level, work towards building a coordinated global framework has already taken place, particularly through the auspices of the G20. Implementation remains some way off, however, a point underscored by the Secretary General of the International Monetary Fund, Dominique Strauss-Kahn, at the World Economic Forum meeting in Davos.<sup>6</sup> At a regional level, progress has been equally glacial. The European Union has introduced a European Systemic Risk Board to be based at the European Central Bank in Frankfurt, with the latter providing secretariat facilities. The aim is to provide an early warning system, capable of heading off problems before they occur, the first step towards adopting a more pre-emptive approach to banking regulation. Dominated by representatives of central banks and regulatory agencies, there is a serious question over lack of industry and professional representation. As such a critical information-gathering mechanism is lost. Unresolved too are significant structural questions. In particular, there is a failure to define what constitutes systemic risk, the responsibilities of specific epistemic communities in ameliorating those undefined risks, and what conceptual re-engineering is required to take cognisance of the limitations of the efficient market hypothesis. The answers to these questions will determine the size and scope of financial markets at national, regional and global levels.

2 J Schumpeter, *Capitalism, Socialism and Democracy* (New York: Harper & Row 1942).

3 H Minsky, *Stabilizing an Unstable Economy* (New York: McGraw Hill Professional 2002), p. 315.

4 Evidence to House Committee on Financial Services, "Regulatory restructuring and the reform of the financial system", Washington DC, 21 October 2008 (J Stiglitz); see also R Bootle, *The Trouble with Markets* (London and Boston: Nicholas Brealey 2009), p. 239; E Connors, "Future fund chief sees day of reckoning for banks", *Australian Financial Review*, 14 January 2009, pp. 1 and 38, quoting David Murray, head of the Australian Future Fund: "Everybody got carried away by the concept of a 'millionaires factory' which was not culturally good. Where you don't want your brightest, or at least too many of them, in jobs which spend time interpreting or arbitrating rules. This is not really effective work and a lot of investment banking is that type of deal structuring, which is not very constructive. It produces over-engineered stuff that is the first to break when anything goes wrong" (at p. 38) For discussion of admission of regulatory fealty to "ideological construct", see Evidence to House Committee on Oversight and Government Reform, Washington DC, 23 October 2008 (A Greenspan).

5 See J O'Brien, "The future of financial regulation: enhancing integrity through design" (2010) *Sydney Law Review*, forthcoming.

6 BBC News, 30 January 2010 <http://news.bbc.co.uk/1/hi/business/8488927.stm> (last accessed 30 January 2010). In an interview with the BBC's economic editor, Stephanie Flanders, Strauss-Kahn suggested there was a serious risk of a race to the bottom in global finance as countries adopted piecemeal changes. In a second interview, the chief economics advisor to President Obama, Larry Summers, argued that the introduction of differing institutional and regulatory rules was not necessarily inconsistent with global rules on capital adequacy or limits on leverage capacity; see S Flanders, "Summers speaks", BBC News Website, 30 January 2010, [www.bbc.co.uk/blogs/thereporters/stephanieflanders/2010/01/summers\\_speaks.html](http://www.bbc.co.uk/blogs/thereporters/stephanieflanders/2010/01/summers_speaks.html) (last accessed 30 January 2010).

The roadblocks to substantive reform can, in turn, be traced to three interlinked factors. First, there is a lack of clarity over what precise combination of incremental factors caused the crisis. This makes it difficult to apportion blame and responsibility and design more effective restraining interlocks. Second, given that the crisis was, in the main, a technically legal failure in which the spirit of regulatory rules or principles was transacted around and responsibility for the impact of ethical degradation of professional norms on market integrity compartmentalised, a failure to address this dimension in policy terms preordains failure. Third, and most problematically, restricting the size of the financial sector presents significant and potentially destabilising challenges to the legitimacy and authority of financial capitalism as a distinct engine of growth.<sup>7</sup> Thus, despite having a seat at the table in the debate over global reform of capital markets, there is a dispiriting lack of detail emanating from Beijing, New Delhi and Brasilia over what precise recalibration is required to enhance the ethical dimension of financial capitalism. This means that the quest for change must begin – but not end – with introspection from those countries most affected.

This article examines the limitations of privileging technical solutions and placing responsibility for early warning systems in the hands of those institutions that remain wedded to outmoded conceptual frameworks which demonstrably were unfit for purpose. Second, it evaluates the possibilities of using independent commissions to provide a more granular investigation of the causes of the crisis, a necessary prerequisite for the introduction of sectoral, professional and epistemic reform. Third, it examines the risk that sub-optimally designed inquiries can exacerbate rather than ameliorate the interlocking political, regulatory and corporate crisis, with particular reference to plans for a banking inquiry in the Republic of Ireland. In the concluding section, it evaluates whether independent commissions can provide a mechanism to re-negotiate the corporate contract in a manner that is capable of external validation and replication – critical factors for the maintenance of legitimacy – or merely privilege the politics of illusion.

## 2 Deflecting blame: the traditional response

The global financial crisis first displayed its symptoms in the residential securitisation finance market in the United States but metastasised ferociously, particularly across the North Atlantic.<sup>8</sup> To be sure, the major identified causes of the meltdown were far from unique.<sup>9</sup> Excessive reliance on short-term calculations, for example – made manifest by flawed remuneration policies – have long exercised the academic and policy communities,

---

7 G Tett, “Asian banks told to seize ‘once in a lifetime’ chance”, *Financial Times*, 30 January 2010, p. 14, quoting Tony Tan, head of the Government Investment Corporation of Singapore, the city state’s largest sovereign wealth fund, questioning the efficacy of a “system of free markets and minimal regulation and large dependence on financial institutions”.

8 The most complete, if US-centric and partially referenced, accounts are to be found in W Cohan, *House of Cards* (New York: Doubleday 2009); A Ross Sorkin, *Too Big to Fail* (New York: Viking 2009); G Tett, *Fool’s Gold* (London: Free Press 2009); for application to economic theory, see J Cassidy, *When Markets Fail* (London: Penguin 2009); Gerald Davis, *Managed by the Markets* (Oxford: OUP 2009).

9 See C Reinhart and K Rogoff, *This Time is Different: Eight centuries of financial folly* (Princeton NJ: Princeton UP 2009), pp. 203–22, arguing that macro-economic “indicators showed the United States at high risk of a deep financial crisis in the run-up to 2007 but many of the [specific] problems were hidden in the ‘plumbing’ of the financial markets” (pp. 220–1); see also C Kindleberger, *Manias, Panics and Crashes: A history of financial crises* (New York: Basic Books 1989).

particularly in the United States.<sup>10</sup> Likewise, the dangers of chrematistic trading have long been recognised, if ignored by policy communities.<sup>11</sup> Less well explored are the cultural and ideational factors that coalesced to form what was presented as the economically rational but were, in fact, essentially ideological constructs. The extent of the global financial crisis has occasioned political rhetoric that holds out the tantalising promise of the most far-reaching review of corporate governance, corporate law and financial regulation in a generation.<sup>12</sup> The real danger, however, is that a reliance on technical considerations as cause or solution for the crisis alone preordains failure, a point highlighted by the French president at the opening session of the World Economic Forum in Davos.<sup>13</sup>

Unfortunately, there is little evidence that legislators have addressed in a meaningful sense these broader cultural factors, preferring instead to focus on rising capital adequacy and quality standards and emphasising structural issues, such as reducing leverage ratios or proposing as yet inchoate plans to restrict proprietary trading, as in the proposal by the Obama administration now under consideration by Congress. This attempt to force a return to utility banking and prevent banking entities from holding stakes in alternative asset classes, such as hedge funds and private equity, derives from past failure to take into consideration the consequences of allowing unregulated expansion of the financial sector or the dynamics of capital market regulation, in particular, the role played by ideational factors in privileging emasculated conceptions of regulatory and corporate responsibility.

Demonising banking executives may serve short-term political purposes but it fails to take into account political culpability. In the United Kingdom, for example, traditional forms of inquiry have been privileged, with predictable results. As with congressional hearings in Washington, in testimony provided to the Treasury Select Committee in Westminster, for example, banking executives claimed that the crisis was the result of a

---

10 See L. Bebchuk and J. Fried, *Pay without Performance* (Cambridge and London: Harvard UP 2004); L. Bebchuk, J. Fried and D. I. Walker, "Managerial power and rent extraction in the design of executive compensation" (2002) 69 *University of Chicago Law Review* 751; for application to the fall of Lehman Brothers and collapse of Bear Stearns, see L. Bebchuk, A. Cohen and H. Spamann, "The wages of failure: executive compensation at Bear Stearns and Lehman 2000–2008", Harvard Law and Economics Discussion Paper, 24 November 2009, <http://ssrn.com/abstract=1513522> (last accessed 24 January 2010).

11 See K. Greenfield, *The Failure of Corporate Law* (Chicago: Chicago UP 2006).

12 See G. Brown, "The global economy", speech delivered at Reuters Building, London, 13 October 2008. Gordon Brown subsequently went further, calling for international coordination and arguing that the G20 needed to "discuss whether we need a better economic and social contract to reflect the global responsibilities of financial institutions to society", press conference, G20 Finance Minister Meeting, St Andrews, Scotland, 7 November 2009; for United States, see B. Obama, "Remarks on financial regulatory reform", press conference, White House, Washington DC, 17 June 2009.

13 Sarkozy described the global financial crisis as a "crisis of globalisation" and noted "the crisis we are experiencing is not a crisis of capitalism. It is a crisis of the denaturing of capitalism – a crisis linked to loss of the values and references that have always been the foundation of capitalism. Capitalism has always been inseparable from a system of values, a conception of civilisation, an idea of mankind. Purely financial capitalism is a distortion, and we have seen the risks it involves for the world economy. But anti-capitalism is a dead end that is even worse. We can only save capitalism by rebuilding it, by restoring its moral dimension. I know that this expression will call forth many questions. What do we need, in the end, if it is not rules, principles, a governance that reflects shared values, a common morality?" See N. Sarkozy, speech delivered at the World Economic Forum, Davos, 27 January 2010.

“perfect storm” or “financial tsunami”; the conflation of factors beyond control.<sup>14</sup> The hearings and actual and proposed changes to legal and tax frameworks create a conspicuous spectacle that only partially and temporarily satisfied national unease at a crisis of confidence in public and corporate governance, which failed to prevent the meltdown and has occasioned the most significant investment by either the US or UK governments in financial services ever seen.<sup>15</sup>

The hearings and legal changes in both the United States and the United Kingdom served six core symbolic functions.<sup>16</sup> In both jurisdictions they were designed to enhance the popularity of the officeholder (or, more accurately, arrest a precipitous decline); provide reassurance that significant action was being taken; simplify a complex problem; assert a normative improvement in governance with applicability; provide an identifiable class of perpetrator, in this case investment banking and the credit-rating agencies; and posit an educative function by suggesting tangible ways in which to inculcate an ethical basis within corporate practice. An exercise in symbolism also requires an effective diffusion mechanism. Crucially, the underlying message must not be diluted by the capacity of elite groups to distort or taint the underlying message.<sup>17</sup> These conditions held firm initially. The scale of intervention fundamentally displaced the power of vested-interest groups. The alacrity with which loans have been paid back, particularly in the United States, however, has reduced the direct influence over internal governance arrangements, particularly executive remuneration, within what are recognised as systemically important industries.

Notwithstanding the calls for an international coordinated response to deal with the moral hazard associated with rescuing institutions deemed to be too big to fail, or increasing rhetoric over the need for these same institutions to devise living wills, actual substantive change has been illusive within both domestic and international domains. Moreover, senior banking figures, such as Goldman Sachs’ chief executive, Lloyd Blankfein, have made it

---

14 Evidence to House Committee on Oversight and Government Reform, “Hearing on the causes and effects of the Lehman Brothers bankruptcy”, Washington DC, 6 October 2008 (R Fuld). This choice of metaphor was also deployed by Alan Greenspan to deflect responsibility; see Evidence to House Committee on Oversight and Government Reform, “Hearing on the role of federal regulators in the financial crisis”, Washington DC, 23 October 2008 (A Greenspan). Many of the British bankers involved in the crisis, past and present, appeared before the Treasury Select Committee. The former chief executive officer of HBOS, Andy Hornby, accepted that the bonus culture played a part in exacerbating systemic risk; see Evidence to Hearing on Banking Crisis, Treasury Select Committee, Westminster, 10 February 2009 (A Hornby). For specific compliance failure within HBOS, see explosive memo from its former head of compliance, Paul Moore, “Memo to Treasury Select Committee”, Westminster, 10 February 2009: “My personal experience of being on the inside as a risk and compliance manager has shown me that, whatever the very specific, final and direct causes of the financial crisis, I strongly believe that the real underlying cause of all the problems was simply this – a total failure of all key aspects of governance. In my view and from my personal experience at HBOS, all the other specific failures stem from this one primary cause.”

15 For the United States, see Troubled Asset Relief Program administered through the Economic Stabilisation Act 2008 and American Recovery and Reinvestment Act 2009; for the United Kingdom changes in banking regulation through the Banking Act 2009 and the use of fiscal policy to impose a 50 per cent tax on banking bonuses. Both serve deeply symbolic purposes, see M Edelman, “Symbols and political quiescence” (1960) 54 *American Political Science Review* 695: “It is only as symbols that these statutes have utility to most of the voters. If they function as reassurances that threats in the economic environment are under control, their indirect effect is to permit greater exploitation of tangible resources by the organized groups concerned than would be possible if the legal symbols were absent.” (at p. 702); see, more generally, M Edelman, *The Symbolic Uses of Politics* (Urbana and Chicago: University of Illinois Press/Illini Books 1964); M Edelman, *Constructing the Political Spectacle* (Chicago: Chicago UP 1988).

16 See B Stolz, “The Foreign Intelligence Surveillance Act of 1978: the role of symbolic politics” (2002) 24 *Law and Policy* 269, at 271–2.

17 See J Hart, “President Clinton and the politics of symbolism: cutting the White House staff” (1995) 10 *Political Science Quarterly* 385, at 397.

clear that the febrile nature of capital markets necessitates at least the possibility of further intervention, dispelling in the process arguments that the moral hazard question has been dispensed with.<sup>18</sup> As such, pronouncements of control have a particularly hollow ring.

Plans by the Obama administration to reduce the capacity of banks engaging in risky behaviour through proprietary trading are a case in point. While laudable, they face a less than assured outcome. The negotiations coincide with pivotal mid-term elections and, as noted above, reflect past policy failure rather than evidence of resolve.<sup>19</sup> It is less than clear that the floor of the Senate or the even more rancorous House of Representatives can provide a venue for considered debate on the regulation of Wall Street,<sup>20</sup> not least because of the Supreme Court's decision to lift prohibitions on corporate funding of political campaigns.<sup>21</sup> Moreover, even if, in the unlikely event that piecemeal change within one component of the regulatory matrix, such as banking corporations, is passed, enormous if unintended consequences for the conceptual underpinning of corporate law and the resulting legal and regulatory frameworks could occur.<sup>22</sup>

Given the scale of the liability borne by the taxpayer as a consequence of individual, corporate and regulatory misjudgments, myopic faith in ideational constructs and the failure to resolve an existential conflict between the demands of public and private law,<sup>23</sup> there is undoubted rhetorical strength in calls for a re-negotiated corporate contract.<sup>24</sup> They are also exceptionally difficult to render operational, not least because of (purposive) ambiguity over what constitutes appropriate terms of reference. If we are, as Sarkozy and Brown have suggested, to re-engineer the corporate contract, it is essential that we understand the forces

- 
- 18 Evidence to Financial Crisis Inquiry Commission, Washington DC, 14 January 2009 (L Blankfein).
- 19 The risks associated with proprietary trading have long been recognised, see S Strange, *Mad Money* (Manchester: Manchester UP 1998).
- 20 S Chan, "Dodd calls Obama's reform plan too ambitious", *New York Times*, 3 February 2010, B1, quoting the Senate Banking Committee chair, Senator Chris Dodd saying that proposals to establish a "resolution agency" to break up systemically dangerous institutions and limiting proprietary trading as "getting precariously close" to excessive ambition.
- 21 D McKittrick, "Lobbyists get potent weapon in campaign ruling", *New York Times*, 22 January 2010, p. 1, reporting the Supreme Courts in *Citizens United v Federal Election Commission* (No. 8-205) to lift bans on corporate treasuries funding political campaigns on the grounds that it violated the First Amendment and quoting President Obama that the ruling provide a "green light to a new stampede of special interest money in our politics"; see also, however, K Strassel, "Bonfire of the populists", *Wall Street Journal*, 29 January 2010, A13, noting the ease with which the Obama administration has turned to baiting Wall Street, thus following a standard pattern. For discussion of the uneasy relationship between Wall Street and Washington, see T McCraw, *Prophets of Regulation* (Cambridge: Harvard UP 1984); S Fraser, *Wall Street: A cultural history* (London: Faber & Faber 2005); K Phillips, *Wealth and Democracy: A political history of the American rich* (New York: Broadway Books 2002), pp. 347–71. For discussion of influence of money in American politics, see E Drew, *The Corruption of American Politics* (New York: Overlook Press 2000); see also F McChesney, *Money for Nothing: Politicians, rent extraction and political extortion* (Cambridge: Harvard UP 1997).
- 22 See P Alessandri and A Haldane, "Banking on the state", presentation at Federal Reserve Bank of Chicago International Banking Conference, Chicago, 25 September, 2009, see [www.bis.org/review/r091111e.pdf](http://www.bis.org/review/r091111e.pdf) (last accessed 4 February 2010) suggesting "distortions [caused by] limited liability" could be resolved by a "re-thinking of capital structure" that involves the introduction of "contingent liability" (p. 8).
- 23 D Millon, "Theories of the corporation" (1990) *Duke Law Journal* 201, at 201–02; see also C Stone, "Corporate vices and corporate virtues: do public/private distinctions matter" (1981) 130 *University of Pennsylvania Law Review* 1441, at 1442; for explication of the normative case for breaking down the artificial boundaries, see H Collins, *Regulating Contracts* (Oxford: OUP 1999), p. 59, noting the need for the "productive disintegration of private law".
- 24 See Sarkozy, Davos speech, n. 13 above. Of critical importance in this reframing is France's impending chairship of the G20, see G Tett, "Do not dismiss Sarkozy's back to the future currency plan", *Financial Times*, 29 January 2010, p. 34, in which the respected capital markets editor notes the speech "reveals more about France's determination to shape the global intellectual debate – at a time when America is looking increasingly confused – than any clear policy initiative".

that “denatured” financial capitalism. There is recognition (but not necessarily optimism) in the United States at least that a more studied approach to the problem is required.<sup>25</sup> The search for root causes is also a policy priority in parts of Europe, although it remains very much open to question whether, with the exception of Iceland, where a truth commission has been established, the current trajectory of official discourse can provide either answers or the intellectual underpinning for a new system of financial regulation at national or international level.

### 3 The role of commissions of inquiry

“We shall not grow wiser,” quipped Fredrich Hayek in his influential defence of free markets “before we learn that much that we have done was very foolish.”<sup>26</sup> Belief in the power of official discourse to provide a compelling independent account of the causes and consequences of a specific failure has been one of the main but not sole justifications for independent review.<sup>27</sup> Other factors include the need to be seen to deal decisively with a matter of pressing public concern, thus defusing short-term political pressures, legitimising governmental responses or providing a route-map for policy change.<sup>28</sup> Official discourse may also serve to legitimate existing public policy. As Burton and Carlin have claimed, it can function as a mechanism “to present failure as temporary, or not failure at all and to re-establish the image of administrative and legal coherence and rationality”.<sup>29</sup> There is considerable evidence, for example, that commissions of inquiry served this function throughout the Northern Ireland conflict and its aftermath.<sup>30</sup> There is no guarantee that this will occur, especially in cases where technological advances and sophisticated uses of that technology allow for cross-referencing of disclosed source material and the creation of alternative narratives.<sup>31</sup> Indeed, following the Hutton Inquiry into the death of a weapons inspector, the cogency of alternative critiques was a critical factor in the decision to cede the Butler Inquiry into the legality of the decision to go to war and the quality of governance arrangements. Its decision to hold proceedings in camera, in turn, created the impetus for the convening of the Chilcott Inquiry, which culminated in a public cross-examination of the former prime minister, Tony Blair, on 29 January 2010. As was to be expected, Blair did not use the appearance to express regret, much to the chagrin of relatives of those killed in Iraq, watching from the public gallery. Nevertheless, the public nature of the hearing did perform a cathartic function. This cathartic capacity extends to

25 “Editorial: the show must not go on”, *New York Times*, 17 January 2010, WK7.

26 F Hayek, *The Road to Serfdom* (Chicago and London: Chicago UP 1943), p. 177.

27 For a useful review, focusing primarily on the Commonwealth, see G Gilligan and J Pratt (eds), *Crime Truth and Justice: Official inquiry, discourse, knowledge* (Uffculme: Willan Publishing 2004).

28 See S Prasser, “Royal commissions and public inquiries: their uses and scope”, in P Weller (ed.), *Royal Commissions and the Making of Public Policy* (South Melbourne: Macmillan Publishing 1994), pp. 1–21, 6–8.

29 F Burton and P Carlen, *Official Discourse: On discourse analysis, government publications, ideology and the state* (London: Routledge & Kegan Paul 1979).

30 J O’Brien, *Killing Finucane* (Dublin: Gill & Macmillan 2005), pp. 127–49.

31 A talismanic example is the Hutton Inquiry in the United Kingdom, set up to investigate the causes of the death of a British weapons inspector who committed suicide after he was disclosed as the primary source for a BBC report that accused the government of “sexing up” intelligence in the lead-up to the invasion of Iraq. The Hutton website allowed for cross-referencing of source material to an extent not seen before. See [www.the-hutton-inquiry.org.uk](http://www.the-hutton-inquiry.org.uk) (accessed 29 January 2010). By contrast, the Iraq Inquiry, chaired by Sir John Chilcott into the reasons for invading Iraq has a much less sophisticated website, which suggests that placing documents into the public domain is less of a priority: see [www.iraqinquiry.org.uk](http://www.iraqinquiry.org.uk) (accessed 29 January 2010). The point here is not that the Chilcott Inquiry is less than robust or is designed blindly to advance government policy. Rather, it is to suggest that commissions with judicial authority have exceptional power to place information into the public domain and allow for electronic cross-referencing, but that that power is infrequently used.

the United States, which has privileged the use of independent commissions to deal with matters of acute public concern, such as Watergate and the 9/11 attacks on Washington and New York. As with the Royal Commission of Inquiry model in the United Kingdom, convening an inquiry provides reassurance that lessons will be drawn and acted upon (although there is no guarantee that the reform agenda will be enacted, in particular, if the investigative body lacks either subpoena power or the willingness to deploy it).<sup>32</sup> The decision by the United States to convene a Financial Crisis Inquiry Commission, under the auspices of the Senate, provides evidence of both dynamics.

In interpreting its terms of reference, the chair of the Financial Crisis Inquiry Commission, Phil Angelides, asserts that the commission has a mandate to provide:

[a] full and fair investigation in the interests of the nation – pursuing the truth, uncovering the facts and providing an unbiased, historical accounting of what brought our financial system and our economy to its knees. This is what the American people deserve and this is what we are obliged to do. In this critical instance, if we do not learn from history, we are unlikely to fully recover from it.<sup>33</sup>

Although the commission has the capacity to subpoena documents, there is no evidence to date that it has done so. Initial public hearings with the nation's top bankers did not elicit granular information about strategic motivations and internal processes.<sup>34</sup> This failing was most apparent in the superficial questioning associated with the credit default swap market. In evidence to the commission, the chief executive of Goldman Sachs, Lloyd Blankfein, rejected charges that the bank was profiteering from betting against the very securities it was marketing. According to Phil Angelides, the practice “sounds to me a little like selling a car with faulty brakes and then buying an insurance policy on the drivers of those cars”.<sup>35</sup> Blankfein claimed Goldman Sachs was compliant with disclosure obligations and was merely fulfilling market desires.<sup>36</sup> The exchange generated more heat than light. The critical issue was why did Goldman Sachs and other banks feel it both morally acceptable to engage in such trading activities and to design their compliance and codes of conduct accordingly?

The Financial Crisis Inquiry Commission is not scheduled to publish its final report until December 2010 so there is still time to influence the trajectory of regulatory reform. Indeed, a useful precedent can be found in the Pecora Hearings established in the aftermath of the Wall Street Crash. Pecora's critique of banking practice provided a narrative to justify the creation of the New Deal regulatory architecture.<sup>37</sup> There is to date, however, no sign

32 This is precisely the reason media outlets opined that it was essential for any inquiry into the financial crisis to have congressional authority, including subpoena power, with the Pecora and Watergate Hearings held up as talismanic of best practice; see “Editorial: questions for reform”, *New York Times*, 29 March 2009, WK8.

33 “Opening remarks”, Financial Crisis Inquiry Commission, Washington DC, 17 September 2009 (P Angelides).

34 See “Editorial”, n 25 above, noting that “the primary aim is not to air issues and foster debate, but to test views, resolve contradictions and arrive at evidence-based conclusions . . . Serious investigative work is the only way to counter the banks' political power and alter a reform effort that is headed in the wrong direction.”

35 Financial Crisis Inquiry Commission, Washington DC, 14 January 2010 (P Angelides).

36 Evidence to Financial Crisis Inquiry Commission, Washington DC, 14 January 2009 (L Blankfein).

37 That architecture included the Securities Act 1933 through which an independent accountant had to certify the authenticity of accounts offers by new entrants to the securities market. This was extended to cover all those trading by the Securities and Exchange Act 1934, which also transferred, in theory, the oversight function to the newly established Securities and Exchange Commission. Thirdly, Congress divined that a major contributing factor to the speculative behaviour and resulting scandal was the role played by the banking sector. Rather than accept assurances that conflicts of interest could be contained, or managed, the Glass–Steagall Act of 1933 ordered the separation of commercial and investment banking. These reforms were progressively hollowed out and in the case of Glass–Steagall repealed through the provisions of the Financial Modernization Act (1999). For background on Pecora Hearings, see C Geisst, *Wall Street* (Oxford and New York: OUP 1999), pp. 196–244.

in the United States of a reform agenda of similar vision. This can be traced to the multiplicity of domestic and foreign policy problems facing the Obama administration, the complexity of the task but also, crucially, a failure to address the critical issue that the president himself has identified; the lack of moral accountability in contemporary markets.<sup>38</sup> Questioning that elicited considered responses from the nation's top bankers on how to design regulatory systems that encompass the need for moral restraint would not only have narrowed and deepened the investigation, it would also have provided a template for moving forward. The failure to do so marks a missed opportunity.

Although the Financial Crisis Inquiry Commission will eventually have a full-time staff of between 40–50 investigators and an operating budget of \$8m, there is a lack of detail about just what it will investigate and how. Moreover, the commission has been exceptionally tardy in creating a communications strategy, a move in sharp contrast to the Congressional Oversight Panel (COP) established to ensure that the Department of Treasury was accountable in managing the Troubled Asset Relief Program.<sup>39</sup> Not only did the COP hold a series of meetings outside the Washington Beltway, it actively solicited comments from the public. Moreover, the COP chair, Elizabeth Warren, used her position to advance significant policy recalibration based on a stated need, she saw as unfulfilled, to understand the root causes rather than merely the symptoms of the crisis. This myopia had, according to the COP, undermined the consistency and coherence of the Treasury's response to the crisis as well as that of other financial services regulators.<sup>40</sup> For the COP then, it was incumbent that any redesign must reflect the inadequacies within the theory and practice of regulation. It remains to be seen whether the Financial Crisis Inquiry Commission will examine these foundational matters, but the lack of policy coherence to date does little to inspire confidence.

Across Europe, policymakers face similar pressures, perhaps nowhere more so than Iceland, where a truth commission has been established alongside a criminal investigation headed by an investigating magistrate brought in from France to assure the public that, where possible, wrongdoing would be prosecuted.<sup>41</sup> The truth commission model allows for the venting and cauterisation of anger and addresses sectoral responsibilities. By providing a holistic mapping of a crisis, it can provide the evidence base on which to recalibrate policy. One of the defining aspects of the South African Truth and Reconciliation Commission was its extensive mapping of sectoral responsibility, including the complicity of the judiciary and the media. Of particularly more significance is the normative justification of introducing a re-distributive agenda that comprises political, social and economic dimensions. Establishing one, however, requires cognisance of the

---

38 Remarks on Financial Regulatory Reform, press conference, White House, Washington DC, 17 June 2009. According to President Obama, "in many ways, our financial system reflects us. In the aggregate of countless independent decisions, we see the potential for creativity – and the potential for abuse. We see the capacity for innovations that make our economy stronger – and for innovations that exploit our economy's weaknesses. We are called upon to put in place those reforms that allow our best qualities to flourish – while keeping those worst traits in check. We're called upon to recognise that the free market is the most powerful generative force for our prosperity – but it is not a free license to ignore the consequences of our actions."

39 For discussion of the role of the COP, see J O'Brien, *Engineering a Financial Bloodbath* (London: Imperial College Press 2009), pp. 98–104.

40 COP, *Accountability for the Troubled Asset Relief Program*, Second Report, Washington DC, 9 January 2009, p. 9: "For the panel, it was important for the Treasury and our financial services regulators to have an analysis of the causes and nature of the financial crisis to be able to craft a strategy for addressing the sources, and not solely the symptoms, of the problem or problems."

41 For background to the Icelandic crisis, see M Lewis, "Wall Street on the tundra", *Vanity Fair*, October 2009 [www.vanityfair.com/politics/features/2009/04/iceland200904](http://www.vanityfair.com/politics/features/2009/04/iceland200904) (last accessed 4 November 2009).

need to address fundamental (if not revolutionary) change.<sup>42</sup> The chair of the Icelandic commission, Justice Pall Hreinsson, argues that “it is paramount that we understand. So that we can change the things we need to, and live with what we have to live with.”<sup>43</sup> Iceland, outside the protection of the European Union, with a small population and facing economic devastation, had little choice but to accept a degree of collective soul-searching. As the Prime Minister, Johanna Siguroardottir puts it:

Icelanders are both angry and full of sorrow and anxiety. They feel betrayed in many ways by the state, by the banks and by our allies. But the anger is also directed inwards – at ourselves as individuals and as a nation. Why did Icelanders let this happen? Sorting out those feelings will be a long and difficult process.<sup>44</sup>

Other countries at the periphery of Europe, including Ireland, attempted to cauterise the problems by blaming global forces. It is a predictable and to an extent self-serving response. In Ireland, tens of thousands have taken to the streets to protest against the costs associated with bailing out the banking sector, in particular the rescue of Anglo Irish Bank, a deeply flawed institution that has become talismanic of poor corporate governance practice.<sup>45</sup> The Irish government has further sought to deflect blame by commissioning a series of semi-private investigations. As will be explored below, this response presents a paradigm case in emasculated responsibility.

#### 4 Banking on the truth?

The scale of the calamity now facing Ireland far exceeds situations faced by any of its European partners, with the possible exception of Greece. Throughout the boom years of the Celtic Tiger the population was encouraged to engage in an act of stunning self-deception. Unsustainable property valuations created not just a speculative commercial and residential bubble but also a speculative economy. In September 2008, Ireland took the unprecedented decision to provide an unlimited guarantee of all banking deposits. The move prompted large capital outflows from the rest of Europe, particularly the United Kingdom. It was designed to protect an increasingly strained domestic banking sector. In a rare admission of failure, the Taoiseach, Brian Cowen, accepted “arrogance” played a role in transforming the country from “unknown prosperity to suddenly [facing] survival

42 The South African Truth and Reconciliation Commission is paradigmatic, see S Leman-Langlois and C Shearing, “Repairing the future: the South African Truth and Reconciliation Commission at work” in G Gilligan and J Pratt (eds), *Crime Truth and Justice: Official inquiry, discourse, knowledge* (Uffculme: Willan Publishing 2004), pp. 222–42, noting that the “truths” established were not “scientific truth. The TRC Report was not science, and it was not meant to be. Commissions, and the TRC provides an excellent example, establish truths but they are not truth-finding in a scientific sense. They are rather modern morality plays that mobilise facts to articulate and promote normative agendas.” (p. 231)

43 S Bowers, “Iceland one year on: small island in big trouble”, *The Guardian*, 28 September 2009 [www.guardian.co.uk/business/2009/sep/28/iceland-crisis-one-year-on](http://www.guardian.co.uk/business/2009/sep/28/iceland-crisis-one-year-on) (last accessed 3 February 2010).

44 A McDonald, “Johanna Siguroardottir interview: extended version”, *New Statesman*, 15 January 2010 [www.newstatesman.com/international-politics/2010/01/iceland-interview-economy](http://www.newstatesman.com/international-politics/2010/01/iceland-interview-economy) (last accessed 16 January 2010).

45 M Wall and S Collins, “Change to cuts strategy ruled out as protests seek ‘fairer’ way”, *Irish Times*, 7 November 2009, p. 1; R Brown, “Failed by Fianna”, *New Statesman*, 11 January 2009 [www.newstatesman.com/economy/2010/01/ireland-irish-social-dublin](http://www.newstatesman.com/economy/2010/01/ireland-irish-social-dublin) (last accessed 16 January 2010). For discussion of the broader issues raised by the failure of the Irish banking system, see F O’Toole, *Ship of Fools* (London: Faber & Faber 2009), in which the cultural commentator notes caustically that one consequence of the decision to nationalise Anglo Irish Bank was that “the state was making its citizens responsible for an institution whose books were the most inventive work of Irish fiction since [James Joyce’s] *Ulysses*” (p. 210).

stakes”.<sup>46</sup> Brian Cowen displayed reticence, however, in accepting political responsibility for corporate and regulatory failure.<sup>47</sup> At the same time, the Irish government has been slow to release information about the underlying fragility of the economy, the dependence of the banking sector on unsustainable practices and the extent to which regulatory and political authorities had knowledge of this vulnerability prior to the collapse and, just as significantly, the introduction of the banking deposit guarantee and subsequent policy recalibration, including the nationalisation of Anglo Irish Bank in January 2009 and the creation of the National Asset Management Agency (NAMA), which is designed to restore the capital adequacy of remaining banks by buying (at a discount) impaired property loan portfolios.

In January 2010, a full year after the government was forced to nationalise Anglo Irish Bank, the Finance Minister, Brian Lenihan, partially changed tack, arguing that:

[the] public is entitled to a full examination of what went wrong in our banking system. More than that, we need an inquiry in order to restore international and domestic confidence in our banks. We need, as a country, to understand the origins of this crisis so that we can ensure that we do not make the same mistakes again.<sup>48</sup>

The solemnity of the announcement, made in the Irish Parliament, mirrored the rhetorical commitment offered by the Financial Crisis Inquiry Commission in the United States. Significantly, however, the terms of reference and method of inquiry differ dramatically. Although the Finance Minister has not foreclosed the possibility of a wide-ranging investigation, a truncated two-stage process is envisaged.

First, the Government will immediately commission two separate reports – one from the Governor of the Central Bank on the performance of the functions of the Central Bank and the Financial Regulator and the second from an independent “wise” man or woman with relevant expertise to conduct a preliminary investigation into the recent crisis in our banking system and to inform the future management and regulation of the sector. These reports will also consider the international, social and macro-economic policy environment, which provided the context for the recent crisis. I expect both reports to be completed by the end of May this year and laid before the Houses shortly thereafter. The second stage of the inquiry will be the establishment of a statutory Commission of Investigation, which will be chaired by a recognised expert or experts of high standing and reputation. The terms of reference for this commission will be informed by the conclusions of the two preliminary reports. The aim will be for the commission to complete its work by the end of this year. Its report will then be laid before the Oireachtas for further consideration and action by an appropriate Oireachtas committee.<sup>49</sup>

The impetus is credited to the newly appointed governor of the Irish Central Bank, Patrick Honohan, who is charged with compiling the first document on regulatory failure (but not, significantly, the interaction with the political establishment). The terms of

---

46 Brian Cowen, speech delivered at the Chamber of Commerce Annual Dinner, Dublin, 5 February 2009, excerpted in H McGee, “Cowen says recession to cut living standards by over 10%”, *Irish Times*, 6 February 2009, p. 1.

47 See J Grant and J Murray Brown, “ISE chiefs say Irish opacity must be stopped”, *Financial Times*, 30 January 2010, p. 14, quoting the chief executive of the Irish Stock Exchange (ISE), Deirdre Somers, saying “companies must consider whether their historical practices, although accepted in the past, will meet market expectation in the future”. The same article quotes the concerns of the chair of the ISE, Pádraig O’Connor, about “a cultural malaise” that must “utterly be changed”.

48 B Lenihan, “Statement by the Minister of Finance on banking”, press release, Dublin, 19 January 2010, [www.finance.gov.ie/viewdoc.aspx?DocID=6166](http://www.finance.gov.ie/viewdoc.aspx?DocID=6166) (last accessed 29 January 2010).

49 Ibid.

reference also depart in fundamental ways, however, from proposals provided by the governor himself the previous month. Then the governor argued that Ireland should follow the United States in convening a broad-ranging commission.

A hearing such as this one is fine, by and large. However, this issue is bigger and more complicated than one that can be accommodated by such a hearing as this where people present evidence and then go away. Also, the question would not be sufficiently answered by a judicial inquiry because one is not simply trying to find out what happened and the sequence of events. We should think in terms of getting experts, including experts in economics and social science and so on, and to blend them with politicians and arrive at a panel somewhat like the US congressional panels which consider particular issues on an ad hoc basis, such as the 11 September events.<sup>50</sup>

As Patrick Honohan intimated in his appearance at the Oireachtas:

the crisis is not simply a question of discovering who did what and who knew what. Uncovering the deep roots of the crisis will require expertise and broad social scientific understanding more than merely forensic skills.<sup>51</sup>

As a former academic, the governor is well placed to begin this process. It is questionable, however, whether he is permitted publicly to disclose information,<sup>52</sup> a point made somewhat mischievously by the opposition Labour deputy leader, Joan Burton, and not altogether convincingly rebutted by the Irish Taoiseach, Brian Cowen. The primary problem with the Irish government's proposal, however, centres on the third component, namely the convening of a statutory Commission of Investigation whose terms of reference will be determined by the initial reports. Much depends on how the governor (if permitted) and Klaus Regling, a former senior official at the German Ministry of Finance and European Commission, appointed to draw up the second scoping document, interpret their brief and, crucially, the degree to which the subsequent Commission of Inquiry interprets both its own mandate and the lessons identified.<sup>53</sup> Moreover, there is a profound lack of transparency in the process, compounded by a lack of direct accountability afforded by public hearing or disclosure of documentary evidence.

A properly constituted Commission of Inquiry has a range of mandated powers including the capacity to subpoena documentary, written and oral evidence.<sup>54</sup> At the same time, however, it is envisaged that the investigation will be held in private unless "a witness requests that all or part of his or her evidence be heard in public and the commission accepts the request"<sup>55</sup> or "the commission is satisfied that it is desirable in the interests of

50 Evidence to the Joint Oireachtas Committee on Economic Regulatory Affairs, Dail Eireann, Dublin, 19 December 2009 (P Honohan). In written remarks, the governor of the Central Bank argued the need for new models of inquiry, stating "In considering how best to do this, I suggest that new models need to be explored. The crisis is not simply a question of discovering who did what and who knew what. Uncovering the deep roots of the crisis will require expertise and broad social scientific understanding more than merely forensic skills." (p. 5)

51 Written Evidence to the Joint Oireachtas Committee on Economic Regulatory Affairs, Dail Eireann, Dublin, 19 December 2009 (P Honohan), p. 5.

52 Central Bank Act 1942, s. 31 (1).

53 In a statement the Minister of Finance, Brian Lenihan, emphasised the need to analyse the "international, social and macro-economic policy environment in which the banking crisis developed". See Department of Finance, "Appointment of independent expert to conduct a preliminary investigation into banking crisis", press release, Dublin, 29 January 2010. Note that this formulation appears to downplay domestic and, in particular, political factors.

54 Commission of Investigation Act 2004, s. 16.

55 *Ibid.*, s. 11(1)(a).

both the investigation and fair procedures to hear all or part of the evidence of a witness in public”.<sup>56</sup> Moreover, the legislation specifically allows those giving evidence to challenge placing anything on the public record that could be deemed commercially sensitive, which is defined as the disclosure of information that:

could reasonably be expected to—(a) materially prejudice the commercial or industrial interests of the person who provided that information to the commission or of a group or class of persons to which that person belongs, or (b) prejudice the competitive position of a person in the conduct of the person’s business, profession or occupation.<sup>57</sup>

In announcing the terms of reference, the Finance Minister, Brian Lenihan, argued that for “an investigation to proceed speedily and cost-effectively, it must be able to conduct its business in private. The only other alternative that allows us to conclusively investigate a matter is a tribunal of inquiry” which would, he argued be too costly and protracted.<sup>58</sup> This is, however, political dissembling. The crisis facing the banking system is not a result of recent inept policy choices; rather it is a failure to learn the lessons exposed in a series of Tribunals of Inquiry convened throughout the late 1990s, which continue their work despite corporate obfuscation and increased political hostility. In part this can be traced to the meandering nature of the main political inquiries – an investigation into political payments made to the former Fianna Fail Taoiseach, Charles Haughey, and Michael Lowry, a former Fine Gael Minister of Communications, and a separate inquiry into corruption in the planning process in County Dublin – that became mired in judicial disputes but which also demonstrated conclusively that corruption extended well beyond the named individuals.<sup>59</sup> The tribunals were convened to demonstrate that Ireland was moving forward and that more accountable governance arrangements had been put in place. Attempts to compartmentalise blame – meaning effectively the denial of responsibility – along with media reporting of the costs eroded confidence in the tribunal as a mechanism of accountable governance. This calamitous failure was masked by the illusion of sustained wealth creation brought about through the inflation of a speculative bubble.

If Ireland is to emerge from the banking crisis it is essential that the nexus between the political establishment, the banking sector and the developers be explored in a much more systematic manner. This appears unlikely. The terms of reference specifically preclude discussion of political responsibility for either preventing the crisis or in responding to it, most notably the shoring up of the Irish banking system through the introduction of the blanket guarantee, the nationalisation of Anglo Irish Bank, the decision not to nationalise the remaining banks, and the decision to create the NAMA.<sup>60</sup> Indeed, the very existence of the NAMA reflects the degradation of Irish corporate, political and regulatory governance. As the operation of the COP demonstrated in the United States, the fact that a rescue operation is ongoing is an insufficient barrier to the introduction of effective ongoing accountability monitoring mechanisms. Moreover, the refusal to release information

---

56 Commission of Investigation Act 2004, s. 11(1)(b).

57 *Ibid.*, s. 36(3).

58 M O’Halloran and M O’Regan, “Lenihan rejects Oireachtas inquiry deciding on facts or individuals”, *Irish Times*, 21 January 2010, p. 5.

59 For discussion of the role of the tribunals, see J O’Brien, *The Modern Prince: Charles J Haughey and the quest for power* (Dublin: Merlin 2002).

60 See O’Brien, *Engineering a Financial Bloodbath*, n 39 above, at pp. 13–21.

provided to the government immediately prior to the introduction of the banking guarantee on the grounds of cabinet confidentiality sets a worrisome precedent.

A freedom of information request made in relation to belatedly disclosed handwritten records of two meetings at the Department of Finance on the night before the guarantee was announced has been rejected by the Office of the Information Commissioner (OIC). A preliminary finding from a senior investigator in the commission had held that:

the public interest in the department [of finance] being held to account for its decision to commit billions of euro to the banking sector in the context of the guarantee would outweigh any damage in confidentiality in its dealings with the sector.<sup>61</sup>

Significantly, the Department of Finance's objection to the OIC was backed by two of Ireland's leading banks, Bank of Ireland and Allied Irish Bank, neither of which were publicly at significant risk at the time and both of which had argued that they were adequately capitalised.<sup>62</sup> One major identified problem in the Irish context was the lack of disclosure about how thinly capitalised the banking sector had become and the degree to which this risk was known by either the banks' boards or the regulator and actively or tacitly colluded in by adherence to government policy. Unless this is investigated, Ireland is prone to repeat its failure. It would appear likely from the *Sunday Times* precedent that the Commission of Investigation will come under significant pressure be forced not to disclose granular information on the grounds that it is commercially sensitive and that the Department of Finance, in particular, will retreat where possible to obfuscation and delay. In sharp distinction to the Icelandic investigation, which includes a degree of contrition, there is no evidence that Ireland is prepared to countenance political culpability. As such, despite nods to principles of transparency, accountability and best practice in investigative forums, official discourse remains rooted in a culture of denial.

## 5 Conclusion: reframing the agenda

In each of the jurisdictions surveyed here, with the exception of Iceland, official discourse has not gone substantially beyond rhetoric in either diagnosing the extent of the problem or its implications for the theory and practice of financial regulation. There is a dynamic interplay between the culpability of individual actors and the cultural and ideational factors that not only tacitly condoned but also actively encouraged the elevation of short-term considerations over longer-term interests within and across the corporate, regulatory and

61 See M Tighe, "Bank bailout meeting to stay secret", *Sunday Times* (Irish Edition), 24 January 2010 [www.timesonline.co.uk/tol/news/world/ireland/article7000036.ece](http://www.timesonline.co.uk/tol/news/world/ireland/article7000036.ece) (last accessed 4 February 2010).

62 The Department of Finance had claimed that the account of the meeting was part of an incorporeal cabinet meeting and should remain undisclosed, see Freedom of Information Act 1997, s. 19(1)(c), authorising non-disclosure of "information (including advice) for a member of the Government, the Attorney General, a Minister of State, the Secretary to the Government or the Assistant Secretary to the Government for use by him or her solely for the purpose of the transaction of any business of the Government at a meeting of the Government". This was upheld by the OIC who argued that "in view of the unprecedented circumstance of this case, the only correct conclusion is to find that the primary use of the information was indeed to transact business of the Government at that incorporeal Government meeting". The decision includes concern that vital records were not disclosed to the OIC because of a "simple oversight . . . [that] calls into question the efforts made by the Department to fully identify all relevant documents at the outset". Moreover, although the OIC allowed the non-disclosure of two key documents, she found that "it is disappointing that it took 9 months and extensive correspondence before the Central Government Department with overall responsibility for implementing FOI policy in the public service finally accepted that most of the records it had strenuously maintained were extremely sensitive and exempt were, in fact, suitable for release". See *Sunday Times* and the Department of Finance, Case 090028 <http://oic.gov.ie/en/DecisionsOfTheCommissioner/LongFormDecisions/Name,11453.en.htm> (last accessed 4 February 2010).

political spheres. This requires that we expand our focus beyond breaches in formal rules (which, in any case, can arguably be transacted around) or principles (that lack the definitional clarity to be enforceable). It is essential to evaluate how these rules and principles are interpreted within specific corporate, professional epistemic communities and how these influence and are influenced by regulatory practice.<sup>63</sup> Moreover, the dangers associated with such an emasculated approach to governance have long been apparent, most recently in the debate over the reprise of private equity, which accompanied the boom and prompted little more than hand-wringing.<sup>64</sup>

The rise of private equity was itself seen in some quarters as an unintended consequence of changed enforcement priorities.<sup>65</sup> In the United States, for example, regulators were under increasing pressure not to exercise instruments of control introduced in the aftermath of financial reporting scandal. Creative enforcement mechanisms, such as mandating governance change in exchange for a decision to stay or drop corporate prosecutions, were presented, with partial judicial justification, as the illegitimate exercise of prosecutorial discretion. More generally, the costs (generated primarily by the audit profession itself) of validating internal control processes are blamed (on the Securities and Exchange Commission) for driving business off-market and offshore. The United Kingdom luxuriated in the apparent strength of its much-vaunted system of risk-based regulation, which on the most charitable reading proved to be chimeric. While the global financial crisis

- 
- 63 This requires sophisticated mapping of regulatory domains, see C Hood, H Rothstein and R Baldwin, *The Government of Risk* (Oxford: OUP 2004), p. 8. It also requires deep ethnographic investigation of actual practice and how innovation is both conceived as a social good and therefore legitimated. The classic example is insurance, see V Zelizer, *Morals and Markets: The development of life insurance in the United States* (New York: Columbia UP 1979). A similar dynamic applied to the emergence of financial derivatives. A social network comprising former regulators, academics and leading practitioners changed perception of the moral utility of options from dubious gamble to respected financial instrument, see D Mackenzie and Y Millo, "Negotiating a market, performing theory: the historical sociology of a financial derivatives exchange" (2003) 109 *American Journal of Sociology* 107. This process can generate a powerful ideational paradigm, see J Nash, "Framing effects and regulatory choice" (2006) 82 *Notre Dame Law Review* 314; see, more generally, T Porter and K Ronit, "Self-regulation as policy process: the multiple and criss-crossing stages of private rule making" (2006) 39 *Policy Sciences* 41; T Prosser, "Regulation and social solidarity" (2006) 33 *Journal of Law and Society* 364, noting that most conflicts in regulation are about fundamental values (p. 372). What is at issue, therefore, is the extent to which obligation is conceived self-reverentially in narrow technical terms or more expansively, taking into account how individual transactions, while legal, may at the same time erode market integrity, see T Arnold, "Rethinking moral economy" (2001) 95 *American Political Science Review* 85: "Constitutive social goods establish and symbolize important senses of self . . . . Insofar as constitutive social goods structure the status and obligations of persons, their value includes the meaningfulness of the relationships and the sense of self generated." (pp. 90–1)
- 64 Financial Services Authority, *Private Equity: A discussion of risk and regulatory engagement*, Discussion Paper 06/06 (London: FSA 2006). Supporters of private equity countered that these risks were overblown, see P Yea, "Do we condemn or cheer the flight to private equity?", *Financial Times*, 15 February 2007, p. 15. Yea, who is chief executive of Europe's largest private equity fund, 3i, was unapologetic: "While it may seem unfair that the private equity model has the advantage, that surely is the point of capitalism – that those with the advantage win." (p. 15)
- 65 McKinsey Report, *Sustaining New York's and the US' Global Financial Services Leadership* (2007), criticising "the multi-tiered and highly complex nature of the US legal system . . . [along with] the lack of coordination and clarity on the ways and means of enforcement . . . [leads to a perception that it is] neither fair nor predictable" (p. 17). The McKinsey Report endorses the findings of a separate investigation, see Committee on Capital Markets Regulation, Interim Report (2006), which suggested the "criminal enforcement system needs better balance" (p. xii). Both feed into and amplify warnings by the US Treasury Secretary to policymakers not to create or maintain "a thicket of regulation", see H Paulson, "Remarks on the competitiveness of US capital markets", speech delivered at National Economic Club of New York, 20 November 2006. Paulson's speech follows exactly the template offered two weeks earlier by the principal figures of the Committee on Capital Market Regulation, see G Hubbard and J Thornton, "Is the US losing ground?", *Wall Street Journal*, 30 October 2006 (online edn).

has roots undoubtedly much deeper than the activities of private equity firms, the reliance on leverage that the asset class both caused and reflected and the calamitous failure to mitigate those dangers at policy level precisely because the debate took place at a primarily technical level have now become apparent.

Understanding the root causes of the global financial crisis requires that the debate is informed by a normative dimension; namely, what is the purpose of the financial sector and what, if any, restraints must be placed on untrammelled growth in order to protect society from externalities, conveniently excised from macro-economic models and legal and regulatory policy? This, in turn, requires a thorough investigation of the ideational terms of reference and how these were embedded and moulded by specific epistemic communities. Placed on a continuum, Iceland has gone furthest in determining sectoral responsibility while Ireland the shortest. At a global level, the concentration of resources on the resolution of technical matters within unstable conceptual frameworks provides little solace that substantive change will occur, leaving intact the privileging of the politics of illusion.